

Perfecting a General Security Interest Against a Series of a Delaware LLC



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The limited liability company has become the entity of choice for business owners of all shapes and sizes. Its characteristics and accompanying rules and regulations are well known by any modern corporate attorney. Banks and other financial institutions have been providing secured loans to limited liability companies (or otherwise secured by the assets of a limited liability company) for decades. While the particular facts and circumstances of any transaction may dictate different requirements, counsel to the lender is usually confident that it has perfected the lender's security interest in the LLC-debtor's assets by receiving an executed general security agreement from the debtor in favor of the lender and subsequently filing a properly completed UCC-1 financing statement in the appropriate filing office located in the debtor's state of formation.

These seemingly clear waters are significantly muddled, however, when counsel's due diligence process reveals that the debtor is a "Series" LLC. A Series LLC is a lesser-known variant of the limited liability company available in a growing number of jurisdictions. In Delaware, owners of a Series LLC may form a single entity (known as the "parent LLC"), providing for any number of distinct "series" under the general umbrella of the parent LLC with differing assets, membership, and management structures for each series. While a full review of the characteristics of the Series

LLC is beyond the scope of this article, one of the major benefits of this entity structure involves the cost savings associated with the streamlined formation and filing process. Only the parent LLC is required to file a certificate of formation and comply with ongoing filing requirements. Pursuant to Section 18-215 of the Delaware LLC Act, business owners may form a Series LLC by filing a certificate of formation with the Secretary of State which includes notice that the LLC has been formed as a “protected series”, including notice of the limitation on liabilities of a series as referenced in Section 18-215(b). No filings are required in connection with the formation of any of the individual series under the general umbrella of the parent LLC.

As highlighted above, lenders seeking to perfect a security interest in all non-realty assets of a debtor in the form of a traditional Delaware LLC would typically look to file a UCC-1 financing statement against the debtor with the Delaware Secretary of State. Under the UCC, a security interest in most non-realty personal property can be perfected by filing a UCC-1 financing statement in the appropriate filing office in the jurisdiction in which the debtor is located. Under the UCC, a debtor that is a “registered organization” is located in its jurisdiction of formation. A “registered organization” is defined under the UCC as “an organization formed or organized solely under the law of a single State or the United States by the filing of a public organic record” (this includes a traditional limited liability company which is formed by the filing of a certificate of formation with the Secretary of State).

Where the borrower is a series of an LLC, the question of where to file becomes more complicated. Historically, under the Delaware LLC Act, a series of an LLC was not considered a “registered organization” because no public record of the series was required to be filed in connection with the establishment of the series. In fact, prior to August 1, 2019, there was no clear mechanism for filing any public record to evidence the establishment of a series of a Delaware LLC.

Under the UCC, the proper jurisdiction for filing against a debtor-entity that is not a “registered organization” is the jurisdiction in which the debtor-entity’s principal place of business is located (or in which the entity maintains its chief executive office if there is more than one jurisdiction in which the entity maintains a place of business). Accordingly, determination of the proper filing office for an unregistered series of an LLC requires additional diligence to determine where the series’ principal place of business (or chief executive office) is located. This creates confusion and uncertainty for lenders seeking to perfect a security interest in the assets of an unregistered series as there is no easily discernable filing office to ensure perfection. The appropriate filing office depends on the representations of the borrower and is subject to change with any change in the borrower’s physical location.

Seemingly in response to this issue, the Delaware legislature amended Article 9 of the Delaware UCC (effective August 1, 2019) to clarify that the term “registered organization” also includes “a series of a registered organization if the series is an organization formed or organized under the law of a single State and the statute of the State governing the series requires that the public organic record of the series be filed with the State.” The Delaware LLC Act was also amended effective August 1, 2019 to provide for the addition of a “registered series” under Section 18-218 of the Act. A “registered series” requires the filing of a “certificate of registered series” setting forth the name of the limited liability company *and* the name of the registered series.

Following the 2019 amendments to the Act, the series described in the pre-amendment version of the Act under Section 18-215 was left in place and is now referred to as a “protected series”. A series formed as a protected series pursuant to the existing Section 18-215 (without the filing of a certificate of registered series) is not a “registered organization” under the UCC. Accordingly, perfection by filing against a protected series requires filing in the jurisdiction in which the series maintains its principal place of business.

In contrast, a series formed as a “registered series” pursuant to the new Section 18-218 (by the filing of a certificate of registered series) is a “registered organization” under the UCC, and perfection by filing can be accomplished by filing in the series’ jurisdiction of formation.

The LLC Act was also amended effective August 1, 2019, to add a new Section 18-219 which provides for the conversion of a protected series into a registered series by the simultaneous filing of (i) a Certificate of Conversion of Protected Series to Registered Series, and (ii) a Certificate of Registered Series.

When a secured transaction involves a series LLC, counsel to the lender should confirm whether the parent LLC has been properly formed as a series LLC by providing notice (by reference to Section 18-215 or 18-218) in the Certificate of Formation that the LLC has been formed as a series LLC. Lender’s counsel should also determine whether the series has been formed under Section 18-215 as a protected series or Section 18-218 as a registered series. Assuming the parent LLC was properly established, this determination should be evident by the section referenced in the parent LLC’s Certificate of Formation.

If the parent LLC was formed pursuant to Section 18-218 providing for the establishment of registered series, lender’s counsel should be sure to obtain and review a copy of the filed Certificate of Registered Series for the debtor-series to confirm the series has been properly established.

If the parent LLC was formed pursuant to Section 18-215 providing for the establishment of protected series, lender’s counsel should consider requiring conversion of the debtor-series to a registered series to avoid potential perfection issues. While perfection by filing against a protected series may be accomplished with some additional diligence to determine the debtor’s principal place of business (or chief executive office), the proper jurisdiction for perfection is subject to change with changes in the debtor’s physical location. Requiring conversion to a registered series will ensure that the lender has filed in the appropriate jurisdiction, and any changes in the debtor’s physical location will have no effect on perfection of the security interest (at least with respect to the lender’s security interest in the types of collateral which may be perfected by filing).

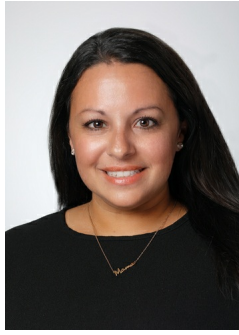
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