

HOUSE BILL REPORT

SB 6531

As Passed House:
February 28, 2006

Title: An act relating to preserving remedies when limited liability companies dissolve.

Brief Description: Preserving remedies when limited liability companies dissolve.

Sponsors: By Senators Weinstein, Fraser and Kline.

Brief History:

Committee Activity:

Judiciary: 2/20/06 [DP].

Floor Activity:

Passed House: 2/28/06, 97-0.

Brief Summary of Bill

- Provides a three year period following dissolution of a limited liability company during which the dissolution of the company does not extinguish any cause of action against the company.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: Do pass. Signed by 9 members: Representatives Lantz, Chair; Flannigan, Vice Chair; Williams, Vice Chair; Priest, Ranking Minority Member; Rodne, Assistant Ranking Minority Member; Campbell, Kirby, Springer and Wood.

Staff: Bill Perry (786-7123).

Background:

A limited liability company (LLC) is a business entity that possesses some of the attributes of a corporation and some of the attributes of a partnership.

Attributes of Corporations and LLCs

Corporations are creatures of statutory law and are created only by compliance with prescribed formal procedures. A corporation is managed by directors and officers, but is owned by shareholders who may have very little direct role in management. Generally, ownership shares are transferable, and each shareholder is liable for corporate debts only to the extent of his or her own investment in the corporation. A corporation is treated as a taxable entity.

General partnerships, on the other hand, are business entities recognized as common law that require no formal creation, and are owned and managed by the same individuals who are each liable for the debts of the partnership. A general partnership is not a taxable entity.

The LLCs were authorized by the Legislature in 1994. An LLC is a noncorporate entity that allows the owners to participate actively in management, but at the same time provides them with limited liability. The Internal Revenue Service has ruled that an LLC with attributes that make it more like a partnership than a corporation may be treated as a non-taxable entity.

A properly constructed LLC, then, can be a business entity in which the ownership enjoys the limited liability of a corporation's shareholders, but the entity itself is not taxed as a corporation.

Dissolution of an LLC

An LLCs may be dissolved in a number of ways, including:

- reaching a dissolution date set at the time the LLC was created;
- the occurrence of events specified in the LLC agreement as causing dissolution;
- by mutual consent of all members of the LLC;
- the dissociation of all members through death, removal or other event;
- judicial action to dissolve the LLC; or
- administrative action by the Secretary of State for failure of the LLC to pay fees or to complete required reports.

Certificate of Cancellation

After an LLC is dissolved, or if an LLC has been merged with another entity and the new entity is not the LLC, the certificate of formation that created the LLC is cancelled.

Cancellation may occur in a number of ways:

- The certificate of formation may authorize a member or members to file the certificate of cancellation upon dissolution, or after a period of winding up the business of the LLC.
- A court may order the filing of a certificate of cancellation.
- In the case of a merger that results in a new entity that is not the LLC, the filing of merger documents must include the filing of a certificate of cancellation.
- In the case of an administrative dissolution of an LLC, there is a two year period during which the LLC may be reinstated before the secretary of state files the certificate of cancellation.

After dissolution of an LLC, but before cancellation of the certificate of formation, members of the LLC or a court appointed receiver may wind up the business of the LLC. A person winding up the affairs of an LLC may prosecute or defend legal actions in the name of the LLC.

Preservation of Remedies

The law governing LLCs has no express provision regarding the preservation of remedies or causes of actions following dissolution of the business entity. There is an implicit recognition of the preservation of at least an already filed claim during the wind up period following dissolution, since the person winding up the affairs is authorized to defend suits against the

LLC. However, there is no provision regarding the preservation of claims following cancellation of the certificate of formation.

The current Business Corporation Act provides that dissolution of a corporation does not eliminate any claim against the corporation that was incurred prior to dissolution if an action on the claim is filed within two years after dissolution. There is no "certificate of cancellation" necessary to end a corporation. *(Note: Another currently pending bill, SSB 6596, would increase this two year period to three years, and would make the provision apply to claims incurred before or after dissolution.)*

Summary of Bill:

Dissolution of a limited liability company will not eliminate any cause of action against the company that was incurred prior to or after the dissolution if an action on the claim is filed within three years after the effective date of the dissolution.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect 90 days after adjournment of session in which bill is passed.

Testimony For: A recent court decision has left many homeowners without a remedy for claims against a dissolved corporation. The same problem exists with respect to claims against LLCs. The Bar Association is working on a comprehensive review of the LLC law, but it is not done yet. This bill addresses only the problem of survival of claims following dissolution.

The bill is a step in the right direction. It affirmatively states that claims, such as homeowners' warranty claims, will survive the dissolution of an LLC. Whether or not there are any assets left to satisfy a claim is a separate problem that will have to be addressed later.

Testimony Against: None.

Persons Testifying: Senator Weinstein, prime sponsor; Alfred Donohue, Forsberg Umlauf, P.S.; and Sandi Swarthout and Michelle Ein, Washington Homeowners Coalition.

Persons Signed In To Testify But Not Testifying: None.