Charitable Choices: The Need for a Uniform Nonprofit Limited Liability Company Act (UNLLCA)

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Uniform laws serve an important role in our society, balancing state autonomy and the need to provide consistent solutions to common problems among the states. The Uniform Law Commission (ULC) is the preeminent authority that promulgates uniform laws. To date, the ULC has promulgated over 150 uniform and model acts. ULC tackles a wide array of issues, including child custody and protection, probate, electronic records, and commercial law. The ULC aims to "provide[ ] states with non-partisan, well-conceived and well-drafted legislation that brings clarity and stability to critical areas of state statutory law."

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1. The Uniform Laws Commission is also commonly referred to as the National Conference of Commissioners on Uniform State Laws (NCCUSL).
2. The American Bar Association, and its sections, committees and working groups (collectively, the "ABA") primarily focus on the development of model laws, though the ULC and the ABA have each ventured into the other’s domain. The ABA and ULC have also worked cooperatively on various model and uniform acts as well. See Model Entity Transaction Act, infra note 69. The third member of this major policy expert triumvirate is the American Law Institute (ALI), focusing primarily on promulgation of restatements of common law. See About ALI, https://www.ali.org/about-ali/ (last visited Nov. 11, 2015).
The law governing nonprofit organization desperately needs uniform guidance. Nonprofits comprise an important part of the economic, social, and civic fabric of American society. As such, they often serve the neediest in communities across the nation while providing a collective economic impact rivaled by few other American industry sectors. Many nonprofits are smaller and less

Conference of Commissioners on Uniform State Laws (NCCUSL), now in its 123rd year, provides states with non-partisan, well-conceived and well-drafted legislation that brings clarity and stability to critical areas of state statutory law. ULC members must be lawyers, qualified to practice law. They are practicing lawyers, judges, legislators and legislative staff and law professors, who have been appointed by state governments as well as the District of Columbia, Puerto Rico, and the U.S. Virgin Islands to research, draft, and promote enactment of uniform state laws in areas of state law where uniformity is desirable and practical. ULC strengthens the federal system by providing rules and procedures that are consistent from state to state but that also reflect the diverse experience of the states; ULC statutes are representative of state experience, because the organization is made up of representatives from each state, appointed by state government; ULC keeps state law up-to-date by addressing important and timely legal issues; ULC’s efforts reduce the need for individuals and businesses to deal with different laws as they move and do business in different states; ULC’s work facilitates economic development and provides a legal platform for foreign entities to deal with U.S. citizens and businesses; Uniform Law Commissioners donate thousands of hours of their time and legal and drafting expertise every year as a public service, and receive no salary or compensation for their work; ULC’s deliberative and uniquely open drafting process draws on the expertise of commissioners, but also utilizes input from legal experts, and advisors and observers representing the views of other legal organizations or interests that will be subject to the proposed laws. ULC is a state-supported organization that represents true value for the states, providing services that most states could not otherwise afford or duplicate. Id.

9. There is some debate around the exact meaning of the term “Nonprofit Organization.” Collectively, they are sometimes referred to as the independent sector, the third sector, the voluntary sector, and the philanthropic sector. See Bruce Hopkins, The Law of Tax-Exempt Organizations 6 (9th ed. 2007) (“The English language has yet to capture the precise nature of this sector; in a sense, none of these appellations is appropriate.”). These organizations are hereinafter referred to collectively as “nonprofits” and singularly each a “nonprofit.” However, experts widely accept the premise that incumbent in the term, at least in the United States, is recognition by the United States Internal Revenue Service as an organization exempt from federal income tax under Internal Revenue Code § 501(c)(3) or other applicable sections. See 26 U.S.C.A. § 501; IRS Pub. 4220, Applying for 501(c)(3) Tax-Exempt Status, http://www.irs.gov/pub/irs-pdf/p4220.pdf (generally describing the requirements for tax exemption).

10. Lester M. Salamon, S. Wojciech Sokolowski & Stephanie S. Geller, Holding the Fort: Nonprofit Employment During a Decade of Turmoil, NONPROFIT ECONOMIC DATA BULLETIN, no. 39, at 2 (2012), http://css.jhu.edu/wp-content/uploads/downloads/2012/01/NED_Nation al_2012.pdf (noting that the nonprofit sector employs eighteen times more employees than the utilities industry, fifteen times more than the mining industry, nearly ten times more than the agriculture industry, five-and-a-half times more than the real estate industry, nearly three times more than the real estate industry and twice as many as the wholesale trade, finance and insurance, and construction industries respectively). The economic importance of the nonprofit sector is also revealed in the human resource contributions reflected in sector productivity, both in employment and volunteer contexts. Id. In 2010, nonprofit organizations employed 10.7 million workers, representing ten percent of the nation’s workforce and making the nonprofit workforce the third largest of all U.S. industries behind retail trade and manufacturing. Id.
sophisticated than their for-profit counterparts; accordingly, they can benefit most from the clarity and stability uniform laws provide to states.11

In 1996, to provide a template for states in addressing the needs of the nonprofit sector, the ULC promulgated the Uniform Unincorporated Nonprofit Associations (UUNAA) as a nonprofit equivalent of the Uniform Partnership Act (UPA), which had been available since 1914.12 Similarly, the American Bar Association (ABA) Business Law Section promulgated the Model Nonprofit Corporation Act (MNCA) and Model Business Corporation Act (MBCA) as separate acts.13 In both contexts, the drafting authorities deemed it best to address the unique characteristics and needs of nonprofits, and those of their for-profit business equivalents, in separate acts.14

However, by addressing the limited liability company and its utility in the nonprofit context, the ULC departed from this longstanding precedent and promulgated one Uniform Limited Liability Company Act (ULLCA) to govern both business and nonprofit ventures.15 This approach fails to give states proper guidance on the mandatory and default provisions nonprofits need to maximize management flexibility and maintain tax exemption and an entity level shield.16

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12. The ULC promulgated the Uniform Partnership Act of 1914, issuing the Revised Uniform Partnership Act (RUPA) in 1997. See UNIF. P’SHP ACT (NAT’L CONFERENCE COMM’RS ON UNIF. STATE LAWS 1997). Similarly, the ULC first promulgated the UUNAA in 1996, and the revised act in 2008 (RUUNAA). See UNIF. UNINCORPORATED NONPROFIT ASS’N ACT. Any references to provisions common to the UUNAA and RUUNAA will be referred to as the “UUNAA.”


14. Id.

15. The ULLCA was promulgated in 1996 and revised in 2006, in both cases providing that an LLC could be organized thereunder for “any lawful purpose,” and thereby allowing the organization of a nonprofit LLC. UNIF. LTD. LIAB. CO. ACT (NAT’L CONFERENCE COMM’RS ON UNIF. STATE LAWS amended 2013). The 1996 ULLCA, and all amendments before 2006, will hereafter be referred to as the “ULLCA.” The 2006 ULLCA, and all amendments thereto will be referred to as the “Revised ULLCA” or “RULLCA.” Any references to provisions common to the ULLCA and RULLCA will be referred to as the “ULLCA.”

This work is an extension of the analysis conducted in *Papa’s Brand New Bag: The Need for IRS Recognition of an Independent Nonprofit Limited Liability Company (N LLC)*, which discusses the importance of the limited liability company (LLC) in the nonprofit context and the devices needed to ensure its full enjoyment by the nonprofit sector. Part I examines the history, goals, and purposes for which the ULLCA and other uniform acts were developed. Part II discusses the important role nonprofits play in American society, the economic challenges they face in advancing their charitable purposes, a selection of the current forms of corporate organization available to them, and the limited liability company’s not yet fully-realized potential in the nonprofit context. Part III discusses the ULLCA’s failure, as presently constructed, to guide states in addressing unique nonprofit characteristics and needs. Specifically, the ULLCA leaves key nonprofit governance matters unaddressed, which puts smaller, less sophisticated nonprofits at risk of failing to meet requirements for Internal Revenue Service (IRS) recognition as an 501(c)(3) tax exempt entity. In comparing the ULLCA to the MNCA and UUNAA, it becomes evident that the ULC can address the ULLCA’s nonprofit deficiencies by including protective provisions similar to those in the MNCA and UUNAA in a Uniform Nonprofit Limited Liability Company Act (UNLLCA). Part IV refutes claims that the UNLLCA is unnecessary, untimely, and encourages an unhealthy proliferation of new entities. Part V concludes that the ULC should promulgate a separate UNLLCA to address the unique needs of nonprofits. The appendix proposes key UNLLCA provisions that closely follow the ULLCA where possible and incorporate key protective provisions contained in the MNCA and UUNAA where appropriate.

I. THE PURPOSE AND HISTORY OF THE UNIFORM LAW COMMISSION

The ULC helps state sovereignty and federal law to coexist, preserving our federal system of government. Most American law is created by fifty interdependent but sovereign states. The Tenth Amendment to the Constitution reserves to the states “[t]he powers not delegated to the United States by the Constitution, nor prohibited by it to the States.” Accordingly, most private law matters (e.g.

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19. *Id.* at 8.
20. *U.S. CONST.*, amend. X.
family law, contract law, business organizations) are left to the state legislatures and courts for regulation. However, this constitutional reservation of powers to the states creates the possibility that the states might enact differing statutes on the same subjects, leading to “confusion and difficulty in areas common to all jurisdictions.”

American businesses consequently face serious, costly, and burdensome challenges in navigating a seemingly byzantine network of regulations spanning multiple federal, state, and local jurisdictions. The uniform laws promulgated by the ULC promote the interstate consistency and predictability businesses need.

This Part describes the historical origins of the ULC and how those origins inform its current mission of providing uniform laws. It then describes the road to the Uniform Limited Liability Corporations Act (ULLCA).

A. A Way To Simplify the Byzantine Network: The Creation of the ULC

As the United States industrialized, state common law decisions and uncodified statutes offered different solutions to the same problems—both within the same state and among the several states. This, combined with the inherent instability of the common law, which by its nature was scattered throughout volumes of cases and difficult to ascertain, became more problematic as interstate commerce increased. The uncertainty of the law under this system led many legal scholars to call for states to codify their respective common laws to alleviate the inconsistency between courts and legislatures. Among these scholars was United States Supreme Court Justice Joseph Story. In 1837, Justice Story wrote a report urging Massachusetts to adopt a legal code so that it would no longer be necessary for attorneys to conduct elaborate case-law research to

21. O’Connor, Foreword to Stein, supra note 3, at 8; see, e.g., Loving v. Virginia, 388 U.S. 1 (1967) (acknowledging that marriage is traditionally left to the states to decide). The UCC provides legal rules and regulations governing commercial and business dealings and transactions. Business conducted in different states should comply with the laws of the different states. “This is because even though the substantive nature of all the commercial acts in the states are the same, there are structural differences in the acts based on the local customs of each state.” Uniform Commercial Code, U.S. Legal, Inc., http://uniformcommercialcode.uslegal.com/ (last visited Nov. 11, 2015).
25. Id.
understand diverse judicial pronouncements of common law principles.26

Early American intrastate conflicts between statutes and common law were accentuated by inconsistencies among states in solving the same problems. As interstate commerce expanded, these conflicts became more apparent.27 Despite the need for consistency and predictability among the laws of the different states, imposing a single federal regulatory scheme across several jurisdictions carried the danger of neglecting the unique needs of each state.28 To unify the legal framework of the states without the threat of federal preemption, states were provided the option to “create a forum by which they could voluntarily agree to develop, and then enact, uniform legislation on important subjects of common concern.”29 Several influential lawmaking organizations emerged to aid in balancing state sovereignty and interstate consistency by promulgating uniform and model laws for adoption by the states.30

This balancing has occurred in different forums. First, in 1889, the ABA appointed a special committee on uniformity laws.31 One year later, New York became the first state to establish a commission on uniform state laws.32 The work in New York and similarly situated states established the framework for what would later be the creation of the ULC.33

By the end of 1891, five additional states adopted acts to appoint commissions on uniform laws, all acting in similar fashion to New

26. See Joseph Story et al., Report of the Commissioners Appointed to Consider and Report upon the Practicability and Expediency of Reducing to a Written and Systematic Code the Common Law of Massachusetts, or Any Part Thereof, 17 AM. JURIST & L. MAG. 17 (1837); Stein, supra note 3, at 13.

27. Stein, supra note 3, at 13.


29. O’Connor, Foreword to Stein, supra note 3, at 8. Because state courts are the interpreters of legislative design, our federal government would not endure if uniform laws were constantly imposed on the states by the national government. “Without a uniform law passed by all the states it is otherwise; state courts retain their authority to interpret what the state uniform law means.” Id.


32. Id. See also Francis M. Burdick, A Revival of Codification, 10 COLUM. L. REV. 118, 122 n.16 (1910) (stating that in 1890, the New York legislature authorized the governor to appoint three commissions to examine certain areas of law and to especially consider whether it would be wise and practicable for New York to invite the other States to send representatives to a convention to draft uniform laws to be submitted for the approach and adoption of the several States). Id. (quoting 1890 N.Y. Sess. Laws 413–14).

33. Rassman, supra note 31, at 177.
York. In early 1891, the ABA Committee on Uniform Laws distributed a questionnaire to better understand several aspects of the uniform law movement: (1) the actions each state had taken towards forming a commission on uniformity of law, (2) the areas of law requiring greater uniformity amongst the states, (3) the areas in which uniformity was desirable, (4) the practicality of uniformity in the respective legal areas, (5) any inconveniences resulting in the State from the present want of uniformity, and (6) how these inconveniences could be remedied.

State responses were generally consistent. The inconveniences posed by variant and conflicting laws among the states were of “perplexity, uncertainty, and confusion, with consequent waste, a tendency to hinder freedom of trade and to occasion unnecessary insecurity of contracts, resulting in needless litigation and miscarriage of justice.” The States also indicated that the greatest area of uniformity desired and urgently needed was in matters directly affecting the business common to the whole country, such as “enforcement of contracts, the collections of debts, the transmission of property, and the nature, validity, negotiability, and construction of commercial paper.” States believed that such desired uniformity could best be secured by concurrent action in the various states.

With the documented support of the states, leading attorneys formed the Conference of State Uniform Law Commissioners, which later became the Uniform Law Commission (ULC), and their first meeting took place on August 24, 1892. Seven states were represented at the first meeting. The meeting minutes proudly referred to this gathering as “the most important juristic work undertaken in the United States since the adoption of the Federal Constitution.” By 1893, twenty states were represented, and by 1900, thirty-five states became members of the ULC.

35. Armstrong, supra note 22, at 20.
36. Id.
37. Id.
38. Id. at 20–21.
39. Id. at 21.
40. See generally Stein, supra note 3.
42. Stein, supra note 3, at 83.
43. Stein, supra note 3, at 18–19.
1896, the Commission promulgated the Uniform Negotiable Instruments Law (NIL). The NIL soon became the first uniform law adopted in every state, signaling the ULC’s prominence as an independent authority on uniform laws.

Since its success with the NIL, the ULC has drafted more than 150 uniform acts relating to business entity law, inter alia, with a general focus on unincorporated entities. Some have achieved success similar to that enjoyed by the NIL, widely accepted and enacted by state legislatures. Other uniform laws have been met with far less enthusiasm, resulting in much more limited state adoption. Still other uniform laws faced universal rejection with no states enacting statutes based on the correlating uniform law.

The mission of the ULC has remained consistent since its founding in August of 1892: to provide “uniformity of law among the states, and to support and protect the federal system of government by seeking an appropriate balance between federal and state law.”

The ULC’s standing is manifested by the role its commissioners have played in developing American Law. Former commissioners include U.S. and State Supreme Court Justices.

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46. O’Connor, Foreword to Stein, supra note 3, at 8.


50. O’Connor, Foreword to Stein, supra note 3, at 9.

51. See generally Stein, supra note 3. Justice William Rehnquist served as a commissioner from Arizona from 1963 to 1969 and was appointed to the U.S. Supreme Court in 1972. Id. at 105. Justice Louis Brandeis served as Commissioner from Massachusetts from 1900 to 1905 and was appointed to the U.S. Supreme Court in 1916. Id. at 40, 105. Justice Wiley Rutledge
Attorneys General, Other Justices and jurists have exhibited their regard for the ULC through appearances before the conference and other commendations of its work. Perhaps Justice Ginsburg best explained the nexus between the ULC’s work and the preservation of the great American experiment in her address at the 2003 ULC annual meeting’s opening session:

A federal system like ours cannot endure if uniformity is exclusively imposed on the constituent states by the central government. No doubt Congress can, within constitutional bounds, achieve national uniformity in the area of the law by enacting a federal statute that preempts the field, making federal courts the sole or the leading interpreters of the legislative design. In contrast to the uniformity a federal measure commands, a Conference-drafted and approved uniform law or model act gives the states the opportunity voluntarily to bind themselves closer as harmoniously functioning components of one nation. States can achieve this voluntary linkage by adopting a Conference-produced uniform law as state law or by looking to a Conference-produced model act for guidance. In either case, state courts, not federal tribunals, will maintain

served as commissioner from Missouri from 1931 to 1934 and was appointed to the U.S. Supreme Court in 1943.  

Id. at 76. Justice David Souter served as commissioner from New Hampshire from 1976 to 1979 and was appointed to the U.S. Supreme Court in 1990.  

Id. at 119. Justice Maurice Hartnett served on ULC from 1961 until his death in 2009 and served on the Delaware Supreme Court from 1994 to 2000. Justice Martha Lee Walters served on ULC since 1992, became the first female President of the ULC in 2006 and has served on the Oregon S. Ct. since 2006.  

Id. at 139.  


52.  

STEIN, supra note 3 (showing that prior to serving as a commissioner Justice Souter was the Attorney General of New Hampshire, William Schnader, commissioner from 1924 to 1967 was the Attorney General of Pennsylvania Attorney General). John Sargent (U.S. Attorney General; served as commissioner from 1911 to 1924).  


53.  


54.  

Legendary scholars including Roscoe Pound, Samuel Williston, John Wigmore and William Prosser all served as commissioners. See STEIN, supra note 3, at 30, 40, 85, 219; see also O’Connor, Forward to STEIN, supra note 3, at 9 (quoting Chief Justice Rehnquist’s expression of what his service as a commissioner meant to him: “My most vivid recollection of the annual meetings is the high quality of the floor debate about a pending proposed uniform law. I have seen many deliberate bodies before and since, but in none were the discussions of the same high quality. . . . We were never compensated for our time as lawyers, but we had the privilege of working in a group of diverse and stimulating members of the profession in a very useful and productive effort to benefit the legal system. Such work is its own reward.”).
controlling interpretive responsibility. In short, by taking the lead in promoting voluntary improvement of state law, the Conference safeguards a non-coercive quarter of our vibrant federal system . . . At the same time, the Conference’s commitment to uniformity, where uniformity is appropriate, works to prevent a vibrant federal system from degenerating into a chaotic one . . . You have earned the trust of state legislatures, in part because the Conference has an admirable track record, one you are striving to maintain . . . You know that uniformity ought not override in areas best left for state-by-state evolution and experiment, for state individuality and diversity, too, are part of the genius of our federal system.55

Uniform laws and the ULC continue to play an important role in helping to maintain the important balance of state sovereignty within our federal system, a balance of which is crucial to the fabric of our nation embodied in the U.S. Constitution.56

B. The Road to the ULLCA

One of the ULC’s most impactful acts is the Uniform Partnership Act (UPA).57 The UPA was first introduced in 1906,58 revisited in 1909,59 and officially promulgated in 1914.60 Work on suggested revisions to the UPA provided proof of the ULC and ABA’s continuing interdependence, with an ABA subcommittee studying and recommending amendments to the act.61 In 1987, the ULC appointed a committee to begin drafting the Revised Uniform Partnership Act (RUPA), with the ABA appointing a companion committee to assist.62 The RUPA was formally promulgated in

56. See generally Stein, supra note 3.
62. Hurst, supra note 57, at 577.
Another significant product of the ULC was the Uniform Limited Partnership Act (ULPA). The ABA served in a similar role regarding the development and promulgation of the ULPA.64

The ULC and ABA also divide responsibilities with respect to the distinguishing characteristics of unincorporated entities, such as the partnership and limited partnership vis a vis the corporation. The ULC first took note of corporations in 1903, and approved a Uniform Business Corporation Act (UBCA) in 1928.65 While that fledgling act struggled to gain acceptance, in 1940, the Committee on Business Corporations of the ABA Section of Commercial Law began drafting a Federal Corporation Act.66 In 1950, the ABA committee promulgated its own MBCA, which addressed the same issue as the ULC’s UBCA, which the ULC renamed as the MBCA that same year. The ABA believed its MCBA was “worthy of uniform adoption” by the states.67 Seeing how well the ABA Committee’s goals aligned with its own, and how much success the ABA enjoyed in having its MBCA adopted by the states, the ULC withdrew its MBCA in 1958.68 Since that time, and with notable exceptions, the ULC has generally confined its work to unincorporated business associations, while the ABA has taken control of drafting model corporation acts.69

63. Id. at 578 (explaining that the RUPA initial drafting process concluded in 1992, but there were a number of revisions until the final amendments were adopted); UNIF. P’SHIP ACT (Nat’l Comm’n on Uniform State Laws 1997).

64. UNIF. LTD. P’SHIP ACT (Nat’l Conference of Comm’rs on Uniform State Laws 1976).


66. Id.


68. Booth, supra note 65, at 64.

69. See Model Entity Transaction Act, Prefatory Note (Nat’l Conference of Comm’rs on Uniform Laws amended 2013), http://www.uniformlaws.org/shared/docs/entity_transactions/meta_final_2014.pdf (“For over 90 years, the ULC has prepared and periodically revised uniform laws governing partnerships and limited partnerships. Similarly, . . . committees of the ABA have prepared . . . model laws for the incorporation of business corporations and nonprofit corporations.”). The ULC has expertise in the law of unincorporated entities and the ABA in the law of corporations. See id. The ABA played a significant role in the revision of the UPA; UNIF. P’SHIP ACT, Prefatory Note (Nat’l Conference Comm’rs on Uniform State Laws 1997). In January of 1986, an American Bar Association subcommittee issued a detailed report that recommended extensive revisions to the UPA. Id. The following year, in response to suggestions from various groups, including an American Bar Association subcommittee, the Drafting Committee recommended numerous revisions to the Act that were approved by the American Bar Association House of Delegates in August, 1994. Id. The ABA also played a significant role in the Uniform Limited Liability Company
Despite this de facto jurisdictional separation, the ULC and ABA continue to collaborate when drafting model and uniform laws. The organizations recognize the need for collaboration as particularly important when specific acts touch upon both incorporated and unincorporated entities.\textsuperscript{70} The fluidity of this jurisdictional construct is illustrated and tested by each organization’s treatment of the limited liability company.\textsuperscript{71} The LLC is a relatively new form of unincorporated business organization that combines corporate-style limited liability for its members and managers, with partnership/sole proprietorship styled management and tax flexibility.\textsuperscript{72}

Originating in the late 1970's and initially burdened by unclear tax status, state LLC legislative activity spiked after the IRS ruled that LLCs could be taxable as partnerships, removing the entity level tax burden incumbent in the corporate business form.\textsuperscript{73} This meteoric rise in state LLC legislative activity predated ULC consideration of a uniform act to address this novel entity, so many states enacted LLC legislation without much guidance.\textsuperscript{74} The ABA drafted

\textbf{Act. Unif. Ltd. Liab. Co. Act (Nat’l Conference of Comm’rs on Unif. State Laws 1996).} The Drafting Committee was assisted by a blue ribbon panel of national experts and other interested and affected parties and organizations. Those represented in the drafting process included the ABA. The Committee met nine times and considered comments by its many knowledgeable advisers and observers, as well as an ABA subcommittee’s earlier work on a prototype.

\textsuperscript{70} See, e.g., Model Entity Transaction Act, Prefatory Note. “After beginning their independent drafting projects, both the ULC and the ABA realized that combining their respective areas of expertise would produce the best product for enactment by the states. They have accordingly combined their efforts so that the Model Entity Transaction Act draws on the expertise of the ULC in the law of unincorporated entities and of the ABA in the law of corporations.” Id.; Model Registered Agents Act (Nat’l Conference of Comm’rs on Unif. Laws 2006); Unif. Bus. Org. Code, art. 1 (Nat’l Conference of Comm’rs on Unif. Laws 2011) (“[The ULC] has traditionally drafted acts governing unincorporated entities and the ABA . . . has traditionally drafted corporate entity statutes. Since [some acts deal] with both unincorporated and incorporated entities, there [is] a consensus on the desirability of having this project conducted as a joint project between [the ULC] and the American Bar Association.”)


\textsuperscript{74} See 9 Mertens Law of Fed. Income Tax’n § 33A:2. Many LLC statutes are based in part on the Prototype Limited Liability Company Act (the Prototype Act), adopted in 1992 by the Subcommittee on Limited Liability Companies of the Partnership and Unincorporated Business Organizations Committee of the American Bar Association’s Business Law Section. The Prototype Act was intended as a tool for drafting LLC legislation. The Prototype Act has
the Prototype Limited Liability Company Act (PLLCA) in 1992, but it was met with far less enthusiasm than its predecessor, the MBCA, enjoyed. In promulgating the ULLCA four years later, the ULC acknowledged the ABA drafting committee’s work and the limited state adoption it achieved. Since its promulgation, the ULLCA has gained prominence, having been approved by the ABA House of Delegates and commonly referenced in textbooks, treatises, and other scholarly works. To date, five states and the U.S. Virgin Islands have adopted the ULLCA.

Since promulgating the ULLCA, the ULC has been criticized for failing to proactively meet its mission of “promoting the principle of uniformity.” In fact, critics accused the ULC of directly contravening its stated mission to promote uniformity, clarity, and stability in this important area of law. They argued that the ULLCA did

served as a model for the LLC acts of several states, including Arkansas, Louisiana, Idaho, Indiana, and Montana. Concepts from the Prototype Act have been included in the LLC legislation of other states and in the ULLCA. Id. (inferring that because the ULLCA was not promulgated until 1996, other states had to rely on the ABA Prototype Act and other tools when drafting their LLC legislation). At least four states—Idaho, Montana, Arkansas, and South Carolina—adopted LLC statutes in whole or in part based on the ABA Prototype Act which was drafted before the ULLCA. See also Elizabeth S. Miller & Robert A. Ragazzo, Nonuniformity of State LLC Statutes: Texas Stays on The Cutting Edge, 19 TEX. PRAC. BUS. (explaining that when the ULLCA was drafted, most states had already passed their own acts or were far along in the process); Larry E. Ribstein & Bruce H. Kobayashi, Uniform Laws, Model Laws and Limited Liability Companies, 66 U. COLO. L. REV. 947 (1995).

75. See UNIF. LTD. LIAB. CO. ACT, Prefatory Note (NAT’L CONFERENCE OF COM’RS ON UNIF. STATE LAWS 2006) (stating the Committee considered the ABA subcommittee’s earlier work on a prototype when drafting the ULLCA. The ULC promulgated the original ULLCA in 1994 and amended it in 1996 to take into account the then newly adopted federal tax “check-the-box” regulations.). The 1996 ULLCA, like most existing state LLC statutes, is classified as a “first generation” statute.

76. See MERTENS, supra note 74 at § 35A:2. In 1996, the Act was approved by the American Bar Association House of Delegates. Id.; Compare Unif. Laws Comm’n, supra note 72, with Prototype Limited Liability Company Act: “The views expressed herein have not been approved by the House of Delegates or the Board of Governors of the American Bar Association or any of its Sections or Committees, and, accordingly, should not be construed as representing the policy of the American Bar Association.” Id; William K. Sjostrom, Jr. Business Organizations—A Transactional Approach 16–17, 179–220 (referring only to the ULLCA when discussing LLC statutes and laws, making no mention of the ABA Prototype Act.); Wayne M. Gazur, The Limited Liability Experiment: Unlimited Flexibility, Uncertain Role, 58 L. & CONTEMP. PROBS. 135 (1995).


78. See About the ULC, supra note 11; see also Ribstein & Kobayashi, supra note 74, at 947–48 (arguing that NCCUSL’s promulgation of the ULLCA in 1996 did not produce higher levels of uniformity than pre-promulgation LLC statutes because “despite their apparent chaos, LLC statutes [had] already [ ] become [largely] uniform”). Interstate competition in the for-profit world had led to a competitive set of pre-promulgation statutes. Kobayashi & Ribstein, supra note 23 at 338–39.
little to increase uniformity among the states, pointing to the ULLCA’s departure from established de facto uniformity among the states. Specifically, the ULC rejected the consensus among the majority of the states having LLC statutes in place; instead, it adopted the minority position at a rate of approximately forty-one percent, threatening to cause reduced uniformity among the states instead of achieving the stated purpose of the ULC’s work. 79 This critique partially explains states’ reluctance to enact the ULLCA.80

The Revised Uniform Limited Liability Company Act (RULLCA), promulgated in 2006, extensively revised the ULLCA to provide a more comprehensive and fully integrated LLC statute. It accounted for the best elements of the ULLCA and two decades of legal developments.81 The RULLCA was again amended in 2011 and 2013 to track the language of similar provisions in other uniform and model unincorporated entity acts.82 Still, only fourteen states have enacted the RULLCA.83 States’ tepid reception of the ULLCA and RULLCA, individually and collectively, supports critics’ contentions that the timing of these uniform acts inhibited their ability to provide uniformity.84

79. See Kobayashi & Ribstein, supra note 23 at 341; see also Ribstein & Kobayashi, supra note 74 at 981–82.

80. See Kobayashi & Ribstein, supra note 23 at 329; see also UNIF. LTD. LIAB. CO. ACT (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 1996). In 2015, only Alabama, Hawaii, Illinois, Montana, South Carolina, South Dakota, Vermont, Virgin Islands, and West Virginia are currently utilizing the ULLCA.

81. UNIF. LTD. LIAB. CO. ACT, Prefatory Note (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2006).

82. See, e.g., id. at § 106(a)–(b) (making the operating agreement binding on the LLC); § 108(b) (allowing the LLC to engage in any lawful activity); §§ 104–05 (providing internal affairs default rules governing the relationship between members and managers of the LLC); § 407 (creating a more flexible management structure and clarifying matters involving duties of the managers and members); § 501(a) (restricting the agency authority of members); § 503 (clarifying the applicability of the charging order concept to LLC membership interests); §§ 404–06 (governing distributions made to members); § 701(5)(B) (providing remedies for oppressive conduct); §§ 801–02 (addressing direct and derivative claims); Art 10 (addressing LLC reorganization transactions).


II. THE HISTORY, VALUE, CHALLENGES, AND OPPORTUNITIES OF THE AMERICAN NONPROFIT SECTOR

Similar to the rich American history of uniform laws, philanthropy and charity are deeply imbedded in America’s social fabric. Although charitable giving was important before colonization of the Americas, the demands of the new world made charity imperative not only to the settler’s survival, but to development of a flourishing society by the establishment of hospitals, schools, and churches. Colonists’ religious values placed the health of the community above that of the individual. These beliefs led them to establish institutions and charitable trusts to care for the poor, sick, and elderly. There was very little distinction between the public and private sphere of charitable responsibility.

Modern nonprofits are extremely diverse in both size and purpose, ranging from small grass-roots initiatives operating with a few employees and budgets of $50,000 a year or less, to multibillion dollar relief organizations like the American Red Cross, which employs over 30,000 people. The evolution and diversification of the nonprofit sector has allowed it to maintain and grow its role in

85. The word philanthropy has a Greek etymology meaning “love of humanity.” Philanthropy is a form of social aid that aims to strengthen society’s foundation by attacking the root of the problem through development of hospitals, educational institutions, and other organizations, with the goal of long-term enhancement of human development. See Michael J. Worth, NONPROFIT MANAGEMENT: PRINCIPLES AND PRACTICE (2013). Charity is a short-term donation with the goal of meeting society’s immediate needs such as feeding the hungry and aiding victims of natural disaster. Id. Today, both philanthropy and charity are important to the nonprofit sector, providing social aid similar to their historic origins, often through nonprofits. See also Horváth, supra note 9.

86. See James J. Fishman, The Development of Nonprofit Corporation Law and an Agenda for Reform, 34 EMORY L.J. 617, 620–23 (1985) (reciting the history of charitable giving in England before the seventeenth century, after the enactment of the English Statute of Charitable Uses of 1601, and its evolution in the United States); see also James J. Fishman, Improving Charitable Accountability, 62 Mo. L. REV. 218, 245 (2003) (citing thirteenth century papal decrees encouraging individuals to donate to charitable or religious purposes. Failure to do so risked “eternal damnation”). England largely led the effort to colonize what is now the United States, with establishment of Jamestown, Virginia in 1607. Many of England’s cultural values and common law were embedded in America’s society as a result of England’s colonization.


88. See Fishman, Development of Nonprofit Corporation, supra note 86, at 620–23; see also Fishman, Improving Charitable Accountability, supra note 86, at 245.

89. Id.

90. See Fishman, Development of Nonprofit Corporation, supra note 86, at 620–23.

American society. Nonprofits fill the void between the public and private sector—supplementing services that government can no longer afford to provide and that businesses won’t provide at a discount.

The work of nonprofits relieves government agencies "of the burden of meeting public needs which in the absence of charitable activity would fall on the shoulders of the Government."92 According to a 1938 Congressional Report commenting on nonprofits’ tax-exempt status, “The Government is compensated for its loss of revenue by its relief from financial burdens which would otherwise have to be met by appropriations from public funds.”93 Additionally, nonprofits can more quickly meet the needs of a specific group or individuals lacking adequate social services without considering bureaucratic red tape, political feasibility, or loyalty calculations.94

Modern nonprofits also enhance the sense of community between citizens, fostering social interaction and community interconnectedness through activities ranging from local after school programs and beach cleanups to volunteer home building initiatives such as Habitat for Humanity.95 Moreover, nonprofits,
such as religious organizations, counseling services,\footnote{96} and environmental protection groups,\footnote{97} provide a wide variety of educational services and help to shape America’s social and cultural values.\footnote{98}

The effects of the nonprofit sector reach far beyond shaping the culture and values of America and providing aid to millions of the country’s neediest citizens. Nonprofit organizations are also a large part of the American economy. In recent years, the nonprofit sector has grown with increasing speed, earning the label of a “growth industry.”\footnote{99} In 2010, there were approximately 1.28 million active nonprofits.\footnote{100} In 2013, the number of active nonprofits grew to approximately 1.463 million nonprofits,\footnote{101} an eighteen percent increase since 2010.\footnote{102}

This growth has produced calculable effects on the United States’ economy. In 2010, nonprofits held over $2.9 trillion in assets, reported over $1.6 trillion in revenue,\footnote{103} and received approximately $344.9 billion from donors and grant makers.\footnote{104} In 2012, the nonprofit sector contributed approximately $887.3 billion...
to the United States economy and accounted for 5.4% to the nation’s gross domestic product.\textsuperscript{105} Nonprofits also produced more revenue than the Federal Government, construction industry, and mining industry combined.\textsuperscript{106} According to the Quarterly Census of Employment and Wages, a report created by the Bureau of Labor Statistics with the cooperation of state governments, the nonprofit sector accounted for 10.1% of the nation’s total private employment in 2010, making it the third largest workforce in the United States, behind only retail trade and manufacturing.\textsuperscript{107} Collectively, nonprofits are extremely valuable to the quality of life in the United States.\textsuperscript{108}

As a result of increasing demand and decreasing traditional government funding, many nonprofits are progressively engaging in commercial profit making businesses in order to gain the necessary revenue to support their charitable mission.\textsuperscript{109} Between 2000 and 2010, public charities increased funding through fees for goods and services, including ticket sales, hospital patient revenues, and tuition payments by 72.4%.\textsuperscript{110} In 2012, approximately fifty percent of public charities’ funding was obtained through fees for goods and services, including ticket sales, hospital patient revenues, and tuition payments.\textsuperscript{111} That same year, private charitable giving constituted approximately 12.9% of the total revenue for public charities.\textsuperscript{112}

As a result of their changing sources of income, modern nonprofits employ “organizational infrastructure” substantially similar to for-profit business ventures.\textsuperscript{113} A viable nonprofit almost certainly must use standard accounting procedures, current information


\textsuperscript{107} Salamon et al., supra note 10.

\textsuperscript{108} See supra notes 85–107 and accompanying text; see also Jenkins, supra note 94, at 1094.


\textsuperscript{111} McKeever & Pettijohn, supra note 105.

\textsuperscript{112} McKeever & Pettijohn, supra note 105, at 1, 5.

technology, marketing plans, fundraising strategists, qualified professionally trained employees, and qualified leaders and managers. In a study by the Nonprofit Overhead Cost Project, researchers found that limitations in the organizational infrastructure compromised the nonprofits’ effectiveness. They also learned that “frequent maintenance associated with ‘free’ but mismatched, outdated computers” hindered a nonprofit's efforts. Additionally, when the nonprofit was not able to hire qualified support staff, the positions were commonly filled with inexperienced staff or “the CEO had to fill that role, thereby neglecting parts of the leadership role. The CEO who grabbed a push broom to sweep out the rain that was coming through the roof during our interview was unable to use that time to think strategically or foster new relationships.” In this environment of increased pressure to create efficiency, streamlined governance promoted through promulgation of a UNLLCA would greatly assist nonprofits in managing this pressure.

The nonprofit governance structure is critically important to organizational viability for at least two key reasons. First, the governance structure can help a nonprofit efficiently and effectively meet new challenges and opportunities presented by constantly evolving social and economic conditions. Second, the governance structure is an important IRS consideration in determining whether a nonprofit is eligible for recognition as a 501(c)(3) organization, exempting the nonprofit from federal income tax and unlocking a host of other attendant public and private financial benefits.

Despite organizational and operational needs similar to for-profit equivalents, nonprofits do not enjoy the full array of entity options available to for-profits. Perhaps the most egregious example is the scant use by nonprofits of the increasingly popular LLC in favor of the much more utilized nonprofit corporation. One reason the

115. Id. at 1.
116. Id.
117. See id. at 1–2. Finding, “[s]ites without experienced finance staff had only rudimentary financial reporting and had limited ability to involve program managers in financial management, perform more sophisticated analysis, or identify financial issues for board and senior management . . . leaving basic functions like payroll, benefits, and network support dependent on a single person in even the largest nonprofit with which we spoke.”
118. Compare Garry W. Jenkins, Incorporation Choice, Uniformity, and Reform of Nonprofit State Law, 47 GA. L. REV. 1113, 1124 (2007) (discussing the nonprofit corporation as the preeminent nonprofit entity), with 2005 ANNUAL REPORT, DIVISION OF CORPORATIONS, DEL. DEP’T OF
LLC is not yet widely used by nonprofits is the limited IRS approval of the LLC in the 501(c)(3) exempt entity context. An equally important reason might be the lack of adequate guidance provided by the ULLCA concerning unique nonprofit governance and operational issues.

For the same reasons that the LLC rose as a prominent and preferred business entity option, an independent, tax-exempt Nonprofit LLC (NLLC) would be beneficial to the nonprofit sector because of its management flexibility and liability shield. The LLC has been recognized as “the triumph of common sense and practical business experience.” A creature of contract, the LLC requires far less formality than business and nonprofit corporations. Many of the details regarding procedures, rights, duties, and activities of the company are governed by the operating agreement, allowing for more flexibility and custom tailoring in order to meet a NLLC’s charitable purpose.

119. The IRS does allow the LLC and NLLC to interact with already established nonprofits in two limited circumstances. First, a § 501(c)(3) exempt entity can form an LLC and enter into a joint venture with a for-profit without losing its tax-exempt status in certain circumstances. See Rev. Rul. 98-15, 1998-1 C.B. 718-19 (1998). Second, a § 501(c)(3) may establish a subsidiary LLC to hold property or operations that carry risk. See I.R.S. Priv. Ltr. Rul. 20-01-34-025 (Aug. 24, 2001). The NLLC subsidiary acts as a pass through entity does not have to file Form 1023 or Form 990. Id. Currently, individuals or non-501(c)(3) entities cannot establish a stand-alone NLLC that will qualify for § 501(c)(3) status. See Richard A. McCray & Ward L. Thomas, Limited Liability Companies as Exempt Organizations (2000), https://www.irs.gov/pub/irs-tege/etopich00.pdf.

120. See infra Part III.

121. See UNIF. LTD. LIABILITY CO. ACT § 304 (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2006).


123. See UNIF. LTD. LIABILITY CO. ACT § 110 cmt.

124. See id.; see also Walker, supra note 99, at 652 (noting that removal of directors, shareholder and director meetings, whether directors can vote by email, take action without meeting, vote by proxy, minutes, resolutions, and bylaws are a few corporate legal requirements which typically are not mandated of an LLC).

125. See UNIF. LTD. LIABILITY CO. ACT § 110(a).

126. See id. at § 110.
While both business and nonprofit corporations are managed by a board of directors, the LLC allows stakeholders to choose either a member-managed structure (where the owners directly control the company’s business affairs in a manner similar to a partnership) or manager-managed structure (where the members select a manager who possesses authority more akin to that held by corporate officers and directors). This LLC management structure provides a smaller nucleus of members and managers with more flexible oversight and control of NLLC daily operations. These members and managers will most likely be more familiar with and more passionate about achieving the mission of the organization. Either management style reduces the burden of observing the rigid, detailed set of corporate law and governance rules.

Furthermore, both the business and nonprofit corporate form carry certain incumbent formalities, including established meeting times, quorum requirements for conducting business at those meetings, and the required taking of formal minutes from those meetings. A business or nonprofit corporation that fails to observe corporate formalities runs the risk of losing its valuable liability shield, leaving the shareholders or members exposed to personal liability for corporate debts and liabilities. In contrast, LLC’s flexible management structure generally removes exposure to those risks by eliminating the mandatory formalities required of businesses or nonprofits.

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127. Victor B. Flatt, Notice and Comment for Nonprofit Organizations, 55 Rutgers L. Rev. 65, 65–66 (2002) (noting that the board’s main responsibility is often fund-raising, not oversight, and that directors are generally unpaid and often not chosen for experience in governance).

128. Unif. Ltd. Liability Co. Act § 407 (Nat’l Conference of Comm’rs on Unif. State Laws 2006). An LLC can also be managed by multiple managers acting in concert, similar to partners or a board of directors. See id. This Article does not necessarily argue for member-managed nonprofit LLC; however, one can envision a future in which that too would be a viable nonprofit option.


130. Id.

131. Walker, supra note 99, at 652 (noting that removal of directors, shareholder and director meetings, minutes, resolutions, bylaws, as well as whether directors can vote by email, take action without meeting, or vote by proxy are a few corporate legal requirements which typically are not mandated for LLCs).

132. See Model Bus. Corp. Act, chs. 7, 8 (Am. Bar Ass’n 2002) (establishing, inter alia, meeting, notice, quorum, and voting requirements for corporate shareholders and directors); Id. at § 16.01(a) (requiring maintenance of all corporate shareholder and director meeting minutes); see also Model Nonprofit Corp. Act chs. 7, 8 (Am. Bar Ass’n 2008) (establishing, inter alia, meeting, notice, quorum, and voting requirements for nonprofit members and directors); Id. at §16.01(a) (requiring maintenance of all corporate member and director meeting minutes).

133. See Kansas Gas & Elec. Co. v. Ross, 521 N.W.2d 107, 112–13 (S.D. 1994) (discussing the factors that justify piercing the corporate veil, including failure to observe corporate formalities).
all corporations. These characteristics make the LLC similar to the unincorporated association and its business equivalent, the partnership, in the management flexibility allowed. And, the LLC still maintains the liability shield more comparable to the traditional corporate form.

The LLC’s flexible governance structure also makes amending governance documents far less byzantine, allowing a NLLC to quickly evolve to meet changing economic needs. The NLLC would allow organizations with fewer resources to streamline their management structure in order to deliver more public benefit without the fear of losing their liability shield.

To further maximize resources available for advancing their charitable purposes, nonprofits often seek § 501(c)(3) recognition. The first, and arguably most important reason nonprofits apply for § 501(c)(3) recognition is to become exempt from federal income tax. Exempt organizations can also take advantage of numerous federal, state, and local tax code subsidies, including reduced postal rates, the ability to issue tax-exempt bonds, exemption from federal unemployment taxes, and exemption from most states income, sales, and property taxes. Nonprofits also seek § 501(c)(3) recognition to entice private donor contributions, which are currently deductible under the income, estate, and

134. See UNIF. LTD. LIABILITY CO. ACT § 304(b) (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2006) (noting that debts, obligations, or other liabilities of an LLC are solely those of the company).

135. Walker, supra note 99, at 635 (citing UNIF. LTD. LIABILITY CO. ACT §§ 501–02 (2006)). Compare UNIF. LTD. LIABILITY CO. ACT § 304(b) (2006) (stating, “[t]he failure of a limited liability company to observe any particular formalities relating to the exercise of its powers or management of its activities is not a ground for imposing liability on the members or managers for the debts, obligations, or other liabilities of the company”), with UNIF. UNINCORPORATED NONPROFIT ASS’N ACT § 8(a) (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2008) (stating that “[a] debt, obligation, or other liability of an unincorporated nonprofit association, whether arising in contract, tort, or otherwise: (1) is solely the debt, obligation, or other liability of the association; and (2) does not become a debt, obligation, or other liability of a member or manager solely because the member acts as a member or the manager acts as a manager”).


138. Section 501(c)(3) of the IRC allows a nonprofit to obtain a special status from the IRS after completing certain administrative and operational requirements. 26 U.S.C. § 501(c)(3) (2006). Although there are at least twenty-eight types of organizations entitled to tax-exempt status, this Article is limited to the examination of § 501(c)(3) tax-exempt nonprofits. See McKeeve & Pettijohn, supra note 105, at 2, 6, 8.


143. IRS Pub. 4220, supra note 9.
gift tax. Moreover, § 501(c)(3) organizations are also eligible to receive substantial government grants to help subsidize the goods and services they provide to the community.

To determine whether an entity qualifies for tax exempt status under § 501(c)(3), the IRS employs organizational and operational tests. The IRS prohibits “private inurement” and requires dedication of the entity’s assets to its articulated exempt purposes. These tests ensure that nonprofits receiving a tax benefit are formed to help improve society through its charitable endeavors.

The organizational test establishes certain mandatory requirements for a nonprofit’s governing documents. The governing documents must expressly declare that the organization is formed “exclusively for one or more of the [philanthropic or charitable] purposes specified” in § 501(c)(3). Additionally, the nonprofit must be established for public, not private, benefit and it must not bestow more than incidental economic benefit to any individual or group. The nonprofit may not use a substantial part of its activities to promote political propaganda or attempt to influence legislation, and it may not directly or indirectly intervene in any

144. 26 U.S.C. §§ 170(c)(2), 2955(a)(2), 2522(a)(2) (2013) (only contributions to public charities are deductible). § 501(c)(3). Organizations are typically divided into two categories: public charities and private foundations. Public charities meet certain public support criteria, such as receiving more than one-third of their support from gifts, grants, gross receipts from admissions, and sales of merchandise. They constitute approximately two-thirds of all registered nonprofits. McKEEVER & PETTIJOHN, supra note 105. Private foundations represent the other third of nonprofit § 501(c)(3) organizations. Only contributions to public charities are deductible for federal tax purposes.

145. McKEEVER & PETTIJOHN, supra note 105.


147. Fishman, Development of Nonprofit Corporation, supra note 86, at 620–23; see also Internal Revenue Serv., Internal Revenue Manual § 7.25.3. A nonprofit organization may be for religious reasons or any one of the § 501(c)(3) tax-exempt purposes including, “scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals.”


149. See supra note 85.

150. 26 C.F.R. § 1.501(c)(3)-1; 26 U.S.C. § 501(c)(3) (including “religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals”).

151. 26 C.F.R. § 1.501(c)(3)-1. Although private benefit and no private inurement do overlap, private inurement has a narrower application, only applying to insiders (“a person having a personal and private interest in the activities of the organization”). 26 C.F.R. § 1.501(a)-1(c). No private benefit applies to even “disinterested” parties. See Am. Campaign Acad. v. C.I.R., 92 T.C. 1053, 1068–69 (1989).

Finally, a nonprofit’s governing documents must expressly distribute its assets for a public purpose upon dissolution.\textsuperscript{154} The operational test requires the nonprofit to actually operate in the manner prescribed by the governing documents, “primarily” and “substantially” accomplishing the “exempt” purpose.\textsuperscript{155} The private inurement prohibition protects charitable assets by preventing any portion of the entity’s net earnings to benefit any private shareholder or individual.\textsuperscript{156} The private inurement prohibition includes excessive compensation, below market rate loans, and disproportionate benefits of any kind.\textsuperscript{157}

To complete the registration process, a nonprofit must file for and obtain an Employer Identification Number from the IRS.\textsuperscript{158} It must notify the IRS that it wishes to operate as a § 501(c)(3) tax-exempt nonprofit by filing a Form 1023 or Form 1023-EZ Application for Recognition of Exemption.\textsuperscript{159} Once the application has been received and approved, the nonprofit has very few ongoing IRS filing requirements, the most notable being the annual information return Form 990.\textsuperscript{160}

\section*{III. Model and Uniform Nonprofit Laws: The Need for a UNLLCA}

The importance of the organization options available to nonprofits has been represented in model and uniform laws designed to facilitate the achievement and preservation of the nonprofit’s preferred tax status, and other organizational objectives. The Model Nonprofit Corporation Act (MNCA) and the Uniform Unincorporated Nonprofit Association Act (UUNAA) are prime examples of efforts to meet these goals and highlight glaring Uniform Limited Liability Company Act (ULLCA) deficiencies in meeting the needs of nonprofits.

\textsuperscript{153} Id.
\textsuperscript{154} 26 C.F.R. § 1.501(c)(3)-1.
\textsuperscript{155} To primarily engage “in activities which accomplish one or more of [the] exempt purposes specified . . . .” Id.
\textsuperscript{156} Id.
\textsuperscript{158} IRS Pub. 4220, supra note 9.
\textsuperscript{159} Id.
\textsuperscript{160} Id. The Form 990-EZ and Form 990-N are also available (if the nonprofit’s gross receipts are below $50,000).
The MNCA and, to a lesser degree, the UUNAA both contain key provisions designed to satisfy the IRS’ organizational and operational tests. Although the MNCA allows a nonprofit corporation to be organized for “any lawful purpose,” it also includes numerous exhaustive provisions protecting against private inurement in the context of the organizational and operational tests.\(^{161}\) The act explicitly prohibits the distribution “of any part of its assets, income, or profits to its members, directors, members of a designated body, or officers.”\(^{162}\) However, a nonprofit corporation is allowed to confer benefits upon or make contributions to members or nonmembers in conformity with its charitable purposes.\(^{163}\) The provisions also require that charitable assets be dedicated to the nonprofit corporation’s charitable purposes and prohibit actions that would result in the diversion of property held in trust.\(^{164}\) The MNCA specifically protects against violation of the operational test by requiring that a nonprofit corporation be operated exclusively for the purposes stated in its organizational documents.\(^{165}\)

The UUNAA contains similar, though less exhaustive, language guarding against the diversion of property held for a charitable purpose.\(^{166}\) The definition of an “unincorporated nonprofit

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\(^{161}\) See, e.g., id. at § 10.09(b).

\(^{162}\) Id. at § 6.40(a).

\(^{163}\) Id. at § 6.41(b).

\(^{164}\) See id. §§ 12.03(a), 10.09(b)–(d), 10.23(a)–(c) (addressing amendments to articles of incorporation and bylaws); id. § 11.01(b)–(d) (addressing mergers). The MNCA also provides examples of activities not considered “lawful.” \textit{Model Nonprofit Corp. Act} § 4 (Am. Bar Ass’n 1952). “Labor unions, cooperative organizations, and organizations subject to any of the provisions of the insurance laws of the State may not be organized under this act.” \textit{Id.} The official comments further clarify that any absence of express prohibitions should not be interpreted as permitting activities that would violate the spirit of the law. \textit{Id.} at § 3.01, cmt.

“The failure to set forth an explicit limitation on a nonprofit’s activities does not mean that an enterprising entrepreneur can improperly and with impunity operate in the nonprofit form. In general, public benefit and religious corporations cannot make distributions to members or controlling persons . . . unreasonable compensation cannot be paid to members or controlling persons . . . in addition, the attorney general has broad power to ensure that a public benefit corporation is not operating for the private benefit of any individual. \textit{See id.} at § 3.02. The MNCA also allows incorporators and other fiduciaries to impose other limitations they find necessary on the use of corporate assets, and allows them to grant the corporation specific express powers. These powers include the power to establish pension and benefit plans for its officers, directors, and employees; the power to carry on a business; the power to make donations; the power to issue guarantees; the power to lend money and invest and reinvest funds; the power to establish conditions for membership and to impose dues and assessments; and the power to enter into a partnership or a joint venture.


\(^{166}\) \textit{Unif. Unincorporated Nonprofit Ass’n Act} § 28(4)(A) (Nat’l Conference of Comm’rs on Unif. State Laws 2011). \textit{But see id.} at § 2, cmt. 8. Interestingly, the commentary suggests that the ULC did not want to include restrictive language pertaining to the operation of an unincorporated nonprofit, fearing that, “[i]mposing a statute of frauds or similar
association,” although seemingly simple, provides great foundational insight on the UUNAA’s purpose.167 This definition explicitly distinguishes between entities that can qualify as unincorporated nonprofit associations and those that cannot.168 The UUNAA further allows the unincorporated association to engage in “profit-making activities,” but restricts the use of those proceeds to nonprofit purposes.169 The comment to this section further distinguishes between permitted and prohibited member relationships to the nonprofit association’s profit-making activities.170 The UUNAA also differentiates between permitted and prohibited distributions,171 an important distinction between the essential nature of an unincorporated nonprofit and that of its business entity counterpart, the partnership.172 This distinction is important because most nonprofits are formed, at least in part, to obtain the tax benefits that accompany recognition by the IRS as an entity exempt from federal income tax.173

The ULLCA follows a general trend wherein states allow an LLC to be formed for “any lawful purpose, regardless of whether for profit.”174 The stated purpose of the RULLCA was to allow LLCs

writing requirement would, therefore, have the effect of excluding most existing UNAs from being able to qualify under the act.” Id.

167. See id. at § 2(8).

168. Id.; see also id. at § 2(8), cmt. 8.

169. Id. at § 5(d).

170. See id. at § 5(d), cmt. 4. “The fact that some or all of the members receive some direct or indirect benefit from a nonprofit association’s profit-making activities will not disqualify an unincorporated nonprofit organization from being a nonprofit association under this act so long as the benefit is in adherence of the nonprofit association’s nonprofit purposes. The distribution of any profits to members for the members’ own use, e.g., a dividend distribution to members, would, however, disqualify the organization from being a nonprofit association because the distribution was not made in furtherance of the nonprofit association’s nonprofit purposes.” Id.


172. See id. at § 5(d), cmt 4.

173. See id. at Refs & Annos.

174. UNIF. UNINCORPORATED NONPROFIT ASS’N ACT § 104 (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2008). “In another paper we found evidence consistent with the hypothesis that this process of spontaneous evolution was assisted by a non-NCCUSL model law, the Prototype Limited Liability Company Act (PLLCA), proposed by a committee of the American Bar Association. That article also showed that NCCUSL’s first [ULLCA], promulgated in 1996, failed to follow the obviously uniformity-maximizing strategy of building on the LLC provisions that the states had most commonly adopted. [ULLCA] instead included idiosyncratic provisions more consistent with the influence on the NCCUSL process of lawyers and other powerful interest groups. This paper indicated that NCCUSL seemed to be working counter to rather than in coordination with the state process of spontaneous uniformity.” Kobayashi & Ribstein, supra note 84, at 331. “As we noted in our earlier articles, states managed to achieve considerable uniformity before the 1996 promulgation of the ULLCA.” Id. at 338–39.
more management flexibility than the original ULLCA without substantially affecting the ability of nonprofits to elect LLC status.\footnote{175} However, the RULLCA changed very little of the ULLCA’s approach to nonprofits, incorporating few substantive amendments in the reorganization and revision process.\footnote{176} The ULC took this conservative approach because it was concerned that providing more detailed guidance on nonprofit application of the LLC could produce negative consequences outweighing any attendant benefits.\footnote{177} However, nonprofits electing LLC status without this specific guidance risk denial of § 501(c)(3) tax-exempt recognition.

The ULLCA, as currently constructed, does not contain adequate protective language for satisfying the IRS’ organizational and operational tests. The ULLCA allows formation of an LLC through the filing of “articles of organization” or a “certificate of organization” without any restrictive language as long as its purpose is lawful, and regardless of whether it is organized for profit.\footnote{178} The ULLCA defines a “member” as a person who is entitled to distributions of net

\footnote{175. \textit{Unif. Ltd. Liability Co. Act} § 108 (Nat’l Conference of Comm’rs on Unif. State Laws 2006); see also \textit{Unif. Law Comm’n, supra} note 72. The ULC stated that they wanted to take the “best elements of the ‘first generation’ LLC statutes” and make the act compatible with Revenue Ruling 88 via the RULLCA.” Id.}

\footnote{176. \textit{Unif. Ltd. Liability Co. Act} § 112(a) (Nat’l Conference of Comm’rs on Unif. State Laws 1996) (“A limited liability company may be organized under this [Act] for any lawful purpose, subject to any law of this State governing or regulating business.”). Section 101(3) defined “Business” as including “every trade, occupation, profession, and other lawful purpose, whether or not carried on for profit.” Id. at § 101(3). The RULLCA § 104 included an amendment to the renumbered “Nature, Purpose and Duration” section to include the “regardless of whether for profit” language previously provided § 101(3) of the ULLCA. Id. at § 101(3); \textit{Unif. Ltd. Liability Co. Act} § 104 (Nat’l Conference of Comm’rs on Unif. State Laws 2006).

\footnote{177. Transcript of Annual Meeting of Nat’l Conference of Comm’rs on Unif. State Laws 5 (Aug. 6, 2003) (on file with author). It is argued by Commissioner Breetz in the transcript of the 2003 Annual Meeting of the National Conference of Commissioners on Uniform State Laws that broadening the ULLCA to include nonprofits would give rise to a heightened analysis by the IRS for NLLCs seeking § 501(c)(3) tax-exemption. \textit{Id.; see also Unif. Ltd. Liability Co. Act} § 108, cmt. (b) (2006). The phrase “any lawful purpose, regardless of whether for profit” encompasses even charitable activities, but this act does not include any comprehensive protections pertaining to charitable assets and purposes. \textit{Id.} Section 1003(b) does contain a “nondiversion” provision, but the provision applies only to the organic transactions contemplated by Article 10. Comprehensive protections must be (and typically are) found in other law, although sometimes that “other law” appears within a state’s non-profit corporation statute. \textit{See, e.g., Min. Stat.} § 317A.811 (2012) (providing restrictions on charitable organizations that seek to “dissolve, merge, or consolidate, or to transfer all or substantially all of their assets” but imposing those restrictions only on “corporations,” which are elsewhere defined as corporations incorporated under the non-profit corporation act).

\footnote{178. \textit{Unif. Ltd. Liability Co. Act} § 108(b) (2006). This provision allows an LLC to be formed for nonprofit purposes. \textit{Id.} “A limited liability company may have any lawful purpose, regardless of whether for profit or not.” \textit{Id.} at § 108. “Although some LLC statutes continue to require a business purpose, this act follows the current trend and takes a more expansive
income generated by the entity.\textsuperscript{179} This definition is fatal to a non-profit’s 501(c)(3) exempt status because nonprofits are, by definition, not allowed to facilitate pecuniary gain by their stakeholders.\textsuperscript{180} This is a key reason why the term “member” is traditionally used to differentiate stakeholders in nonprofit corporation statutes from the owners and primary beneficiaries of a business corporation, called “shareholders.”\textsuperscript{181} However, the ULLCA does not distinguish between members as defined and utilized in a traditional business context and members as intended in most nonprofit context.\textsuperscript{182} The merged meanings give rise to issues of private inurement in the operation and dissolution of the LLC.\textsuperscript{183} The ULLCA further allows for and directs the distribution of earnings by the LLC to its members.\textsuperscript{184} This allowance expressly violates the organizational and operational tests.\textsuperscript{185} Additionally, the ULLCA has no prohibition against allowing members to derive some or all benefits from their own LLC.\textsuperscript{186}

\textsuperscript{179} UNIF. LTD. LIABILITY CO. ACT § 401 (1996). The default rule for the ULLCA is equal distribution of shares upon dissolution. However, nonprofits are prohibited by the IRS prohibition against private inurement. \textit{Id.} at § 501(c)(3).


\textsuperscript{181} See \textit{MODEL BUS. CORP. ACT} § 1.40(21) (AM. BAR ASS’N 2002). “Shareholder[’] means the person in whose name shares are registered in the records of a domestic or foreign business corporation or the beneficial owner of shares to the extent of the rights granted by a nominee certificate on file with such a corporation.” \textit{But see} \textit{MODEL NONPROFIT CORP. ACT} § 37(i), 1.40(56), 1.40(37) (AM. BAR ASS’N 2008); \textit{MODEL BUS. CORP. ACT} ch. 14(A) (AM. BAR ASS’N 2002). The MNCA defines a member as one who has the right to “select or vote for the election of directors or delegates or to vote on any type of fundamental transaction.” \texti{MODEL NONPROFIT CORP. ACT} § 37(i) (AM. BAR ASS’N 2008). This is valid because a stakeholder, regardless if they are a shareholder or a member, in any nonprofit is prohibited from private inurement or pecuniary gain.

\textsuperscript{182} UNIF. LTD. LIABILITY CO. ACT § 102 (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2006).

\textsuperscript{183} See \textit{id.} at §§ 404, 707 (2006)

\textsuperscript{184} \textit{Id.} at § 102. The ULLCA § 102 defines distribution as a “transfer of money or other property from a limited liability company to another person on account of a transferable interest” or in the person’s capacity as a member. \textit{Id.}

\textsuperscript{185} Treas. Reg. 1.501(c)(3)-1(c)(2) and tax court prohibition against distribution of earnings for the benefit of private individuals. 26 C.F.R. § 1.501(c)(3)-1(c)(2) (2014); \textit{see also} UNIF. LTD. LIABILITY CO. ACT § 102 (2006) (defining distributions); \textit{Unif. Ltd. Liability Co. Act} § 404(a) (2006) (allowing for redemption of assets to be conveyed in equal shares among members and persons).

\textsuperscript{186} Unif. Ltd. Liability Co. Act § 404(a) (NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS 2006); \textit{see also} Wendy L. Parker Rehabilitation Foundation, Inc., T.C. Memo. 1986-348 (the IRS has held that even a thirty percent interest or benefit by the members of a nonprofit is private inurement and therefore prohibited and violates laws governing an entity’s § 501(c)(3) tax-exempt status).
Because the ULLCA does not address the unique needs and characteristics of nonprofits, an ad hoc, uneven patchwork of legislation, developed by states seeking to correct and supplement the confused guidance of the ULLCA, grows in the void. This patchwork illustrates the need for a UNLLCA to provide that guidance. Tennessee, Kentucky, Minnesota and North Dakota have enacted a few of the most prominent examples of the patchwork of NLLC legislation.

In 1991, Tennessee adopted the Nonprofit Limited Liability Company Act. In doing so, Tennessee authorized nonprofit, tax-exempt corporations to organize an LLC as the sole member, allowing the LLC to qualify as a disregarded entity for federal income purposes and still serve the parent’s purposes.

In 2006, Kentucky similarly amended its LLC Act to allow NLLCs to be formed for “nonprofit purposes.” Kentucky’s Nonprofit Limited Liability Company Act defines “nonprofit purposes” by reference to the purposes clause contained in that state’s Nonprofit Corporation Act. The Act also requires that NLLCs “shall not


188. Walker, supra note 99, at 663.

189. Id. at 646; see also Tenn. Code Ann. §§ 48-101-701 to -708 (2011).

190. Walker, supra note 99, at 646–47; See Tenn. Code Ann., § 48-101-704 (2011) (“A nonprofit corporation may organize a nonprofit LLC by filing articles of organization prominently designating it as a nonprofit limited liability company with the office of the secretary of state consistent with the Tennessee Limited Liability Company Act; provided, that an LLC shall qualify as a nonprofit LLC only if the LLC is disregarded as an entity for federal income tax purposes. No more than one (1) nonprofit corporation may be a member of a nonprofit LLC.”) A NLLC means a limited liability company: "(A) That is disregarded as an entity for federal income tax purposes; and (B) Whose sole member is a nonprofit corporation, foreign or domestic, incorporated under or subject to chapters 51–68 of this title and who is exempt from franchise and excise tax as not-for-profit as defined in § 67-4-2004(33); (4) ‘Parent nonprofit corporation’ means a nonprofit corporation that is the sole member of a nonprofit corporation; and (5) ‘Subsidiary nonprofit corporation’ means a nonprofit corporation whose sole member is a nonprofit corporation.” (designed to facilitate compliance with Announcement 99-102). See also Tenn. Code Ann. § 48-101-702.


192. See Ky. Rev. Stat. Ann. § 275.005 (“A limited liability company may be organized under this chapter for any lawful purpose, including the provision of one (1) or more professional services conducted in or outside the Commonwealth. Except as otherwise provided in K.R.S. 273.150, if the purpose for which a limited liability company is organized or its activities make it subject to one (1) or more special provisions of law, the limited liability company shall also comply with those provisions.”). A "[n]onprofit limited liability company" means "a
have or issue membership interests in the limited liability company, and no distribution shall be paid, and no part of the income or profit of the limited liability company shall be distributed to its members or managers."

In 2009, Minnesota and North Dakota each codified NLLC laws separately from those in which for-profit LLC are located. Each expressly authorizes formation of an LLC for a nonprofit purpose and warns that the provisions do not guarantee exempt entity tax treatment. However, each also incorporates by reference provisions found in the state’s nonprofit corporation statute and aligned with the IRS’ organizational and operational tests. Similar to Kentucky’s Nonprofit Act, the North Dakota Nonprofit Limited Liability Company Act also states “an individual may not be a member of, or own any financial rights or governance rights in, a nonprofit limited liability company.”

Despite the example set by these modern day trailblazers, numerous other states follow the ULLCA, permitting NLLCs to exist, but


193. Ky. Rev. Stat. Ann. § 275.520(1); Walker, supra note 99 at 664; see Ky. Rev. Stat. Ann. § 275.005; Unif. Ltd. Liability Co. Act discussion supra note 182, which explicitly authorizes the making of distributions of earnings or assets to members before dissolution of the LLC; see also Ky. Rev. Stat. Ann. §§ 275.520, 275.525, 275.530. An inadvertent contradiction between section 275.520 (prohibiting the issuance of membership interests) and section 275.015(11) (defining an LLC as having at least one member) further illustrates the need for the clarity a uniform act could provide.


195. See Minn. Stat. Ann. § 322B.975 (2009) (incorporating formation of a NLLC into its LLC Act including a separate section stating the non-distribution constraint and limitation on distribution of assets on dissolution, and incorporating provisions that would apply to a nonprofit corporation (e.g., provisions addressing conflicts of interest). "The status of a nonprofit limited liability company under this chapter is not determinative of its tax treatment . . . A nonprofit limited liability company engaging in conduct that is regulated by another statute is subject to the limitations of the other statute." See also N.D. Cent. Code Ann. §§ 10-36-01 to 09 (2011) (“The status of a nonprofit limited liability company under this chapter is not determinative of its tax treatment”); see Minn. Stat. § 322B.975(5)(20), 975(6)(20); see also Minn. Stat. §§ 317A.171, 317A.251, 317A.255, 317A.257, 317A.671, 317A.735, 317A.751, 317A.811, 317A.813 (treating the NLLC in the context of its general limited liability company act, incorporating by reference relevant provisions of the state’s nonprofit corporation act).

196. Walker, supra note 99 at 664; see N.D. Cent. Code Ann. § 10-36-05. The Act limits membership to § 501(c)(3) organizations or governmental entities or units, but not the number of members. See N.D. Cent. Code Ann. § 10-36-05; see also N.D. Cent. Code Ann. §§ 51-22-01, 13-10-02 (each defining an individual as a natural person as distinguished from corporations, partnerships and other legal persons).
providing little detailed guidance. Currently, Alabama, California, District of Columbia, Florida, Idaho, Iowa, Minnesota, Nebraska, New Jersey, South Dakota, Utah, and Wyoming have all enacted the RULLCA. In 2015, Illinois, New Mexico, and South Carolina introduced the RULLCA into their legislatures. It is clear from the enactment of state nonprofit legislation that there is a trend towards recognizing and more widely using NLLCs. This trend also underscores the ULLCA’s failure to properly address the important and unique needs of nonprofits in a timely and uniform manner. To remedy the ULLCA’s failure to include a more robust set of provisions that meet the operational and organizational tests, a Uniform Nonprofit Limited Liability Company Act (UNLLCA) would incorporate provisions similar to those found in the MNCA and UUNNA. This should protect NLLCs from suffering the plethora of private inurement pitfalls discussed above. The adoption of a UNLLCA would also remedy the resulting patchwork legislative approach employed among the states.

IV. ARGUMENTS AGAINST A UNLLCA

This Part will present three arguments against UNLLCA promulgation and a response to each. The first argument is that a UNLLCA is unnecessary because the ULLCA’s nonprofit permissive and protective language resembles provisions embedded in the UUNAA. The second argument is that a separate UNLLCA is premature because the IRS only recognizes the NLLC whose membership is restricted to recognized exempt entities, making the LLC exempt as a disregarded entity by virtue of its member’s recognized exemption. The third argument is that a UNLLCA would contribute to an uncontrollable proliferation of legal entities and a waste of legislative resources.

UNLLCA critics might first argue that similarities between the ULLCA’s nonprofit permissive and protective language and those

197. See e.g., FL. STAT. ANN. § 605.0108 (2014); WY. STAT. ANN. § 17-29-104 (2010); 31 ME. REV. STAT. ANN. § 1504 (2014) (recently amending their Limited Liability Company Acts to incorporate provisions to supplement the gaps left by the ULLCA).


199. Id.

200. See Walker, supra note 99, at 674; see also UNIF. LTD. LIABILITY CO. ACT § 108(b), cmt. (b) (NAT’L CONFERENCE OF COM’RS ON UNIF. STATE LAWS 2006).

201. See infra Appendix, at §§ 102 cmt., 107 cmt., 404 cmt., 405(a), 705 cmt., 707 cmt.
in the UUNAA render a separate act designed specifically for nonprofit LLC’s an unnecessary exercise. They would point to the similar ULLCA and the UUNAA codification of the flexible management structure embodied in their respective constituent entities, the LLC and the unincorporated nonprofit association. Both acts dispense with many of the corporate formalities codified in the MNCA. Accordingly, these critics would argue that the ULLCA and UUNAA provide sufficient alternative to the MNCA for nonprofits, making the UNLLCA unnecessary. However, key differences between the ULLCA and the UUNAA illustrate the need for a UNLLCA. The UUNAA recognizes that unincorporated associations, like partnerships, are eligible for formation without formal organizing documents. In contrast, the ULLCA acknowledges that the LLC cannot exist without its organizers and management adhering to a delineated list of formalities, less arduous than a corporation, but more involved than the partnership or the unincorporated association.

The ULLCA also attempts to serve the needs of business and nonprofit LLC’s in the same act. As discussed earlier in this Article, Section 108 of the Revised ULLCA (RULLCA) allows an LLC to be formed for generating profits to be distributed to the owners of the LLC, and alternatively as a nonprofit entity. The ULC explains that the provision was drafted to allow the LLC to be flexible enough for use in business or nonprofit contexts. In doing so, the ULC recognized a trend amongst the states in favor of this expanded view.

This ULLCA fails to provide the comprehensive set of protections embedded in the Model Nonprofit Corporation Act (MNCA),


203. See Unif. Ltd. Liability Co. Act § 407; see also Unif. Unincorporated Nonprofit Ass’n Act, Prefatory Note (“An unincorporated nonprofit association (UNA) is a nonprofit organization that is not a charitable trust or a nonprofit corporation or any other type of association organized under statutory law that is authorized to engage in nonprofit activities. A UNA is, thus, a default organization. As such, it is the nonprofit equivalent of a general partnership, which is the default for-profit organization.”) Id.


205. Unif. Unincorporated Nonprofit Ass’n Act, Prefatory Note.


209. Id.
Accordingly, the ULLCA’s omission of protective provisions necessary to address the unique nature of the NLLC threatens the NLLC’s ability to meet the IRS’ 501(c)(3) organizational and operational tests. Most of the key provisions in both versions of the ULLCA provide rules crafted with for-profit ventures in mind, providing instructions for distributing the assets of the entity. Of course, LLC organizers and members remain free to vary these terms in the articles of organization or operating agreement. Individual states can also choose to include protective provisions as a part of enabling statutes without the guidance of the ULLCA. However, without uniform guidance, nonprofits and state legislatures may be at a loss for how to make these changes effectively.

The diversity in treatment of the NLLC, driven by the absence of more complete guidance in the ULLCA, reveals a substantive flaw in the theory that the flexible purposes clause and scant protections embedded in the ULLCA sufficiently guide states in crafting NLLC statutes. This diversity of approaches further underscores the overlooked need for and utility of default provisions that address the distinctions between nonprofit law and business law in a comprehensive manner similar to the MNCA. This absence of guidance on key nonprofit governance matters has caused a patchwork of state NLLC laws. By promulgating a UNLLCA, the ULC can provide states with the guidance promised by its important deliberations. Without such guidance, the ULC risks leaving unfulfilled the stated purpose of uniform laws: to prospectively provide states with well-conceived and well-drafted legislation, not to simply follow the path already charted by other states.

Additionally, neither the ULLCA nor the UUNAA provide adequate guidance regarding the Attorney General’s role in protecting and preserving charitable assets for tax-exempt purposes. This is worrisome, especially in light of the MNCA’s systematic incorporation of provisions outlining this role for the attorney general. Although not expressly required for exemption under section

212. See id. at § 404 (regulating distributions to members before dissolution).
213. See id. at §§ 104–05.
214. A noteworthy collection of states has chosen that path, enacting NLLC statutes with significantly more attention dedicated to addressing the issues that distinguish the NLLC from its for-profit counterpart, while aiding the NLLC in meeting the IRS’ operational and organizational tests. See supra Part III, discussing states that have taken such alternative path.
215. See supra note 8.
§ 501(c)(3), attorney general oversight of certain nonprofit activity has long been recognized as key in protecting charitable assets and furthering the nonprofit’s articulated exempt purposes. The attorney general’s involvement in the protection of charitable assets can be traced to this nation’s English common law roots, transmitted to America with the establishment of the original colonies, and enduring as a core component of nonprofit regulatory schemes.

Today, the attorney general’s role as guardian of the public trust can be seen in examples throughout the nation. The California Attorney General’s Office empowers its Charitable Trust Section to regulate “charities and the professional fundraisers who solicit on their behalf. The purpose of this oversight is to protect charitable assets for their intended use and ensure that the charitable donations contributed by Californians are not misapplied and squandered through fraud or other means.” Similarly, the Texas Attorney General has the power to review transactions involving the sale or conversion of non-profit, charitable corporations to for-profit entities and to intervene in any proceeding involving a charity on behalf of the interest of the general public in Texas.

The MNCA conscientiously incorporates the attorney general’s important charitable oversight role through delineated functions that include approval power over a merger or sale of assets by a nonprofit corporation. The approval of the attorney general, or appropriate court, must also be obtained before a nonprofit corporation can amend its articles of incorporation or bylaws in a way

216. Fishman, Development of Nonprofit Corporation, supra note 86, at 677 (discussing the history and development of nonprofit corporation law and the need for higher accountability and standards of conduct because charities are largely self-regulated).

217. Fishman, Improving Charitable Accountability, supra note 86, at 259 (“Today, the attorney general represents the state and the public, promoting accountability by charities and fiduciaries.”); see also Fishman, Development of Nonprofit Corporation, supra note 86, at 621.

218. See Charities, OFFICE OF THE ATT’Y GEN., STATE OF CAL. DEP’T OF JUSTICE, http://oag.ca.gov/charities (last visited Nov. 11, 2015). The section investigates and brings legal actions against charities and fundraising professionals that misuse charitable assets or engage in fraudulent fundraising practices. The attorney general also maintains a registry of charitable trusts, helps charities operate legally through various guides and publications, and offers guidance to state citizens on charitable giving.


220. See MODEL NONPROFIT CORP. ACT § 9.03 (AM. BAR ASS’N 2008) (“If a domestic or foreign nonprofit corporation or eligible entity may not be a party to a merger or sale of its assets without the approval of the [attorney general], the [department of insurance] or the [public utility commission], the corporation or eligible entity shall not be a party to a transaction under this [chapter] without the prior approval of that [agency].”).
that would result in the diversion of charitable assets from its nonprofit purposes.\footnote{221} The attorney general must be notified by the plaintiff in a lawsuit seeking to remove a nonprofit corporate director,\footnote{222} by the plaintiff in a derivative action within ten days of commencing the lawsuit,\footnote{223} and by the charitable corporation itself of its intent to dissolve before the delivery of its articles of dissolution to the secretary of state.\footnote{224} Perhaps most potent of these provisions is the attorney general’s veto power concerning the diversion of “property held in trust or otherwise dedicated to a charitable purpose” through more general sale, lease, and other means of disposing charitable corporate assets.\footnote{225} The UUNAA empowers the attorney general in a fashion similar to MNCA § 11.01 concerning mergers and membership exchanges.\footnote{226} However, beyond that provision, the only other UUNAA reference to the attorney general in a protective charitable capacity is mentioned in the comments to § 25, providing that “[a]n action to recover improper distributions could be brought by the UNA or by a member as a derivative action, if authorized by state law. The Attorney General may also have authority under state law to bring a disgorgement action.”.\footnote{227}

The ULLCA contains a singular reference to the attorney general’s protective charitable capacity in the context of mergers, interest exchanges, conversions, and domestication.\footnote{228} This approach ignores distributions made in the normal course of business

\footnote{221. See id. at § 10.09. (“Property held in trust by a nonprofit corporation or otherwise dedicated to a charitable purpose may not be diverted from its purpose by an amendment of its articles of incorporation unless the corporation obtains an appropriate order of [court] (the attorney general) to the extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the nondiversion of charitable assets.”).}

\footnote{222. Id. at § 8.09(e).}

\footnote{223. Id. at § 13.09.}

\footnote{224. Id. at § 14.02.}

\footnote{225. Id. at § 12.03. (“Property held in trust or otherwise dedicated to a charitable purpose may not be diverted from its purpose by a transaction described in Section 12.01 or 12.02 unless the nonprofit corporation obtains an appropriate order from [court] (the attorney general) to the extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the nondiversion of charitable assets.”); see also §11.01(b), (c), (d) (containing similar language with respect to mergers and membership exchanges).}

\footnote{226. Compare Unif. Unincorporated Nonprofit Ass’n Act § 31(e) (Nat’l Conference of Comm’rs on Unif. State Laws 2008), with Model Nonprofit Corp. Act § 11.01 (Am. Bar Ass’n 2008).}

\footnote{227. See Unif. Unincorporated Nonprofit Ass’n Act at § 25, cmt.}

and upon dissolution,\textsuperscript{229} other transfers occurring outside of transactions addressed in Article 10,\textsuperscript{230} and amendments to the certificate of organization and operating agreement that may result in a diversion of charitable assets from dedicated nonprofit purposes.\textsuperscript{231} Provisions similar to those provided in the MNCA would yield more comprehensive protection of charitable assets and the entity’s tax exempt status, and such provisions should be included in a UNLLCA.\textsuperscript{232}

Moreover, the UNLLCA focuses on the limited IRS recognition of LLC use by nonprofits, restricting membership in the LLC to recognized 501(c)(3)s and allowing the LLC to be used as a disregarded entity, while maintaining its member’s recognized exemption.\textsuperscript{233} Critics question the value of committing the time, effort, and resources necessary to convince the IRS to adjust its position yet again and recognize a freestanding NLLC entity with individuals as members.\textsuperscript{234} They doubt the likelihood that the IRS will change its position and infer that such change is unimportant because the nonprofit corporation already conforms to IRS requirements.\textsuperscript{235} However, the IRS has demonstrated consistent movement towards permitting a greater range of entity options, as opposed to a retrenchment in recognition.\textsuperscript{236}

Before 1958, the corporation was burdened from a tax perspective vis a vis the partnership and sole proprietorship because the corporation was forced to endure double taxation in exchange for a full liability shield.\textsuperscript{237} The establishment of the Subchapter S election,\textsuperscript{238} granting the tax benefits of the partnership while allowing preservation of the corporate liability shield, served as a powerful

\textsuperscript{229} See id. at §§ 404–05; see generally id. at art. 7 (generally addressing matters of the dissolution and winding up of the company).
\textsuperscript{230} See id. at art. 5 (addressing transferrable interests and the rights of transferees and creditors).
\textsuperscript{231} See generally id. at art. 2.
\textsuperscript{232} See infra Appendix, at §§ 102 cmt., 107 cmt., 404 cmt. 405(a), 705 cmt., 707 cmt.
\textsuperscript{233} See Walker, supra note 99, at 675.
\textsuperscript{234} Id.
\textsuperscript{235} Id.
\textsuperscript{236} See Rev. Rul. 98-15, 1998-1 C.B. 718 (providing that a joint venture between a non-profit and a for-profit was permissible, and distinguishing it from another joint venture held to be impermissible by the IRS).
\textsuperscript{238} Id. at 15–16, 73–75; see also 26 U.S.C. §1361(b)(1)(A)–(D). I.R.C. subchapter S allows a corporation to be treated as a disregarded entity, a tax treatment comparable to that which partnerships receive under I.R.C. subchapter K, by adhering to certain restrictions, including the number of shareholders, classes of stock and types of persons who can be shareholders.
example of the impact tax policy has on the design and use of the corporate form in a variety of contexts. 239

The tax code has served in a similar catalytic capacity for the LLC. In 1988, the IRS formally recognized the LLC as an entity eligible for tax treatment as either a corporation or a partnership. 240 Before Ruling 88-76, few states were willing to risk enacting legislation to enable an entity whose tax status, and corresponding viability as a business option, was questionable. 241 This ruling, and the expansion of LLC-related state legislative activity that followed, marked an end to the doubt that previously impeded recognition and utilization of the LLC and validated the trailblazers who believed in the IRS’ view of the LLC could and would evolve. 242 The IRS further cemented the LLC’s status as a viable business entity option in 1996 by issuing the “check the box” regulations, allowing a single member LLC to qualify as a disregarded entity. 243

The evolving IRS position concerning the use of the LLC in the nonprofit context also illustrates that it is likely the IRS will recognize the NLLC as an independent entity without membership restrictions in the future. Within two years of issuing the “check the box” regulations, the IRS reversed its prior refusal to grant private letter ruling requests involving any use of an LLC for nonprofit purposes, approving the use of the LLC as a disregarded entity and allowing the nonprofit member to maintain its tax exempt status. 244 Although the IRS has, to date, restricted its approval of LLC nonprofit recognition to circumstances in which membership of the LLC is restricted to exempt entities, there is also no articulated tax policy that would prevent the IRS from continuing to evolve in its view of the NLLC as it has with the LLC in the business context. As

239. Small Bus. Investment Act of 1958, Pub. L. 85-699, Title I, § 102 (1958); see also I.R.C. § 7704(b) (reclassifying publicly traded partnerships and treating them as corporations for tax purposes) (discussed in Cheryl D. Block, Corporate Taxation Examples and Explanations 34 (2010)).
244. See Rev. Rul. 98-15, 1998-12 I.R.B. 6 (providing the test under which the IRS would allow a charitable organization operating an acute care hospital to continue qualifying as a § 501(c)(3) exempt entity after forming an LLC with a for-profit corporation and contributing all of its assets to the LLC, which would then operate the hospital); see also Ann. 99-102, 1999-43 I.R.B. 545 (confirming that an LLC will be treated as a disregarded entity and be afforded the exempt status of its nonprofit member).
Wyoming and other pioneer states that enacted LLC legislation before Revenue Ruling 88-76 proved, state legislation can precede and influence tax policy. The ULC has acknowledged missing an opportunity to provide leadership to states by promulgating the ULLCA after most states had already enacted LLC statutes. The UNLLCA offers an opportunity for the ULC to provide timely guidance not just to the states, but to the IRS as well.

Lastly, critics might also view the UNLLCA as promoting an unnecessary and unwarranted proliferation of new entities in the face of calls for unification. This criticism overlooks the fact that the LLC is already one of a select number of entities currently permitted by a large majority of states, addressed by the ULC, and recognized by the IRS. Although the corporation remains the dominant nonprofit entity form, trusts and unincorporated associations have long histories in the nonprofit world and are both formally acknowledged in the IRC. The nonprofit corporation’s dominance is primarily due to the absence of the double taxation consequence encountered in the business context. Most nonprofits form corporations with the intent of gaining recognition by the IRS as a tax exempt entity while maintaining a full liability shield. These benefits generally outweigh desires for the management flexibility available in trusts and unincorporated nonprofit associations. It is worth noting that there are fewer options available to nonprofits in balancing tax, liability, and management considerations than there are in the business world. The NLLC is

245. See Geu, supra note 241, at 45.


248. See generally Walker, supra note 99.

249. See Fifth-Third Union Trust Co. v. Comm’r, 56 F.2d 767 (6th Cir.1932); I.R.S. Gen. Couns. Mem. 15,778 118 (1935) (providing that trusts are considered corporations for purposes of qualifying for exemption under § 501(c)(3); see also I.R.C. § 7701(a)(3) (2012) (including unincorporated associations which are taxed as corporations in the definition of corporations and qualifying them for exemption under § 501(c)(3)).


251. Id.

252. Id. at 48–63.

an equitable step towards placing the nonprofit community on par with the business community, not simply a warrantless addition to a crowded field of entity options.

The LLC is already recognized, albeit in a more limited context, as an option for nonprofits in the ULLCA and most state statutes. These statutes vary in wording, but each seeks to assist nonprofits in operating within the parameters the IRS has set for LLC use. The diversity in treatment of the NLLC by particular states demonstrates its importance to the residents of those states as expressed through their duly elected representatives as well as the need for the uniformity that uniform laws are designed to provide. The UNLLCA would not add another entity. It would clarify the already legitimate uses of the NLLC.

V. CONCLUSION

The ULLCA as currently promulgated fails to properly guide states in addressing the unique needs of nonprofits. The ULC attempted to accommodate business and nonprofits in the ULLCA. However, it failed to provide a comprehensive set of protective charitable provisions necessary for obtaining and maintaining tax exempt entity status under § 501(c)(3). While allowing an LLC to be formed for nonprofit purposes, many other ULLCA provisions controvert these purposes by permitting and shepherding activity that expressly violates federal tax laws aimed at protecting these purposes. States adopting this approach whole cloth leave their smaller, less sophisticated, and more vulnerable nonprofits at risk of the IRS denying or revoking the nonprofit’s tax exemption.

As a result, an ad hoc, uneven patchwork of state legislation, developed by states seeking to correct and supplement the confused guidance of the ULLCA, grows in the void. Because the number of pioneer states enacting more specific NLLC legislation is still relatively small, the ULC still has the opportunity to provide better guidance in this important area of nonprofit law. These needs are addressed for corporations by protective charitable provisions embedded in the MNCA, an act based largely on the Model Business Corporations Act (MBCA), and to a lesser extent for unincorporated associations by the UUNAA, an act substantially similar to the

254. See supra note 175; see also TENN. CODE ANN. § 48-101-701 et seq; MINN. STAT. ANN. § 322B.03 et seq, N.D. CENT. CODE ANN. § 10-36-01 et seq; DEL. CODE ANN. tit. 6, § 18-106(a) (2015); KY. REV. STAT. ANN. § 275.015 (2011).

255. See id.
Uniform Partnership Act (UPA). The ULC, recognized as the premier authority on uniform laws, should take a similar approach and promulgate a UNLLCA to address these deficiencies in current LLC law. The UNLLCA would better meet the stated purpose of uniform laws by providing states more complete and appropriate guidance in this important area of nonprofit law.

As this Article seeks to facilitate the creation of much needed uniform law, the following appendix proposes key features of a Uniform Nonprofit Limited Liability Company Act (“UNLLCA”). The UNLLCA is largely based on the RULLCA256 and follows the RULLCA to account for the similarities in the essential nature of the LLC as contemplated in the business context and that of the nonprofit equivalent proposed in the appendix. To address the unique characteristics and needs of nonprofits that are not adequately addressed in the RULLCA, the UNLLCA draws inspiration from and adopts language, where appropriate, from the MNCA257 and the UUNAA as each of the acts were developed in similar position vis a vis their respective business counterparts. By adopting this language, the ULC can better meet its mission to provide uniform codes for states, while facilitating nonprofit growth.

256. See supra note 15.
257. See supra notes 162–166.
The nonprofit limited liability company (NLLC) is a nonprofit entity substantially similar to the limited liability company (LLC) more commonly used in the business context. Accordingly, the Uniform Nonprofit Limited Liability Company Act (UNLLCA) is primarily based on the Uniform Limited Liability Company Act (2006) (ULLCA) as promulgated by the Uniform Law Commission (ULC). The UNLLCA seeks to honor and retain the core essence of the ULLCA, while addressing the unique needs of nonprofits, seeking to use the LLC entity form. The UNLLCA addresses important protective nonprofit provisions missing from the ULLCA by incorporating pertinent sections of the Model Nonprofit Corporation Act (MNCA) as promulgated by the American Bar Association and the ULC’s Uniform Unincorporated Nonprofit Association Act (2008) (UUNAA), which is designed to meet IRS organizational and operational tests for determining eligibility as a 501(c)(3) exempt entity.

Because of the strong correlation between the UNLLCA and the ULLCA, the articles and sections for which substantive edits are unnecessary to address nonprofit needs are marked with a short explanatory note following the article or section number and title. Ellipsis are used to represent unedited language contained in sections also containing other text edited to address nonprofit needs or otherwise to ensure formatting accuracy and consistency.

[ARTICLE] 1
GENERAL PROVISIONS

SECTION 101. SHORT TITLE. This [act] may be cited as the Uniform Nonprofit Limited Liability Company Act.

COMMENT

The short title is amended to indicate that this act governs nonprofit limited liability companies.

SECTION 102. DEFINITIONS. In this [act]:
SECTION 103. KNOWLEDGE; NOTICE.  

SECTION 104. GOVERNING LAW.  

SECTION 105. OPERATING AGREEMENT; SCOPE, FUNCTION, AND LIMITATIONS.  

(c) An operating agreement may not:  

(12) vary the right of a member to approve a merger, interest exchange, conversion, or domestication under Section 1023(a)(2), 1033(a)(2), 1043(a)(2), or 1053(a)(2) of this Act;  

(13) vary the required contents of a plan of merger under Section 1022(a), plan of interest exchange under Section 1032(a), plan of conversion under Section 1042(a), or plan of domestication under Section 1052(a); or  

(14) except as otherwise provided in Sections 106, restrict the rights under this [act] of a person other than a member or manager.  

(d) Subject to subsection (c)(7), without limiting other terms that may be included in an operating agreement, the following rules apply:  

(1) The operating agreement may specify the method by which a specific act or transaction that would otherwise violate the duty of loyalty may be authorized or ratified by one or more disinterested and independent persons after full disclosure of all material facts.

258. Sections 103 and 104 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.
(2) To the extent the operating agreement of a member-managed limited liability company expressly relieves a member of a responsibility that the member otherwise would have under this [act] and imposes the responsibility on one or more other members, the agreement also may eliminate or limit any fiduciary duty of the member relieved of the responsibility which would have pertained to the responsibility.

(3) If not manifestly unreasonable, the operating agreement may:

(A) identify specific types or categories of activities that do not violate the duty of loyalty; and

(B) alter the duty of care, but may not authorize conduct involving bad faith, willful or intentional misconduct, or knowing violation of law.

. . . .

COMMENT

Subsection (c)(12) is deleted because the section refers to a “special litigation committee,” a litigation mechanism provided in a corporate business context, but not in the nonprofit context. The three subsequent subsections are renumbered accordingly. Subsection (c)(14), as amended above, deletes the reference to Section 107(b) because that section addresses rights of a “transferee,” a concept generally antithetical to nonprofit law. Subsection (d)(1)(B) is deleted because distributions to members will be generally prohibited under nonprofit law. Subsections (d)(3)(A) and (D) are deleted because elimination of the duty of loyalty (and certain other fiduciary duties) is generally prohibited under nonprofit law.

SECTION 106. OPERATING AGREEMENT; EFFECT ON LIMITED LIABILITY COMPANY AND PERSON BECOMING MEMBER; PREFORMATION AGREEMENT.

. . . .

(d) The manager(s) of a nonprofit limited liability company formed without members may agree or assent to terms providing that upon the formation of the company the terms will become the operating agreement.
This section should be edited to allow the LLC manager(s) to execute the operating agreement in a LLC formed without members. The MNCA allows nonprofit corporations to be formed without members, and permits a self-perpetuating board of directors. This characteristic is unique to nonprofits as there are no entity owners and entity membership, while appropriate, is not essential to nonprofit entity viability.

SECTION 107. OPERATING AGREEMENT; EFFECT ON THIRD PARTIES AND RELATIONSHIP TO RECORDS EFFECTIVE ON BEHALF OF LIMITED LIABILITY COMPANY.

(a) An operating agreement may specify that its amendment requires the approval of a person that is not a party to the agreement or the satisfaction of a condition. An amendment is ineffective if its adoption does not include the required approval or satisfy the specified condition.

(b) If a record delivered by a limited liability company to the [Secretary of State] for filing becomes effective and contains a provision that would be ineffective under Section 105(c) or (d)(3) if contained in the operating agreement, the provision is ineffective in the record.

(c) Subject to subsection (b), if a record delivered by a limited liability company to the [Secretary of State] for filing becomes effective and conflicts with a provision of the operating agreement:

1. the agreement prevails as to members, persons dissociated as members, transferees, and managers; and

2. the record prevails as to other persons to the extent they reasonably rely on the record.

(d) Property held in trust by a nonprofit LLC or otherwise dedicated to a charitable purpose may not be diverted from its purpose by an amendment of the nonprofit LLC’s operating agreement unless the LLC obtains an appropriate order of [court] [the attorney general] to the extent required by and pursuant to the law of this state on the nondiversion of charitable assets.

(e) Unless a nonprofit LLC obtains an appropriate order of [court] [the attorney general] under the law of this state dealing with the nondiversion of charitable assets, an amendment of its operating agreement may not affect:

1. any restriction imposed upon property held by the LLC by virtue of any trust under which it holds that property; or

2. the existing rights of persons other than its members.
(f) A person who is a member or otherwise affiliated with a charitable LLC may not receive a direct or indirect financial benefit in connection with an amendment of the operating agreement unless the person is itself a charitable entity. This subsection does not apply to the receipt of reasonable compensation for services rendered.

**COMMENT**

Subsection (b) of the ULLCA is deleted as it refers to transfer and distribution rights which are generally prohibited under nonprofit law. The new subsections (b) and (c) are a result of renumbering. Subsections (d), (e), and (f) add protective provisions similar to those found in the MNCA for preservation of the entity’s charitable purpose, including oversight by the attorney general or the appropriate court to prevent amendment of the LLC operating agreement causing a charitable LLC to lose its tax exempt status.

**SECTION 108. NATURE, PURPOSE, AND DURATION OF LIMITED LIABILITY COMPANY.**

(a) A limited liability company is an entity distinct from its member(s).

(b) A limited liability company may have any lawful purpose, regardless of whether for Profit, but profits from any activities must be used or set aside for the company’s nonprofit purposes.

(c) A limited liability company has perpetual duration.

**COMMENT**

Subsection (b) of the ULLCA is amended to restrict LLCs’ use of profits to advancing nonprofit purposes. See Uniform Unincorporated Nonprofit Association Act (UUNAA) § 5(d).

**SECTION 109. POWERS.**

. . . . .

**SECTION 110. APPLICATION TO EXISTING RELATIONSHIPS.**

. . . . .

259. Sections 109 through 111 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.
SECTION 111. SUPPLEMENTAL PRINCIPLES OF LAW.

SECTION 112. PERMITTED NAMES.
(a) The name of a limited liability company must contain the phrase “nonprofit limited liability company” or “nonprofit limited company” or the abbreviation “N.L.L.C.”, “N.LLC”, “N.L.C.”, or “NLC”. “Limited” may be abbreviated as “Ltd.”, and “company” may be abbreviated as “Co.”


Comment

Subsections (a) and (d) of the ULLCA are amended to ensure the name of a nonprofit LLC is distinguishable from other authorized nonprofit and business entities.

SECTION 113. RESERVATION OF NAME.

SECTION 114. REGISTRATION OF NAME.

SECTION 115. REGISTERED AGENT.
SECTION 116. CHANGE OF REGISTERED AGENT OR ADDRESS FOR REGISTERED AGENT BY LIMITED LIABILITY COMPANY.

. . . .

SECTION 117. RESIGNATION OF REGISTERED AGENT.

. . . .

SECTION 118. CHANGE OF NAME OR ADDRESS BY REGISTERED AGENT.

. . . .

SECTION 119. SERVICE OF PROCESS, NOTICE, OR DEMAND.

. . . .

SECTION 120. DELIVERY OF RECORD.

. . . .

SECTION 121. RESERVATION OF POWER TO AMEND OR REPEAL.

. . . .

[ARTICLE] 2
FORMATION; CERTIFICATE OF ORGANIZATION
AND OTHER FILINGS

SECTION 201. FORMATION OF LIMITED LIABILITY COMPANY; CERTIFICATE OF ORGANIZATION.

. . . .

(d) A nonprofit limited liability company is formed when the certificate of organization becomes effective.

COMMENT

Subsection (d) is amended to remove the requirement of at least one member. This section is edited to allow the LLC manager(s) to form the operating agreement in a LLC formed without members. The MNCA allows nonprofit corporations to be formed without members, and permits a self-perpetuating board of directors. This characteristic is unique to nonprofits as there are no entity owners and entity membership, while appropriate, is not essential to nonprofit entity viability.
SECTION 202. AMENDMENT OR RESTATEMENT OF CERTIFICATE OF ORGANIZATION.

. . .

(e) Except as provided in subsections (f), (g), and (h) of this section, an amendment to the articles of organization does not affect a cause of action existing against or in favor of the nonprofit company, a proceeding to which the company is a party, or the existing rights of persons other than members of the company or persons referred to in the articles. An amendment changing a company’s name does not abate a proceeding brought by or against the company in its former name.

(f) Property held in trust by a nonprofit company or otherwise dedicated to a charitable purpose may not be diverted from its purpose by an amendment of its articles of organization unless the company obtains an appropriate order of [court] [the attorney general] to the extent required by and pursuant to the law of this state dealing with the nondiversion of charitable assets.

(g) Unless a nonprofit company obtains an appropriate order of [court] [the attorney general] under the law of this state dealing with the nondiversion of charitable assets, an amendment of its articles of organization may not affect:

(1) any restriction imposed upon property held by the company by virtue of any trust under which it holds that property; or

(2) the existing rights of persons other than its members.

(h) A person who is a member or otherwise affiliated with a charitable company may not receive a direct or indirect financial benefit in connection with an amendment of the articles of organization unless the person is itself a charitable entity. This subsection does not apply to the receipt of reasonable compensation for services rendered.

COMMENT

Subsections (e) through (h) add protective provisions, including oversight by the Attorney General or the appropriate court to prevent amendment of the LLC articles of organization causing a charitable LLC to lose its tax exempt status.
SECTION 203. SIGNING OF RECORDS TO BE DELIVERED FOR FILING TO [SECRETARY OF STATE].

. . . .

SECTION 204. SIGNING AND FILING PURSUANT TO JUDICIAL ORDER.

. . . .

SECTION 205. LIABILITY FOR INACCURATE INFORMATION IN FILED RECORD.

. . . .

SECTION 206. FILING REQUIREMENTS.

. . . .

SECTION 207. EFFECTIVE DATE AND TIME.

. . . .

SECTION 208. WITHDRAWAL OF FILED RECORD BEFORE.

. . . .

SECTION 209. CORRECTING FILED RECORD.

. . . .

SECTION 210. DUTY OF [SECRETARY OF STATE] TO FILE; REVIEW OF REFUSAL TO FILE; DELIVERY OF RECORD BY [SECRETARY OF STATE].

. . . .

SECTION 211. CERTIFICATE OF GOOD STANDING OR REGISTRATION.

. . . .

SECTION 212. [ANNUAL] [BIENNIAL] REPORT FOR [SECRETARY OF STATE].

. . . .

261. Sections 203 through 212 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.
[ARTICLE] 3
RELATIONS OF MEMBERS AND MANAGERS TO PERSONS DEALING WITH LIMITED LIABILITY COMPANY

. . . .

[ARTICLE] 4
RELATIONS OF MEMBERS TO EACH OTHER AND TO LIMITED LIABILITY COMPANY

SECTION 401. BECOMING MEMBER.
. . . .

(d) A person may become a member without making or being obligated to make a contribution to the limited liability company.

(e) A nonprofit company is not required to have members.

(f) The articles of organization or operating agreement of a membership company may establish criteria or procedures for admission of members.

(g) A person may not be admitted as a member without the person’s consent.

(h) If a membership company provides certificates of membership to the members, the certificates shall not be registered or transferable except as provided in the articles of organization or operating agreement.

(i) A person is not a member of a nonprofit company unless the person meets the definition of a “member” in Section 102, regardless of whether the company designates or refers to the person as a member.

(j) Except as provided in the articles of organization or operating agreement, a member of a membership company may not transfer a membership or any right arising therefrom.

(k) Where the right to transfer a membership has been provided, a restriction on that right shall not be binding with respect to a member holding a membership issued before the adoption of the restriction unless the restriction is approved by the affected member.

(l) Except as provided in its articles of organization or operating agreement, a membership company may admit members for no

262. Article 3 will remain as printed in the RULLCA. The title appears for readers’ convenience.
consideration or for such consideration as is determined by the existing members or managers. The consideration may take any form, including promissory notes, intangible property, or past or future services. Payment of the consideration may be made at such times and upon such terms as are set forth in or authorized by the articles of organization, operating agreement, or other authorization.

COMMENT

Subsection (d)(1) is deleted as it refers to a “transferable interest,” generally prohibited under nonprofit law. Subsections (e) through (l) add a requirement that a person must consent to being a member before they are a member, restrictions on transfer of members interests, an allowance of admission procedures established in the articles of organization and operating agreement, a reference to the definition of “member,” and a flexible consideration provision.

SECTION 402. FORM OF CONTRIBUTION.

SECTION 403. LIABILITY FOR CONTRIBUTIONS.

SECTION 404. SHARING OF AND RIGHT TO DISTRIBUTIONS BEFORE DISSOLUTION.

COMMENT

Section 404 is deleted in its entirety as it addresses distributions of company profits to members generally prohibited under nonprofit law.

SECTION 405. LIMITATIONS ON DISTRIBUTIONS.

(a) Except as otherwise provided in subsection (b), a nonprofit company may not pay dividends or make distributions to a member or manager.

(b) An unincorporated nonprofit association may:

263. Sections 402 and 403 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.
(1) pay reasonable compensation or reimburse reasonable expenses to a member or manager for services rendered;
(2) confer benefits on a member or manager in conformity with its nonprofit purposes;
(3) repurchase a membership and repay a capital contribution made by a member to the extent authorized by its governing principles; or
(4) make distributions of property to members upon winding up and termination to the extent permitted by Section 702.

COMMENT

The provisions of this section, generally providing guidance for distributions in a business LLC, are replaced with provisions protecting nonprofit charitable purposes. See UUNAA § 25.

SECTION 406. LIABILITY FOR IMPROPER DISTRIBUTIONS.264

SECTION 407. MANAGEMENT OF LIMITED LIABILITY COMPANY.

SECTION 408. REIMBURSEMENT; INDEMNIFICATION; ADVANCEMENT; AND INSURANCE.

SECTION 409. STANDARDS OF CONDUCT FOR MEMBERS AND MANAGERS.
(e) In a manager-managed limited liability company, the following rules apply:

(1) Subsections (a), (b), and (c) apply to the manager or managers and not the members.
(2) The duty stated under subsection (b)(3) continues until winding up is completed.
(3) Subsection (d) applies to managers and members.

264. Sections 406 through 408 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.
(4) Subject to subsection (d), a member does not have any duty to the company or to any other member solely by reason of being a member.

**COMMENT**

Subsection (e) through (h), and (i)(4) and (5) are deleted as the subsections allow for variance of the duty of loyalty generally prohibited under nonprofit law. See UUNAA §17(b), comment subsection (b). Subsection (i)(1) is amended to accommodate the deletions.

**SECTION 410. RIGHTS TO INFORMATION OF MEMBER, MANAGER, AND PERSON DISSOCIATED AS MEMBER.**

**COMMENT**

Subsection 410(g) is deleted as the section refers to transfer rights generally prohibited under nonprofit law. Section 410 otherwise generally remains as printed in ULLCA (2006).

**[ARTICLE] 5**

**COMMENT**

Article 5 is deleted in its entirety as the article generally refers to transferable interests generally prohibited under nonprofit law.

**[ARTICLE] 6**

**DISSOCIATION**

**SECTION 601. POWER TO DISSOCIATE AS MEMBER; WRONGFUL DISSOCIATION.**

(a) A person has the power to dissociate as a member at any time, rightfully or wrongfully, by withdrawing as a member by express will under Section 602(1).
(b) A person’s dissociation as a member is wrongful only if the dissociation is in breach of an express provision of the operating agreement.

(c) A person that wrongfully dissociates as a member is liable to the limited liability company and, subject to Section 801, to the other members for damages caused by the dissociation. The liability is in addition to any debt, obligation, or other liability of the member to the company or the other members.

(d) A member may resign as a member in accordance with the governing principles. In the absence of applicable governing principles, a member may resign at any time.

(e) Unless the governing principles provide otherwise, resignation of a member does not relieve the member from any unpaid capital contribution, dues, assessments, fees, or other obligation incurred or commitment made by the member before resignation.

COMMENT

Subsection (b)(2) is deleted as the subsection refers to business dissociation inapplicable under nonprofit law. Subsections (d) and (e) are added to address withdrawal of a nonprofit limited liability company member.

SECTION 602. EVENTS CAUSING DISSOCIATION.

A person is dissociated as a member when:

(5) the person is expelled as a member by the affirmative vote or consent of all the other members if:

(A) it is unlawful to carry on the limited liability company’s activities and affairs with the person as a member;
(B) the person is an entity and:
   (i) the company notifies the person that it will be expelled as a member because the person has filed a statement of dissolution or the equivalent, the person has been administratively dissolved, the person’s charter or the equivalent has been revoked, or the person’s right to conduct business has been suspended by the person’s jurisdiction of formation; and
   (ii) not later than 90 days after the notification, the statement of dissolution or the equivalent has not been withdrawn, rescinded, or revoked, the person has not
been reinstated, or the person’s charter or the equivalent or right to conduct business has not been reinstated; or
(C) the person is an unincorporated entity that has been dissolved and whose activities and affairs are being wound up;

. . . .

(8) in the case of a person that is not an individual, the existence of the person terminates; or
(9) the limited liability company dissolves and completes winding up.

COMMENT

Subsections (5)(B), (8), (9), and (10) are deleted as the subsections refer to transferrable interests generally prohibited under nonprofit law. Subsections (12) through (15) are deleted as the subsections refer to matters more appropriately addressed, to the extent dissociation is permitted, in Article 10. Subsections (11) and (16) are renumbered as (8) and (9).

SECTION 603. EFFECT OF DISSOCIATION.

. . . .

COMMENT

Subsection (a)(3) of the ULLCA is deleted as it refers to transferrable interests generally prohibited under nonprofit law. Section 603 otherwise generally remains as printed in ULLCA (2006).

[ARTICLE] 7
DISSOLUTION AND WINDING UP

SECTION 701. EVENTS CAUSING DISSOLUTION.
(a) A limited liability company is dissolved, and its activities and affairs must be wound up, upon the occurrence of any of the following:

(1) an event or circumstance that the operating agreement states causes dissolution;
(2) the affirmative vote or consent of the members;
(3) the affirmative vote or consent of the managers if the nonprofit limited liability company has no members or no member can be located and the nonprofit limited liability company’s operations have been discontinued for at least three years, by the managers or, if the association has no current manager, by its last manager.

(4) on application by a member, the entry by [the appropriate court] of an order dissolving the company, if the applicant establishes good cause; or

(5) the signing and filing of a statement of administrative dissolution by the [Secretary of State] under Section 708.

(b) In a proceeding brought under subsection (a)(4)(C), the court may order a remedy other than dissolution.

(c) A charitable limited liability company must give the attorney general notice in the form of a record that it intends to dissolve before the time it delivers articles of dissolution to the secretary of state.

COMMENT

Subsection (a)(3) is amended to provide for dissolution by managers of a nonprofit limited liability company organized without members, or a dormant nonprofit limited liability company whose last known members cannot be located. Subsection (a)(4) amends the required grounds for requesting judicial dissolution, using “good cause” as the standard. See UUNAA §27. Subsection (c) adds attorney general notice as a protective charitable measure. See MNCA §14.02(g).

SECTION 702. WINDING UP.

(c) If a dissolved nonprofit limited liability company has no members, the last manager may wind up the activities and affairs of the company.

(d) [The appropriate court] may order judicial supervision of the winding up of a dissolved limited liability company, including the appointment of a person to wind up the company’s activities and affairs on the application of a member or manager, if the applicant establishes good cause.
Subsection (c) is amended to replace the legal representative of the last member with the last managers for winding up the nonprofit limited liability company. Subsection (d) is deleted as it refers to rights of transferees generally prohibited under nonprofit law. Subsection (e) has been renumbered as subsection (d) and amended to allow a manager to apply for dissolution, particularly in nonprofit limited liability companies without members.

SECTION 703. RESCINDING DISSOLUTION.

SECTION 704. KNOWN CLAIMS AGAINST DISSOLVED LIMITED LIABILITY COMPANY.

SECTION 705. OTHER CLAIMS AGAINST DISSOLVED LIMITED LIABILITY COMPANY.

(d) A claim not barred under this section or Section 704 may be enforced against a dissolved limited liability company, to the extent of its undistributed assets.

COMMENT

Subsection (d) is amended to remove references to distributions to members generally prohibited under nonprofit law. Section 705 otherwise generally remains as printed in ULLCA (2006).

SECTION 706. COURT PROCEEDINGS.

SECTION 707. DISPOSITION OF ASSETS IN WINDING UP.

(a) Winding up and termination of an unincorporated nonprofit association must proceed in accordance with the following rules:

(1) All known debts and liabilities must be paid or adequately provided for.

265. Sections 703 and 704 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.

266. Section 706 will remain as printed in the RULLCA. This section title appears for readers’ convenience.
(2) Any property subject to a condition requiring return to the person designated by the donor must be transferred to that person.

(3) Any property subject to a trust must be distributed in accordance with the trust agreement.

(4) Any remaining property must be distributed as follows:

(A) as required by law other than this [act] that requires assets of an association to be distributed to another person with similar nonprofit purposes;

(B) in accordance with the association’s governing principles or in the absence of applicable governing principles, to the members of the association per capita or as the members direct; or

(C) if neither subparagraph (A) nor (B) applies, under [cite the unclaimed property law in this state].

(b) Property held in trust or otherwise dedicated to a charitable purpose may not be diverted from its purpose by the dissolution of a nonprofit limited liability company unless and until the nonprofit limited liability company obtains an order of [court] [the attorney general] to the extent required by and pursuant to the law of this state dealing with the nondiversion of charitable assets.

(c) A person who is a member or otherwise affiliated with a charitable limited liability company may not receive a direct or indirect financial benefit in connection with the dissolution of the charitable limited liability company unless the person is a charitable corporation, charitable limited liability company or an unincorporated entity that has a charitable purpose. This subsection does not apply to the receipt of reasonable compensation for services rendered.

**COMMENT**

The language of Section 707 is replaced to comply with charitable distribution restrictions required under nonprofit law. See UUNAA §28; MNCA §§ 6.40, 6.41, 14.05(c) and (d).

**SECTION 708. ADMINISTRATIVE DISSOLUTION.**

. . . .

**SECTION 709. REINSTATEMENT.**

267. Sections 708 through 710 will remain as printed in the RULLCA. These section titles appear for readers’ convenience.
SECTION 710. JUDICIAL REVIEW OF DENIAL OF REINSTATEMENT.

[ARTICLE] 8
ACTIONS BY MEMBERS

SECTION 803. PROPER PLAINTIFF.

COMMENT
Subsection (2) should be deleted as that subsection refers to derivative litigation rights of someone who has not been admitted as a member of the LLC; such rights being inapplicable as nonprofit LLC membership is generally restricted and nontransferable. Section 803 otherwise generally remains as printed in ULLCA (2006).

SECTION 805. SPECIAL LITIGATION COMMITTEE.

COMMENT
Section 805 is deleted in its entirety as neither the MNCA nor the UUNAA provide for Special Litigation Committees.

SECTION 806. PROCEEDS AND EXPENSES.

SECTION 807. NOTICE TO ATTORNEY GENERAL.
The plaintiff in a proceeding under this [article] must notify the attorney general within ten days after commencing the proceeding if it involves a charitable LLC.

268. Article 8 will generally remain as printed in the RULLCA. Two exceptions are noted in comments to Sections 803 and 805. These section titles appear for readers’ convenience.
269. This section will remain as printed in the RULLCA. This section title appears for readers’ convenience.
This section provides notice to the Attorney General of an action involving a charitable LLC.

[ARTICLE] 9
FOREIGN LIMITED LIABILITY COMPANIES

SECTION 901. GOVERNING LAW.²⁷⁰

SECTION 902. REGISTRATION TO DO BUSINESS IN THIS STATE.

SECTION 903. FOREIGN REGISTRATION STATEMENT.

SECTION 904. AMENDMENT OF FOREIGN REGISTRATION STATEMENT.

SECTION 906. NONCOMPLYING NAME OF FOREIGN LIMITED LIABILITY COMPANY.

SECTION 907. WITHDRAWAL DEEMED ON CONVERSION TO DOMESTIC FILING ENTITY.

A registered foreign limited liability company that converts to a domestic entity whose formation requires delivery of a record to the [Secretary of State] for filing is deemed to have withdrawn its registration on the effective date of the conversion.

COMMENT

This section is amended to remove language referencing conversion to a limited liability partnership, a business entity that would not qualify as a nonprofit.

SECTION 908. WITHDRAWAL ON DISSOLUTION OR CONVERSION TO NONFILING ENTITY.

²⁷⁰ Sections 901 through 906 will remain as printed in the RULLCA. These section titles appear for readers' convenience.
(a) A registered foreign limited liability company that has dissolved and completed winding up or has converted to a domestic or foreign entity whose formation does not require the public filing of a record shall deliver a statement of withdrawal to the [Secretary of State] for filing. The statement must state:

. . . .

COMMENT

This section is amended to remove language referencing a limited liability partnership, a business entity that would not qualify as a nonprofit. The requirements remain as printed in ULLCA (2006).

SECTION 909. TRANSFER OF REGISTRATION. 271

. . . .

SECTION 910. TERMINATION OF REGISTRATION.

. . . .

SECTION 911. WITHDRAWAL OF REGISTRATION OF REGISTERED FOREIGN LIMITED LIABILITY COMPANY.

. . . .

SECTION 912. ACTION BY [ATTORNEY GENERAL].

. . . .

[ARTICLE] 10
MERGER, INTEREST EXCHANGE, CONVERSION, AND DOMESTICATION272

. . . .

SECTION 1003. REQUIRED NOTICE OR APPROVAL.

. . . .

271. Sections 909 through 912 will generally remain as printed in the RULLCA. These section titles appear for readers' convenience. Other supplemental treatment of foreign limited liability companies, including conversions of foreign business entities to domestic nonprofit limited liability companies and domestic business entities to foreign nonprofit limited liability companies are beyond the scope of this work.

272. This section will remain as printed in ULLCA (2006). The section title appears for readers' convenience. Commentary is provided to explain the importance of Section 1003.
COMMENT

As with the ULLCA, this subsection employs protections identical to those in the MNCA and UUNAA to supplement gaps in state laws governing the nondiversion of charitable property to other uses. As with ULLCA, MNCA, and UUNAA, this subsection requires approval of the effect of transactions under this act by the appropriate arm of government supervising nonprofit entities. An approval or order obtained under this section may impose conditions or specify the disposition of assets or liabilities in a manner different than would otherwise be the case, superseding the provisions of this act specifying the effects of a transaction.