

Illinois Limited Liability Company Act Gets Major Overhaul

Effective July 1, 2017, Illinois has substantially revised the Illinois Limited Liability Act. The Amendments contain significant changes to the Act, which was introduced in 1994. Emphasizing “freedom of contract,” the Amendments permit an Illinois LLC and its members to craft an LLC Agreement (or “operating agreement”) specifically tailored to the economic and governance arrangement that best suit their needs. The operating agreement overrides any default statutory provisions in all but a few select circumstances

The amendments to the Illinois Limited Liability Company Act continue a trend towards favoring the freedom of contract associated with this hybrid partnership-corporate entity.

The Amendments, signed into law as Public Act No. 99-627 [are a comprehensive, 112-page restatement of the Illinois LLC Act](#) that will affect the management and economic rights of Illinois LLCs, their managers, and members. The Amendments impact anyone that is involved with an existing Illinois LLC or is considering forming one.

SUMMARY OF MAJOR CHANGES

- *Redemption of Dissociating Member's Interest* - The most significant change is the elimination of the requirement from Section 35-55(a) that a member managed LLC redeem a dissociated member's interest. Section 35-60, outlining the timeline and procedure, for redeeming a dissociated member's interest, has also been deleted. With these changes, it is critical that LLC owners determine the nature and extent of any buy-sell rights that the members desire in the LLC agreement.

- *Management Provision* – Section 15-1(a) of the LLC Act received a noticeable overhaul. The Articles of Organization filed with the Illinois Secretary of State in connection with forming the LLC will no longer require the organizers to specify whether the LLC is member- or manager-managed. The Amendment provides that unless the operating agreement provides otherwise, the LLC will be member-managed. This is a significant change and a trap for the unwary. Like other parts of the Amendments, this Section elevates the importance of preparing an LLC Agreement and specifying its management structure
- *Impact of Members' Fiduciary Duties* – The new Section 15-5(c) significantly rewrites the rules governing member fiduciary duties. The default provision in Section 15-3 remains unchanged, but the amendments permit an operating agreement to “restrict or eliminate a fiduciary duty, other than the duty of care.” This restriction or elimination must be “clear and unambiguous.” The new clause will enable LLC members, if agreed upon, to act in a manner that was previously deemed “disloyal” to the LLC.
- *Access to Books and Records* – The LLC Act’s books-and-records provisions, Sections 1-40 and 10-15, received a much-needed facelift. Under the new law, a member is entitled to a wide-range of information, but the rights of access contain some limits so that the sought-after records must affect the members’ interest (either economic or management). This replaces the previous, vague regime where members were entitled, arguably, to records of any kind. The amendments also require former members (called “transferees”) to state a proper purpose for access to LLC records. And they remove a gaping hole about when an LLC had to respond to an information request. Now,

The LLC Act's statutory changes remove some much-needed ambiguity concerning members' rights to books and records. The amendments further eliminate the mandate that an LLC must purchase a dissociated member's interest.

the law requires a response within 10 days, which may simply be an identification of a later “reasonable time” within which the LLC may respond. The amendments also enable an LLC to impose other conditions on the receipt of records, including the designation of information as trade-secret material.

- *Enforcement of Operating Agreement* – Section 15-5(f) and (g) are entirely new clauses that impact contract enforcement. In particular, the statute now provides that an LLC itself may enforce terms of the operating agreement (such as a non-compete clause affecting members) even if it does not “manifest[] assent to the operating agreement.” This cures a problem when only the members in their individual capacities sign an operating agreement. Additionally, Section 15-5(g) provides that a person who becomes a member of an LLC “is deemed to assent to the operating agreement.” Though many contracts require such assent, the formality of a joinder agreement is no longer required to bind a new member to all terms that may affect his or her management and economic rights.
- *Oral Agreements* – The definition of “Operating Agreement” has been amended to include those that are “oral, in a record, implied, or in any combination thereof.” Though this change should not impact many LLCs, it will likely introduce a new layer of analysis as to the duties and obligations of LLC members who have only informal planning documents, e-mails, or conversations. Although it will always be preferable to have a written LLC Agreement, the change will enable members to rely on a pattern of practice, even if not documented, to establish their respective rights in the LLC.

The Amendments continue the trend of emphasizing the flexibility of the LLC form of entity and its associated “freedom of contract.” With this freedom however, comes the heightened importance of a properly drafted LLC agreement that contains appropriate terms reflecting the business arrangement of the LLC, its members and managers.

If you have any questions about the matters addressed in this *CCM Alert*, please contact the following CCM author or your regular CCM contact.

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