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LLCS AND WILLS BY STEPHEN TAYLOR

Oast & Hook has previously examined the growing popularity of the limited liability company ("LLC") as a valuable tool for estate and business succession planners and their clients. See "Limited Liability Companies: The Entity of Choice for Estate and Business Planning," *Oast & Hook News*, Aug. 5, 2011. A recent decision by the Supreme Court of Virginia helps to more clearly define this area of law while specifically addressing the ability of an LLC member to transfer this member's interest.

A member's interest in an LLC is comprised of two distinct and divisible interests. The first, the "control" interest, encompasses the member's right to participate in the administration and operation of the LLC, in consultation with the other members. The second, the "financial" interest, encompasses the sharing of profits and losses of the LLC and the right to distributions from the LLC's income and assets. A trap for the unwary is failing to consider these interests as separate and distinct when planning for succession.

Virginia's Limited Liability Company Act provides that, unless otherwise stated in the LLC's articles of organization or operating agreement, a membership interest is assignable in whole or in part – but such an assignment only entitles the assignee to receive "any share of profits and losses and distributions to which the assignor would be entitled." Va. Code Ann. § 13.1-1039(A). This is considered the "financial" interest.

Addressing the "control" interest, the Act provides, "An assignment does not entitle the assignee to participate in the management and affairs of the limited liability company or to become or to exercise any rights of a member." *Id.* Unless otherwise provided in the LLC's articles of organization or operating agreement, an assignee of a financial interest may become a member only "by the consent of a majority" of those members exercising direct control of the LLC. Va. Code Ann. § 13.1-1040(A).

In light of these principles, the question arises whether membership in a Virginia LLC may be transferred by a last will and testament, and, if so, whether both the financial and control interests are transferrable. This question was recently addressed by the Supreme Court of Virginia in *Ott v. Monroe*, 282 Va. 403, 719 S.E.2d 309 (2011).

In *Ott*, a dispute over the management of an LLC arose after the controlling member died, leaving his entire estate to his daughter. The daughter claimed that her father's will effectively transferred his membership in the LLC to her, including both his "control" interest as well as his "financial" interest. Conversely, the remaining and current managing member argued that the daughter only inherited her father's "financial" interest – i.e., the right to share in the LLC's profits and losses and to receive distributions to which he would be entitled.

The Supreme Court found that the LLC's operating agreement permitted the deceased member to transfer his membership interest to his daughter by his will. The Court then turned its attention to examining section 13.1-1039 of the Code, which provides the statutory guidance for assignments of membership interest. While the default rule permitting assignability of membership interest may be modified in the LLC's articles of organization or operating agreement, the Court determined that the Code does not permit such modification of the rule providing that an assignment of membership interest "does not entitle the assignee to participate in the management and affairs of the limited liability company or to become or to exercise any rights of a member." As the Court definitely stated, "it is not possible for a member unilaterally to alienate his personal control interest in a limited liability company."

The Court's opinion does appear to suggest, however, that it may be possible to for a member to transfer his control interest in an LLC, but to do so requires clear and specific language in the operating agreement. The operating agreement in *Ott* provided that a member "may transfer all or any portion of the Member's Interest at any time" to the member's spouse, children, or descendants. The Court held that this provision did not specifically permit the transfer of a member's control interest without the consent of the other members. Accordingly, if members want the ability to transfer or assign their control interests, then they must clearly and specifically provide for such transfer in the operating agreement.

The *Ott* case reminds us of the importance of comprehensive estate and business succession planning to ensure that your plan works the way in which you intended. Proper advance planning can prevent an *Ott*-type scenario from occurring. The attorneys at Oast & Hook are available to discuss the development and implementation of your comprehensive estate and business succession plan.

The attorneys at Oast & Hook assist families with their estate, financial, insurance, long-term care, veterans' benefits, and special needs planning issues.

Stephen Taylor is an elder law attorney with Oast & Hook, and he practices in the areas of estate planning, estate and trust administration, business planning, and litigation. Mr. Taylor is licensed to practice law in Virginia and North Carolina.

Ask Allie

O&H: Allie, we've heard about another busy office cat. Please tell us about her.

Allie: Sure! Hidey is black shorthaired cat who works at MufflerMania in Westmont, New Jersey. A woman had brought her car to the garage when she heard meowing noises coming from the car; Hidey was found unharmed inside the front of the car behind the bumper. The garage owner and his wife offered Hidey food and water, and soon she settled into her new life at the garage. She is the garage's receptionist and greets the customers when they come through the door. Although her duties take up a large part of her day, she still finds time to take naps, usually across the appointment book or a calculator on the desk. She might be tempted by the stream of cars going through the garage each day, but she has decided that the life of a stowaway is not for her. What a great story! I enjoyed my time as an office cat, and now I'm enjoying my retirement. Time for my morning stretches . . . See you next week!

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