

Considerations for LLC Operating Agreements:

LLC §417(a) requires members to be signatories to the operating agreement, but there is no requirement for the LLC to be a party to the agreement. Other states, such as Delaware, specifically provide that "a limited liability company is bound by its limited liability company agreement whether or not the limited liability company executes the limited liability company agreement." *Delaware Limited Liability Company Act § 18-101(7)*. No counterpart language exists in the New York LLC. Although one would expect that the provisions of the operating agreement would bind the LLC, there is limited case law, and therefore other outcomes are possible under New York law.

Consent of any member adversely affected is needed to amend the operating agreement with respect to the obligations of members of a LLC to make contributions. LLC §417(b).

LLC §501 allows contributions to be paid in cash, in kind property or services, or a note or other monetary obligation. The operating agreement should set forth the permissibility, forms and value of non-cash contributions. If the operating agreement fails to do so, non-cash contributions, particularly contributions in the form of services, may not be given credit and the contributor may be found to have no interest in the assets of the LLC or any distribution. *See*

If the operating agreement provides for initial contributions to be made in cash, notwithstanding the fact that it may also provide for the general allowance of non-cash contributions, courts may not give effect to the non-cash contribution as consideration for a membership interest and instead find no such membership interest acquired. *See KSI Rockville, LLC v. Eichengrun*, 305 A.D.2d 681, 760 N.Y.S.2d 520 (2d Dept. 2003); *Mizrahi v. Cohen*, 2012 NY Slip Op 50030 (Kings Cty. Sup. Court 2012). Therefore, the operating agreement should be specific as to the form of initial and subsequent contributions, the value of non-cash contributions, and the value and extent of other compensation to be provided for services rendered.

“The rule that any ambiguities in a contract must be construed against the drafter applies to the operating agreement of a limited liability company.” *Matter of Fassa Corp.*, 31 Misc. 3d 782 (Nassau Cty. Sup. Court 2011).

If the operating agreement is silent or there is no agreement with respect to a certain issue, courts will supplement or substitute the minimum requirements applicable to operation of an LLC under the LLC law. These are the default provisions that the court will adopt as the operating agreement in the case that the members have failed to do so.

LLC §502(c) allows the members to provide any desired consequences in the operating agreement for the failure of a member to perform his or her promises to the LLC, including the right to terminate the member's interest in the LLC. Possible breaches include a member's failure to fully satisfy capital contribution requirements, either as part of the initial capital contribution, a subsequent capital call, or to provide the services which were promised in exchange for membership interests.

Possible remedies for failure to satisfy obligations to the LLC are forfeiture of voting or management rights, liability for damages, right of other members or the LLC to purchase the defaulting member's interest at a reduced valuation, or even absolute forfeiture. In addition to providing for the effect of expulsion or removal and withdrawal, the members should also provide for the valuation of the member's interest if any event is to lead to a forced liquidation or buyout on expulsion

Withdrawal from a LLC is not authorized unless provided for in the operating agreement, and if withdrawal is not so authorized, a member may not withdraw prior to dissolution. LLC § 606(a).

Upon withdrawal, a member is entitled to whatever distribution is called for in the operating agreement, and absent that, the fair value of his or her interest at the time of withdrawal. LLC §509. As such, absent anything to the contrary in the operating agreement, withdrawal or removal of a member would entitle the member to the fair value of his or her interest.

Because valuation could be the subject of litigation, it is well-advised to set forth a formula that can change depending on whether the withdrawal is warranted. Possible bases for predetermining the formula for valuation on exit include the following: Appraisal by an evaluator or accountant chosen by the LLC; a value determined by the managers or managing members, in good faith; or a value determined by multiple evaluators or accountants chosen by the withdrawing member and the LLC (using the mean or median or providing for the evaluator or accountants to agree independently on a third accountant for the final value determination). Other circumstances may suggest fixing the value at the contribution amount and subtracting damages or costs incurred by the LLC as a result of member misconduct.

Sample clauses:

_____ Rights of Creditors and Third Parties under Agreement. The Agreement is entered into among the Company and the Members for the exclusive benefit of the Company, its Members, and their successors and assignees. The Agreement is expressly not intended for the benefit of any creditor of the Company or any other Person. Except and only to the extent provided by applicable statute, no such creditor or third party shall have any rights under the Agreement or any agreement between the Company and any Member with respect to any Capital Contribution or otherwise.

_____ Execution of Additional Instruments. Each Member hereby agrees to execute such other and further statements of interest and holdings, designations, powers of attorney and other instruments necessary to comply with any laws, rules or regulations.

_____ Telephonic Conferences. The Members and/or Managers may participate in a meeting of Members or a meeting of Managers, as the case may be, by means of conference telephone or similar communications equipment by means of which all Persons participating in the meeting can hear each other, and such participation in a meeting shall constitute presence of the Person at the meeting.

____ Non recourse to Other Members. Except as provided by applicable law or as expressly provided in this Agreement, upon dissolution, each Member shall receive a return of his or her Capital Contribution solely from the assets of the Company. If the assets of the Company remaining after the payment or discharge of the debts and liabilities of the Company is insufficient to return any Capital Contribution of any Member, such Member shall have no recourse against any other Member.