THE 2015 AMENDMENTS TO THE KENTUCKY BUSINESS ENTITY STATUTES

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I. INTRODUCTION

As a further component to the efforts to ensure that Kentucky has the most up-to-date business entity statutes available in the country, the 2015 General Assembly passed, and Governor Beshear signed, a series of revisions and additions to those laws. Essentially, these new statutes can be divided into three divisions. Initially, there are a series of miscellaneous changes across the range of business statutes, which revisions are generally intended to provide additional clarity as to applicable rules. Second, there are adopted a series of additions and revisions to the Nonprofit Corporation Acts, revisions which generally speaking bring the law of nonprofit corporations more into line with that of business corporations. Third, there has been adopted the Kentucky Unincorporated Nonprofit Association Act, an entirely new organizational form which will provide certainty for arrangements that previously have had no statutory basis. After a review of the legislative history of this Act and technical revisions addressing the workings of the office of the Secretary of State, these statutes will be reviewed in the order just set forth.

II. LEGISLATIVE HISTORY

This legislation was introduced to the Kentucky General Assembly as House Bill 440 under the sponsorship of Speaker Pro Tem Jody Richards, Representative Tom Kerr, and Representative Chris Harris. H.B. 440 was referred to the House Judiciary Committee where it was called for a hearing by Chairman John Tilly on February 26; it received a unanimous vote in its favor and was recommended to the consent calendar. The bill was heard on the House floor on March 2; the vote was 94 in favor and 0 against. Transmitted to the Senate, the bill was assigned to the Judiciary Committee. Called by Chairman Westerfield on March 9, the bill received unanimous approval and was recommended to the consent calendar. The bill was approved by the entire Senate on March 11 with 36 votes in

favor and 0 votes against.[1] The Bill was signed by Governor Beshear on March 20. The legislation's effective date was June 24, 2015.[2]

III. SECRETARY OF STATE

The statutory authority for the Secretary of State to accept electronic signatures has been supplemented to include filings by a statutory trust as well as those by an unincorporated nonprofit association.[3] In addition, the Secretary of State has been granted the express authority to redact documents filed pursuant to the Kentucky Business Entity Filing Act of such information whose disclosure is otherwise prohibited.[4] By way of example, were the articles of incorporation, in addition to listing the initial directors, to recite their Social Security Numbers, were there a statute providing Social Security Numbers should not be set forth in a public record, the Secretary of State would have the authority to redact them from the filed document.

IV. BUSINESS CORPORATIONS

A. Conforming the Aspirational and Indemnification Standards

With respect to business corporations, one change made corrects a typographical error that can be dated to 1988. At that time, in the course of drafting the Kentucky Business Corporation Act, it being based upon the then existing version of the Model Business Corporation Act, a decision was made to define the aspirational standard of a director as including the more subjective "honestly" in place of the more objective "reasonably."[5] However, even as this change was made with respect to the aspirational standard, a similar change was not made with respect to the standard for affording a director indemnification; that provision continued to utilize "reasonably." In order to address this differential and provide for the intended consistency between the aspirational

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1. On March 11, the House concurred to the Senate Committee Substitute by a vote of 98 in favor and 0 against.

2. *See* Ky. Att'y Gen. Op. 15-008 (April 2, 2015).

3. *See* KY. REV. STAT. ANN. § 14.105(1) (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 1.

4. *See id.* § 14A.2-010(13).

5. *Compare id.* § 271B.8-300(1)(c) ("honestly"), *with* MODEL BUS. CORP. ACT § 8.30 (AM. BAR ASS'N 2011) ("reasonably").

standard and the standard for indemnification, KRS section 271B.8-510 has been revised to delete "reasonably," substituting in place thereof "honestly."[6]

B. Qualification by Foreign Insurance Companies

Having its roots in the law of business corporations, but now set forth in the Kentucky Business Entity Filing Act,[7] a revision has been made for when a foreign corporation must qualify to transact business.[8] Specifically, prior to the enactment of the Kentucky Business Corporation Act, foreign insurance companies were exempt from the obligation to qualify to transact business with the Kentucky Secretary of State.[9] Foreign insurance companies are subject to merit review before they are afforded a Certificate of Insurance by the Commissioner of Insurance. No such merit review is undertaken by the Secretary of State's office in affording a foreign business entity a Certificate of Authority.[10] Re-adopting the rule that existed prior to 1988, foreign insurance companies holding a Certificate of Authority from the Department of Insurance will not separately be required to qualify to transact business by a filing with the Secretary of State.[11] Consequent to this amendment, it is clear that a foreign insurer will have the capacity to initiate suit in Kentucky notwithstanding that it has not received, from the Secretary of State a Certificate of Authority.[12] Nevertheless, there is no less protection afforded to those who may need to bring suit against a foreign insurer. Rather, each foreign insurer transacting business in Kentucky is deemed to have appointed the Secretary of State as its registered agent.[13]

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6. *See* KY. REV. STAT. ANN. § 271B.8-510(1)(b) (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 8.

7. *See generally* Thomas E. Rutledge & Laura A. D'Angelo, *The Kentucky Business Entity Filing Act: An Introduction*, 74 BENCH & BAR 6 (Sept. 2010); Thomas E. Rutledge & Laura K. Tzanetos, *The Kentucky Business Entity Filing Act: The Next Step Forward in the Rationalization of Business Entity Law*, 38 N. KY. L. REV. 423 (2011).

8. *See also generally* Thomas E. Rutledge, *Kentucky, Doing Business in States Other than the State of Incorporation* (BNA Corporate Practice Series Portfolio 84).

9. *See* KY. REV. STAT. ANN. § 271A.520(1) (West 2015), *repealed by* 1988 Ky. Acts, ch. 23, § 248 ("No foreign corporation, *except a foreign insurance company*, shall have the right to transact business in this state until it shall have procured a certificate of authority to do so from the Secretary of State.") (emphasis added).

10. *See id.* § 14A.9-030.

11. *See id.* § 14A.9-010(7).

12. *See id.*; *see also id.* § 286.2-670 (addressing the bringing of suit by a foreign insurer not holding a certificate of insurance).

13. *See id.* § 304.3-230(1)–(2):

This is not to say, however, that a foreign insurer is precluded from qualifying to transact business with the Secretary of State. The application for the Certificate of Authority will need to identify the Secretary of State as the registered agent and office.[14] Qualification with the Secretary of State may be necessary if, for example, the insurer desires to transact business under a name other than its real name.[15]

C. Simplification of Merger Filings

Changes made to the Business Corporation and Limited Liability Company Acts simplify the filings that must be made upon a merger. Under the prior system, in order to effect a merger, both articles of merger and the agreement and plan of merger were filed with the Secretary of State.[16] In many circumstances, this necessitated the filing of documents containing business information that would be considered confidential. Kentucky has now adopted the more modern approach,[17] and the only filing required to effectuate a merger is the articles of merger.[18] The requirements for the articles of merger have been slightly revised to ensure that the minimum information necessary is on the public record.[19]

> (1) Upon issuance of a certificate of authority to do business in this state, the following shall be deemed to have appointed the Secretary of State as their attorney to receive service of lawful process issued against them in this state: (a) Foreign or alien insurers; (b) Domestic reciprocal insurers; (c) Domestic Lloyd's insurers; (d) Qualified self-insurers.
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> (2) Such appointment shall be irrevocable, shall bind any successor in interest or to the assets or liabilities of the insurer, and shall remain in effect as long as there is in force in this state or elsewhere a contract that would give rise to a cause of action in this state, made by the insurer, or liabilities or duties arising therefrom.

14. *See id.* § 304.3-230(2) ("irrevocable"); *see also id.* § 14A.9-030(i)(g).

15. *See* KY. REV. STAT. ANN. § 365.015(2)(a) (West 2015).

16. *See id.* § 271B.11-050(1), prior to amendment by 2015 Ky. Acts ch. 34, § 9 ("deliver to the Secretary of State for filing articles of merger or share exchange setting forth (a) the plan of merger or share exchange"); *id.* § 275.360, prior to amendment by 2015 Ky. Acts ch. 34, § 56 ("deliver to the Secretary of State for filing artides of merger… setting forth: … (b) the plan of merger").

17. *See, e.g.*, DEL. CODE ANN. tit. 8, § 251(c) (West 2014); MODEL BUS. CORP. ACT § 11.06 (AM. BAR ASS'N 2011).

18. *See* KY. REV. STAT. ANN. § 271B.11-050 (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 9; *id.* § 275.360, *amended by* 2015 Ky. Acts, ch. 34, § 56.

19. *See id.*; *id.* § 275.360. In so doing, certain actions such as amendment of the organic documents of the entity surviving the merger must be set forth in the articles of merger in order

D. The Appropriate Court for Forum Selection

There has been added to the Business Corporation Act the defined term "appropriate court."[20] The term "appropriate court" is otherwise now utilized as determining where a corporation has the option of requiring that derivative actions or actions to compel the production of corporate records be filed.[21] Note that in Kentucky, the requirement must be set forth in the articles of incorporation; a bylaw provision to the same effect is not authorized by statute.[22]

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to be operative. *See id.* § 271B.11-060, *amended by* 2015 Ky. Act, ch. 34, § 10; *id.* § 275.365, *amended by* 2015 Ky. Acts, ch. 34, § 57.

20. *Id.* § 271B.1-400(1), *amended by* 2015 Ky. Acts, ch. 34, § 6.

21. *See id.* § 271B.7-400(7).

22. *Compare* Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934 (Del. Ch. 2013), *with* City of Providence v. First Citizens BancShares, Inc., 99 A.3d 229, 233-34 (Del. Ch. 2014) (both upholding venue selection provisions of corporate bylaws). The 2015 Delaware General Assembly amended the DGCL to address forum selection provisions in either the certificate of incorporation or the bylaws. Under the new provisions, it is clear that either the certificate or the bylaws may provide that (a) the Delaware courts are the exclusive jurisdiction for consideration of internal corporate claims or, in the alternative, (b) the courts of a foreign jurisdiction or a permissible venue for the resolution of disputes over internal affairs provided that the Delaware courts as well remain an available venue. At the same time, and this is made express in the official comment released with the statute, neither the certificate nor the bylaws may purport to identify the courts of a jurisdiction outside of Delaware as the exclusive venue for the resolution of internal corporate claims: the statute "invalidates such a provision selecting the courts in a different State, or an arbitral forum, if it would preclude litigating such claims in the Delaware courts."

The referenced definition of "internal corporate claims" of section 115 is to "claims, including claims in the right of the corporation, (i) that are based upon a violation of the duty by a current or former director or officer or stockholder in such capacity, or (ii) as to which this title confers jurisdiction upon the Court of Chancery."

Unresolved by the statute is whether and to what degree the corporation's artides or bylaws may impose additional restrictions upon derivative actions. *See, e.g.*, ATP Tours, Inc. v. Deutscher Tennis Bund, 91 A.3d 554, 557–59 (Del. 2014) (holding that by amendment of the bylaws the board of a nonprofit corporation could impose upon the members thereof a fee shifting provision in the event of a derivative action that "does not obtain a judgment on the merits that substantially achieves, in substance and amount, the full remedy sought."); *See also* 18 OKLA. STAT. ANN. tit. 18, § 1126 (West 2015). *But see Delaware Proposal Would Restrict Fee-Shifting Corporate Bylaws, Charters*, 30 CORP. COUNSEL WEEKLY 73 (Mar. 11, 2015) (reviewing Delaware proposal limiting fee-shifting bylaws); *See also* Joseph A. Grundfest & Kristen A. Savelle, *The Brouhaha Over Inter-Corporate Forum Selection Provisions: A Legal, Economic and Political Analysis*, 68 BUS. LAW. 325 (Feb. 2013). The 2015 Delaware General Assembly passed amendments to the Delaware General Corporation Law providing, essentially, that fee shifting provisions in either the certificate or the bylaws will not be effective. Specifically, Senate Bill 75, with respect to stock corporations (the contrary rule as set forth in *ATP Tours* for nonstock/nonprofit corporations was not modified), added a new subsection (f) to section 102 to provide:

> The certificate of incorporation may not contain any provision that would impose liability on a stockholder for the attorneys' fees or expenses of the

E. Exclusivity of the Dissenter Rights Remedy

A technical but important revision has been made to the exclusivity provision of the dissenter rights' statute. At one time, major corporate actions such as a merger, sale of substantially all assets or amendment of the articles of incorporation required the consent of all shareholders, a rule that protected the shareholder's vested property interest in the contractual terms of the venture.[23] This state of the law permitted opportunistic rent seeking by minority shareholders, whose approval was required for significant transactions.[24] Responding to pressures to permit significant transactions upon less than a unanimous consent, the various state legislatures reduced the applicable voting thresholds to less than unanimity.[25] At the same time, in order to ameliorate the impact upon

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> Corporation or any other party in connection with an internal corporate claim, as defined in § 115 of this title.

In a similar vein, there is added to section 109 of the DGCL:

> The bylaws may not contain any provision that would impose liability on a stockholder for the attorneys' fees or expenses of the Corporation or any other party in connection with an internal corporate claim, as defined in § 115 of this title.

The referenced definition of "internal corporate claims" of section 115 is to "claims, including claims in the right of the corporation, (i) that are based upon a violation of the duty by a current or former director or officer or stockholder in such capacity, or (ii) as to which this title confers jurisdiction upon the Court of Chancery."

23. *See, e.g.*, Voeller v. Neilston Warehouse Co., 311 U.S. 531, 535 n.6 (1941); *In re* Valuation of Common Stock of McLoom Oil Co., 565 A.2d 997, 1004 (Me. 1989) ("The appraisal remedy has deep roots in equity. The traditional rule through much of the 19th century was that any corporate transaction that changed the rights of common share holders required unanimous consent. The appraisal remedy for dissenting shareholders evolved as it became clear that unanimous consent was inconsistent with the growth and development of large business enterprises. By the bargain struck in enacting an appraisal statute, the shareholder who disapproves of a proposed merger or other major corporate change gives up his right of veto in exchange for the right to be bought out—not at market value, but at 'fair value.'") (citations omitted); *In re* Enstar Corp., No. 7802, 1986 WL 8062, at *5 (Del. Ch. July 17, 1986); Chi. Corp. v. Munds, 172 A. 452, 455 (Del. Ch. 1934); 12B WILLIAM MEADE FLETCHER, FLETCHER'S CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 5906.10 (2009).

24. *See, e.g.*, Salomon Bros. Inc. v. Interstate Bakeries Corp., 576 A.2d 650, 651–52 (Del. Ch. 1989) ("[V]eto power at common law 'made it possible for an arbitrary minority to establish a nuisance value for its shares by refusal to cooperate.'") (quoting *Voeller*, 311 U.S. at 535 n. 6 (1941)); *In re* Shore, 67 A.D.2d 526 (N.Y. App. Div. 1979).

25. *See, e.g.*, 12B FLETCHER, *supra* note 23 ("Consequently, statutes were enacted conferring wide powers on the majority or a specified percentage of the stock to amend the charter, sale, consolidate, merge, etc.") (citation omitted); Shawnee Telecom Resources Inc. v. Brown, 354 S.W.3d 542, 552–56 (Ky. 2011) (recognizing that dissenter rights were created to compensate corporate shareholders for the loss of a common law right). As early as the 1928 Uniform

the shareholder's property rights in the terms of the existing venture,[26] dissenter rights were codified,[27] affording minority participants in the venture the ability to, upon objecting to the proposed change in the business, extract a proportionate interest in the venture's value for investment elsewhere.[28] Dissenter rights became more important with the development of the cash-out merger,[29] morphing from a liquidity

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Business Corporation Act (the predecessor to the Model Business Corporation Act), a merger could be approved by a vote of two-thirds of the shareholders. *See* MODEL BUS. CORP. ACT § 44(II); *see also* KY. REV. STAT. ANN. § 271.415(2) (West 2015), *repealed by* 1972 Ky. Acts, ch. 274, § 165 (permitting a sale of corporate assets with the approval of a majority of the shareholders).

26. *See, e.g.*, Yanow v. Teal Indus., Inc., 422 A.2d 311, 317 n. 6 (Conn. 1979) ("the appraisal remedy has been described as an adequate quid pro quo for statutes giving the majority the right to override the veto of a dissenting shareholder"); Ala. By-Prods. Corp. v. Cede & Co., 657 A.2d 254, 258 (Del. 1995) (describing appraisal as "a limited legislative remedy developed initially as a means to compensate shareholders of Delaware corporations for the loss of their common law right to prevent a merger or consolidation by refusal to consent to such transactions"); Reynolds Metals Co. v. Colonial Realty Corp., 190 A.2d 752, 755 (Del. 1963) (characterizing dissenter rights as "compensation" for the loss of the right to block fundamental transactions); *Salomon Bros.*, 576 A.2d at 651 ("The judicial determination of fair value pursuant to § 262 is a 'statutory right . . . given the shareholder as compensation for the abrogation of the common law rule that a single shareholder could block a merger.'") (quoting Francis I. duPont & Co. v. Universal City Studios, 343 A.2d 629, 634 (Del. Ch. 1975)); *In re Enstar Corp.*, 1986 WL 8062, at *5 (characterizing dissenter rights as "compensation" for the loss of the right to block fundamental transactions); Hariton v. Arco Elecs., Inc., 182 A.2d 22, 25 (Del. Ch. 1962) (appraisal remedy given to shareholders in "compensation" for loss of right to prevent a merger), *aff'd*, 188 A.2d 123 (Del. 1963); *Chi. Corp.*, 172 A. at 455 ("In compensation for the lost right [of a stockholder to defeat a merger transaction] a provision was written into the modern statutes giving the dissenting stockholder the option completely to retire from the enterprise and receive the value of his stock in money."); 12B FLETCHER, *supra* note 23.

27. For a review of the adoption of the appraisal remedy and its development since that time, *see* Robert B. Thompson, *Exit, Liquidity and Majority Rule: Appraisal's Role in Corporate Law*, 84 GEO. L. REV. 1 (1995). In 2007, Kentucky's partnership, limited partnership and LLC acts were amended to expressly provide, in those organizational contexts, that dissenter rights would exist only if provided for by private agreement. These amendments preclude the argument that dissenter rights are a matter of common law that protect the interests of partners and LLC members. *See* Thomas E. Rutledge, *The 2007 Amendments to the Kentucky Business Entity Statutes*, 97 KY. L.J. 229, 248 (2008-09).

28. As such, upon certain transactions, a minority shareholder may cause to be set aside the otherwise applicable rules described as alternatively "defensive asset partitioning," or "capital lock-in." *See* Henry Hansmann & Renier Kraackman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 393–95 (2000); Margaret Blair, *Locking In Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century*, 51 UCLA L. REV. 387 (2003); *see also* Lynn Stout, *On the Nature of Corporations*, 2005 U. ILL. L. REV. 253 (2005).

29. Under the Kentucky enactment of the Uniform Business Corporation Act there was no provision for the issuance of cash to a shareholder in a corporation taking part in a merger. *See* 1946 Ky. Acts, ch. 141; *see also* KY. REV. STAT. ANN. § 271.470 (West 2015), *repealed by* 1972 Ky. Acts, ch. 274, § 165. By the 1972 adoption of the Model Business Corporation Act, cash was

mechanism to a check on the majority's valuation of the minority's interest in the venture.[30] It has long been the rule that the exercise of dissenter rights are the exclusive remedy of shareholders who are in opposition to a proposed organic change to the corporate structure.[31] Essentially, absent extraordinary circumstances, a shareholder entitled to dissenter rights had those rights as their exclusive remedy, and they could not attack the substance of the proposed transaction.

This clear exclusivity has in recent years been violated. Essentially, taking out of context the declaration of the Kentucky Supreme Court in Steelvest v. Scansteel that "breach of fiduciary duty is equivalent to fraud,"[32] and by referencing the fraud exception to the exclusivity of dissenter rights,[33] plaintiffs had argued that having voted against a particular corporate action but not having exercised dissenter rights, shareholders may pursue claims of breach of fiduciary duty against the directors.[34] This converts a cause of action that arises in contract, namely what is the value of the shares held by the objecting shareholders, into a cause of action arising in tort, namely has there been a breach of fiduciary duty and, if so, what is the value thereof.

Under the revised statute, with respect to a transaction in which the shareholders are afforded dissenter rights, that will be their exclusive remedy – save an application for injunctive relief prior to the consummation of the action.[35] This opportunity to seek injunctive relief

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permitted consideration in a merger. *See id.* § 271A.355(2)(c), *repealed by* 1988 Ky. Acts ch. 23, § 248.

30. *See* Thompson, *supra* note 27, at 22.

31. *See* KY. REV. STAT. ANN. § 271A.405(1) (West 2015), *repealed by* 1988 Ky. Acts, ch. 23, § 248 ("Any shareholder making such demand shall thereafter be entitled only to payment as in this section provided and shall not be entitled to vote or to exercise any other rights of a shareholder."). The prior law on dissenter rights was silent as to exclusivity. *See id.* § 271.490. In *Yeager v. Paul Semonin Co.*, 691 S.W.2d 227, 228 (Ky. Ct. App. 1985), notwithstanding the exclusivity language of the statute, the Court wrote that a minority shareholder was not restricted to the dissenter rights remedy. However, the suit was ultimately found groundless as the shareholder could point to no fraud. *Id.* at 228–29.

32. Steelvest, Inc. v. Scansteel Servs. Ctr. Inc., 807 S.W.2d 476, 487 (Ky. 1991); *see also* Sahni v. Hock, 369 S.W.3d 39, 49 (Ky. Ct. App. 2010) (Taylor, J., dissenting) ("In Kentucky it is black letter law that the breach of a fiduciary duty is equivalent to fraud.") (citing *Steelvest, Inc.*, 807 S.W.2d at 476).

33. *See* KY. REV. STAT. ANN. § 271B.13-020(2), prior to amendment by 2015 Ky. Acts ch. 34, § 11 ("A shareholder entitled to dissent and obtain payment for his shares under this chapter shall not challenge the corporate action creating his entitlement unless the action is unlawful or fraudulent with respect to the shareholder or the corporation.").

34. *See, e.g.*, Opinion and Order at 7, May 28, 2013, Snyder v. Baumgardner, Case No. 09-CI-4445 (Jeff. Circuit Ct. Div. 4; Judge Charles L. Cunningham, Jr.).

35. *See* KY. REV. STAT. ANN. § 271B.13-020(2) (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 11. This rule is consistent with that of many foreign jurisdictions. *See, e.g.*, Brandt v. Travelers

will address situations including the absence of actual authority to effect the transaction because there has not been the necessary vote of the shareholders or a failure to make adequate disclosure to the shareholders as to the terms of the proposed transaction.

V. FIDUCIARY DUTIES IN BANKING CORPORATIONS

A last-minute addition to H.B. 440[36] revised KRS section 286.3-065, it addressing the fiduciary duties applicable to the directors of a bank. The first amendment to the provision expanded it to include bank officers; previously it addressed only directors.[37] Second, and on a more substantive level, while retaining the previous aspirational standard requiring that a director "exercise such ordinary care and diligence as necessary and reasonable to administer the affairs of the bank in a safe and sound manner,"[38] the statute placed certain outer limits on the director's conduct.

Initially, prior to its amendment, KRS section 286.3-065 set forth the fiduciary duties of the director of a bank; the statute was silent as to the obligations of officers.[39] The statute, as revised, is equally applicable to the directors and the officers of a bank. Ultimately, the substantive standard, namely that the director (and now officer) act "in good faith and with such ordinary care and diligence as necessary and reasonable to administer the affairs of the bank in a safe and sound manner" has been retained.[40] There has been added, however, a standard of culpability for monetary damages requiring any of gross negligence, willful or reckless misconduct, a knowing violation of the law or an improper personal benefit.[41] This differential in the aspirational standard from the standard of culpability for monetary damages has precedent in other Kentucky

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Corp., 665 A.2d 616 (Conn. 1995); Oshu v. Ridinger, 589 S.E.2d 905 (N.C. Ct. App. 2004); *cf*. Santa Fe Industries, Inc. v. Green, 430 U.S. 462 (1977) (holding that in connection with short form merger in which minority shareholders were afforded state law dissenter rights, minority shareholders could not bring federal 10(b) action alleging fraud in the purchase/sale of securities).

36. This provision was added in the Senate Judiciary Committee Substitute that was later concurred to by the House on March 11. This section of H.B. 440 is the only one not drafted by the author.

37. *See* KY. REV. STAT. ANN. § 286.3-065 (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 77.

38. *See id.* § 286.3-065(1) (re-codifying the first sentence of KRS § 386.3-065 prior to amendment by 2015 Ky. Acts, ch. 34, § 77).

39. *Compare id.* § 271B.8-420 (obligations of the officers of a business corporation), *with id.* § 273.229 (obligations of the officers of a nonprofit corporation).

40. *Compare id.* § 286.3-065(1), *amended by* 2015 Ky. Acts, ch. 34, § 77, *with id.* § 286.3-065 prior to amendment.

41. *Id.* § 286.3-065(1).

business entity law.[42] It has now provided the directors and officers, in the discharge of their duties, are entitled to rely upon information, opinions, reports and statements prepared by either certain subsets of the board or certain independent legal parties.[43] That said, no reliance is permitted if the director has knowledge that makes the reliance unreasonable.[44] With respect to the burden of proof, it is laid upon the person bringing the action for monetary damages, they being obligated to prove "by clear and convincing evidence" the breach of the duties as well as causation.[45]

VI. PARTNERSHIPS & LIMITED PARTNERSHIPS

A. Dissolution of a Limited Partnership

An amendment to the Kentucky Uniform Limited Partnership Act (2006) makes express that a limited partnership shall dissolve when the same person is the only general and only limited partner.[46] This is not a change in the law as the definition of a "limited partnership" already incorporated this rule,[47] but now it is clearer and precludes the (incorrect) argument that the requirement of two partners applies only at the moment of the partnership's formation.

B. Suits Against Partnerships and Limited Partnerships

The statute governing legal actions brought against a limited partnership subject to the Kentucky Revised Uniform Limited Partnership

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42. *See, e.g.*, *id.* § 271B.8-300(1) (aspirational standard of corporate directors); *id.* § 271B.8-300(5)(b) (standard of culpability for monetary damages).

43. KY. REV. STAT. ANN. § 286.3-065 (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 77; *accord id.* § 271B.8-300(3). It should be noted that while the Business Corporation Act allows a director to rely upon an officer or employee who they honestly believe to be reliable and competent in the matter under question, a bank director is similarly allowed to rely upon another director. *Compare id.* § 386.3-065(1)(a) ("one (1) or more officers, directors, or employees of the bank whom the officer or director reasonably believes to be reliable and competent in the matters presented."), *with id.* § 271B.8-300(3)(a) ("one (1) or more officers or employees of the corporation to the director honestly believes to be reliable and competent in the matters presented.").

44. *Id.* § 286.3-065(2); *id.* § 271B.8-300(4).

45. *See id.* 286.3-065(3); *accord id.* § 271B.8-300(6).

46. *Id.* § 362.2-801(6).

47. *See id.* § 362.2-102(14) ("'Limited partnership,' except in the phrases 'foreign limited partnership' and 'foreign limited liability limited partnership,' means an entity, having one (1) or more general partners and one (1) or more limited partners, which is formed under this subchapter by two (2) or more persons or becomes subject to this subchapter under KRS 362.2-974(1) and (2). The term includes a limited liability limited partnership.").

Act has been clarified. In 1994, KRS section 362.605 was created, providing that a general partnership may be sued in its "common name."[48] Such suits eliminate the requirement that all general partners be named in order to bring an action against a general partnership, and are useful when it is anticipated that the assets of the partnership will be sufficient to satisfy the creditor's claim.[49] That statute did not, however, address what is the "common name" of the general partnership.[50] At the same time, consequent to the linkage of the general and limited partnership laws,[51] this provision has at times been applied to the effect that, in order to bring suit against a limited partnership, it is necessary to name not only the general partners but also the limited partners.[52]

As revised, the reference to the "common name" of a general partnership has been revised to reference the "real name"; what is the real name of a partnership will be determined by the assumed name statute.[53] A limited partnership may be sued in its real name, that as well being determined under the assumed name statute.[54] Where it is not necessary to access the individual assets of the general partners, they need not be named in the action.[55] However, if it is desired that the general partners be personally liable for any judgment rendered, they must as well be named as parties to the action.[56]

C. Limited Partnership Derivative Actions

To the derivative action provisions of the Kentucky Uniform Limited Partnership Act (2006)[57] there has been added language enabling courts to order plaintiffs to pay defendants' costs and expenses incurred in defending a proceeding or a portion thereof "commenced without reasonable cause or for an improper purpose."[58] This is the same standard employed in the derivative action provision newly added to the

48. *See id.* § 362.605.
49. KY. REV. STAT. ANN. § 362.605 (West 2015).
50. *See id.*
51. *See id.* § 362.523.
52. *See also id.* § 362.401(10) ("Partner means a limited partner or a general partner.").
53. *See id.* § 365.015(1)(b).
54. *Id.*
55. KY. REV. STAT. ANN. § 362.605 (West 2015).
56. *See id.* §§ 362.605(2)–(3).
57. *Id.* § 362.2-932.
58. *See id.* § 362.2-935(3). With respect to the apportionment of costs on a claim by claim basis, *see also* Wanandi v. Black, No. 2013-CA-000459-MR, 2015 WL 2084511, at *16 (Ky. Ct. App. May 1, 2015) (citing Ky. Farm Bureau Mut. Ins. Co. v. Burton, 922 S.W.2d 385, 389–90 (Ky. Ct. App. 1996)).

LLC Act and already existing in the Unincorporated Cooperative Association and Statutory Trust Acts.[59]

VII. THE STATUTORY TRUST ACT

Several technical revisions have been made to the Kentucky Uniform Statutory Trust Act.[60] The first pair of amendments go to the provision of the Statutory Trust Act listing items that may be included in the governing instrument.[61] As such, neither these provisions is of themselves operative; rather, they are only enabling. First, it is provided that the statutory trust may itself serve as the beneficial owner associated with a series.[62] This provision will facilitate the use of a statutory trust with series as a holding company. The second provision will allow a statutory trust, in effect, to waive the entity rule as to ownership of its property,[63] thereby permitting each of the beneficial owners associated with either the statutory trust or a series thereof to be deemed the owner, as tenants in common with the other beneficial owners, of the property of the statutory trust or the property associated with the series.[64] This provision will be employed in highly lawyered transactions in which a statutory trust is used for structuring a tenancy-in-common (TIC) ownership. A new provision, it also governing a series of a statutory trust, sets forth a default rule to the effect that, absent contrary private ordering, every beneficial owner of the statutory trust will be associated with each series thereof.[65]

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59. *See* KY. REV. STAT. ANN. § 275.337(8)(a) (West 2015); *id.* § 272A.13-050(2)(a); *id.* § 386A.6-110(9)(a).

60. *See generally* Thomas E. Rutledge, *The Kentucky Uniform Statutory Trust Act (2012): A Review*, 40 N. KY. L. REV. 93 (2012–13); *see also* Thomas E. Rutledge & Ellisa O. Habbart, *The Uniform Statutory Trust Entity Act: A Review*, 65 BUS. LAW. 1055 (Aug. 2010).

61. KY. REV. STAT. ANN. § 386A.1-030 (West 2015).

62. *Id.* § 386A.1-030(4)(r).

63. *See id.* § 386A.1-030(4)(s).

64. *Id.*

65. *Id.* § 386A.4-010(7). There was also corrected a typographical error in the Statutory Trust Act. *See id.* § 386A.4-020(6), *amended by* 2015 Ky. Acts, ch. 34, § 63. In addition, revisions to KRS § 360.027 make express that a statutory trust falls within its scope. *See id.* § 360.027, *amended by* 2015 Ky. Acts, ch. 34, § 65. This revision is admittedly redundant of existing law. *See id.* § 446.010(6). Still, it avoids ambiguity and addresses any failure to reference the general definition provisions.

VIII. LIMITED LIABILITY COMPANIES

A. Suits By or On Behalf of an LLC

A new section has been added to the Limited Liability Company Act to set forth rules applicable to derivative actions in LLCs.[66] While the LLC Act as originally adopted did not provide expressly for derivative actions, neither did it preclude them.[67] Clearly such actions exist under the rules of equity,[68] and the Kentucky courts have both entertained express derivative actions with respect to LLCs and otherwise maintained the direct versus derivative distinction.[69] By means of this new statute, it being based upon that adopted by the Kentucky General Assembly in

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66. *See id.* § 275.337.

67. *See, e.g.*, Thomas E. Rutledge & Lady E. Booth, *The Limited Liability Company Act: Understanding Kentucky's New Organizational Option*, 83 KY. L.J. 1, 41 n. 202 (1994-95) ("The LLC Act does not provide for derivative actions as a means of recovering misappropriated assets or opportunities. However, the LLC Act in no way forbids such suits."); CARTER G. BISHOP & DANIEL S. KLEINBERGER, LIMITED LIABILITY COMPANIES: TAX AND BUSINESS LAW ¶ 10.07[2] (Supp. 2015) ("Many LLC statutes expressly authorize derivative actions, but some do not. This distinction should make little difference. Derivative litigation began in the corporate context over 150 years ago without the benefit of statutes, and remains essentially equitable in nature."); *see also generally* Thomas E. Rutledge, *Who Will Watch the Watchers?: Derivative Actions in Nonprofit Corporations*, 103 KY. L. J. ONLINE 31 (2015).

68. *See also* KY. REV. STAT. ANN. § 275.003(1) (West 2015).

69. *See*, *e.g.*, Pixler v. Huff, Civ. Act. No. 3:11-CV-00207-JHM, 2012 WL 3109492, at *2–4 (W.D. Ky. July 31, 2012) (applying the direct versus derivative distinction **as** traditionally applied to corporations and determining whether certain claims brought by a member could be brought only on a derivative basis); *id.* at *3 ("Therefore, Plaintiff may maintain her claims against the Defendants only where she has suffered an injury that is separate and distinct from that which would be suffered by other members or the LLC as an entity."); R.C. Tway Co. v. High Tech Performance Trailers, LLC, No. 3:2012-CV-00122, 2013 WL 842577, at *3 (W.D. Ky. Mar. 5, 2013) ("Each of the claims identified above clearly alleges that High Tech or Hanusosky violated some duty it owed directly to [Performance Trailers], thus causing [Performance Trailers] injury. As [Performance Trailers] is the allegedly injured party for each of these claims, it is the one that is entitled to enforce the rights granted by substantive law. Accordingly, [Performance Trailers] is not a nominal party, but instead is a real party in interest as to those claims."); Chou v. Chilton, Nos. 2009-CA-002198-MR, 2009-CA-002284-MR, 2014 WL 2154087 (Ky. Ct. App. May 23, 2014) ("[The LLC] and not Chou himself would benefit from any recovery for breach of the operating agreement, fraud, misappropriation, breach of fiduciary duty or gains taken by the defendants. While Chou may or may not receive funds from [the LLC] on dissolution of that company, any wrongs for breach of the operating agreement, fraud, misappropriate, breach of fiduciary duty or gains taken by the defendants perpetrated by any of the [defendants] or possibly [a separate LLC controlled by the defendants] would be wrongs against [the LLC] and not Chou individually."); Turner v. Andrews, 413 S.W.3d 272 (Ky. 2013) (rejecting effort by the sole member of an LLC to bring on his own behalf (rather than on behalf of the LLC), a claim for lost profits.); *see also* Gross v. Adcomm, Inc., No. 2014-CA-001031-MR, 2015 WL 8488900 (Ky. Ct. App. 2015) (purported direct action by corporation against director/shareholder dismissed for failure of authorization).

2012 with respect to statutory trusts,[70] there are set forth the procedural limitations and requirements as to bringing a derivative action.[71] With this addition to the LLC Act, Kentucky law is brought more consistent with that of Delaware, the Revised Uniform Limited Liability Company Act, and the Revised Prototype Limited Liability Company Act.[72] Not addressed is the question of whether the operating agreement may (a) modify (presumably by raising additional thresholds) the standing requirements or (b) alter the rules for the potential for fee shifting. That said, neither should be possible. Initially, while such is of itself not determinative, the provision's modification by the operating agreement is not provided for.[73] Second, the parties to an operating agreement may not, by private ordering, alter or limit the equitable powers of the court, by means of a derivative action, to review and as necessary correct abuses and breaches of duty.[74]

The distinction between a direct and derivative action, the former involving a unique injury to the plaintiff while the latter involving an injury to the LLC as a distinct legal person, has been incorporated into the statute.[75] A direct action is not subject to the standing, procedural and pleading requirements of a derivative action.[76] A derivative action is subject to: (i) a demand requirement or the pleading of futility[77] and (ii)

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70. *See* KY. REV. STAT. ANN. § 386A.6-110 (West 2015).

71. *See id.* § 275.337.

72. *See* DEL. CODE ANN. tit. 6, §§ 18-1001–1004 (West 2015) (governing derivative actions in Delaware LLCs); REVISED PROTOTYPE LTD. LIAB. CO. ACT §§ 901–908, 67 BUS. LAW. 117, 194–198 (Nov. 2011) (governing derivative actions); REVISED UNIF. LTD. LIAB. CO. ACT § 902, 6B U.L.A. 523 (2008). Looking at the states adjoining Kentucky, all of their LLC Acts, except that of Indiana, expressly provide for derivative actions. *See* OHIO REV. CODE ANN. §§ 1705.49–1705.52 (West 2015); TENN. CODE ANN. § 48-249-801 (West 2015); MO. ANN. STAT. § 347.173 (West 2015); W. VA. CODE ANN. § 31B-11-1101 (West 2015); VA. CODE ANN. § 13.1-1042 (West 2015).

73. *Compare* KY. REV. STAT. ANN. § 275.170 (West 2015) ("Unless otherwise provided in a written operating agreement"); *id.* § 275.220 (same).

74. *See id.* § 275.003(1) ("Unless displaced by particular provisions of this chapter, the principles of law and equity shall supplement this chapter."); *In re* Carlisle Etcetera, No. 10280-VCL, 2015 WL 1947027 (Del. Ch. Apr. 30, 2015); BISHOP & KLEINBERGER, *supra* note 67, ¶ 10.07[3] ("However, derivative suits began as, and remain, essentially equitable in nature. It is questionable (at best) whether private agreements can restrain a court's power to do equity.") (citations omitted).

75. *See* KY. REV. STAT. ANN. § 275.337 (West 2015); *accord id.* § 386A.6-110(i); *id.* § 362.2-931(1)–(2); *see also* CMS Inv. Holdings, LLC v. Castle, No. 9468-VCP, 2015 WL 3894021, at *7–8 (Del. Ch. June 23, 2015) (applying direct versus derivative distinction under Delaware law).

76. *See also* Marhula v. Grand Forks Curling Club, Inc., 863 N.W.2d 503 (N.D. 2015) (action challenging termination of membership in nonprofit corporation is not subject to derivative action requirements).

77. KY. REV. STAT. ANN. §§ 275.337(2)–(4) (West 2015); *accord id.* § 271B.7-400(2); *id.* § 362.2-832, -934; *id.* § 272A.13-010, -060; *id.* § 386A.6-110(2).

the requirement of member status at the time the action is commended and at the time of the complained of actions.[78] All proceeds of the action are property of the LLC.[79] Dismissal or settlement of the derivative action requires court approval.[80] The proper venue for a derivative action is the circuit court of the county in which the LLC maintains its registered office.[81] If the derivative action results in substantial benefit to the LLC, the court may require it to pay the plaintiff-member's reasonable expenses, including counsel fees.[82] Conversely, to the extent the suit or an aspect thereof was brought without reasonable cause or for an improper purpose, the court may order the plaintiff member to pay each defendants' reasonable expenses, including counsel fees.[83]

It is to be expected that disputes as to the alignment of the LLC will oft occur. Where an individual or other minority of the members asserts they are vindicating the LLC's rights through a derivative action, the LLC will typically, at least initially, be aligned as a plaintiff. An argument may

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78. *Id.* § 275.337(3). The requirement of having been a member at the time of the action complained of may be derived from an assignor if the assignment was by operation of loss or pursuant to the terms of the operating agreement; *accord* § *id.* 271B.7-400(1); *id.* § 272A.13-020(1); *id.* § 362.2-933; *id.* § 386A.6-110(3).

79. *Id.* § 275.337(5).

80. *Id.* § 275.337(6); *accord id.* § 271B.7-400(3); *id.* § 272A.13-040; *id.* § 386A.6-110(6).

81. *Id.* § 275.337(7). Almost never may a derivative action be brought in federal court on the basis of diversity jurisdiction. The LLC will be either a plaintiff or a defendant in a derivative action. *See, e.g.*, Gabriel v. Preble, 396 F.3d 10 (1st Cir. 2005) (regarding the plaintiff or defendant alignment of the entity). And as the entity will have the citizenship of all members, there will never be diversity of citizenship. *See, e.g.*, Lotan v. Horizon Properties LLC, No. 14 Civ. 3134(PAC), 2014 WL 2210536, at *1 (S.D.N.Y. May 27, 2014) ("Plaintiffs common citizenship with the LLC destroys complete diversity.") (citing Bischoff v. Boar's Head Provisions Co., Inc., 436 F. Supp.2d 626, 634 (S.D.N.Y. 2006) ("There is no dispute that as long as [Plaintiff] may bring derivative claims on behalf of [the LLC] is a true defendant that destroys complete diversity in this case.")); Richardson v. Edward D. Jones & Co., 744 F. Supp. 1023 (D. Colo. 1990); Gen. Tech. Applications, Inc v. Exro Ltda., 388 F.3d 114 (4th Cir. 2004); Cook v. Toidze, 950 F. Supp. 2d 386, 391 (D. Conn. 2013) ("If the action at hand is a derivative suit, the [LLC] is not a nominal party.").

82. KY. REV. STAT. ANN. § 275.337(8)(b) (West 2015); *accord id.* § 272A.13-050(2)(b); *id.* § 362.2-935(2); *id.* § 386A.6-110(9)(b); *see also* Toler v. Clark Rural Electric Cooperative Corp., 512 S.W.2d 25, 26–27 (Ky. 1974) (affirming denial of attorney's fees in shareholder litigation that successfully obtained judgment setting aside election of board of directors as "a pecuniary benefit [to the corporation] is a prerequisite to recovery" of attorney fees); Orbit Gas Co. v. Arnett, 620 F.2d 304, 304 (6th Cir. 1980) (in reliance on *Toler*, holding that a pecuniary benefit is a prerequisite to recovery of fees and costs in derivative litigation on behalf of a Kentucky corporation).

83. KY. REV. STAT. ANN. § 275.337(8)(a) (West 2015); *accord id.* § 272A.13-050(2)(a); *id.* § 362.2-953(3); *id.* § 386A.6-110(9)(a). With respect to the need to apportion costs on a claim by claim basis, *see* Wanandi v. Black, No. 2013-CA-000459-MR, 2015 WL 2084511, at *16 (Ky. Ct. App. May 1, 2015) (citing Ky. Farm Bureau Mut. Ins. Co. v. Burton, 922 S.W.2d 385, 389-90 (Ky. Ct. App. 1996)); Hunt v. North American Stainless, No. 2015-CA-000088-MR (Ky. Ct. App. 2016) ("Simply because a party succeeds under one claim under KRS Chapter 337 does not mean all of the party's attorney fees within the same litigation can be recovered.").

be made that the initial alignment should be as a defendant as the suit has two components, namely (a) against the LLC for failure to bring a direct action to vindicate its rights and (b) against the person or persons who are alleged to have injured the LLC.

Where the LLC is initially aligned as a plaintiff, realignment as a defendant may be appropriate where there is animosity (when will there not be?) between the minority-member plaintiff and those exercising control over the LLC. This treatment reorganizes that even as the minority may have the right to, on the LLC's behalf, initiate and maintain a derivative action, the majority members or the manager who are the target of the suit will typically retain control over the LLC. Still being controlled by the targets of the suit, animosity may dictate the LLC's alignment as a defendant.[84]

Still on the topic of lawsuits involving LLCs, the provision governing authority to bring suit on behalf of an LLC has been streamlined.[85] This provision, KRS section 275.335, was itself based upon section 1102 of the 1992 Prototype Limited Liability Company Act, that having been the primary source for the drafting of the original Kentucky LLC Act.[86] The provision, being charitable, was significantly over complicated and curious in several respects.

Initially, KRS section 275.335 is an exception to the generally applicable rule of LLC management set forth in KRS section 275.165. Pursuant thereto, if the LLC is member-managed, then all decisions as to the LLC's management, a class of action that would otherwise include initiating a lawsuit on its behalf, would require the approval of a majority-in-interest of the members.[87] Alternatively, if the LLC is manager-managed, the decision for the LLC to bring suit would be made by the managers with the members not having a voice therein.[88] But then KRS section 275.335 is an exception to KRS section 275.165.

Under KRS section 275.335, which only addresses how an LLC may be authorized to bring suit, a per-capita majority of the members may authorize a member to on the LLC's behalf bring suit. Particular to this circumstance: (i) an alternative mechanism for counting the members is

84. *See, e.g.*, Hildebrand v. Lewis, 281 F. Supp. 2d 837, 844–45 (E.D. Va. 2003).

85. KRS § 275.335 is not a derivative action provision. In a derivative action, assuming no realignment consequent to animosity, the entity is a nominal defendant. In a suit brought under KRS § 275.335, the LLC is the plaintiff.

86. *See* Rutledge & Booth, *supra* note 67, at 9.

87. *See* KY. REV. STAT. ANN. §§ 275.165(1), .175(1) (West 2015).

88. *See id.* § 275.165(2).

utilized;[89] (ii) in the case of a vote of the members a disinterested limitation is sometimes imposed; [90] and (iii) the restriction of exclusive management of a manager-managed LLC to the managers is eliminated. If the LLC is manager-managed, suit may be initiated by a majority of the managers, but an interested manager is barred from participation in that vote.[91] While the different rules as to disinterestedness between members and manager votes was perhaps nonsensical, it was driven by the statutory language.[92] All of these rules are subject to modification in a written operating agreement.[93]

Irrespective of whether the LLC is member-managed or manager-managed, unless a written operating agreement provides a contrary rule,[94] the members remain empowered to cause legal action to be initiated by the LLC.[95] This capacity exists even in a manager-managed LLC in which the managers have "exclusive power to manage the business and affairs of the [LLC]."[96] If the members are considering whether the

89. Under KRS § 275.165, through cross-reference to KRS § 275.175(3), members vote in proportion to their respective capital contributions to the LLC. For purposes of authorizing suit under KRS § 275.335, members vote on a per-capita (one member = one vote) basis.

90. *See id.* § 275.335(1)(a).

91. *See id.* § 275.335(3). Managers, absent a contrary provision in the operating agreement, vote per capita. *See id.* § 275.175(1); *see also* 2007 Ky. Acts, ch. 137, § 110; Rutledge, *supra* note 27, at 258.

92. *See* KY. REV. STAT. ANN. § 275.335(2) (West 2015). The distinction between the second sentence of each of § 275.335(1) and (2) arises out of the former's application when reference needs to be made to § 275.335(2) while the latter does not. For ease of comparison:

2nd sentence, KRS § 275.335(1) (emphasis added)	2nd sentence, § 275.335(2)
In determining the vote required under KRS 275.175, the vote of any member who has an interest in the outcome of the suit that is adverse to the interest of the limited liability company shall be excluded;	In determining the required vote, the vote of any manager who has an interest in the outcome of the suit that is adverse to the interest of the limited liability company shall be excluded.

93. *Id.* § 275.335(1).

94. *Id.* There is to date a dearth of guidance as to what would constitute "otherwise provided in a written operating agreement." At one end of the spectrum would be a multi-paragraph provision addressing how suit may be brought on behalf of the LLC – no real question there arises. In contrast is the statement in the operating agreement of a manager-managed LLC that "all management decision on behalf of the LLC shall be made by the managers." Some might argue this is insufficient to constitute "otherwise provided in a written operating agreement." Alternatively, "all management decisions on behalf of the LLC, including bringing suit on its behalf, shall be made by the manager" likely would be sufficient.

95. *Id.*

96. *See id.* § 275.165(2).

LLC should bring suit, the members vote per-capita, and the suit is authorized if it is approved by more than one-half of the members "eligible to vote thereon."[97] The statute does not explain or expand upon who is or is not a member "eligible to vote thereon";[98] the next sentence of the statute does not fill that role. The second sentence of KRS section 275.335(1)(a) provides:

> In determining the vote required under KRS 275.175, the vote of any member who has an interest in the outcome of the suit that is adverse to the interest of the limited liability company shall be excluded (emphasis added).

This provision is applicable only if the operating agreement has required[99] that all members approve the LLC bringing the action. Thus, in the face of a requirement of unanimity, the member "who has an interest in the outcome of the suit that is adverse to the interest of the [LLC] shall be excluded."[100] Where, in contrast, the applicable operating agreement is silent as to bringing suit, there is not a statutory directive to exclude from the determination of whether one-half of the number of members have approved doing so have an interest adverse to that of the LLC. While a court could find such an exclusion to be what is intended by "eligible to vote thereon," it will do so without support from the statute itself or the commentary to the Prototype LLC Act.[101] Alternatively, if the operating agreement provides, inter alia, "that all decisions as to the management and affairs of the company will be made by a majority-in-interest of the members," and the agreement is silent as to both bringing suit and barring conflicted members from voting, it may be credibly argued that the written operating agreement has "otherwise provided" and no exclusion based upon an alleged adverse interest is appropriate.

In that an action under KRS section 275.335 is bought by the LLC, it will be aligned as the plaintiff in the action, and any member or manager acting on the LLC's behalf should not be named as a party except to the extent, if any, they are pursuing individual claims.[102]

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97. *Id.* § 275.335(1)(a).

98. *See* KY. REV. STAT. ANN. § 275.335 (West 2015).

99. Any requirement would have to be in writing. *See id.* ("Unless otherwise provided in a written operating agreement"); *id.* § 275.175(1) ("Unless otherwise provided in the articles of organization, a written operating agreement, or this chapter . . . .").

100. *Id.* § 275.335(1)(a).

101. Section 275.335, as enacted in 1994, was based upon section 1102 of the Prototype Limited Liability Company Act (1992).

102. *See* KY. REV. STAT. ANN. § 275.335(1) (West 2015) ("a suit on behalf of the [LLC]"); *id.* § 275.330 (an LLC may sue or be sued in its own name); *id.* § 275.155 (a member is not a proper party to an action by or against LLC except as to individual claims or liabilities).

It needs to be recognized that KRS section 275.335 is by its terms a quite limited provision. It addresses only the approval of bringing a suit on behalf of the LLC; it says nothing about the prosecution and settlement of the suit. These lacuna can be quite troubling in the case of a suit arising out of a dispute internal to the LLC. Consider Lilliput LLC having eleven members, one holding a 60% interest, and ten other members, each holding a 4% interest. Lilliput LLC, which is member-managed, has no written operating agreement and is as to these matters governed by the default rules of the LLC Act.[103] Irrespective of whether Gulliver, the 60% member, is or is not eligible to vote thereon,[104] a group of seven of the various 4% members are a clear per-capita majority, and they decide the LLC should bring suit against Gulliver. Assume as well that the suit is against Gulliver for misappropriation of the LLC's assets. KRS section 275.335 does not provide that the suit is after filing under control of the members who on the LLC's behalf initiated it, and it does not provide that any member not "eligible to vote thereon" is after initiation barred from participating in any company actions involving the suit. Specifically, KRS section 275.335(1) does not say that Gulliver may not, as the majority-in-interest member of Lilliput LLC, direct the LLC's legal counsel to drop the suit.[105] This is not to say that Gulliver has free reign to do exactly that. Rather, such an action may violate his obligation to avoid self-dealing and may even constitute waste of the LLC's property. A court sitting in equity[106] could find that Gulliver may not so act, but in so doing the court will not be relying upon the words of KRS section 275.335. Alternatively, a court could (and likely should) determine that after the suit is brought KRS section 275.175 controls and that it is not for the court to write protections not provided for in the LLC Act or the operating agreement.

As revised, the statute is significantly simplified. First, an individual member may, on behalf of LLC, initiate a legal action in its name when authorized to do so by more than one half (per capita) of the members entitled to vote with respect to whether that action should be brought. As previously, this right of the members to bring on the LLCs behalf a lawsuit exist irrespective of whether the LLC is member-managed or manager-managed.[107] A member will be disqualified from participation in this vote if they have an interest in the outcome that is adverse to the

103. *See id.* § 275.003(3).
104. *See id.* § 275.003(1).
105. *See also* Ky. S. Ct. R. 1.13.
106. *See* KY. REV. STAT. ANN. § 275.003(1) (West 2015).
107. *Id.* § 275.335(2).

interest of the LLC.[108] Any member vote to bring action must be in a record signed or otherwise approved by the members giving the authorization.[109] The statute now references the articles of organization (the prior statute referred to the operating agreement) to determine whether management is vested in the managers.[110] The prior provision introduced an unfortunate substantive analysis, this in contrast to the normal positive review of an LLC being either member-managed or manager-managed as provided in the election made in the articles of organization. By changing the reference from the operating agreement to the articles of organization, it is intended that this determination likewise be a positive one made based upon the provision of the articles of organization. Legal action may be brought by any manager authorized by more than one half of the number of managers authorized to vote on the action.[111] The same rule as to the capacity to vote of a member is applied as well to the managers, namely not having an interest adverse to that of the LLC.[112] Also, consistent with the rules as to member action, the action of the managers must be in a record form signed or otherwise approved the necessary threshold of the managers.[113]

There are at least three particularly curious implications of this provision. First, it is important to recognize that this is the only provision in the LLC Act in which the members vote on a per capita, rather than a per contributed capital, basis.[114] Second, clumsy drafting within the operating agreement can easily add confusion to this point.[115] For example, a provision in the operating agreement providing "except as may be required by the LLC Act, all decisions will be made by a majority of the members" could be interpreted as overriding both (i) the per capita voting provision, it here being assumed that "majority" refers to the members voting on the basis of contributed capital, or some rule other than per capita, and (ii) the provision excluding from participation in that vote those members having an interest adverse to the LLC. In effect, such a provision could be read to preclude a majority of the minority members from, on the LLCs behalf, bringing action to challenge the majority member's self-interested transactions with the LLC and to recover the benefits derived therefrom.[116] Of course, in such a

108. *Id.* § 275.335(3).
109. *See id.* § 275.335(4).
110. *See id.* § 275.335(2).
111. *See id.* § 275.335(1).
112. KY. REV. STAT. ANN. § 275.335 (West 2015).
113. *See id.* § 275.335(4).
114. *See id.* § 275.175.
115. *Id.*
116. *See also id.* § 275.170(2).

circumstance, a derivative action may be brought. Third, it needs to be recognized that this provision has and continues to address only the authority to initiate legal action.[117]

As clarified in the amendments, the prosecution of an action brought on behalf of the company remains a matter of company management to be governed by the terms of the operating agreement.[118] Unless there is a vote sufficient to amend the operating agreement, authority to prosecute the action is vested as determined by the members; whether or not the suit should be continued is not governed by KRS section 275.335. Again, careful drafting of the operating agreement is necessary in order to avoid this admittedly surprising result. For example, returning to a suit initiated by a majority of the minority members to, on the LLC's behalf, seek recovery from the majority member for the benefits of self-interested transactions with the company, even if the majority member cannot vote with respect to its initiation because he or she has an interest adverse to the LLC, that same majority member could conceivably determine that the suit should be dismissed.[119]

B. Default Rule of No Compensation

A provision added to the LLC Act makes express that a member of an LLC, in rendering services to the LLC, is not entitled to compensation for having done so.[120] Subject to modification in a written operating

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117. *See id.* § 275.335.

118. KY. REV. STAT. ANN. § 275.335 (West 2015).

119. *See, e.g.*, *Kastern v. MOA Investments, LLC*, 731 N.W.2d 383 (Wisc. App. 2007). Therein, after suit was brought on behalf of an LLC charging the majority with having diverted company assets and other misfeasance, they amended the operating agreement to in effect cause the suit's dismissal. Specifically:

> On June 1, 2005, approximately four months after Marie commenced this action, a consent resolution was adopted amending DD's operating agreement to permit members with a financial interest in the outcome of pending actions to vote to dismiss such actions, to require members asserting or maintaining a derivative action without approval of a supermajority to indemnify DD for all costs and attorney fees incurred in the action, and to impose a one year limitation on claims asserted by a member against the company or other members. Under the amendment, the supermajority voted to dismiss Marie's lawsuit and hired counsel to pursue dismissal.

120. *See* KY. REV. STAT. ANN. § 275.165(4). A default rule of no compensation avoids disputes over "I'm entitled to" absent agreement to the contrary. *See also* CanCan Development, LLC v. Manno, No. 6429–VCL, 2015 WL 3400789, at *16–17 (Del. Ch. May 27, 2015) (holding that manager's compensation, not set forth in operating agreement but unilaterally set by manager, is subject to entire fairness test); *accord* Calma v. Templeton, 114 A.3d 563, 577, 589 (Del. Ch. 2015) (noting that director fees are subject to the entire fairness test). These citations to Delaware law

agreement, this rule carries forward the rule that a partner is not, absent a contrary agreement, entitled to compensation for services performed on behalf of the partnership[121] and is consistent with the rule that a member qua member is not an "employee" of the LLC.[122]

C. Judicial Supervision of Dissolution

The LLC Act has been amended to provide for judicial supervision of the winding up even where the dissolution itself is not judicial in nature.[123] This provision will have application where, for example, the

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on entire fairness are not meant to imply that in the context of a Kentucky LLC the taking of unauthorized compensation would be subject to the entire fairness test. *See* KY. REV. STAT. ANN. § 275.170(3) (West 2015).

121. *See* KY. REV. STAT. ANN. § 362.235(6); *id.* § 362.1-401(8)*; see also* UNIF. P'SHIP ACT § 401(h) 6 (pt. I) U.L.A. 133 (2001); UNIF. P'SHIP ACT § 18(f) 6 (pt. II) U.L.A. 101 (2001). This no compensation rule is a basis, in the context of partnerships, of the Unfinished Business Doctrine. *See, e.g.*, Jewel v. Boxer, 156 Cal. App. 3d 171, 203 Cal. Rptr. (Cal. Ct. App. 1984); Laford v. Sweeney, 343 P.3d 939 (Colo. 2015). *But see In re* Thelen, 20 N.E. 3d 264 (N.Y. 2014). *See also* Thomas E. Rutledge & Tara A. McGuire, *Conflicting Views as to the Unfinished Business Doctrine*, 46 TEX. J. BUS. L. 1 (2015).

122. Assuming that the LLC member is treated as a partner for tax purposes, he or she cannot be treated as an employee of the LLC. *See* Rev. Rul. 69-184, 1969-1 C.B. 256; I.R.S. Gen. Couns. Mem. 34,001 (Dec. 23, 1969); I.R.S. Gen. Couns. Mem. 34,173 (July 25, 1969); *see also* Borkowski v. Commonwealth, 139 S.W.3d 531, 533–34 (Ky. Ct. App. 2004) (member of LLC is not an "employee" for purposes of unemployment insurance benefits); KY. REV. STAT. ANN. § 342.012 (absent special endorsement, member of LLC not covered by workers compensation insurance); Bowers v. Ophthalmology Group, LLP, No. 5:12–CV–00034–JHM, 2012 WL 3637529, at *6 (W.D. Ky. Aug. 22, 2012), *vacated on other grounds*, 733 F.3d 647 (6th Cir. 2013) ("One's status does not change from partner to employee simply because the partner is out-numbered and finds herself in a minority position among the other partners . . . Bowers was a partner in Ophthalmology Group, not an employee."); RESTATEMENT (THIRD) OF EMPLOYMENT LAW § 1.03 (2015) ("Unless otherwise provided by law, an individual is not an employee of an enterprise if the individual through an ownership interest controls all or part of the enterprise."); 54 Alan J. Tarr, PARTNER STATUS, USC LAW SCHOOL 54TH INSTITUTE ON MAJOR TAX PLANNING ¶ 606.1(c) (2012) ("A partner rendering services in his capacity as a partner is not an employee of the partnership. This mutual exclusivity characterization is made clear in various provisions, especially in the context of employment taxes."); *Paying Yourself*, IRS (May 31, 2013), http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Paying-Yourself ("Partners are not employees and should not be issued a Form W-2 in lieu of Form 1065, Schedule K-1, for distributions or guaranteed payments from the partnership."); Self-Employment Tax Treatment of Partners in a Partnership That Owns a Disregarded Entity, *available at* https://www.federalregister.gov/articles/2016/05/04/2016-10383/self-employment-tax-treatment-of-partners-in-a-partnership-that-owns-a-disregarded-entity. The same rule would apply if the LLC were classified for tax purposes as a disregarded entity; the sole member cannot be that sole member's employee. *See also* Ky. Emp'rs Mut. Ins. v. Ellington, 459 S.W.3d 876, 882-83 (Ky. 2015) (sole proprietor is not an employee of the sole proprietorship). Assuming the LLC is taxed as a partnership, agreed compensatory payments to a member will be treated as guaranteed payments under Code § 708. *See also Model LLC Operating Agreement Organizational Checklist*, 69 BUS. LAW. 1251, 1264–65 (2014).

123. KY. REV. STAT. ANN. § 275.290(5) (West 2015).

company has dissolved in accordance with its operating agreement or otherwise, but the members either failed to proceed with the winding up and liquidation process or are unable to agree as to how it should be accomplished. This provision is consistent with the law governing business corporations[124] and the LLC Acts of many other states.[125]

D. Clarity as to Reservation of Voting Rights to the Members

Distributed throughout the LLC Act are default rules for voting, addressing both the topics upon which a vote of the members is required and the voting threshold for action, namely:

Default Voting Thresholds Under the Kentucky LLC Act		
Action	**Default Threshold**	**KRS**
Approve Sale of Substantially All Assets	Majority-in-Interest of the Members	§ 275.247
Approve Conversion to LP	All of the Members	§ 275.372(2)
Initial Adoption of Operating Agreement	All of the Members	§ 275.015(20)[126]
Amend Operating Agreement	Majority-in-Interest of the Members	§ 275.175(2)(a)
Admit Assignee as Member	Majority-in-Interest of the Members other than the assignor	§ 275.265(1)
Remove a Member as a Member after Assignment of All Interest in the LLC	Majority-in-Interest of the Members other than the assignor	§ 275.280(1)(c)2
Admit New Member	All of the Members	§ 275.275(1)
Waive Agreement to Contribute	All of the Members	§ 275.200(4)
Approve Voluntary Dissolution	All of the Members	§ 275.285(3)

124. *See id.* § 271B.14-300(4); *see also id.* § 272A.12-060(3); *id.* § 386A.8-050(2).

125. *See, e.g.*, MINN. STAT. ANN. § 322B.83 (West 2015); TENN. CODE ANN. § 48-245-801 (West 2012).

126. *But see* KY. REV. STAT. ANN. § 275.365(11) (West 2015) (allowing majority-in-interest of the members approving a merger to adopt the operating agreement of the successor LLC, it being binding upon all members in the successor-by-merger LLC); Thomas E. Rutledge, *The 2010 Amendments to Kentucky's Business Entity Laws*, 38 N. KY. L. REV. 383, 397–99 (2011).

Default Voting Thresholds Under the Kentucky LLC Act		
Action	**Default Threshold**	**KRS**
Approve Merger	Majority-in-Interest of the Members	§ 275.350(1)
Amend Articles of Organization	Majority-in-Interest of the Members	§§ 275.030(2), 275.175(1)
Approve Act in Contravention of Written Operating Agreement	Majority-in-Interest of the Members	§ 275.175(2)
Amend Articles of Organization to Change Management Structure	Majority-in-Interest of the Members	§ 275.175(2)(c)
Appointment of Managers[127]	Majority-in-Interest of the Members	§ 275.165(2)(a)
Bring Suit in Name of LLC	Half by number of the disinterested members	§ 275.335
Waive Duty of Loyalty	Majority-in-Interest of the disinterested members	§ 275.170(2)
Permit Voluntary Resignation of a Member from a Manager-Managed LLC Where That Right Is Not Already Set Forth in a Written Operating Agreement	All of the Members	§ 275.280(3)

The members, as a default rule that may be modified by private ordering, retain the right to vote on these matters even if the LLC is manager-managed.[128] The LLC Act has been, however, not nearly as clear on this point as would be desired. It is provided that where the company elects in its articles of organization to be manager-managed, "the manager or managers shall have the exclusive power to manage the business and affairs of the [LLC]," with this delegation authority being subject to the "extent otherwise provided in the articles of organization, the operating agreement, or this chapter."[129] It would have been helpful if the statutory language were more express to the effect that the mere fact that the company is manager-managed does not, of itself, constitute

127. Only if the LLC is manager-managed.
128. KY. REV. STAT. ANN. § 275.175 (West 2015).
129. *Id.*

an election out of the requirement that the members act upon these particular matters. An amendment to the LLC Act now makes clear that as to the enumerated actions, and absent contrary private ordering, although the LLC is manager-managed, they require member approval.[130] Still, care needs to be exercised to avoid inadvertent contrary private ordering. The statement in the operating agreement "Except as otherwise required by the Act, all decisions as to the business and affairs of the Company shall be made by the Managers . . ." could be interpreted as being sufficient to abrogate the right of the members to vote on the items listed in KRS section 275.175(2).[131]

E. Nonprofit LLCs

The balance of the provisions dealing with limited liability companies relate to nonprofit LLCs.[132] When the LLC Act was originally enacted, it was not anticipated that the LLC would be used for nonprofit purpose. However, in Mercy Regional Emergency Medical System, LLC v. John Y. Brown, III, the Franklin Circuit Court held that an LLC need not have a business purpose in order to be validly organized in Kentucky.[133] In response thereto, skeletal revisions were made to the LLC Act in 2007 to, inter alia, impose limitations on self-inurement, etc. in nonprofit LLCs, tracking the law of nonprofit corporations.[134] These revisions were driven by the view that typically the nonprofit LLC creates significant opportunities for abuse. However, in the summer of 2012, the Internal Revenue Service issued important guidance on the use of limited liability companies as subsidiaries of section 501(c)(3) and similar tax-exempt organizations.[135]

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130. *See id.* §§ 275.175(3)(d)–(j).

131. The author does not suggest this is the proper interpretation of what is likely simply a poorly drafted provision. *See also* Lenticular Europe, LLC v. Cunnally, 693 N.W.2d 302, 308 (Wis. Ct. App. 2005) ("When the legislature provides a specific default term on a topic and the operating agreement does not explicitly refer to that topic, it is reasonable to conclude the parties did not intend to override that default term.").

132. With respect to nonprofit LLCs generally, *see, e.g.*, Richard A. McCray & Ward L. Thomas, *Limited Liability Companies as Exempt Organization Update*, IRS, http://www.irs.gov/pub/irs-tege/eotopicb01.pdf (last visited Jan. 1, 2016); David S. Walker, *A Consideration of an LLC for a 501(c)(3) Nonprofit Organization*, 38 WILLIAM MITCHELL L. REV. 627 (2012); *see also generally* Cassady V. "Cass" Brewer, *Nonprofit and charitable uses of LLCs*, in RESEARCH HANDBOOK ON PARTNERSHIPS, LLCS AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS (Robert W. Hillman & Mark J. Loewenstein eds., 2015).

133. Cir. Action No. 98-CI-01357 (Franklin Cir. Ct. Feb. 16, 1999).

134. *See also* Rutledge, *supra* note 27, at 250.

135. I.R.S. Notice 2012-52, 2012-35 I.R.B. 317. Pursuant to this direction, donations made to a single member LLC wholly owned by a 501(c)(3) organization are for purposes of deductibility to be treated as having been made to the to the tax-exempt parent corporation.

Under the revised statute, a nonprofit LLC may be organized either without members or with members, but if it has members, they themselves must be organized for nonprofit purposes.[136] Nonprofit LLCs are exempt from the definitional requirement that an LLC must have at least one member.[137] For that reason, nonprofit LLCs are exempt from the rule that an LLC must dissolve when it lacks a member.[138]

While the typical rule of non-inurement applies in a nonprofit LLC, that rule does not apply if the members are themselves nonprofit organizations.[139] Regardless of the nature of the members, the income and profit of the nonprofit LLC may not be distributed to managers,[140] but reasonable compensation may be paid to members and managers for services rendered.[141]

If the only members of the nonprofit LLC are themselves nonprofit organizations, the otherwise applicable prohibition against member loans is inapplicable.[142] Still, irrespective of the character of the members, a nonprofit LLC may not make loans to the managers.[143] Because in a nonprofit LLC without members the management structure will be almost entirely a matter of private ordering, those matters must be set forth in a written operating agreement.[144] This requirement of a written operating agreement is a limitation on the general rule that an operating agreement, in addition to being written, may be oral or arise out of a course of conduct.[145]

A provision added to the LLC Act will permit a nonprofit corporation to convert into a nonprofit LLC.[146] The limitation upon this provision is that the only permitted member of the converted nonprofit LLC must be a section 501(c)(3) or 501(c)(4) organization; an affirmative statement to that effect is required in the articles of organization filed to effect the conversion.[147] This conversion mechanism is available for all nonprofit corporations organized in Kentucky.[148] It is also available to foreign

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136. *See* KY. REV. STAT. ANN § 275.520 (West 2015), *amended by* 2015 Ky. Acts, ch. 34, § 48. Previously a nonprofit LLC was precluded from having members.

137. *See id.* § 275.015(12), *amended by* 2015 Ky. Acts, ch. 34, § 45; *see also id.* § 275.015(19), *amended by* 2015 Ky. Acts, ch. 34, § 45.

138. *See id.* § 275.285(7).

139. *Id.* § 275.520.

140. *Id.*

141. *See id.*; *accord id.* § 273.237.

142. KY. REV. STAT. ANN § 275.525 (West 2015).

143. *Id.*; *accord id.* § 273.241.

144. *See id.* § 275.175(4).

145. *See id.* § 275.015(21).

146. *See id.* § 275.376(13).

147. *Id.*

148. KY. REV. STAT. ANN § 275.376(13) (West 2015).

nonprofit corporations unless the law of the jurisdiction of incorporation forbids a conversion as contemplated by this provision.[149]

The statute is of course silent as to the federal and state taxation of any donation or contribution to a nonprofit LLC. As is the case with the nonprofit corporation, the ability to deduct contributions is a distinct issue addressed under federal tax law; mere organization as a nonprofit organization does not of itself give rise to the ability to deduct contributions. The 2016 Kentucky General Assembly exempted these non-profit LLCs from the sales and use tax.[150]

IX. AMENDMENTS TO THE NONPROFIT CORPORATION ACTS

While constituting significantly less than the desperately needed complete rewrite of the Kentucky Nonprofit Corporation Acts,[151] a series of amendments to the existing law addressed some of the Acts' logistical limitations.

Initially, a comprehensive definition of what constitutes "notice" has been added to the act, defining how notice is to be provided to either a director or a member.[152] Based upon the current provision from the Kentucky Business Corporation Act,[153] this provision importantly provides "notice by electronic transmission is written notice." The provision adopted a mailbox rule as to communications to members.[154] Any notice to a domestic nonprofit corporation or to a foreign nonprofit corporation authorized to transact business in Kentucky may be addressed to the organization's registered agent at its registered office, to the corporation, or its secretary at the principal office address.[155] In furtherance thereof, new defined terms have been added for "deliver/delivery," "effective date of notice," "electronic transmission/electronically transmitted," "notice," "sign" and "signature."[156]

The provision addressing notice of a special meeting of the members has been revised to delete references to how the notice is to be given.[157] Those issues are now addressed in the new notice provision.[158]

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149. *Id.*

150. *See* KY. REV. STAT. ANN. § 139.495 as amended by 2016 Ky. Acts, ch. 110, § 13.

151. *Id.* §§ 273.161–.390.

152. *Id.* § 273.162.

153. *See id.* § 271B.1-410.

154. *See id.* § 273.162(3).

155. KY. REV. STAT. ANN § 273.162(4) (West 2015); *accord id.* § 271B.1-410(4); *see also id.* § 14A.4-040(1).

156. *See id.* § 273.161(17)–(21).

157. *See id.* § 273.197.

158. *See id.* § 273.162.

With respect to meetings by unanimous consent, previously the statute provided, in one section, mechanisms by which both the Board of Directors and the members could act by unanimous consent.[159] Adopting the model employed in the Business Corporation Act, written consent of the Board of Directors and members are now separately discussed.[160] Under a new section, patterned off of the equivalent provision of the Business Corporation Act,[161] the directors may act by written consent, provided that, absent specification of the different date, the action is effective when the last director signs the consent.[162] It is further provided that action by written consent has the effect of a meeting vote.[163] Note that while the written consent must be signed by each director, pursuant to the new definition of "sign," which includes an electronic signature,[164] a unanimous consent may be executed by email.[165] In parallel to the adoption of a new provision uniquely addressing board action by unanimous consent, the existing KRS section 273.377 has been revised in order to restrict its application to written consent of the members.[166] This provision has also been supplemented in order to track the equivalent language from the Business Corporation Act, specifically KRS section 271B.7-210. Again, as the signature of each member is required, it may now be delivered electronically.[167] It should be noted that this provision, with respect to unanimous consent, applies to any "regular or special meeting" of the Board of Directors; it does not by its terms expressly extend to any meeting of a board committee.[168]

Language newly added to KRS section 273.217 will allow directors to participate in any regular or special meeting by "any means of communication by which all directors participating my simultaneously

159. *See id.* § 271B.8-210 (1989) (amended 2015).

160. *See id.*

161. KY. REV. STAT. ANN § 273.375. (West 2015).

162. *Id.* § 271B.8-210.

163. *See id.* § 273.375; *accord id.* § 271B.8-210(3) ("A consent signed under this section shall have the effect of a meeting vote and may be described as such in any document.").

164. *See id.* § 273.161(21).

165. This express rule is cumulative to the prior law to the same effect. *See id.* § 369.102(8) (defining an "electronic signature" as "an electronic sound, symbol, or process attached to or logically associated with a record and executed or adopted by a person with the intent to sign the record."); *id.* § 369.107(4) ("If a law requires a signature, an electronic signature satisfies the law.").

166. *See id.* § 273.377.

167. The Business Corporation Act allows the articles of incorporation to reduce the threshold for a "unanimous" consent to a threshold as low as 80%. *See* KY. REV. STAT. ANN. § 271B.7-040(2) (West 2015). No similar capacity is provided for in the Nonprofit Corporation Acts.

168. *See id.* § 273.377; *see also id.* § 273.221 (addressing the composition and functioning of board committees).

hear each other during the meeting."[169] A member so participating is deemed present at the meeting.[170]

Simply confirming the law as it is always existed even while not set forth in the statute, it has been made express that a director may not vote by proxy.[171]

Previously, the statute did not set forth a minimum notice as to the meeting of the Board of Directors.[172] A new provision, consistent with the Kentucky Business Corporation Act,[173] sets that minimum notice at two days.[174] A longer or shorter minimum notice may be provided for in the bylaws. Language already in the statute providing, inter alia, that the notice of a regular or special board meeting need not describe the business to be transacted, has been re-codified as KRS section 273.223(2). Likewise, already existing language to the effect that attendance at a meeting constitutes a waiver of any defect with respect to the notice absent an objection on that basis has been re-codified as KRS section 273.223(3). Lastly, existing language with respect to the calling of a special meeting of the Board of Directors by court order[175] has been re-codified as subsection (4) of KRS section 273.223.

The provisions dealing with the voluntary dissolution of a nonprofit corporation have been modified to conform with the procedure under the Business Corporation Act. Under the prior law, articles of dissolution

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169. *See id.* § 273.217(2); *accord id.* § 271B.8-200(2) (creating statutory authority for a board member participating in a meeting by phone or other means of electronic communications.).

170. *Id.* § 273.217(2).

171. *See id.* § 273.217(4); *see also* Haldeman v. Haldeman, 197 S.W. 376, 381 (Ky. 1917) ("Neither can they [directors] vote by proxy."); Ky. Att'y Gen. Op. 74-645 (Aug. 29, 1934) (proxy may not be given by directors of nonprofit corporations); ABA CORPORATE DIRECTOR'S GUIDEBOOK 18 (6th ed. 2011) ("A director is expected to commit the required time to prepare for, attend regularly and participate (in person when feasible) in board and committee meetings. A director may not participate or vote by proxy; personal participation is required (which may take place by telephone or video when in-person participation is not possible.)"); MODEL BUS. CORP. ACT § 8.20, § 25 cmt. at 206 (AM. BAR. ASS'N 2002); 2 WILLIAM MEADE FLETCHER, FLETCHER'S CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 427 (perm ed., rev. vol. 2014) ("The directors of a corporation generally cannot vote at directors' meeting by proxy, but must be personally present and act themselves . . . . Their personal judgment is necessary, and they cannot delegate their duties or assign their powers.") (citations omitted); 3 WILLIAM W. COOK, A TREATISE ON THE LAW OF CORPORATIONS HAVING A CAPITAL STOCK 2257 (Chicago, Callaghan & Co. 1908) ("Directors, of course, cannot act or vote by proxy.") (citation omitted); ARTHUR W. MACHEN, JR., A TREATISE ON THE MODERN LAW OF CORPORATIONS § 1455 (Boston, Little, Brown & Co. 1908) ("Directors cannot vote by proxy.") (citations omitted); *id.* § 1458 ("At a Directors' meeting, votes by proxy cannot be received or counted, and the Directors have no power by resolution to alter this rule.") (citations omitted).

172. *See* KY. REV. STAT. ANN. § 273.223 (1968) (amended 2010 & 2015).

173. *See id.* § 271B.8-220(2).

174. *See id.* § 273.223(1).

175. *See* Rutledge, *supra* note 126, at 417.

were filed on behalf of a nonprofit corporation only after the dissolution had been completed, including at the time when "all debts, obligations and liabilities of the corporation have been paid and discharged or that adequate provision has been made therefor."[176] Conforming the procedures to those employed in the Business Corporation Act,[177] after dissolution is authorized, articles of dissolution shall be filed with Secretary of State along with a copy of the plan of distribution pursuant to which of the corporation's assets will be distributed or conveyed.[178] The corporation's dissolution will be effective upon the filing of the articles of dissolution.[179] The Secretary of State is directed to forward a copy of the articles of dissolution to the Secretary of Revenue.[180] Thereafter, consistent with the equivalent provision of the Business Corporation Act,[181] the existence of the corporation continues after the filing of the articles of dissolution, but the corporation's purpose of the business is limited to winding up and liquidating its business.[182] To that end, it is specifically provided that the dissolution of the corporation does not "abate or suspend" the rule of limited liability otherwise enjoyed.[183]

Consistent with the Business Corporation Act, the Board of Directors is empowered to hold meetings of the members, whether special or regular, exclusively by means of remote communication.[184]

As previously noted, it is now possible to convert a nonprofit corporation into a nonprofit LLC.[185]

Proposed additions to the Nonprofit Corporation Acts which would have put in place robust and comprehensive rights to indemnification and advancement for the directors and officers of a nonprofit corporation, based upon the language employed in the Kentucky Business Corporation Act,[186] were deleted at the request of the Kentucky Nonprofit Network.[187]

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176. *See* KY. REV. STAT. ANN. § 273.313(4) (1988) (amended 2015).

177. *See id.* § 271B.14-030; *accord id.* § 272A.12-110; *id.* § 275.315; *id.* § 362.1-805; *id.* § 386A.8-020.

178. *Id.* § 273.313.

179. *See id.* § 273.313(3); *see also id.* § 14A.2-070.

180. *See id.* § 273.313(2).

181. *See id.* § 271B.14-050.

182. KY. REV. STAT. ANN § 273.302 (West 2015); *accord id.* § 275.300(2); *id.* § 362.2-803(1); *id.* § 272A.12-060(1); *id.* § 386A.8-040.

183. *See id.* § 273.302.

184. *See id.* § 273.195.

185. *See id.* § 275.376.

186. *See id.* §§ 271B.8-500–580.

187. *Compare* H.B. 440 as submitted on February 12, sections 76 through 84, *with* House Judiciary Committee Sub (Feb. 26, 2015) (previous sections 76-84 deleted); *see also* KY. REV. STAT. ANN. §§ 271B.8-500–8-580 (West 2015).

X. UNINCORPORATED NONPROFIT ASSOCIATIONS ACT

The adoption in Kentucky of the Revised Uniform Unincorporated Nonprofit Association Act[188] is important in that, with this new statute, there is the for the first time in Kentucky an analytic paradigm and body of default law[189] by which such organizations may be assessed. Prior to this enactment, Kentucky has lacked such a body of law even as unincorporated nonprofit associations have been organized and operated.[190] Further, for the first time it will be possible for an unincorporated nonprofit association organized in Kentucky to effect for its participants the benefits of limited liability.

The Kentucky Uniform Unincorporated Nonprofit Association Act (hereinafter "KyNPAA")[191] is largely a default statute, setting forth rules as to particular matters that are applicable absent contrary agreement with respect to the topic. In light of their expected informality there are minimal requirements that the agreement be reduced to a writing.

An important defined term used in the law of unincorporated nonprofit associations is the "governing principles."[192] Roughly equivalent to a partnership's partnership agreement or a LLC's operating agreement,[193] and including the "established practices,"[194] the governing principles are the agreements of the members[195] as to the purpose and operation of the association. The governing principles may be oral, written, or arise from a course of conduct.[196] The managers[197] are bound by the governing principles.

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188. REV. UNIF. UNINC. NONPROFIT ASS'N ACT, 6B U.L.A (Supp. 2014) 177. It is important to note that the Kentucky adoption is of the 2008 version of the uniform act and is not of the "harmonized" act last edited in 2014.

189. REV. UNIF. UNINC. NONPROFIT ASS'N ACT Prefatory Note, 6B U.L.A. (Supp. 2014) 178 ("A UNA is, thus, a default organization.").

190. Partnership law has not been the default as a partnership must have a for-profit purpose. *See* KY. REV. STAT. ANN. § 362.175(1) (West 2015); *id.* § 362.1-201(1); *see also* THOMAS E. RUTLEDGE & ALLAN W. VESTAL, ON KENTUCKY PARTNERSHIPS AND LIMITED PARTNERSHIPS 49–50 (Univ. of Ky., Office of Continuing Legal Educ. ed., 2010).

191. *See* KY. REV. STAT. ANN. § 273A.165 (West 2015).

192. *See id.* § 273A.005(3)*; accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2(2), 6B U.L.A. 180 (Supp. 2014).

193. *See* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2, cmt. 2; *see also* KY. REV. STAT. ANN. §§ 362.1-101(11), 275.015(20) (West 2015).

194. *See* KY. REV. STAT. ANN. § 273A.005(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2(1); *see also id.* § 2 cmt. 1 ("'Established practices' are essentially equivalent to the commercial law concepts of course of performance and course of dealing.").

195. KY. REV. STAT. ANN. § 273A.005(3) (West 2015); *see also* KY. REV. STAT. ANN. § 275.065(1)(c) (West 2015)*; accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 16(a)(3), 6B U.L.A. 197 (Supp. 2014).

196. KY. REV. STAT. ANN. § 273A.005(3) (West 2015).

A. Formation, Purpose & Powers

An unincorporated nonprofit association is a default structure; it exists if its definition is by a particular venture met;[198] there is no requirement of an intent to form an unincorporated nonprofit association. In fact, there is not even a requirement that the participants in the venture be aware of the possibility of consciously forming an unincorporated nonprofit association.[199]

An unincorporated nonprofit association is considered to be an entity distinct from its members and managers[200] and enjoys perpetual duration[201] while being vested with all powers of an individual necessary or convenient to carrying out its purpose.[202] While limited for-profit activities are permitted, the proceeds thereof must be applied to the non-profit purpose.[203]

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197. *See* KY. REV. STAT. ANN. §§ 273A.005(3)–(4) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2(2)–(3).

198. *See* KY. REV. STAT. ANN. § 273A.005(11) (West 2015) (defining unincorporated non-profit association); *see also id.* § 273A.1-010(6) (defining non-profit purpose). This latter definition is non-uniform, and is based upon KRS § 273.167. Note that existing organizations, if they fall within the definition of an unincorporated nonprofit association, will be governed by this act. *See id.* § 273A.155(1); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 4(a); *see also id.* § 4(a) cmt. 1 ("This act applies to pre-existing UNAs formed in the enacting state, as well as to all UNAs formed in the state after the effective date of the Act."). With respect to the statutory treatment of an unincorporated nonprofit association as a "entity," this positive statement of organizational law controls over the statement set forth in *Customer Due Diligence Requirements for Financial Institutions*, RIN 1506-AB25 at 58, where it was stated that "This is because neither a sole proprietorship nor an unincorporated association is an entity with legal existence separate from the associated individual or individuals that in effect create a shield permitting an individual to obscures his or her identity." (Citation omitted). Simply put, the statement made by the Financial Crimes Enforcement Network of the Department of Treasury is incorrect as to the law of unincorporated nonprofit associations.

199. *See* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2, cmt. 8.

200. *See* KY. REV. STAT. ANN. § 273A.010(1) (West 2015); *accord* UNIF. UNINC. NONPROFIT ASS'N ACT § 5(a), 6B U.L.A. 186 (Supp. 2014). Still, the act does not define the consequences of "entity" characterization. *See also* Thomas E. Rutledge, *External Entities and Internal Aggregates: A Deconstructionist Conundrum*, 43 SUFFOLK U.L. REV. 655 (2009); J. William Callison, *Indeterminacy, Irony and Partnership Law*, 2 STAN. AGORA 73, 73-76 (2001), http://agora.stanford.edu/agora/libArticles2/agora2v1.pdf; David Millon, *The Ambiguous Significance of Corporate Personhood*, 2 STAN. AGORA 3, 39-58 (2001), http://agora.stanford.edu/agora/libArticles2/agora2v1.pdf.

201. *See* KY. REV. STAT. ANN. § 273A.010(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 5(b), 6B U.L.A. 186 (Supp. 2014).

202. *See* KY. REV. STAT. ANN. § 273A.010(3) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 5(c), 6B U.L.A. 186 (Supp. 2014).

203. *See* KY. REV. STAT. ANN. § 273A.010(4) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 5(d), 6B U.L.A. 186 (Supp. 2014).

B. Name Requirements, Annual Report

The name requirements for a Kentucky Unincorporated Nonprofit Association ("KyUNPA") are set forth in the Kentucky Business Entity Filing Act (KRS. ch. 14A) and are dependent in part upon whether the KyUNPA has filed a certificate of association.[204] Regardless of whether a certificate is filed, a KyUNPA may not include in its name any of "incorporated," "corporation," "Inc.," "Corp.," "company," "partnership" or "cooperative." If a certificate of association is filed, the name of the KyUNPA must include either "Limited" or "Ltd."[205] Further, that real name as set forth on the certificate of association must be distinguishable from any name of record with the Secretary of State.[206] If the KyUNPA has not filed a certificate of association it should not include "Limited" or "Ltd." in its name as doing so would be misleading. Absent filing a certificate of association the name distinguishability standard is not applicable.

The assumed name statute has been revised to define the real name of a KyUNPA and to allow a KyUNPA to file an assumed name.[207] A KyUNPA, subject to distinctions based upon whether or not a particular KyUNPA has or has not filed a certificate of association, is subject to the assumed name statute.[208]

The application of the rules governing annual reports to KyUNPAs is dependent upon whether or not the particular KyUNPA has filed a certificate of association. If no certificate of association is filed, then there is no annual report required.[209] Conversely, if a certificate of association has been filed, an annual report is required.[210]

C. Liability for Association Debts & Obligations; Limited Liability

The members and other participants in an unincorporated nonprofit association are, as a default, each liable for its debts and obligations.[211]

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204. *See also* KY. REV. STAT. ANN. § 273A.030 (West 2015).

205. *See id.* § 14A.3-010(16).

206. *See id.* § 14A.3-010(1); *see also id.* § 14A.1-070(20) (defining "name of record with the Secretary of State").

207. *See id.* § 365.015.

208. *See* KY. REV. STAT. ANN. § 365.015 (West 2015).

209. *See id.* § 14A.6-010(7)(d).

210. *See id.* § 14A.6-010(6).

211. The mere fact of "entity" characterization of an unincorporated nonprofit association does not compel that the members thereof enjoy limited liability. For example, while a partnership may be treated as an entity, the partners are jointly and severally liable for the partnership's debts and obligations absent election of limited liability partnership status. *See id.* § 362.1-201; *id.* § 362.1-306(1); *id.* § 362.1-306(3). Consequently, there is at best limited utility in defining a particular form of business organization as being an "entity"; the term itself has no

While the Uniform Act, by fiat, reversed the rule and afforded limited liability ab initio, this policy has not been carried forward in Kentucky. Rather, under Kentucky law, limited liability is available if and only if the association makes a filing with the Secretary of State.[212] The rationale for this treatment is the protection of third-party creditors. In every instance under Kentucky law, limited liability is conditional upon a state filing. That filing, whether denominated articles of incorporation, articles of organization, certificate of limited partnership, statement of registration, or otherwise,[213] puts third parties on notice that there exists a business organization with whom they are or may be doing business,[214] and that they as creditors may (absent a guarantee or other credit enhancement) look only to the assets of the business for satisfaction of their claims.[215] The grant of limited liability to the participants in the venture is only from the time of filing with the Secretary of State.[216]

Affording the participants in an unincorporated nonprofit association limited liability from its debts and obligations absent a public filing would do violence to the symmetry existing in all of the other business entity statutes. Further, the model employed in the Uniform Act is an invitation to abuse. Persons could contract and then assert they did so on behalf of a subsequently conceived unincorporated nonprofit association. While a variety of laws could be utilized by a creditor to impose personal liability upon the direct actors,[217] there is no policy basis for requiring a creditor,

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intrinsic meaning in that there is no defined set of consequences that necessarily follow from that label. *See also supra* note 200.

212. KY. REV STAT. ANN. § 273A.030(1) (West 2015).

213. *See id.* § 271B.2-020 (West 2015) (articles of incorporation); *id.* § 272A.3-010 (articles of association); *id.* § 273.247 (articles of incorporation); *id.* § 275.025 (articles of organization); *id.* § 362.555 (statement of registration); *id.* § 362.1-931 (statement of qualification); *id.* § 362.2-201 (certificate of limited partnership); *id.* § 386A.2-010 (certificate of trust).

214. *See, e.g.*, *id.* § 275.025(7); *id.* § 386A.2-010(6)(a).

215. In parallel, while a partnership may come into existence without a state filing, partners enjoy limited liability if and only if a filing is made with the state on the public record. *See, e.g.*, *id.* § 362.555; *id.* § 362.1-931.

216. *See, e.g.*, *id.* § 14A.2-070(1); *id.* § 271B.2-030; *id.* § 271B.2-040; *id.* § 272A.3-010(2); *id.* § 275.025(7); *id.* § 275.095; *id.* §§ 386A.2-010(1), (6).

217. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY §§ 6.01–6.03 (2006). In *Perry v. Ernest R. Hamilton Associates*, Inc., 485 S.W.2d 505 (Ky. 1972), an individual retained an engineering firm to lay out a proposed subdivision, but did not disclose that proposed subdivision was owned by a corporation. When that engineering firm sued to collect on the fees, and the individual cited the existence of the corporation as a defense to personal liability, the court held the individual was personally liable for the fees as he had failed to disclose the existence of the corporation or to put the engineering firm on notice that it was dealing with a corporation. *See also* Water, Waste & Land, Inc. v. Lanham, 955 P.2d 997 (Colo. 1998); Hopkins Advertising and Public Relations, Inc. v. Morris, No. 541071, 1997 WL 306653, at *1, 2 (Conn. Super. May 29, 1997) (where individual signed agreement without noting that he did so as agent for an LLC and did not disdose the existence of

who has acted in good faith and in reliance upon the public record, to incur the costs of demonstrating the application of those laws. Kentucky long ago abandoned the notion that nonprofit organizations are in some manner shielded from liability for the consequences of their actions.[218] In the same vein, those who act on behalf of a nonprofit organization are liable for the consequences of their individual actions. Those acting on behalf of an unincorporated nonprofit association are responsible for the debts they create, or permit to be created, unless creditors are put on notice of an election of limited liability.

The filing by which limited liability is elected is a "certificate of association."[219] The certificate of association must set forth:

- the name of the association;
- its mailing address;
- its registered office and agent; and
- its purpose.[220]

The filing fee for a certificate of association is $15.00.[221]

In accordance with the law governing other forms of business organizations, the grant of limited liability effected by the filing of a certificate of association will not protect an individual from liability for their own negligence, wrongful acts, or misconduct.[222]

In the absence of the filing of certificate of association consequent to which the members enjoy limited liability in any suit brought against the association, the judgment rendered thereon will not be binding upon a member ab initio unless that member was named as a party. There are, however, a series of provisions pursuant to which, in the absence of certificate of association, the members may, consequent to their

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the LLC principal, he took on personal liability on that obligation); Hosale v. Warren, No. 01A01-9810-CV-00523, 1999 WL 548538 (Tenn. Ct. App. July 29, 1999); Baumstein v. Myklebust, No. 01-0614, 2001 WL 869506 (Wis. Ct. App. Aug. 2, 2001).

218. *See, e.g.*, Mulliken v. Jewish Hosp. Ass'n of Louisville, 348 S.W.2d 930 (Ky. 1961)*; see also* Gillum v. Good Samaritan Hosp., 348 S.W.2d 924 (Ky. 1961). *Contra* Emery v. Jewish Hosp. Ass'n, 236 S.W. 577 (Ky. 1921).

219. *See* KY. REV. STAT. ANN. § 273A.030(1) (West 2015).

220. *See id.* § 273A.025. The name of the association is subject to KRS § 4A.3-010, and the registered office/agent are subject to KRS § 14A.4-010. The effective time and date of the certificate will be determined under KRS § 14A.2-070. Changes in registered office/agent will be made as provided in KRS § 14A.2-040, and the principal office address may be changed as provided in KRS § 14A.5-010.

221. *See id.* § 14A.2-060(1)(p).

222. *See id.* § 273A.030(2); *accord id.* § 271B.6-220(2); *id.* § 272A.5-030(3); *id.* § 275.150(3); *id.* § 362.1-306(4); *id.* § 362.2-303(2); *id.* § 362.2-404(4); *id.* § 386A.3-040(6).

personal liability for the debts and obligations of the association, be required to satisfy that judgment.[223]

D. Suits By or Against an UNPA

A UNPA may sue or be sued in its own name.[224] A suit against a UNPA in which a statement of association has been filed, and thereby a registered agent designated, may be initiated by service on the registered agent.[225] Where no registered agent has been designated, service may be completed as otherwise provided by law.[226] The capacity to sue or be sued in its own name is a common characteristic of business organizations.[227] This capacity extends to suits by a member or manager against the UNPA, or a UNPA suit against a member or manager.[228] If a UNPA has filed a certificate of association and thereby has elected limited liability for its members and other constituents,[229] a member or manager is not a proper party to the action simply by reason of their status as a member or manager.[230] This provision is not uniform and has no equivalent in the Uniform Unincorporated Nonprofit Association Act.[231]

Even where the UNPA has not filed a statement of association, and thereby elected limited liability, a judgment against the association is not enforceable against a member or manager thereof unless and until

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223. *See id.* § 273A.040(2). This provision is not uniform. It is important to recognize that subsection (2) of KRS § 273A.040 does not create an exception to the rule of limited liability available to the members of an unincorporated nonprofit association from the filing of the certificate of association. Where a certificate of association is in place, the members, qua members, are not liable for the debts and obligations of the association. Subsection (2) of KRS § 273A.040, addressing when a judgment creditor of an association may levy against the assets of the member, is inapplicable if the members enjoy limited liability. Rather, this provision applies if and only if no certificate of association is in place, providing, *inter alia*, that the assets of the association must first be exhausted before the assets of any individual member may be attached in satisfaction of the judgment unless one of the explicated exceptions applies.

224. *See id.* § 273A.035(1); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 9(a), 6B U.L.A. 191 (Supp. 2014). This capacity extends beyond traditional suits in court to administrative and alternative dispute resolution such as arbitration. *See id.*, cmt. 2.

225. *See* KY. REV. STAT. ANN. § 273A.045 (West 2015); *see also id.* §§ 273A.030(1)(c), 14A.4-040(1); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 11, 6B U.L.A. 193 (Supp. 2014).

226. *See* KY. REV. STAT. ANN. § 273A.045 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 11, 6B U.L.A. 193 (Supp. 2014) 193*; see also* KY. R. CIV. P. 4.04.

227. *See, e.g.*, KY. REV. STAT. ANN. § 271B.3-020(1)(a) (West 2015); *id.* § 272A.1-060(1); *id.* § 275.330; *id.* § 362.605; *id.* § 362.1-307(1); *id.* § 386A.3-060(1).

228. *See* KY. REV. STAT. ANN. § 273A.035(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 9(b), 6B U.L.A. 192 (Supp. 2014).

229. *See* KY. REV. STAT. ANN. § 273A.025 (West 2015).

230. *See id.* § 273A.035(3); *accord id.* § 275.155.

231. *See also id.* § 275.155.

certain conditions have been satisfied.[232] A creditor may include as parties to the action some or all of the members or managers and conceivably be awarded a judgment against them coincident with the receipt of a judgment against the association. In that instance the judgment against the member or manager may be immediately enforced and need not wait upon a determination that the association is unable to satisfy the judgment. A change in the membership or management of a UNPA will not abate a pending action by or against it.[233]

If the UNPA has filed a certificate of association, the proper venue for an action against an association is the county in which its principal place of business is maintained or, if the principal place of business is not in Kentucky, the county in which its registered office is located.[234] Where the UNPA has not filed a certificate of association, the rules applicable to general partnerships are adopted to determine proper venue.[235]

E. Members

Every UNPA must have two or more members; a single-member UNPA does not satisfy the statutory definition and is not governed by this Act.[236]

A member of a UNPA is not by reason of that status an agent of the association.[237] Except as may be otherwise provided in the governing principles,[238] members vote on a per-capita basis[239] with a majority vote controlling.[240] Unless delegated in the governing principles to the managers, there is expressly reserved to the members the right to vote

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232. *See id.* § 273A.040 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 10, 6B U.L.A. 193 (Supp. 2014).

233. *See* KY. REV. STAT. ANN. § 273A.050 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 12, 6B U.L.A. 195 (Supp.2014).

234. *See* KY. REV. STAT. ANN. § 273A.055(1) (West 2015). The provision is not uniform.

235. *See id.* § 273A.055(2). This provision is similar to, but departs from, the Uniform Act. *See* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 13, 6B U.L.A. 195 (Supp. 2014).

236. *See* KY. REV. STAT. ANN. § 273A.005(11) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2(8), 6B U.L.A. 181 (Supp. 2014).

237. *See* KY. REV. STAT. ANN. § 273A.060 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 15, 6B U.L.A. 196 (Supp. 2014). *Contra* KY. REV. STAT. ANN. § 362.1-301(1) (West 2015) (each partner, qua a partner, is an agent of the partnership in connection with its ordinary business); *see also* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 15, cmt. 1, 6B U.L.A. 196 (Supp. 2014).

238. *See also* KY. REV. STAT. ANN. § 273A.005(3) (West 2015) (defining of "governing principles").

239. *See id.* § 273A.070(1)(b); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 16(a)(2), 6B U.L.A. 197 (Supp. 2014).

240. *See* KY. REV. STAT. ANN. § 273A.070(1)(a) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 16(a)(1), 6B U.L.A. 197 (Supp. 2014).

on certain matters.[241] There are left to the governing principles rules as to notice of, quorum for, and other procedural rules for member meetings.[242] While a member is not, consequent to that status, in a fiduciary relationship with either the UNPA or any other member thereof,[243] each member is bound by an obligation of good faith and fair dealing.[244]

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241. *See* KY. REV. STAT. ANN. § 273A.070(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 16(a), 6B U.L.A. 197 (Supp. 2014).

242. *Compare* KY. REV. STAT. ANN. § 273A.070(3) (West 2015) (this language is not uniform), *with* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 16(b)–(c), 6B U.L.A. 197 (Supp. 2014).

243. *See* KY. REV. STAT. ANN. § 273A.075(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT §17(a), 6B U.L.A. 197 (Supp. 2014). Statements that a particular participant in a venture does not, consequent to their position, stand in a fiduciary relationship, have precedence in other Kentucky law. *See*, *e.g.*, KY. REV. STAT. ANN. § 275.170(4) (West 2015) (members in a manager-managed LLC do not owe fiduciary obligations); *id.* § 362.2-305(1) (limited partners, as limited partners, do not owe fiduciary duties.) Of course, the absence of fiduciary duties is not dependent upon an affirmative-statutory statement to that effect. *See* Griffin v. Jones, No. 5:12-CV-00163-TBR, 2016 WL 109287 (W.D. Ky. March 21, 2016) (holding that shareholders in a Kentucky corporation do not stand in a fiduciary relationship with one another); *see also* Thomas E. Rutledge, *Shareholders Are Not Fiduciaries – A Positive and Normative Analysis of Kentucky Law*, 51 LOU. L. REV. 535 (2012–13).

244. *See* KY. REV. STAT. ANN. § 273A.075(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 17(b), 6B U.L.A. 198 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 275.003(7) (West 2015) (obligation of good faith and fair dealing in LLC); *id.* § 362.1-404(4) (obligation of good faith and fair dealing in general partnership); *id.* § 362.2-408(4) (obligation of good faith and fair dealing in limited partnership). In Kentucky, every contract incorporates and imposes upon the parties thereto an obligation of good faith and fair dealing. *See* Farmers Bank and Trust Co. of Georgetown; Kentucky v. Willmott Hardwoods, Inc., 171 S.W.3d 4, 11 (Ky. 2005) ("Within every contract there is an implied covenant of good faith and fair dealing, and contracts impose on the parties thereto a duty to do everything necessary to carry them out."). The implied covenant of the good faith and fair dealing obligates a party to a contract to do "everything necessary" to carry out the contract. *In re* Tolliver, 464 B.R. 720, 742-43 (Bankr. E.D. Ky. 2012) (citing Harvest Homebuilders LLC v. Commonwealth Bank and Trust Co., 310 S.W.2d 218, 220 (Ky. App. 2012); Ranier v. Mount Sterling Nat'l Bank, 812 S.W.2d 154, 156 (Ky. 1991)); Ram Eng'g & Constr., Inc. v. Univ. of Louisville, 127 S.W.3d 579, 585 (Ky. 2003). Oden Realty Co. v. Dyer, 45 S.W.2d 838, 840 (Ky. 1932) (noting that there is as well a negative burden to not act to "prevent [] the creation of the condition under which payment would be due . . . ."); Crestwood Farm Bloodstock v. Everest Stables, Inc., 751 F.3d 434 (6th Cir. 2014); James T. Scatuorchio Racing Stable, LLC v. Walmac Stud Management, LLC, No. 5: 11–374–DCR, 2014 WL 2113096, at *8 (E.D. Ky. May 20, 2014). The implied covenant informs the interpretation of the agreed upon terms of the contract; it does not provide extra-contractual terms. *See, e.g.*, Winshall v. Viacom Int'l, 55 A.3d 629 (Del. Ch. 2011).

The covenant of good faith and fair dealing will not preclude a party from exercising their contractual rights. *See, e.g.*, Scheib v. Commonwealth Anesthesia, P.S.C., No. 2010–CA–000781–MR, 2011 WL 5008089, at *5 (Ky. Ct. App. Oct. 21, 2011); *Willmott Hardwoods*, 171 S.W.3d at 11; *see also* United Propane Gas, Inc. v. Federated Mut. Ins. Co., Nos. 2005-CA-001101-MR, 2005-CA-001111-MR, 2007 WL 779443, at *3 (Ky. Ct. App. Mar. 16, 2007) ("Since Federated had a right to settle under the contract and therefore was merely exercising a contractual right, and UPG has otherwise cited us to no specific policy provision alleged to have been breached, we affirm the

A person becomes a member in a UNPA in accordance with its governing principles or, in the absence of governing principles as to admission of members, by a vote of a majority of the incumbent members.[245] On those same terms, a member may be suspended, dismissed, or expelled from the association.[246] Resignation, suspension, dismissal, or termination of a member will not relieve that person of unsatisfied obligations to the association.[247] A member may resign at any time unless the governing principles impose limitations upon the right to resign.[248] Unless a contrary rule is set forth in the governing principles, a member's interest in the association is not transferrable.[249]

F. Management

Every UNPA is required to be managed by "managers"[250] who have the authority to make all decisions on the association's behalf except those reserved to the members.[251] Managers are selected by a majority

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circuit court's award of summary judgment on the breach of contract claim."); Hunt Enters. v. John Deere Indus. Equip. Co., 18 F. Supp. 2d 697, 700 (W.D. Ky. 1997) (stating that the covenant of good faith and fair dealing, "does not preclude a party from enforcing the terms of the contract . . . It is not 'inequitable' or a breach of good faith and fair dealing in a commercial setting for one party to act according to the express terms of a contract for which it bargained"). Another important point is that the implied covenant does not serve to preclude self-dealing conduct, but rather only police it at the margins by protecting the express contractual terms. *See, e.g.*, Scatuorchio Racing Stable, LLC v. Walmac Stud Management, LLC, 2014 WL 2113096, *9 (E.D. Ky. 2014) ("As to allegations that "constitute self dealing," a party may act in its own interest and not breach the covenant of good faith and fair dealing, as long as its discretion is not used in a way that is contrary to the spirit of the agreement.").

245. *See* KY. REV. STAT. ANN. § 273A.080(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 19(1), 6B U.L.A. 199 (Supp. 2014). *Contra* KY. REV. STAT. ANN. § 362.235(7) (West 2015) (in the absence of a different rule in the partnership agreement, admission of a new partner requires the unanimous consent of all incumbent partners); *id.* § 362.1-401(9) (same); *see also id.* § 273A.070 (members vote per capita with a simple majority controlling); *id.* § 273A.065(1)(a).

246. *See* KY. REV. STAT. ANN. § 273A.080(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 18, 6B U.L.A. 199 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 273A.65(1)(a) (West 2015).

247. *See* KY. REV. STAT. ANN. § 273A.080(2) (West 2015); *id.* § 273.085(2); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 18, 6B U.L.A. 199 (Supp. 2014).

248. *See* KY. REV. STAT. ANN. § 273A.085(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 19, 6B U.L.A. 199 (Supp. 2014).

249. *See* KY. REV. STAT. ANN. § 273A.090 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 20, 6B U.L.A. 200 (Supp. 2014).

250. *See* KY. REV. STAT. ANN. § 273A.095(5) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 22(5), 6B U.L.A. 202 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 273A.005(4) (West 2015) (defining "manager."); *accord* REV. UNIF. NONPROFIT ASS'N ACT § 2(3), 6B U.L.A. 180 (Supp. 2014).

251. REV. UNIF. NONPROFIT ASS'N ACT § 2(3), 6B U.L.A. 180 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 273A.065 (West 2015).

of the members,[252] and there is no requirement that a manager be a member.[253] If the members do not elect or otherwise designate managers, then every member is as well a manager.[254] Each manager has an equal vote, and the managers act by a majority.[255] There exists no requirement as to a minimum number of managers beyond one.[256] Each of these rules may be altered in the governing principles.[257]

Managers owe to the association fiduciary duties of care and loyalty.[258] The statutory formula for the duties of care and loyalty owed to the association by the managers thereof is unique as contrasted to other formulas employed in Kentucky's business entity statute. For that reason it is crucial that the focus be upon the words employed; loose analogy to the laws of other organizations is not proper.[259]

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252. KY. REV. STAT. ANN. § 273A.095(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 22(1), 6B U.L.A. 202 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 273A.070(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 16(a)(2), 6B U.L.A. 197 (Supp. 2014).

253. KY. REV. STAT. ANN. § 273A.095(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 22(2), 6B U.L.A. 202 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 271B.8-020 (West 2015) (director of corporation not required to be a shareholder therein); *id.* § 275.165(2)(b) (manager of LLC not required to be a member therein). *Contra id.* § 272A.8-030(1) (director of unincorporated cooperative association must be a member therein).

254. *See* KY. REV. STAT. ANN. § 273A.095(3) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 22(3), 6B U.L.A. 252 (Supp. 2014).

255. *See* KY. REV. STAT. ANN. §§ 273A.095(4)–(6) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT §§ 22(4), (6), 6B U.L.A. 202 (Supp. 2014).

256. *Contra* KY. REV. STAT. ANN. § 273.211(1) (West 2015) (nonprofit corporation required to have not fewer than three directors).

257. *See id.* § 273A.095 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 22, 6B U.L.A. 202 (Supp. 2014).

258. *See* KY. REV. STAT. ANN. § 273A.100 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 23(a), 6B U.L.A. 203 (Supp. 2014) (stating expressly that the duties are owed to the association; it is clear that they are not owed to the members either individually or collectively); *see also* 1400 Willow Council of Co-Owners, Inc. v. Ballard, 430 S.W.3d 229 (Ky. 2013); Baptist Physicians Lexington, Inc. v. New Lexington Clinic, P.S.C., 436 S.W.3d 189, note 4 (Ky. 3025); BSA Mull, LLC v. Garfield Investment Company, Nos. 310989, 311911, 315359, 315544, 2014 WL 4854306, *6 (Mich. Ct. App. Sept. 30, 2014) ("The LLCA's requirement that a manager discharge duties 'in the best interest of the [LLC],' MCL 450.4404(1), indicates that a manager's fiduciary duties are owed to the company, and not the individual members."); *accord* Sires v. Linden Shores Ass'n, No. X04HHDCV146054149S, 2015 WL 3798173 (Conn. Super. Ct. May 27, 2015) ("A condominium association owes a duty of care and loyalty [to] all unit holders collectively but owes no fiduciary duty directly to any individual unit holder . . . .").

259. *See also* Pannell v. Shannon, 425 S.W.3d 58, 67-68 (Ky. 2014). In *Pannell*, the court stated:

> [The] common law of business entities has largely been abrogated by the adoption of the various statutes like the Kentucky Business Corporation Act and the Kentucky Limited Liability Company Act. In fact, "limited liability companies are creatures of statute controlled by Kentucky Revised Statues

The fiduciary duty standard, which is not identified as being subject to modification in the governing principles, obligates each manager to manage in good faith, in a manner the manager honestly believes to be in the best interest of the association, and on an informal basis.[260] Reliance upon the opinions and information provided by others is conditionally appropriate.[261] A related-party transaction (which would otherwise violate the duty of loyalty) may be approved or ratified after full disclosure by a majority of the disinterested members.[262] The governing principles may limit the exposure of a manager to liability for breach of the fiduciary standards, provided that failure does not fall within certain prescribed conduct.[263]

Pursuant to a non-uniform provision, rules as to notice, quorum, and other procedural requirements for manager meetings shall be set by the governing principles.[264]

> (KRS) Chapter 275," not primarily by the common law. To the extent that common law doctrines could arguably govern limited liability companies, the Kentucky Limited Liability Company Act is in derogation of common law, KRS 275.003(1), and the traditional rule of statutory construction that require[s] strict construction of statutes which are in derogation of common law shall not apply to its provisions. Thus, to the extent the statutes conflict with common law, the common law is displaced.
>
> This Court must therefore first look at the controlling statutory law.

Id. (citations omitted).

260. KY. REV. STAT. ANN. § 273A.100(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 23(b), 6B U.L.A. 203 (Supp. 2014).

261. KY. REV. STAT. ANN. § 273A.100(2) (West 2015). In 1988, the General Assembly passed a "Good Samaritan" statute preduded personal liability of uncompensated directors for the consequences of actions: (i) undertaken in good faith; (ii) within the scope of official functions and duties; and (iii) not caused by willful or wanton misconduct. *Id.* § 411.200. Presumably this statute could be applied to the managers of an unincorporated nonprofit association. The differential between the standards of this statute and the substantive requirements of the law governing directors of a nonprofit corporation and the managers of an unincorporated nonprofit association is potentially troubling. The issue was resolved in 1991 by an opinion of the Attorney General finding that KRS section 411.200 is unconstitutional in that it violates Sections 14 and 54, and potentially violates Section 241, of the Kentucky Constitution. *See* Ky. Att'y Gen. Op. 91-89, 1991 WL 533922 (June 3, 1991).

262. *See* KY. REV. STAT. ANN. § 273A.100(3) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 23(c), 6B U.L.A. 203 (Supp. 2014). Note that a "fair to the association" defense to a related party transaction is not provided for. *Accord* KY. REV. STAT. ANN. § 275.170(3) (West 2015); *id.* § 362.1-404(5); *id.* § 362.2-408(5); *id.* § 386A.5-070(3); *see also id.* § 386B.10-030(1). *Contra id.* § 271B.8-310(1)(c).

263. *See* KY. REV. STAT. ANN. § 273A.100(5) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 22(e), 6B U.L.A. (Supp. 2014) 203. Any such limitation must be in a record.

264. *See* KY. REV. STAT. ANN. § 273A.105 (West 2015). *Contra* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 24, 6B U.L.A. 204 (Supp. 2014) The partnership, limited partnership and LLC acts likewise leave to private ordering questions of notice, quorum and other procedural issues.

G. Inspection of Books and Records

Members in their capacity as members and managers in their capacity as managers have the right to inspect association books and records.[265] The right of inspection is collared by the requirement of a proper purpose, and a limitation to information "material to the member's or Manager's rights and duties under the governing principles."[266] The Kentucky act is not uniform as to the right of the association to limit access to and use of association information.[267] Essentially, where the uniform act would defer to the association to unilaterally impose limitations on access to and use of information, the Kentucky Act looks to the governing principles for such limitations, and unless set forth in written governing principles assented to by the member or manager seeking inspection, the association bears the burden of showing the reasonableness thereof.[268] While former members and managers are afforded inspection rights, it is difficult to imagine how they satisfy the requirement that the books and records sought be "material to the member's or manager's rights and duties under the governing principles."[269]

H. Property; Statement of Authority

A UNPA may hold in its name real, personal, and intangible property.[270] With respect to real property, the UNPA may file a "statement of authority" by which there is made a public record of the capacity of a person to on its behalf affect a transfer of the real property.[271] Note that in the Kentucky enactment, the definition of the "statement of authority" set forth as subsection (1) of section 7 of the

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265. *See* KY. REV. STAT. ANN. § 273A.110(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 25, 6B U.L.A. 204 (Supp. 2014). It bears noting that there is no requirement that any particular records be maintained by the association. Ergo, the right of inspection applies to what records have been maintained. *See also* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 25, cmt., 6B U.L.A. 205 (Supp. 2014).

266. KY. REV. STAT. ANN. § 273A.110(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 25, 6B U.L.A. 204 (Supp. 2014).

267. *Compare* KY. REV. STAT. ANN. § 273A.110(3) (West 2015), *with* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 25(b), 6B U.L.A. 205 (Supp. 2014).

268. This non-uniform language was adopted from the Kentucky LLC Act. *See* KY. REV. STAT. ANN. § 275.185(5) (West 2015).

269. *See id.* § 273A.110(4).

270. *Id.* § 273A.015(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 6(1), 6B U.L.A. 187 (Supp. 2014).

271. *See* KY. REV. STAT. ANN. § 273A.020 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 7, 6B U.L.A. 187 (Supp. 2014).

uniform act has been moved to the table of defined terms.[272] The statement of authority has precedent in partnership law.[273] Filed with the title records of the county clerk where the transfer would be recorded, a statement of authority is conclusive as to the authority of the person executing the transfer on the association's behalf as to a grantee without notice of a limitation on the authority who gives value.[274] A statement of authority has a maximum term of five years.[275] Note that there is no requirement of a statement of authority to transfer real property held in the name of a UNPA. Rather, it is an optional mechanism by which to avoid questions as to the capacity of the person signing on behalf of the UNPA. A grantee with those concerns, or a title insurer seeking to avoid those questions, may insist that a statement of authority be filed on record prior to the property transfer.

I. Finance

An unincorporated nonprofit association may not pay dividends or make other distributions to its members, except to a limited degree upon dissolution.[276] Still, without violating the limits against dividends/distributions, an unincorporated nonprofit association may pay reasonable compensation,[277] reimburse expenses,[278] confer benefits on its members consistent with its nonprofit purpose,[279] repay a capital contribution, or repurchase a membership if doing so is authorized by the governing principle.[280] In the event of an improper distribution, a member may bring a derivative action.[281]

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272. *See* KY. REV. STAT. ANN. § 273A.005(10) (West 2015).

273. *See id.* § 362.1-303 (West 2015); *see also* RUTLEDGE & VESTAL, *supra* note 190, at 59–61.

274. *See* KY. REV. STAT. ANN. § 273A.020(7) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 7(h), 6B U.L.A. 187 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 362.1-303(4)(b) (West 2015).

275. *See* KY. REV. STAT. ANN. § 273A.020(6) (West 2015); *accord* REV. UNIF. UNIF. UNINC. NONPROFIT ASS'N ACT § 7(g), 6B U.L.A. 187 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 362.1-303(7) (West 2015).

276. *See* KY. REV. STAT. ANN. § 273A.115(1) (West 2015); *id.* § 273A.130(4)(b); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(a), 6B U.L.A. 207 (Supp. 2014); *id.* § 29(4)(B).

277. *See* KY. REV. STAT. ANN. § 273A.115(2)(a) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(b)(1), 6B U.L.A. 206 (Supp. 2014).

278. *See* KY. REV. STAT. ANN. §§ 273A.115(2)(a), 120(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(b)(1), 6B U.L.A. 206 (Supp. 2014); *id.* § 27(1).

279. *See* KY. REV. STAT. ANN. § 273A.115(2)(b) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(b)(2), 6B U.L.A. 206 (Supp. 2014).

280. *See* KY. REV. STAT. ANN. § 273A.115(2)(c) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(b)(3), 6B U.L.A. 206 (Supp. 2014).

281. *See* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26 cmt. 3, 6B U.L.A. 206 (Supp. 2014); *see also* Rutledge, *supra* note 67.

It should be recognized that the Unincorporated Nonprofit Association Act twice addresses reimbursement of expenses. It does so, however, using two different formulas; whether this differential is intentional is open to question. In the initial provision, the association has a permissive ("may") capacity to "reimburse reasonable expenses to a member or manager for services rendered."[282] The second provision, which is set forth as a mandatory "shall" (subject to a contrary provision the governing principles),[283] obligates the association to "reimburse a member or manager for authorized expenses reasonably incurred in the course of the member's or manager's activities on behalf of the association."[284] The commentary provided to the act is silent as to explanation of this apparent duplication.

An unincorporated nonprofit association has the capacity, but not the obligation, to indemnify its members and managers from debts, obligations, or liabilities incurred on behalf of the association, provided that the person seeking indemnification has, in the case of a member who is not a manager, acted in good faith or, in the case of a manager, discharged their fiduciary obligations.[285] In a rare application of the statute of frauds in the statute, the right to indemnification may be broadened or limited in the governing principles provided the broadening or limitation is in record form.[286]

J. Dissolution

An unincorporated nonprofit association may be dissolved:

- as provided in the governing principles as to either time or method;[287]
- when the governing principles are silent, with the approval of a majority of the members;[288]

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282. *See* KY. REV. STAT. ANN. § 273A.115(2)(a) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(b)(1), 6B U.L.A. 206 (Supp. 2014).

283. *See also* KY. REV. STAT. ANN. §§ 446.110(20), (29) (West 2015) (defining, respectively, "may" and "shall").

284. REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 27, 6B U.L.A. 207 (Supp. 2014).

285. *See* KY. REV. STAT. ANN. § 273A.120(2) (West 2015); *id.* § 273A.075; *id.* § 273A.100; *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 27, 6B U.L.A. 207 (Supp. 2014); *id.* §§ 17, 22.

286. *See* KY. REV. STAT. ANN. § 273A.120(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 26(b), 6B U.L.A. 207 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 273A.005(8) (West 2015) (defining "record"); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 2(6), 6B U.L.A. 180 (Supp. 2014).

287. KY. REV. STAT. ANN. § 273A.125(1)(a) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 28, 6B U.L.A. 207 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 275.285(1) (West 2015).

- if the activities of the association have been discontinued for at least three years, by its current or last managers;[289]
- by court order;[290] or
- under other law.[291]

Consistent with the law governing other business organizations, an unincorporated nonprofit association continues its existence after dissolution.[292] Upon dissolution, the debts and obligations of the association are to be satisfied,[293] assets held subject to trust or requiring return to the donor are to be conveyed in accordance therewith,[294] with the remaining assets distributed to other persons with similar nonprofit purposes, to the members, or as directed by the appropriate court.[295]

It should be noted that, unlike most other business organization statutes, the KyNPAA does not afford a mechanism by which known creditors of an association may be notified of its dissolution and afforded a limited period of time in which to tender claims.[296] Likewise, the KyNPAA does not provide a notice-filing mechanism by which unknown creditors can be notified of the dissolution or the winding up and

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288. *See* KY. REV. STAT. ANN. § 273A.125(1)(b) (West 2015); *id.* § 273A.065(1)(e); *id.* § 273A.075(1); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT §§ 15, 16, 27, 6B U.L.A. 196–97, 207 (Supp. 2014).

289. *See* KY. REV. STAT. ANN. § 273A.125(1)(c) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 28(a)(3), 6B U.L.A. 207 (Supp. 2014).

290. *See* KY. REV. STAT. ANN. § 273A.125(1)(d) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 28(a)(4), 6B U.L.A. 207 (Supp. 2014). Note that the statute is silent as to the standard to be employed by the courts in determining whether or not to dissolve the association. The comment states that "it is impossible or impracticable to continue the UNA, for example because of a deadlock" as a basis of dissolution. *See* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 28, cmt. 2, 6B U.L.A. 208 (Supp. 2014). Likewise, the statute is silent as to who has standing to move for judicial dissolution. *Contra* KY. REV. STAT. ANN. § 271B.14-300 (West 2015); *id.* § 275.290(1).

291. *See* KY. REV. STAT. ANN. § 273A.125(1)(e) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 27(1)(4), 6B U.L.A. 207 (Supp. 2014).

292. *See* KY. REV. STAT. ANN. § 273A.125(2) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 27(b), 6B U.L.A. 207 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 271B.14-050(1) (West 2015); *id.* § 272A.12-060(1); *id.* § 275.300(2); *id.* § 386A.8-040(1).

293. *See* KY. REV. STAT. ANN. § 273A.130(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 28, 6B U.L.A. 208 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 271B.14-050(1) (West 2015); *id.* § 275.310(1); *id.* § 272A.12-070(1); *id.* § 362.1-807(1); *id.* § 362.2-803(2)(b); *id.* § 386A.8-040(1)(c).

294. *See* KY. REV. STAT. ANN. § 273A.130(2), (3) (Westlaw); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT §§ 29(2), (3), 6B U.L.A. 208 (Supp. 2014); *see also* KY. REV. STAT. ANN. § 273.333(3)(b) (West 2015).

295. *See* KY. REV. STAT. ANN. § 273A.130(4) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 29(4), 6B U.L.A. 209 (Supp. 2014).

296. *See, e.g.*, KY. REV. STAT. ANN. § 271B.14-060 (West 2015); *id.* § 272A.12-080; *id.* § 275.320; *id.* § 386A.8-060.

liquidation of an association.[297] As a consequence of these omissions, it will often be difficult to determine, on behalf of a nonprofit unincorporated association, that all creditor claims against the association's assets have been satisfied.[298] The absence of these provisions of the uniform act is curious in that they are standard provisions in another uniform unincorporated entity laws.[299]

K. Mergers

The uniform act provides for mergers between unincorporated nonprofit associations with other organizational forms.[300] These provisions have not been carried forward into the Kentucky enactment. As such, until such time as Kentucky adopts a comprehensive "junction box" act governing all organic transactions and entity forms, unincorporated nonprofit associations lack the capacity to enter into a merger.

L. Relationship to Other Law; Uniformity

Principles of law and equity supplement the Act.[301] It is important to recognize that an KyNPAA is its own freestanding body of law. It is not directed or otherwise indicated that the laws of partnerships, corporations (whether for-profit or not-for-profit), limited liability companies (whether for-profit or not-for-profit) or any other body of organizational law shall serve as the "gap filler" when either the agreement as to a particular venture or the unincorporated nonprofit association act are silent.[302] Rather, when the statute and the private ordering of a particular association are silent, general principles of law and equity should be referenced.[303]

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297. *See, e.g.*, *id.* § 271B.14-070; *id.* § 272A.12-090; *id.* § 275.325; *id.* § 386A.8-070.

298. Dissolution of an unincorporated nonprofit association will often be first be reflected in the public record by administrative dissolution consequent to failure to file an annual report, a fate reserved to those associations which file a certificate of association. *See* KY. REV. STAT. ANN. § 14A.7-010(1)(a) (West 2015).

299. *See, e.g.*, REV. UNIF. LTD. LIAB. CO. ACT § 703, 6B U.L.A. 502 (2008); *id.* §§ 704, 509 (2008); *see also* UNIF. LTD. COOP. ASSOC. ACT § 1208; 6A U.L.A. 286 (2008); *id.* §§ 1209, 287.

300. *See* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 30, 6B U.L.A. 210 (Supp. 2014).

301. *See* KY. REV. STAT. ANN. § 273A.150(1) (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 3(c), 6B U.L.A. 184 (Supp. 2014).

302. *See also* KY. REV. STAT. ANN. § 362.1-202(2) (West 2015) (partnership law does not govern organizations formed under another statute); *id*. § 362.175(2) (partnership law does not govern organizations formed under another statute); *id*. § 271B.1-400(4) (a corporation is subject to this act); *id*. § 275.020; *id*. § 386A.1-020(32) (a statutory trust is "formed under this chapter.").

303. *See id.* § 273A.155(1).

If another statute governs a particular form of unincorporated nonprofit association, to the extent of an inconsistency with this act, the other act will control.[304]

It is directed that the act be construed to promote uniformity among the states that have adopted the act.[305] Similar provisions appear in other of Kentucky's adoption of uniform acts.[306] It needs to be appreciated that this dictate extends only so far as the Kentucky enactment of the statute is consistent with the uniform act. Where the statutory language employed in Kentucky departs from the language employed in the uniform act,[307] uniformity is obviously not the intended result, and cases and commentary from other states are of diminished or no value as interpretive aids.

M. Tax Treatment

Expressly not considered herein are questions involving federal and state income taxation of an unincorporated nonprofit association. These issues are at a minimum challenging in that, ab initio, an unincorporated nonprofit association is not a "corporation" falling within section 501 of the Internal Revenue Code. While the Kentucky Unincorporated Nonprofit Association Act does set forth a default organizational paradigm for these often informal organizations, these tax complexities may caution against the intentional utilization of this form by persons who are not otherwise well-versed in the tax consequences of this form.

XI. PUBLIC BENEFIT CORPORATIONS

There was submitted to the 2015 General Assembly H.B. 11,[308] proposing amendments to the Kentucky Business Corporation Act which would create an elective status of a "public benefit corporation" (hereinafter "PBC"). The primary effect of PBC status would be increased flexibility in the board of directors to pursue certain goals that in and of

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304. *See id.* § 273A.150(2); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 3(a), 6B U.L.A. 184 (Supp. 2014).

305. KY. REV. STAT. ANN. § 273A.140 (West 2015); *accord* REV. UNIF. UNINC. NONPROFIT ASS'N ACT § 32, 6B U.L.A. 213 (Supp. 2014).

306. *See, e.g.*, KY. REV. STAT. ANN. § 272A.17-010 (West 2015); *id.* § 362.1-971; *id.* § 362.2-971; *id.* § 386A.10-010.

307. *See, e.g.*, *id.* § 273A.025 (requiring the filing of a certificate of association in order for the members and managers to enjoy limited liability).

308. Similar legislation was proposed to the 2014 General Assembly. *See* 2014 Ky. H.B. 66. Likewise, a proposal to provide for benefit corporations was presented to the 2016 Kentucky General Assembly. *See* 2016 Ky. H.B. 50. While this bill was passed favorably out of the House, it did not receive a hearing in the Senate.

themselves do not maximize shareholder value. This proposal, however, did not pass the 2015 General Assembly and as such PBC status is not provided for under Kentucky law. Nonetheless, a review of the proposal is a worthwhile endeavor.

If one starts with the supposition that the board of directors of a business corporation is obligated to maximize shareholder value,[309] PBC status expressly permits the board of directors, in the discharge of their fiduciary obligations, to consider the defined public benefits. What those public benefits are will be defined on a case-by-case basis of each benefit corporation in its articles of incorporation. Thereafter, actions of the board of directors in applying corporate assets to those purposes will not in and of itself constitute a breach of the directors' (supposed) obligation to maximize shareholder value.

Under existing law, there exists significant flexibility to in the articles of incorporation specify a "public benefit" and authorize the board of directors to discharge corporate assets in furtherance thereof. For example, the articles could specify a maximum amount that could be devoted to the public benefit measured in terms of a fixed amount (e.g., $100,000 per year), an amount per share, or a percentage of a measure such as net income or EBITDA. So long as that determination is sanctioned by the shareholders, and absent insolvency, distributions in accordance therewith will not violate a director's duty to act "in the best

309. Whether or not that is actually the law is open to significant debate. Proponents of this view cite the now nearly century-old decision rendered by the Michigan court in *Ford v. Dodge* and cite as well the more recent decision of the Delaware Chancery Court in the eBay litigation. *See* Ford v. Dodge, 170 N.W. 668 (Mich. 1919); eBay Inc. v. MercExchange, LLC., 547 U.S. 388 (2006)*; see also In re* Trados Inc. Shareholder Litig., 73 A.3d 17, 37 (Del. Ch. 2013) ("In terms of the standard of conduct, the duty of loyalty therefore mandates that directors maximize the value of the corporation over the long-term for the benefit of the providers of equity capital, as warranted for an entity with perpetual life in which the residual claimants have locked in their investment."); *In re* Novell, Inc. Shareholder Litig., No. 6032–VCN, 2013 WL 322560, at *7 (Del. Ch. May 1, 2013) ("There is no single path that a board must follow in order to maximize stock holder value, but directors must follow a path of reasonableness which leads toward that end.")*; see also* Leo Strine, *A Job is Not a Hobby*: *The Judicial Revival of Corporate Paternalism and Its Problematic Implications*, 41 J. CORP. L. 71 (2015). Others have put forth cogent arguments that shareholder maximization is in fact not the obligation of the board of directors. *See, e.g.*, Lynn A. Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 VA. L. BUS. REV. 163 (2008); LYNN A. STOUT, THE SHAREHOLDER VENTURE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC (2012). Under Kentucky law, a board of directors, in the discharge of its fiduciary obligations, is permitted to consider the interests of constituencies other than the shareholders. This provision is not restricted in its application to situations involving possible changes in control. *See* KY. REV. STAT. ANN. § 271B.12-210(4) (West 2015) ("or otherwise"); *see also* Rutheford B. Campbell, *Kentucky Corporate Fiduciary Duties*, 93 KY. L.J. 551, 562 (2005). As such, there is statutory authority for the proposition that the board of directors of a Kentucky corporation does not have a shareholder wealth maximization obligation.

interest of the corporation."[310] Consequently, it is open to debate whether there is under Kentucky corporate law the need for a PBC status and the resulting flexibility to avoid a wealth maximization obligation.

310. *See also* KY. REV. STAT. ANN. § 271B.8-300(1)(c) (West 2015).