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## 2014 Amendments Affecting Delaware Alternative Entities and the Contractual Statute of Limitations

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On August 1, 2014, amendments to Delaware's alternative business entity statutes,<sup>2</sup> as well as the statute of limitations applicable to Delaware contracts,<sup>3</sup> became effective. These amendments (the "2014 Amendments") represent a continuing effort by Delaware to create a flexible statutory framework for alternative business organizations and transactions involving business entities generally. This article briefly summarizes the more significant 2014 Amendments.

### Statute of Limitations for Contract Based Claims Under Delaware Law

Delaware law currently permits parties to a Delaware contract to opt into a 20-year statute of limitations for contractual claims by executing the contract "under seal." If the contract is not executed under seal, however, the statute of limitations for a breach of contract claim is generally 3 years (or 4 years in the case of contracts governed by Article 2 of the Delaware Uniform Commercial Code). An amendment to the Contractual Limitations Statute (the "Limitations Amendment") gives contracting parties the ability to extend the statute of limitations for a period of up to 20 years for claims arising out of Delaware contracts without needing to execute the contract under seal, as long as the contract involves at least \$100,000 and is in writing.<sup>4</sup> The "period" that may be specified in the written document include a specific period of time, a period of time determined by the occurrence of a particular event or an indefinite period of time (in each case, which would nonetheless be limited to 20 years).

The Limitations Amendment is an important one for business entities, including corporations and non-Delaware entities, engaged in all types of transactions. Merger agreements, acquisition and sale agreements, subscription agreements and other business contracts are

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<sup>2</sup> The Delaware Revised Uniform Partnership Act, 6 *Del. C.* § 15-101, *et seq.* ("DRUPA"), the Delaware Revised Uniform Limited Partnership Act, 6 *Del. C.* § 17-101, *et seq.* ("DRULPA"), the Delaware Limited Liability Company Act, 6 *Del. C.* § 18-101, *et seq.* ("DLLCA"), and the Delaware Statutory Trust Act, 12 *Del. C.* § 3801, *et seq.* ("DSTA" and, collectively with DRUPA, DRULPA, and DLLCA, the "Alternative Entity Statutes").

<sup>3</sup> 10 *Del. C.* § 8106 (the "Contractual Limitations Statute").

<sup>4</sup> Specifically, the Limitations Amendment provides: "[A]n action based on a written contract, agreement or undertaking involving at least \$100,000 may be brought within a period specified in such written contract, agreement or undertaking provided it is brought prior to the expiration of 20 years from the accruing of the cause of such action."

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often governed by Delaware law. In those agreements, the parties often intend, and such agreements provide, for certain contractual provisions to survive longer than Delaware's 3-year statute of limitations. For example, representations, warranties and other covenants often state that they survive indefinitely. Similarly, indemnification obligations are often intended to survive for a period longer than 3 years. Prior to the Limitations Amendment, notwithstanding the language of the contract, a claim for breach of any such representation, warranty or other covenant or for indemnification would be limited by the 3-year statute of limitations. This required courts to determine when the action giving rise to the breach or the right to indemnification arose, from which time the limitations period would begin to run. In many cases, this would be at the time of the closing of a transaction, and, therefore, there was only a 3-year window in which a party could exercise its rights, even though the parties clearly intended otherwise in the contract. Consistent with Delaware's general policy of freedom of contract, the Limitations Amendment ensures that such extensions, and the intention of the contracting parties, are enforceable, notwithstanding the failure to have executed the contract under seal.

The Limitations Amendment provides parties great flexibility in extending the statute of limitations. However, care must be taken in drafting the relevant contractual language when seeking to extend the statute of limitations. For example, it is unclear if language that simply provides for the "applicable statute of limitations period" or that certain matters "survive closing" will result in the application of anything other than the 3-year contractual statute of limitations.

With the enactment of the Limitations Amendment, the statute of limitations applicable to contracts governed by Delaware law can be made longer than in any other state. As a result, parties that might have otherwise governed their contracts by non-Delaware law should now give serious consideration to governing such contracts by Delaware law. In this regard, Delaware has a very favorable choice of law statute that, if properly complied with, ensures that the choice of Delaware law to govern a contract will be respected by a Delaware court.

### Consents with Future Effective Times

In merger and acquisition transactions, the buyer generally replaces management of the target simultaneously with the closing. As a result, the outgoing management of the target typically will not want to authorize any actions of the target to be effective at or after the closing, when such management is being replaced, and the parties prefer that the incoming management authorize such actions. In order to pre-position such authorizations prior to the closing, however, the incoming management needs to do so at a time before it is actually managing the target, although such authorizations are not intended to take effect until the closing, at which time it becomes the management of the target. For example, often acquisition transactions include a financing component, whereby the buyer will need the target entity to obtain a loan at the closing with some or all of the loan amounts to be used by the buyer to purchase the target. In such instance, the incoming management typically negotiates the loan and the related loan terms and documents with the lender, and then authorizes such matters, prior to the closing, with such authorization only to be effective at the time of the closing and when it is actually managing the entity.

Similarly, in the equity investment context, the incoming limited partners of a limited partnership or members of a limited liability company often will enter into a subscription

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agreement in connection with their investment in the entity. Such subscription agreement is entered into prior to the closing of the investment, and before the investors are actually admitted to the entity as limited partners or members, as the case may be. However, the subscription agreement can include provisions relating to matters (e.g., consents, waivers and powers of attorney) that are being given in the investor's capacity as a limited partner or member and are only intended to take effect upon the closing and their admission to the entity in such capacity.

In response to a 1999 case,<sup>5</sup> which recently resurfaced as a concern primarily in the context of mergers and acquisitions, the Alternative Entity Statutes have been amended to clarify that, unless otherwise provided in the entity's governing agreement, a person, whether or not then a partner (in the case of a general or limited partnership), a member or manager (in the case of a limited liability company), or a beneficial owner or trustee (in the case of a statutory trust) may consent in such capacity to any matter, with such consent to be effective at a future time (including a time determined upon the happening of an event), provided that such person is a general partner, limited partner, member, manager, beneficial owner, or trustee, as the case may be, upon the effectiveness of the consent at such future time.<sup>6</sup>

This amendment will enable the customary prior approvals often used in transactions, including such acquisition financing transactions and equity investments, so that a person that will become a general partner, limited partner, member, manager, beneficial owner, or trustee, as the case may be, upon the closing of the transaction may execute in advance a consent in such capacity to authorize an action or other matter and effectively "escrow" such consent until such closing, at which time it becomes effective. The amendment will also give comfort to attorneys relying on such consents in providing due authorization and execution legal opinions under Delaware law.

### Revocation of Dissolution

In certain circumstances, a limited partnership or limited liability company can unintentionally dissolve or dissolve at a time when some or all of the partners or members prefer that the entity continue without dissolution. In such circumstances, if the dissolution of the entity is not revoked, DRULPA and DLLCA mandate that such dissolved entity commence winding-up its affairs and limit its activities only to those things that are in furtherance of its winding-up.

Before the 2014 Amendments took effect, the dissolution of a limited partnership or a limited liability company (other than a judicial dissolution) could be revoked before the filing of a certificate of cancellation with the Secretary of State of the State of Delaware (the "Secretary of State") only (1) with the consent of all of the remaining partners (and/or the personal representative of the last remaining limited partner if there was no remaining general partner and/or limited partner) or all of the remaining members (or the personal representative of the last remaining member), as well as any other person whose approval was required under the governing agreement to revoke a dissolution, or (2) if the dissolution was caused by a vote of the partners or members, with the consent of all partners or members that voted for the dissolution.

<sup>5</sup> *AGR Halifax Fund, Inc. v. Fiscina*, C.A. No. 17226 (Del. Ch. Aug. 3, 1999).

<sup>6</sup> A similar amendment relating to consents by directors of Delaware corporation has been made to Section 141(f) of the Delaware General Corporation Law.

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Pursuant to the 2014 Amendments, DRULPA and DLLCA now provide for less stringent consent requirements as well as additional mechanisms for revoking a dissolution, subject to the terms of the governing agreement. DRULPA and DLLCA both now expressly state that if a governing agreement provides the manner in which a dissolution may be revoked, it may be revoked in that manner. More importantly, DRULPA and DLLCA provide that, unless a governing agreement prohibits revocation of dissolution, a dissolution (other than a judicial dissolution) can be revoked prior to the filing of a certificate of cancellation with the Secretary of State in the following situations (and in each case effective as of the occurrence of the event specified below):

1. When the dissolution is caused by the affirmative vote or written consent of the requisite number or percentage interest of partners, members, or other persons, as applicable, by that same vote or written consent (without regard to whether it comes from the identical partners or members that caused such dissolution, but still subject to obtaining the approval of any other person whose approval is required under the governing agreement to revoke a dissolution contemplated by this clause).
2. When the dissolution is caused by the occurrence of a particular event or at a time prescribed in the governing agreement, by the affirmative vote or written consent of the persons needed to amend such provision in the governing agreement (and any other person whose approval is required under the governing agreement to revoke a dissolution contemplated by this clause).
3. When the dissolution of a limited partnership is caused by an event of withdrawal of a general partner (including the last remaining general partner) or the occurrence of an event that causes the last remaining limited partner to cease to be a limited partner, by the affirmative vote or written consent of (a) all remaining general partners, if any, and (b) the limited partners (or if there is more than one class or group of limited partners, then by each class or group of limited partners) who own more than two-thirds of the then-current percentage or other interest in the profits of the limited partnership, or if there is no remaining limited partner, the personal representative of the last remaining limited partner or the assignee of all of the limited partners' partnership interests in the limited partnership (and any other person whose approval is required under the partnership agreement to revoke a dissolution contemplated by this clause). The person(s) electing to revoke a dissolution pursuant to this clause must also admit to the entity a general and/or limited partner, as the case may be.
4. When the dissolution of a limited liability company occurs because its last remaining member ceases to be a member, by the affirmative vote or written consent of the personal representative of the last remaining member or the assignee of all of the limited liability company interests in the limited liability company (and any other person whose approval is required under the limited liability company agreement to revoke a dissolution contemplated by this clause). The person(s) electing to revoke a dissolution pursuant to this clause must also admit to the entity a member.

The additional flexibility afforded by the 2014 Amendments can be illustrated by the following fairly common situations. In a single member limited liability company, the loss of that single member, including a transfer of all of its limited liability company interest without the transferee being actually "admitted" as a substituted member, is an event of dissolution of the entity. Such dissolution is typically not the intent of the parties, and often this is not discovered until years after the transfer (which may also include several intervening

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transfers). Prior to the 2014 Amendments, the dissolution of the entity could only be revoked by the personal representative of the originally transferring member. Under the 2014 Amendments, however, the ultimate assignee (and current owner) of such limited liability company interest is now permitted to revoke the dissolution even though such assignee has not been admitted as a member.

Similarly, the partnership agreement of a limited partnership fund often provides for a specific term for the fund (typically subject to certain rights of extension), at the expiration of which the fund dissolves. At times, following the expiration of the term, many or all of the partners desire for a successful fund to continue rather than commence winding-up its affairs. The 2014 Amendments enable such continuation by providing that the partners can revoke the dissolution by the same vote necessary to amend the provisions of the partnership agreement that provide for the term and the dissolution of the fund upon its expiration. It is important to note, however, that often such partnership agreements provide that no amendment can be made which adversely affects some or all of the limited partners without the consent of such limited partners, and the specific wording of such a provision can greatly impact the vote that is required to revoke the dissolution of a fund caused by the expiration of its term. In fact, Delaware case law suggests that, based on the particular language used, such a provision could potentially require as much as a 100% vote of the partners.

It is worth stressing that a governing agreement may provide other means to revoke a dissolution and that the foregoing revocation mechanisms provided by the 2014 Amendments are intended to be in addition to any such means set forth in the governing agreement, unless the governing agreement specifically provides otherwise. Consequently, to the extent that the parties do not want a dissolution of the entity that is caused as a result of particular actions or events to be revoked, the governing agreement should be carefully drafted to clearly provide that there is no right to revoke a dissolution caused by such actions or events. Otherwise, depending on the cause of dissolution, there may still be a right to revoke such dissolution under DRULPA or DLLCA, as applicable.

### Books and Records Demands Through Attorneys and Agents

DRUPA, DRULPA and DLLCA have been amended to provide that a partner of a general partnership, a limited partner of a limited partnership and a member of a limited liability company may make a books and records demand either in person or through an attorney or other agent. When an attorney or other agent makes a books and records demand, such demand must be accompanied by a power of attorney or such other writing that authorizes the attorney or other agent to act on behalf of the partner, limited partner or member, as the case may be.

### Maintenance of and Access to Records

DRULPA and DLLCA have been amended to confirm that limited partnerships and limited liability companies must maintain a current record that identifies the name and last known business, residence, or mailing address of each partner, in the case of a limited partnership, or member and manager, in the case of a limited liability company. In addition, upon written request by the communications contact of such entity (note that under current law, every Delaware limited partnership and limited liability company is already required to maintain a “communications contact” who is authorized to receive communications from its registered agent), the limited partnership or the limited liability company, as the case may be, must

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provide such communications contact the name, business address, and business telephone number of a natural person who has access to such records.

### Usury Defense Unavailable Among Beneficial Owners and Trustees

DSTA has been amended to clarify that a defense of usury does not apply to obligations of a beneficial owner or trustee of a statutory trust owed to a beneficial owner or trustee of a statutory trust when the obligations arise under the governing instrument of the statutory trust or a separate agreement in writing. This amendment is consistent with amendments previously made to the other Alternative Entity Statutes.

### Prescribing Trustee Approval Requirements in a Governing Instrument

DSTA has been amended to confirm that a statutory trust's governing instrument may designate specific trustees, a certain number of trustees, or a threshold percentage of trustees whose vote is required to approve any action on behalf of a statutory trust. If the governing instrument is silent on this matter, then, unless otherwise provided in DSTA, the vote of a majority of the trustees (or, in the event that such action requires the approval of a particular class, group, or series of trustees, then a majority of such class, group, or series) will be sufficient to approve such action.

### Use of Word "Bank" Restricted in Names of Statutory Trusts

DSTA has been amended to prohibit, with limited exceptions, the use of the word "bank," and any variation thereof, in name of a statutory trust. This amendment is consistent with amendments previously made to the other Alternative Entity Statutes.

### Survival of Rights and Interests in Merging, Consolidating, Converting, Transferring or Domesticating Statutory Trusts

DSTA has been amended to confirm that in the event of a merger, consolidation, conversion, or transfer to another jurisdiction of a statutory trust or a conversion or domestication of another entity to a statutory trust, the rights or securities of, or interests in, such statutory trust or other entity may remain outstanding. These amendments are consistent with amendments previously made to the other Alternative Entity Statutes.

### Conclusion

By clarifying existing law where clarifications were deemed beneficial and creating more flexibility where additional contractual freedoms were viewed as advantageous, the 2014 Amendments continue Delaware's leadership as the jurisdiction of choice for the formation and utilization of all types of business entities.

Please do not hesitate to contact a member of the Delaware team with any questions or if you need assistance with a Delaware entity or transaction.

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