



Ohio Legislative Service Commission

Bill Analysis

Aida S. Montano

S.B. 181*

131st General Assembly
(As Reported by H. Judiciary)

Sens. Obhof and Schiavoni, Bacon, Eklund, Seitz, LaRose, Beagle, Brown, Burke, Coley, Hughes, Jones, Lehner, Manning, Oelslager, Patton, Sawyer, Tavares, Thomas, Yuko

BILL SUMMARY

Corporations

- Revises the list of persons considered directors or officers of a corporation.
- Prescribes the fiduciary duties of a corporate officer.
- Specifies the standard for determining whether a corporate officer will be liable for violating the officer's duties.

Limited liability companies (LLC)

- Modifies the list of actions a limited liability company (LLC) operating agreement is prohibited from doing.
- Specifies that, despite the list of prohibited actions that an operating agreement of an LLC may not perform, a written agreement, including a written operating agreement, that modifies, waives, or eliminates the duty of loyalty, the duty of care, or both for one or more members, managers, or officers must be given effect.
- Specifies that it is the policy of Ohio's LLC Law to give maximum effect to the principle of freedom of contract and to the enforceability of operating agreements.
- Modifies a member's duty of loyalty to the LLC and the other members.
- Specifies that an LLC may have, but is not required to have, officers.

* This analysis was prepared before the report of the House Judiciary Committee appeared in the House Journal. Note that the list of co-sponsors and the legislative history may be incomplete.

- Creates certain fiduciary duties of an LLC officer, unless either a written operating agreement for the LLC or a written agreement with an officer establishes additional fiduciary duties or the duties of an officer have been modified, waived, or eliminated elsewhere in the Revised Code.
- Specifies the standard for determining whether an officer of an LLC will be found liable for violating the officer's duties.
- Adds an LLC's officers to the list of persons who are not personally liable to satisfy any judgment, decree, debt, or obligation of an LLC solely by reason of the person's position.
- Specifies that the law governing LLCs applies to all LLCs formed under Chapter 1705. of the Revised Code, whether the LLC has one or more members or whether it is formed by filing articles of organization or by merger, consolidation, or conversion.

CONTENT AND OPERATION

Corporations

Officers of corporations

The bill revises the persons considered directors or officers of a corporation. Under existing law, the officers of a corporation must consist of a president, a secretary, a treasurer, and, if desired, a chairman of the board, one or more vice presidents, and such other officers and assistant officers as may be deemed necessary. The officers are elected by the directors, and the chairman of the board must be a director. Unless the articles or the regulations otherwise provide, none of the other officers need be a director.

The bill relocates the provision specifying that the chairperson must be a director and eliminates a provision specifying that the chairperson is an officer of the corporation. Under the bill, unless otherwise provided in the articles or regulations or in a resolution of the directors, the chairperson of the board is not an officer of the corporation.¹ None of the officers need to be a director unless the articles or the regulations otherwise provide or the directors determine that there is to be a chairperson of the board who is to be an officer.²

¹ R.C. 1701.56(A)(4).

² R.C. 1701.64(A).

Corporate officer's fiduciary duties

The bill provides that, unless the articles, the regulations, or a written agreement with an officer establishes additional fiduciary duties, the only fiduciary duties of an officer are the duties to the corporation set forth in the following paragraph.³

An officer must perform the officer's duties to the corporation in good faith, in a manner the officer reasonably believes to be in or not opposed to the best interests of the corporation, and with the care that an ordinarily prudent person in a like position would use under similar circumstances. In performing an officer's duties, an officer is entitled to rely on information, opinions, reports, or statements, including financial statements and other financial data, that are prepared or presented by any of the following:⁴

- One or more directors, officers, or employees of the corporation who the officer reasonably believes are reliable and competent in the matters prepared or presented;
- Counsel, public accountants, or other persons as to matters that the officer reasonably believes are within the person's professional or expert competence.

Additionally, the bill specifies that in any action brought against an officer, the officer will not be found to have violated the officer's duties as listed above unless it is proved by clear and convincing evidence that the officer has not acted in good faith, in a manner the officer reasonably believes to be in or not opposed to the best interests of the corporation, or with the care that an ordinarily prudent person in a like position would use under similar circumstances. An officer will not be considered to be acting in good faith if the officer has knowledge concerning the matter in question that would cause reliance on information, opinions, reports, or statements that are prepared or presented by any of the persons listed above to be unwarranted.⁵

Corporate officer's liability in damages

An officer will be liable in damages for a violation of the officer's duties only if it is proved by clear and convincing evidence in a court of competent jurisdiction that the officer's action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the corporation or undertaken with reckless disregard for the

³ R.C. 1701.641(A).

⁴ R.C. 1701.641(B).

⁵ R.C. 1701.641(C).



best interests of the corporation. However, this does not apply if, and only to the extent that, at the time of an officer's act or omission that is the subject of the complaint, either of the following is true:⁶

- The articles or the regulations of the corporation state by specific reference that the provisions do not apply to the corporation.
- A written agreement between the officer and the corporation states by specific reference that the provisions do not apply to the officer.

The bill specifies that nothing in the provisions described above under "**Corporate officer's fiduciary duties**," affects the duties of an officer who acts in any capacity other than the officer's capacity as an officer, nor affects any contractual obligations of an officer to the corporation.⁷

Limited liability companies (LLC)

Application of LLC law

The bill states that provisions of the Revised Code governing LLCs apply to all LLCs formed under Chapter 1705, whether the LLC has one or more members or whether it is formed by a filing under R.C. 1705.04 (filing articles of organization with the Secretary of State) or by merger, consolidation, or conversion.⁸

Operating agreements

The bill modifies the contents of an operating agreement of a limited liability company (LLC). Under existing law, an operating agreement is prohibited from doing any of a list of several specified actions. One of the prohibited actions is to eliminate the duties of a manager under R.C. 1705.29(B) (fiduciary duties a manager owes to the LLC). Under continuing law, the operating agreement may prescribe in writing the standards by which performance is to be measured or identify activities that do not violate the manager's duties. The bill modifies this prohibition to specify that *the articles or* the operating agreement may prescribe in writing the above referenced standards or identify the above described activities or may provide that a manager who is a member

⁶ R.C. 1701.641(D).

⁷ R.C. 1701.641(E).

⁸ R.C. 1705.031.



of the LLC or who is serving as the representative of a member owes to the LLC and the other members only the duties that would be owed by the member.⁹

Additionally, the bill prohibits an LLC's operating agreement from eliminating the fiduciary duties of an officer. However, the articles or the operating agreement (1) may provide that an officer who is a member of the LLC or who is serving as the representative of a member owes to the LLC and the other members only the duties that would be owed by the member or (2) may prescribe in writing the standards by which performance is to be measured or specify activities that do not violate the officer's duties.¹⁰

The bill specifies that, despite the list of actions that an operating agreement may not perform, a written agreement, including a written operating agreement, that modifies, waives, or eliminates the duty of loyalty, the duty of care, or both for one or more members, managers, or officers must be given effect.¹¹

Freedom of contract

The bill specifies that it is the policy of the LLC law, subject to the limitations of described in "**Operating agreements**," above, to give maximum effect to the principle of freedom of contract and to the enforceability of operating agreements. Except as provided in "**Operating agreements**," above, the default rules relating to the rights and obligations between and among the members, managers, and officers of an LLC in the Revised Code may be modified by the operating agreement or by the articles of organization.¹²

Member's duty of loyalty to LLC

The bill revises the duty of loyalty an LLC member owes to the LLC and to the other members. Under existing law, a member's duty of loyalty to the LLC and the other members is limited to the following:¹³

- To account to the LLC and hold as trustee for the LLC any property, profit, or benefit derived by the member in the conduct and winding up of

⁹ R.C. 1705.081(B)(6).

¹⁰ R.C. 1705.081(B)(7).

¹¹ R.C. 1705.081(C).

¹² R.C. 1705.081(D).

¹³ R.C. 1705.281(B).



the LLC's business or derived from a use by the member of the LLC's property, including the appropriation of an LLC opportunity;

- To refrain from dealing with the LLC in the conduct or winding up of the LLC's business as or on behalf of a party having an interest adverse to the LLC;
- To refrain from competing with the LLC in the conduct of the LLC's business before the dissolution of the LLC.

The bill eliminates the duty to refrain from competing with the LLC in the conduct of the LLC's business before the dissolution of the LLC. Additionally, the bill modifies the duty to refrain from dealing with the LLC in the conduct or winding up of the LLC's business as or on behalf of a party having an interest adverse to the LLC. Under the bill, the member has the existing duty as just described or the duty to satisfy the requirements of R.C. 1705.31(A)(1)(a), (b), or (c).¹⁴ That section specifies that, unless otherwise provided in the operating agreement, no contract, action, or transaction is void or voidable with respect to an LLC because it is between or affects the company and one or more of its members, managers, or officers, or because it is between or affects the company and any other person in which one or more of its members, managers, or officers are members, managers, directors, trustees, or officers or have a financial or personal interest, or because one or more interested members, managers, or officers participate in or vote at the meeting that authorizes the contract, action, or transaction, if any of the following applies:¹⁵

- The material facts as to the relationship or interest and as to the contract, action, or transaction are disclosed or are known to the members or managers, and the members or managers, in good faith reasonably justified by those facts, authorize the contract, action, or transaction by the affirmative vote of a majority of the disinterested members or managers, even though the disinterested members or managers constitute less than a quorum.
- The material facts as to the relationship or interest and as to the contract, action, or transaction are disclosed or are known to the members entitled to vote on the contract, action, or transaction, and the contract, action, or transaction is specifically approved at a meeting of the members held for that purpose by the affirmative vote of the members entitled to exercise a

¹⁴ R.C. 1705.161 and 1705.281(B)(2) and (3).

¹⁵ R.C. 1705.31(A)(1)(a), (b), and (c) – not in, but referred to in, the bill.

majority of the voting power of the company held by persons not interested in the contract, action, or transaction.

- The contract, action, or transaction is fair to the company as of the time it is authorized or approved by the members or managers.

Existing law specifies that a member may lend money to and transact other business with the LLC and as to each loan or transaction the rights and obligations of the member are the same as those of a person who is not a member, subject to other applicable law. The bill eliminates the provision that states that a member may lend money to and transact other business with the LLC and instead specifies that, if a member has satisfied the requirements of R.C. 1705.31(A)(1)(a), (b), or (c) (described in the preceding paragraph) with respect to a contract, action, or transaction, the rights and obligations of the member with respect to that contract, action, or transaction are the same as those of a person who is not a member, subject to other applicable law.¹⁶

Officers of an LLC

The bill specifies that an LLC may have, but is not required to have, officers.¹⁷

Under the bill, unless either a written operating agreement for the LLC or a written agreement with an officer establishes additional fiduciary duties or the duties of an officer have been modified, waived, or eliminated as specified elsewhere in the Revised Code, the only fiduciary duties of an officer to the LLC or its members are the following:¹⁸

- If the individual is a member of the LLC or serving as the representative of a member and the individual is not a manager of the LLC, then the individual owes the duties that would be owed by a member.
- If the individual is a member of the LLC or serving as the representative of a member and the individual is a manager of the LLC and in that capacity owes the duties that would be owed by a member, then the individual owes the duties that would be owed by a member.
- If the two duties listed above do not apply, the individual owes to the LLC the duties of an officer described in the following paragraph.

¹⁶ R.C. 1705.281(F).

¹⁷ R.C. 1705.291.

¹⁸ R.C. 1705.292(A).



An officer of an LLC must perform the officer's duties in good faith, in a manner the officer reasonably believes to be in or not opposed to the best interests of the LLC, and with the care that an ordinarily prudent person in a like position would use under similar circumstances.

An officer of an LLC must not be found to have violated the officer's duties unless it is proved by clear and convincing evidence in any action brought against the officer that the officer has not acted in good faith, in a manner the officer reasonably believes to be in or not opposed to the best interests of the LLC, or with the care that an ordinarily prudent person in a like position would use under similar circumstances. An officer will not be considered to be acting in good faith if the officer has knowledge concerning the matter in question that would cause reliance on information, opinions, reports, or statements that are prepared or presented by any of the persons listed under "**Reliance upon information prepared or presented by certain individuals**," below, to be unwarranted.¹⁹

LLC officer's liability in damages

The bill specifies that an officer will be liable in damages for a violation of the officer's duties only if it is proved by clear and convincing evidence in a court of competent jurisdiction that the officer's action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the LLC or undertaken with reckless disregard for the best interests of the company. This does not apply if, and only to the extent that, at the time of an officer's act or omission that is the subject of complaint, either of the following is true:²⁰

- The LLC's articles or operating agreement state by specific reference that the provisions do not apply to the LLC.
- A written agreement between the officer and the LLC states by specific reference that the provisions do not apply to the officer.

This bill specifies that nothing in R.C. 1705.292 affects the duties of an officer who acts in any capacity other than the officer's capacity as an officer, and that nothing in that section affects any contractual obligations of an officer to the LLC.²¹

¹⁹ R.C. 1705.292(B) and (C).

²⁰ R.C. 1705.292(D).

²¹ R.C. 1705.292(E).



Reliance upon information prepared or presented by certain individuals

The bill revises the list of persons entitled to rely on opinions, reports, or statements of LLC members, employees, or related professionals. Under existing law, in performing duties or exercising authority, a member or manager of an LLC is entitled to rely on information, opinions, reports, or statements, including, but not limited to, financial statements and other financial data, that are prepared or presented by the following persons:

- One or more members, managers, officers, or employees of the company who the member or manager reasonably believes are reliable and competent in the matters prepared or presented;
- Counsel, public accountants, or other persons as to matters that the member or manager reasonably believes are within the person's professional or expert competence.

The bill expands this provision to specify that, in performing the duties to or exercising the authority on behalf of an LLC, an officer of an LLC is entitled to rely on information, opinions, reports, or statements prepared or presented by any of the persons described above.

Personal liability of member, manager, or officer of LLC

The bill revises the liability of members, managers, and officers of an LLC. Under existing law, an LLC's members and managers are not personally liable to satisfy any judgment, decree, or court order or are not personally liable to satisfy in any other manner, a debt, obligation, or liability of the company solely by reason of being a member or manager of the LLC. Nothing in the law governing LLCs affects any personal liability of an LLC's member or manager for the member's or manager's own actions or omissions.

The bill adds an LLC's officers to the list of persons not personally liable as described in the paragraph above. Additionally, the bill specifies that the failure of an LLC or any of its members, managers, or officers to observe any formalities relating to the exercise of the LLC's powers or the management of its activities is not a factor to consider in, or a ground for, imposing liability on the members, managers, or officers for the debts, obligations, or other liabilities of the company.²²

²² R.C. 1705.48(B), (C), and (D).

HISTORY

ACTION	DATE
Introduced	06-10-15
Reported, S. Civil Justice	10-13-15
Passed Senate (32-0)	10-14-15
Reported, H. Judiciary	---

S0181-RH-131.docx/emr

