

Series LLCs: The Asset Protection Dream Machines?

Amanda J. Bahena*

I. INTRODUCTION	800
II. BACKGROUND	801
A. <i>Series LLCs Defined</i>	801
1. <i>The Development of Series LLCs</i>	801
2. <i>Following Delaware's Lead: Series LLCs in Other States</i>	803
B. <i>Asset Segregation in SLLCs</i>	804
C. <i>Series LLCs and Unanswered Bankruptcy Issues</i>	806
D. <i>Can a Series File for Bankruptcy?</i>	806
E. <i>Will Bankruptcy Courts Allow Series Limited Liability?</i>	807
III. ANALYSIS	808
A. <i>Unincorporated Corporate Divisions in Bankruptcy</i>	808
B. <i>Corporate Groups in Bankruptcy: Entity and Enterprise Law</i>	809
1. <i>Bankruptcy and Entity Law</i>	809
2. <i>Bankruptcy and Enterprise Law</i>	810
C. <i>Liability within SLLCs Must Be Predictable: Four Possible Standards</i>	812
1. <i>The Importance of Predictable Liability</i>	812
i. <i>Liability Is Important</i>	812
ii. <i>Liability Must Be Predictable</i>	814
2. <i>Possible Standards for Liability Boundaries Within SLLCs</i>	814
i. <i>Option 1: Impenetrable Boundaries Between Series</i>	815
ii. <i>Option 2: Entity Law with Exceptions</i>	816
iii. <i>Option 3: Enterprise Law</i>	817
iv. <i>Option 4: No Boundaries Between Series in Bankruptcy</i>	819
IV. RECOMMENDATION	819
A. <i>Bankruptcy Courts Should Not Permit a Series to File for Bankruptcy</i> Independently of Its SLLC	820
B. <i>Bankruptcy Courts Should Not Permit Series Limited Liability</i>	821
1. <i>Eliminating Series Limited Liability Improves Predictability and Fairness</i> ..	821
i. <i>Series Engaging in a Common Business</i>	821
ii. <i>Series External Integration</i>	822
iii. <i>Series Internal Integration</i>	823
2. <i>Neither a Rebuttable Presumption of Limited Liability nor Enterprise</i> <i>Law Is Practical in SLLC Bankruptcies</i>	824
V. CONCLUSION	824

* J.D., The University of Iowa College of Law, 2010; M.A., The University of Warwick, England, 2007; B.A., Iowa State University, 2004. I would like to thank my husband Carlos for his unending support and my daughter Celia for being a wonderful distraction.

I. INTRODUCTION

In uncertain economic times, bankruptcy and asset protection become hot topics. Businesses begin looking for new ways to avoid bankruptcy and shield their assets from creditors if bankruptcy is unavoidable. The series limited liability company (SLLC) represents the growing popularity and increasing sophistication of asset protection strategies.¹ An SLLC has the potential to be the next evolutionary step in limited liability companies (LLCs).² An SLLC partitions its “assets, debts, obligations, liabilities, and rights among” separate series, or “cells.”³ Through this asset and liability segregation, the SLLC might provide the next business structure that helps businesses avoid bankruptcy and protect assets.⁴

Throughout this Note, the hypothetical businesswoman, Julie, will highlight the potential benefits and unresolved legal issues of SLLCs. Julie wants to form a business to buy and sell Amazing, Boring, and Clunky widgets. However, she has two main concerns. First, given the state of the economy, demand for Boring widgets might be low for the next few years. Julie must sell both Amazing and Boring widgets, but she is afraid that low Boring sales will drive her business into bankruptcy. Julie is also worried that Clunky widgets might break and cause liability issues, driving her new company into bankruptcy. Julie’s lawyer Lucy suggested forming an SLLC to decrease the risk of total bankruptcy. Julie is nervous. She knows that SLLCs are not yet widely used because of a number of unresolved legal issues regarding SLLCs.⁵

Two related questions affect the value of an SLLC as an asset-protection mechanism in bankruptcy: (1) whether an individual series in an SLLC can file for bankruptcy, and if so, (2) whether bankruptcy courts will shield the wider SLLC from that series’ liabilities. Part II of this Note introduces the SLLC and presents the unresolved issues regarding the treatment of SLLCs in bankruptcy.⁶ Part III of this Note explains how a series in an

1. See Christopher J. Redmond, *The International Scene, Offshore Estate Planning: Haven for International Insolvency Litigation*, AM. BANKR. INST. J. 12, 12 (Oct. 17, 1998) (explaining how asset protection planning is a growing industry); Normal M. Powell, *Delaware Alternative Entities: The Benefits and Burdens of Contractual Flexibility*, PROB. & PROP., Jan.–Feb. 2009, at 11 (noting that the use of SLLCs is “beginning to surface”).

2. Dominick T. Gattuso, *Series LLCs: Let’s Give the Frog a Little Love*, 17 BUS. L. TODAY 33, 33 (July/Aug. 2008).

3. *Id.* at 33. A series may “hav[e] separate rights, powers or duties with respect to specified property or obligations of the [LLC] or profits and losses associated with specified property or obligations. . . .” DEL. CODE ANN. tit. 6, § 18-215(a) (2008).

4. See Powell, *supra* note 1, at 11 (suggesting that alternative entities such as SLLCs might be used to “legally isolat[e] assets in a given transaction from the consequences of a future insolvency”).

5. Gattuso, *supra* note 2, at 33, 36 (“[I]n the words of some commentators, the Series LLC is untested, unpredictable, and too risky to employ for anyone but the most sophisticated individuals.”); see also *ALL-ABA Conference: Choice of Business Entity*, CCH RES. NETWORK NEWSL. (Limited Liability Company Guide (LLC Advisor)) No. 138, Feb. 2007 [hereinafter *Choice of Business Entity*] (identifying unresolved issues of SLLC bankruptcy and tax treatment and treatment of SLLCs by non-SLLC states as key reasons individuals do not form SLLCs). In 2008, the IRS issued private letter ruling 200803004 indicating that each series within an SLLC can be treated as a separate entity for tax purposes. Charles Rubin, *Rubin on Tax, IRS Allows Separate Entity Treatment for Series LLC*, May 6, 2008. <http://rubinontax.blogspot.com/search/label/Series%20LLC>. The drafters of the 2006 Revised Uniform Limited Liability Company Act did not include SLLC provisions in the Act given the uncertainties surrounding the legal treatment of SLLCs. Gattuso, *supra* note 2, at 33.

6. See *infra* Part II (explaining the SLLC and issues resulting from the companies).

SLLC is a hybrid between an unincorporated corporate division and a corporation in a corporate group.⁷ It then summarizes the laws governing unincorporated corporate divisions and corporate groups in bankruptcy with a focus on entity and enterprise law as applied to corporate groups.⁸ Finally, Part III concludes by explaining why it is important that series liability be predictable.⁹

Courts can ensure that liability within SLLCs is predictable by defining the clear legal boundaries and legal entity status of a series within an SLLC. This Note presents four alternatives for how bankruptcy courts could treat series liability boundaries in bankruptcy. The four alternatives include establishing impenetrable boundaries, establishing a rebuttable presumption of separate entity status, using enterprise law to determine whether individual series are engaged in one “enterprise,” or precluding liability boundaries in all circumstances.¹⁰ Part IV of this Note recommends that bankruptcy courts not allow a series to file for bankruptcy individually, because a series is not a stand-alone legal entity.¹¹ It then recommends that if bankruptcy courts do allow a series to file individually for bankruptcy, that the courts not uphold series limited liability.¹² This approach will decrease litigation, improve predictability, and enhance overall fairness. This Note concludes that the detriments of using SLLCs for asset protection in bankruptcy far outweigh the benefits.

II. BACKGROUND

SLLCs take the popular LLC to another level by providing the opportunity to segregate liability, control, and profit-sharing within a single entity.¹³ This section summarizes the SLLC’s history, legislation, current uses, and benefits, with a focus on the benefits of asset segregation. It then summarizes the unanswered bankruptcy issues surrounding the SLLC.

A. Series LLCs Defined

1. The Development of Series LLCs

SLLCs evolved from asset-segregating business structures that have existed in offshore financial centers for decades.¹⁴ Like its asset-segregating ancestors, an SLLC partitions its assets, debts, obligations, liabilities, and rights among separate series, or

7. See *infra* Part III.A–B (discussing the combined characteristics of an unincorporated corporate division and a corporation in a corporate group).

8. *Id.*

9. See *infra* Part III.C.1 (arguing the importance of predictability).

10. See *infra* Part III.C.2 (explaining the four alternatives courts have in series liability bankruptcy).

11. See *infra* Part IV.A (arguing against individual series bankruptcy).

12. See *infra* Part IV.B (recommending bankruptcy courts uphold series limited liability to those series that file individually).

13. Michael E. Mooney, *Series LCC: The Loaves and the Fishes of Subchapter K*, in TAX LAW COURSE HANDBOOK SERIES, at 361 (Practising Law Institute) PLI Tax Law and Estate Planning, Course Handbook Series N. 14290, 2008 available at 813 PLI/Tax 355 (Westlaw).

14. *Choice of Business Entity*, *supra* note 5. These offshore corporate structures include segregated portfolio companies and protected cell companies, which are used primarily by the banking and insurance industries to segregate liabilities and assets into “vaults” or “cells.” Gattuso, *supra* note 2, at 33.

“cells.”¹⁵ In 1996, Delaware became the first state to enable the formation of SLLCs through the Delaware Limited Liability Company Act (DLLCA).¹⁶ Delaware’s SLLC legislation has since served as a model for other states.¹⁷ Under Delaware law, an SLLC is formed by: (1) allocating the LLC’s property, obligations, or assets among its series;¹⁸ (2) setting forth in the operating agreement a method to maintain separate and distinct records for each series;¹⁹ and (3) including a notice of the limitation of series liability in the master LLC’s certificate of formation.²⁰ Furthermore, each series may designate its own class of members or managers, and each may set its own business purpose or investment objective.²¹

An SLLC may prove an efficient alternative to traditional methods of separating assets and segregating risks, given the relatively low filing fees and legal costs required to establish each series.²² Under the DLLCA, an SLLC series can, “in its own name, contract, hold title to assets . . . , grant liens and security interests, and sue and be sued.”²³ The DLLCA also grants limited liability to series—the DLLCA limits the enforcement of “debts, liabilities, obligations and expenses incurred, contracted for or otherwise existing with respect to a particular series . . . to that series only, and not against the assets of the [LLC] generally or any other series thereof. . . .”²⁴ To obtain limited liability, the DLLCA requires series separateness and notice of limited liability; each series must maintain separate records of the assets it holds, and the LLC’s certificate of formation must include a notice of the limitation of series’ liabilities.²⁵

15. Gattuso, *supra* note 2, at 33. A series “may have separate rights, powers or duties with respect to specified property or obligations of the [LLC] or profits and losses associates with specified property or obligations.” DEL. CODE ANN. tit. 6, § 18-215(a) (West Supp. 2010).

16. Gattuso, *supra* note 2, at 33. Originally, Delaware Business Trust Act was going to feature the “series” concept for use in mutual funds and highly financed asset securitizations, but the series concept found a wider application in the DLLCA. Ann E. Conaway, *A Business Review of the Delaware Series: Good Business for the Informed*, in WHAT BUSINESS LAWYERS MUST KNOW ABOUT DELAWARE LAW DEVELOPMENTS 2008, at 653 (PLI Corp. Law and Practice, Course Handbook Series No. 14533, 2008) available at 1677 PLI/Corp645 (Westlaw).

17. Gattuso, *supra* note 2, at 33; see also *infra* Part II.A.2 for a discussion of SLLC legislation in the other states.

18. DEL. CODE ANN. tit. 6, § 18-215(b) (West Supp. 2010).

19. “Records maintained for a series that reasonably identify its assets, including by specific listing, category, type, quantity, computational or allocational formula or procedure . . . will be deemed to account for the assets associated with such series separately from the other assets of the [LLC], or any series thereof.” *Id.*

20. Conaway, *supra* note 16, at 669–70.

21. DEL. CODE ANN. tit. 6, § 18-215(a), (e) (West Supp. 2010). These provisions should also be included in the operating agreement of the master LLC. Conaway, *supra* note 16, at 657–58.

22. Traditional methods largely consist of segregating assets into various related corporations or LLCs, which involve higher filing and transaction costs than SLLCs. Rubin, *supra* note 5 (“For SLLCs, “since there is only one entity filed with the applicable state, costs for forming new entities are avoided, administrative fees and costs are reduced, and one filing with the SEC possibly can be used for multiple [series].”). Note that lower filing costs are not an advantage in Illinois, because the Illinois SLLC statute requires a separate filing to establish each series. 805 ILL. COMP. STAT. ANN. 180/37-40(d) (West Supp. 2009).

23. DEL. CODE ANN. tit. 6, § 18-215(c) (West Supp. 2010) (This provision was added to the DLLC in 2007).

24. *Id.* at § 18-215(b) (emphasis added).

25. *Id.* A certificate of formation that includes a limitation on series liability constitutes notice of the limited liability of series if the certificate of formation is filed in the office of the Secretary of State. *Id.* It may be sufficient notice under the DLLC to state in the operating agreement that “the LLC is a ‘series’ limited

SLLCs were originally designed for use in asset securitization and the organization of investment companies.²⁶ Thus, in its most traditional and common application, a series is “an administrative subunit of an investment [LLC],”²⁷ such as a mutual fund. Legal uncertainties regarding SLLC liability shields are of less concern in this traditional context, which utilizes SLLCs for their administrative efficiencies²⁸ rather than their liability-protection capabilities.

SLLC use is no longer limited to the “traditional” uses. SLLCs are also used by some estate planners to separate assets by beneficiary.²⁹ SLLCs may also be useful in real estate management and development to segregate various properties, or useful for businesses with multiple assets under different ownership, such as a taxi cab or mobile home business.³⁰ A series has even been utilized to own a personal speedboat.³¹

2. Following Delaware’s Lead: Series LLCs in Other States

Seven states and Puerto Rico have since followed Delaware’s lead and enacted legislation that enable the formation of SLLCs.³² These states have closely modeled their laws after Delaware’s SLLC legislation. However, the Illinois and Iowa statutes share a key difference. Unlike other SLLC states, Illinois and Iowa explicitly define a series within an SLLC as a “separate legal entity.”³³

Notably, the Revised Uniform Limited Liability Companies Act (Re-ULLCA), which was approved for adoption by states in 2006, does not contain any SLLC

liability company “with all the limitations provided by law.” Conaway, *supra* note 16, at 703.

26. Thomas E. Rutledge, *Again, for the Want of a Theory: The Challenge of the “Series” to Business Organization Law*, 46 AM. BUS. L.J. 311, 313 (2009) (describing the history of the series).

27. *See id.* (describing the features of a series).

28. *Id.* For example, each series can hold different investment assets and have different investors, but there only needs to be one board of directors for all of the series and one SEC filing. *Id.*

29. Mark A. Sargent & Walter D. Schwidetzky, *Series LLCs*, in LIMITED LIABILITY COMPANY HANDBOOK § 3:85 (West 2009).

30. Christopher S. McLoon & Margaret C. Callaghan, *The Dangerous Charm of the Series LLC*, 2 ME. B.J. 226, 227 (2009) (suggesting that the ability of the SLLC “to provide for diversity of ownership, segregation of liability, and streamlined administration” make the SLLC “seem like an ideal business entity” in these scenarios).

31. *GxG Mgmt. LLC v. Young Bros. & Co.*, Civil No. 05-162-B-K, 2007 WL 551761, at *1 (D. Me. Feb. 21, 2007).

32. The seven states include Illinois, Iowa, Nevada, Oklahoma, Tennessee, Texas and Utah. 805 ILL. COMP. STAT. ANN. 180/37-40 (West Supp. 2009); IOWA CODE ANN. §§ 489.1201–489.1207 (West 2009); NEV. REV. STAT. ANN. §§ 86.291(2), 86.296, 86.1255 (West 2008); OKLA. STAT. ANN. tit. 18 § 2054.4 (West 2008); TENN. CODE ANN. §§ 48-202-101 (41), 48-249-309 (West Supp. 2010); TEX. BUS. ORGS. CODE ANN. §§ 101.601–101.621 (Vernon 2009); UTAH CODE ANN. §§ 48-2c-606, 607 (West 2008); P.R. LAWS ANN. tit. § 3426p (West 2008).

33. 805 ILL. COMP. STAT. ANN. 180/37-40(b) (West 2008) (“A series...[is] treated as a separate entity to the extent set forth in the articles of organization.”); IOWA CODE ANN. § 489.1201(3) (West 2009) (“A series meeting all of the conditions of subsection 2 shall be treated as a separate entity to the extent set forth in the certificate of organization.”). Illinois’s filing requirement for series is also more stringent than other states. Illinois requires the SLLC to file a certificate of designation, which lists the series’s name and names of the series’s members or managers, with the Secretary of State for each series which is to have limited liability. 805 ILL. COMP. STAT. ANN. 180/37-40(b), (d) (West 2008). The series’s name must contain the full name of the LLC yet be distinguishable from sibling series. 805 ILL. COMP. STAT. ANN. 180/37-40(b) (West 2008). See Gattuso, *supra* note 2, at 38, for a detailed comparison of Illinois and Delaware SLLC legislation.

provisions.³⁴ The Re-ULLCA drafting committee considered following Delaware and the other SLLC states, but ultimately rejected the notion of the SLLC.³⁵ The drafting committee explained their concerns:

Originally devised by sophisticated Delaware lawyers for their “funds” clients, series are now being (mis)used to subdivide assets of operating businesses and to provide unwarranted hopes of low cost “asset protection.” What’s good for Delaware and highly sophisticated deals is not necessarily good for the LLC law of other states.³⁶

It will be interesting to see how many states agree with the concerns of the Re-ULLCA drafting committee.

It is unclear how states that do not have SLLC-enabling legislation will treat foreign SLLCs. The full faith and credit provision of the U.S. Constitution generally requires state courts to recognize foreign SLLCs.³⁷ However, a state might refuse to recognize certain SLLC features if the state found an overriding public policy against those features.³⁸

To date, only one case has addressed the treatment of a foreign SLLC by a non-SLLC state. In *GxG Management, LLC v. Young Bros. & Co., Inc.*, a federal district court in Maine looked to Delaware law to determine whether a series in a Delaware SLLC could be joined as a party in the underlying tort action.³⁹ Maine had no SLLC-enabling legislation, yet the Maine court recognized the “unique relationship” between a Delaware SLLC and its series.⁴⁰ The court found that under the DLLC, the series was a “series of interest” of the master SLLC, not a “truly separate legal entity capable of independently pursuing its own legal claims.”⁴¹ Thus, the first judicial pronouncement on series standing does not bode well for the SLLC.

B. Asset Segregation in SLLCs

One of the primary attractions of SLLCs is the possibility of segregating assets and liabilities.⁴² Asset segregation can serve various goals, including aligning creditors with

34. Daniel S. Kleinberger & Carter G. Bishop, *The Next Generation: The Revised Uniform Limited Liability Company Act*, 62 BUS. LAW. 515, 542 (2007).

35. *Id.*

36. *Id.* at 542 (quoting Daniel S. Kleinberger, *Progress Report on the Revised Uniform Limited Liability Company Act (“ULLCA”) and the Issue of “Corpufuscation”*, PUBOGRAM Vol. XXII, no. 2, at 9 (March 2006)).

37. Dem A. Hopkins, *Annual ALI-ABA Satellite Conference Looks at New Developments in Limited Liabilities*, CCH RES. NETWORK NEWSL. (Limited Liability Company Guide (LLC Advisor)) No. 128, Apr. 2006.

38. *Id.*

39. *GxG Mgmt v. Young Bros. and Co.*, Civil No. 05-162-B-K, 2007 WL 551761 at *7 (D. Me. 2007). The Maine court looked to the DLLC to determine whether the master LLC had the capacity to pursue legislation on behalf of its series or in the alternative, whether the individual series had the capacity to sue in its own name. *Id.*

40. *Id.* at *1.

41. *Id.* at *1–2. Note that this case was decided before the 2006 amendment to the DLLCA adding the right for a series to sue in its own name.

42. ROBERT L. SYMONDS, JR. & MATTHEW J. O'TOOLE, SYMONDS & O'TOOLE ON DELAWARE LIMITED LIABILITY COMPANIES § 5.22[A] (CCH Research NetWork 2007).

assets, separating “high risk” and “low risk” assets, and “judgment-proofing” a business.⁴³ The ability of executives to align creditors with assets in a segregated business structure “may prove cost effective because it . . . achiev[es] [asset-specific securitization] without resort to traditional security devices, such as mortgages and pledge agreements,” which come with higher transaction costs.⁴⁴ Asset segregation through SLLCs might also provide an alternative to forming several separate entities.⁴⁵

A second function of asset segregation is to “judgment-proof” an entity, or in other words, to make an entity “bankruptcy remote.”⁴⁶ In bankruptcy, most or all of a “judgment-proof” entity’s assets are insulated from the bankruptcy estate.⁴⁷ “Judgment-proofing” can be accomplished by segregating assets and liabilities into related but legally separate entities.⁴⁸ A debtor “isolates the most valuable assets of the business in an entity other than the one that conducts the liability-producing business activity.”⁴⁹ Each entity must be shielded from the liabilities of its sister entities.⁵⁰ Then, when the entity with the most liability and the fewest assets files for bankruptcy, assets of other entities are protected from collection.⁵¹ Limiting liability in this way is a principal reason that most large companies consist of numerous corporate entities.⁵²

An SLLC might limit liability in two ways.⁵³ First, the SLLC could establish Series A as an undercapitalized operating company and allow Series B to acquire assets to be used by Series A.⁵⁴ “Alternatively, if [Series A] already owns its operating assets, [the SLLC] could cause [Series A] to sell [or otherwise transfer] those assets to [Series B] and [have Series B] lease them back” to Series A.⁵⁵ In both situations, the structure might result in judgment-proofing: Series A’s operations could generate liabilities that Series A’s assets would be unable to pay.⁵⁶

While these asset-segregation strategies leave the assets of the liability-producing entity open to collection by creditors, the assets held by the other business entities are usually protected from collection.⁵⁷ If the liability-generating entity files for bankruptcy,

43. Lynn M. LoPucki, *The Death of Liability*, 106 YALE L.J. 1, 20 n.76 (1996).

44. William H. Widen, *Report to the American Bankruptcy Institute: Prevalence of Substantive Consolidation in Large Public Company Bankruptcies from 2000 to 2005*, 16 AM. BANKR. INST. L. REV. 1, 27–28 (2008).

45. SYMONDS & O’TOOLE, *supra* note 42, § 5.22[A].

46. Katherine D. Kale, *Securitizing the Enterprise: Enterprise Liability and Transferred Receivables in Bankruptcy*, 20 BANKR. DEV. J. 311, 312 (2003).

47. Filing for bankruptcy creates a bankruptcy “estate,” which holds the debtor’s legal and equitable property interests. *Id.* at 316–17.

48. LoPucki, *supra* note 43, at 19–30.

49. *Id.* at 20.

50. See Redmond, *supra* note 1, at 38 (“The whole concept of . . . asset protection . . . is to avoid the payment of valid obligations.”).

51. LoPucki, *supra* note 43, at 20–22.

52. *Id.* at 20.

53. See Steven L. Schwarcz, *The Inherent Irrationality of Judgment Proofing*, 52 STAN. L. REV. 1, 29 (1999) (listing the two methods that parent-subsidiary structure may be used for judgment-proofing).

54. *Id.*

55. *Id.*

56. *Id.* Schwarcz notes that the extent of transfers between related entities and undercapitalization may be limited by fraudulent conveyance law, “veil-piercing,” and substantive consolidation. *Id.* at 32–38.

57. See LoPucki, *supra* note 43, at 4, 22 (noting that asset-segregation does not completely judgment-proof a business, because assets of the liability-producing entity remain subject to collection).

its debts will be discharged, and its sister entities continue as though nothing happened.⁵⁸ The SLLC, with its internal divisions and low filing costs, might become the next asset-protection dream machine. However, this depends on bankruptcy courts.

This brings us back to Julie, who is hoping to take advantage of the SLLC's judgment-proofing potential. Julie is considering forming a Delaware SLLC, "Widgets, LLC," with three series: "Widgets, LLC, Series A," "Widgets, LLC, Series B," and "Widgets, LLC, Series C." However, she is still not sure how to allocate her assets among the three series. She might place her Amazing assets in Series A, her Boring assets in Series B, and her Clunky assets in Series C. Through this arrangement, Julie hopes to protect her valuable Amazing widgets from collection by creditors if things go terribly wrong with her Boring or Clunky widgets. For example, the Clunky widget inventory is not very valuable. If a Clunky malfunction results in tort liability, it is unlikely the Clunky assets and revenues alone will cover a resulting settlement or judgment. In such a circumstance, Julie hopes that a bankruptcy court would allow Series C to file bankruptcy and shield the valuable Amazing and Boring widgets from Series C's creditors.

C. Series LLCs and Unanswered Bankruptcy Issues

Two key unresolved issues determine whether an SLLC can offer Julie asset-protection in bankruptcy. The first is whether a bankruptcy court will allow a series to file for bankruptcy individually.⁵⁹ The second is whether a bankruptcy court will uphold series liability limitations created under state laws.⁶⁰ Case law provides no guidance on these issues because no SLLC series has attempted to file for bankruptcy, and no bankruptcy court has ever analyzed an SLLC's internal liability shields.⁶¹

D. Can a Series File for Bankruptcy?

If an insolvent series is to protect the rest of its SLLC from its liabilities, the insolvent series must be able to file for bankruptcy individually.⁶² A series may file for bankruptcy only if it is a "person" under the Bankruptcy Code (the Code).⁶³ Because the Code does not mention LLCs or SLLCs, courts must interpret the Code's definition of "person."⁶⁴ In the Bankruptcy Code, "[t]he term 'person' includes individual[s], partnership[s], and corporation[s],"⁶⁵ but that list is not exhaustive.⁶⁶ For example, LLCs are not mentioned in the definition of "person," but bankruptcy courts generally treat them as such.⁶⁷ No court has yet determined a series's "personhood" for bankruptcy

58. *Id.* at 20–22.

59. *Choice of Business Entity*, *supra* note 5.

60. Gattuso, *supra* note 2, at 37.

61. *Choice of Business Entity*, *supra* note 5.

62. *Id.*

63. 11 U.S.C. §§ 101(13), 301(a), 303(a) (2006).

64. Only a "debtor" may file for bankruptcy, and a "debtor" must be a "person." 11 U.S.C. § 109 (2006). Therefore, only a "person" may file for bankruptcy.

65. 11 U.S.C. § 101(41) (2006). "Corporation" is defined under 11 U.S.C. § 101(9) (2008).

66. 11 U.S.C. § 102(3) (2006) ("In this title—'includes' and 'including' are not limiting.").

67. Ann K. Wooster, *Issues Concerning Bankruptcy Proceedings of Limited Liability Companies*, 37 A.L.R. Fed. 2d 129, § 4 (2009); Thomas F. Blakemore, *Limited Liability Companies and the Bankruptcy Code*:

purposes.

To some extent, series are treated as “persons” within the Delaware, Illinois, and Iowa state statutes. Delaware amended its DLLC Act in 2006 to define a series as a “person.”⁶⁸ In part, this allows a series to act as a separate legal entity in many respects: it can sue and be sued; make contracts; and buy, sell, and own property.⁶⁹ The Illinois and Iowa statutes are similar: they treat a series “as a separate legal entity to the extent set forth in the articles of incorporation.”⁷⁰ However, a bankruptcy court is not bound by those state statute definitions in deciding whether a series is a “person” under the Code.⁷¹ Under the supremacy doctrine, once a bankruptcy process begins, federal law trumps state law in determining the rights of the parties.⁷²

E. Will Bankruptcy Courts Allow Series Limited Liability?

Whether a bankruptcy court will uphold series liability shields created under state law depends on choice of law and equitable issues. First, choice of law in bankruptcy is complex.⁷³ While bankruptcy laws are federal, state laws largely govern the business entity structure and collection remedies.⁷⁴ Under the Supremacy Clause, federal bankruptcy law preempts state law when the two are inconsistent.⁷⁵ Bankruptcy courts attempt to preserve the pre-bankruptcy rights, remedies, and legitimate expectations of creditors.⁷⁶ Because creditors originally based their expectations on state corporate and collection laws, bankruptcy courts attempt to uphold state corporation law when possible.⁷⁷

Second, the bankruptcy courts have a wide range of both legal and equitable remedies at their disposal.⁷⁸ The underlying principles of bankruptcy law are equitable:

A Technical Review, AM. BANKR. INST. J., June 1994, at 12. *See, e.g., In re Midpoint Dev., L.L.C.*, 313 B.R. 486, 488–89 (Bankr. W.D. Okla. 2004) (analogizing LLCs to corporations and partnerships and finding that, given the similarities of LLCs to corporations, there was no reason to exclude LLCs from being debtors under the Bankruptcy Code), *rev'd on other grounds* by 466 F.3d 1201 (10th Cir. 2006).

68. DEL. CODE ANN. tit. 6, § 18-101(12) (2008) (defining “person” as “a natural person, partnership . . . , corporation, government . . . or any other individual or entity (*or series thereof*) in its own or any representative capacity, in each case, whether domestic or foreign” (emphasis added)).

69. Conaway, *supra* note 16, at 700–01.

70. ILL. COMP. STAT. ANN. 180/37-40(b) (West 2008); IOWA CODE ANN. § 489.1201(3) (West 2009).

71. LYNN M. LOPUCKI & ELIZABETH WARREN, SECURED CREDIT: A SYSTEMS APPROACH 92 (5th ed. 2006); *see* Conaway, *supra* note 16, at 698 (suggesting that the inclusion of “series” within the DLLCA definition of “person” was for specific business reasons, such as to allow a series to sue, and “does not answer the question of ‘personage’ for federal bankruptcy purposes”).

72. *Id.*

73. *See* LOPUCKI & WARREN, *supra* note 71, at 91–92 (explaining bankruptcy choice of law).

74. *Id.*

75. *Id.*; Kale, *supra* note 46, at 316 (“[I]n many respects, federal and state laws ‘are interpreted and applied to eliminate inconsistencies so that no preemption occurs.’ Thus, non-bankruptcy rights should be respected in bankruptcy unless some bankruptcy policy compels a different result.”). “Simply put, the basic federal rule in bankruptcy is that state law defines the substance of claims.” *Id.* at 317.

76. Kale, *supra* note 46, at 316–17.

77. *See* *Butner v. United States*, 440 U.S. 48, 55 (1979) (stating that “[p]roperty interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently . . . in a bankruptcy proceeding. Uniform treatment . . . by both state and federal courts . . . reduce[s] uncertainty”).

78. *See generally* PHILLIP I. BLUMBERG, THE LAW OF CORPORATE GROUPS: BANKRUPTCY LAW 9–12

bankruptcy law attempts “to achieve fair treatment for creditors and other claimants,” both by fairly distributing assets among general creditors and by protecting creditors and public investors against manipulation by the debtor and insiders.⁷⁹ To carry out such ends, Bankruptcy Code § 105(a) permits a bankruptcy court to “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]”⁸⁰ However, in dispensing equitable remedies, the courts do not simply ignore legal ramifications.⁸¹

III. ANALYSIS

Structurally, an SLLC is a hybrid between a traditional LLC, or traditional corporation, and a corporate group. A traditional LLC or corporation might separate into unincorporated divisions for convenience. Unlike series in an SLLC, these unincorporated divisions have no separate legal authority by statute.⁸² A corporate group consists of separate, *incorporated* entities, such as corporations or LLCs. The affiliated entities of a corporate group may be organized in parent-subsidiary or brother-sister relationships, and they “collectively conduct . . . a common business for the maximization of the profits of the group.”⁸³ A series in an SLLC straddles the line between the unincorporated divisions in a corporation and the corporations that make up a corporate group. Therefore, bankruptcy laws governing corporate groups and corporate divisions provide a base for deciding personhood and limited liability issues for SLLCs.

A. Unincorporated Corporate Divisions in Bankruptcy

A corporation is a “person,” under the Bankruptcy Code, and therefore a corporation may file for bankruptcy.⁸⁴ However, bankruptcy courts do not consider an unincorporated division a “person,” and therefore a division cannot file for bankruptcy independently of its larger corporation.⁸⁵ Similarly, corporate divisions enjoy no limited liability, because they are not separate “persons.”⁸⁶ Therefore, a creditor of one division can collect from the assets of another division.

(1985) [hereinafter BLUMBERG] (explaining how bankruptcy courts have used legal remedies, such as entity law; and equitable remedies, such as substantive consolidation, to achieve bankruptcy goals).

79. *Id.* at 9; see also *Begier v. Internal Revenue Serv.*, 496 U.S. 53, 58 (1990) (identifying “[e]quality of distribution among creditors” as a “central policy of the Bankruptcy Code”).

80. 11 U.S.C. § 105(a) (2006).

81. Kale, *supra* note 46, at 337 (“Section 105 should not be construed as a mandate for bankruptcy judges to do whatever they find just or equitable.” (quoting DOUGLAS G. BAIRD, *ELEMENTS OF BANKRUPTCY* 6 (2001))).

82. Unincorporated Operating Division, 9 FLETCHER CYCLOPEDIA CORPORATIONS § 4233.50 (2008).

83. BLUMBERG, *supra* note 78, at 337.

84. 11 U.S.C. § 101(41) (2006).

85. See Unincorporated Operating Division, 9 FLETCHER CYCLOPEDIA CORPORATIONS § 4233.50 (2008) (explaining that unincorporated corporate divisions are not legal “persons”).

86. Because a division in a corporation is not considered a legal “person,” or separate legal entity, it cannot sue, own property, contract, or shield the larger corporation from its liabilities. *Id.*

B. Corporate Groups in Bankruptcy: Entity and Enterprise Law

The bankruptcy law governing corporate groups is more complex. To begin, a corporation in a corporate group may file individually for bankruptcy because corporations are “persons” under the Bankruptcy Code.⁸⁷ Additionally, liability is usually limited between corporations in a corporate group.⁸⁸ However, bankruptcy courts may use their equitable powers to allow creditors of one corporation to collect from the assets of another corporation in the group.⁸⁹ Bankruptcy courts decide whether to uphold or disregard corporate liability boundaries based on bankruptcy law goals.⁹⁰ The underlying principles of bankruptcy law are equitable: ensuring fairness to creditors and other claimants and ensuring equality of distribution.⁹¹ When dealing with corporate groups, courts achieve these goals through a combination of entity and enterprise law.⁹² The following subsections discuss entity and enterprise law in detail.

1. Bankruptcy and Entity Law

Entity law is concerned with formal legal boundaries.⁹³ Legal boundaries prevent creditors of one entity from collecting the assets of a related entity.⁹⁴ Entity law assumes that each corporation is a separate legal entity with its own legal rights and duties.⁹⁵ Entity law emerged when most corporations were very small and closely held, and courts used entity law primarily to shield corporate owners from personal liability.⁹⁶ Later, as corporate groups arose, courts applied entity law to establish the separate legal personality and limited liability of each corporation within the corporate group.⁹⁷ Within corporate groups, entity law protects the assets of one corporation from the creditors of other corporations in the corporate group.⁹⁸

87. 11 U.S.C. § 101(41) (2006).

88. BLUMBERG, *supra* note 78, at 5.

89. See *infra* Part III.B.1 for a discussion of veil-piercing and Part III.B.2. for a discussion of equitable subordination.

90. BLUMBERG, *supra* note 78, at 696 (listing the bankruptcy goals of “protect[ing] the interests of creditors” and ensuring “the equitable distribution of the assets of the debtor’s estate”).

91. *Id.* at 26–27 (discussing how courts use substantive consolidation to further the equitable goals of the Bankruptcy Code); Kale, *supra* note 46, at 331–32 (explaining that Bankruptcy Code § 105(a), which vests the bankruptcy courts with general equitable powers, permits those courts to use substantive consolidation); see *supra* text accompanying note 80 for the text of § 105(a) (permitting a bankruptcy court to “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code] . . .”).

92. See generally BLUMBERG, *supra* note 78 (explaining the history and application of entity and enterprise law in the context of corporate group bankruptcies).

93. *Id.* at 6 (“Entity law is essentially concerned with the form, not the substance, of corporate existence. It gives primary attention to the extent of formal separation of the affiliated companies of the group.”).

94. See generally *id.* at 3–8 (discussing the development of the entity concept as a method of protecting shareholder–investors from the liabilities of a firm).

95. *Id.* at 4. Entity law was first applied to limit the liability of shareholders to their own capital stock investments and then, as corporate law evolved, to shield shareholders from corporate liability. *Id.*

96. BLUMBERG, *supra* note 78, at 3–4.

97. See *id.* at 5 (suggesting that recognizing the separate legal personality of each enterprise within a corporate group was unnecessary, as the law already separates the group’s investors from the overall enterprise, and that such recognition “extended legal consequences of a most serious nature to a structural fragmentation of the enterprise among the various companies of the group”).

98. *Id.*

Under traditional entity law, the only way to cross formal boundaries between related corporations is to “pierce the corporate veil.”⁹⁹ Courts allow creditors to “pierce the veil” only in “exceptional circumstances,” when creditors can show a lack of formal separation between affiliates of a corporate group.¹⁰⁰ “Veil-piercing” involves a case-by-case application of rigid, technical requirements, and its application varies widely among courts.¹⁰¹

2. Bankruptcy and Enterprise Law

While entity law focuses on the *formalities* of the corporate structure, enterprise law reflects the *substantive realities* of corporate existence.¹⁰² Enterprise law recognizes that corporations within a corporate group often act as a single enterprise with a unified goal, rather than as distinct entities.¹⁰³ The basic theory behind the doctrine is that the various legal entities that are operated as the same enterprise should share both the rewards *and* the risks of that enterprise.¹⁰⁴ If successfully invoked, enterprise liability permits creditors to cross corporate boundaries and collect from the larger group, or enterprise.¹⁰⁵

Enterprise law evolved as an alternative to more rigid entity law principles.¹⁰⁶ “In its more conservative version, enterprise liability is virtually indistinguishable from [liberally] piercing of the corporate veils within corporate groups.”¹⁰⁷ In its more radical version, it calls for the complete disregard of entities, leaving it up to the courts to determine the scope of the enterprise.”¹⁰⁸ Since the late 1930s, judges have turned to enterprise law to address the gap between mechanical “piercing the veil” jurisprudence and the reality of a corporation’s structure and practices.¹⁰⁹ Enterprise law has expanded as courts have recognized the importance of reflecting economic realities in debtor-creditor law.¹¹⁰ The availability of enterprise principles has begun to erode the use of entity law in corporate group bankruptcies.¹¹¹ Yet this process has been uneven across

99. *Id.* at 7.

100. *Id.*

101. See BLUMBERG, *supra* note 78, at 7–8 (“Not surprisingly [this case-by-case] approach has produced hundreds of irreconcilable cases under a doctrine that gives little guidance for the prediction of other cases.” (citing fraud requirements of certain courts, such as *Luckett v. Bethlehem Steel Corp.*, 618 F.2d 1373, 1379 (10th Cir. 1980); *Maule Indus., Inc. v. Gerstel*, 232 F.2d 294, 297 (5th Cir. 1956); *Duffy v. Treide*, 78 F.2d 17, 20 (4th Cir. 1935) and citing requirements that a subsidiary be shown to be a “sham” or “shell” from *In re Novman*, 32 Bankr. 562, 569 (Bankr. W.D. Mo. 1983)).

102. BLUMBERG, *supra* note 78, at 6.

103. Kale, *supra* note 46, at 313.

104. *Id.*

105. *Id.*

106. See BLUMBERG, *supra* note 78, at 700–01 (discussing how enterprise law has developed “against a background of entity law”).

107. LoPucki, *supra* note 43, at 67.

108. *Id.*

109. BLUMBERG, *supra* note 78, at 16 (stating that piercing the veil jurisprudence “is preoccupied with the degree of formal separation between the affiliates of the group and ignores their economic interrelationship. It disregards the reality that the affiliated corporations are conducting fragmented parts of a single business under common direction for the maximization of the income of the group as a whole”).

110. For a list and explanation of remedies available under enterprise law, see *id.* at 13–37 (discussing “the increasing acceptance of enterprise law”).

111. *Id.* at 702–03.

legal issues and bankruptcy courts.¹¹²

Substantive consolidation serves as the enterprise law alternative to veil-piercing.¹¹³ In substantive consolidation, courts combine assets and liabilities of affiliated debtors into one bankruptcy estate and eliminate intercompany claims and guarantees.¹¹⁴ Judges created this remedy to reach bankruptcy court goals of ensuring both fairness to creditors and equality of distribution.¹¹⁵ Courts can apply substantive consolidation when the overall fairness to creditors as a whole outweighs the negative effect on any one creditor.¹¹⁶ As courts developed the doctrine of substantive consolidation, many courts insisted that substantive consolidation should be used “sparingly” and only when necessary to achieve reorganization or protect creditor interests.¹¹⁷ However, “a torrent of decisions have frankly acknowledged the need for substantive consolidation when dealing ‘with the increasing appearance before the bankruptcy courts of large parent companies with their multi-tiered subsidiaries.’”¹¹⁸ Substantive consolidation is now the dominant bankruptcy technique courts use to reorganize and liquidate large public companies.¹¹⁹

112. *See id.* at 703 (explaining that entity law remains strong in parent-subsidiary obligation rules. Liability of a parent for the obligations of an insolvent subsidiary is still addressed almost exclusively through limited liability principles).

113. *See id.* at 432–34 (comparing “piercing the veil” jurisprudence to substantive consolidation).

114. BLUMBERG, *supra* note 78, at 26. For an in-depth discussion of the history, theory and application of substantive consolidation, see Kale, *supra* note 46, at 331–39.

115. *Id.* at 26–27 (explaining that substantive consolidation “rests on the equity jurisdiction of the [bankruptcy] courts,” because substantive consolidation is not expressly authorized by any statute); Kale, *supra* note 46, at 331–32 (“Bankruptcy courts have ordered substantive consolidation by virtue of their general equitable powers under [Bankruptcy Code] § 105(a).”).

116. BLUMBERG, *supra* note 78, at 26. The most common feature in substantive consolidation orders is the related debtors’ operation as integrated aspects of a single business. *Id.* at 27. Other factors include creditor expectations, feasibility of debtor reorganization, commingled operations, existence of intragroup loans and guarantees, and creditor’s difficulties in establishing proof of prejudice from consolidation. *Id.* at 27–28.

117. *Chem. Bank N.Y. Trust Co. v. Kheel*, 369 F.2d 845, 847 (2d Cir. 1966); *Pension Benefit Guar. Corp. v. Oumient Corp.*, 711 F.2d 1085, 1092–93 (1st Cir. 1983) (suggesting substantive consolidation be “granted if absolutely necessary for achieving reorganization or protecting creditors’ economic interests”). Originally, substantive consolidation was used only when (1) the companies disregarded their separateness so significantly that their creditors relied on the breakdown of entity borders and treated them as one legal entity, or (2) assets and liabilities became so scrambled after a bankruptcy petition that separating them would be prohibitive and hurt all creditors. *In re Owens Corning*, 419 F.3d 195, 211 (3d Cir. 2005), *amended by* No. 04-40802005 U.S. App. LEXIS 18043 (3d Cir., Aug. 23, 2005), *cert. denied* No. 05-941 2006 U.S. LEXIS 3492, 3493 (May 1, 2006).

118. BLUMBERG, *supra* note 78, at 27; *see In re Vecco Constr. Indus., Inc.*, 4 Bankr. 407, 409 (Bankr. E.D. Va. 1989) (“Due to the organizational makeup evidenced by the now common-place multi-tiered corporations in existence today, substantive consolidation of a parent corporation and its subsidiaries has been increasingly utilized as a mechanism to deal with corporations coming within the purview of the Act. . . . The liberal trend in allowing consolidation of proceedings, as evidenced by recent case law, arises from the result of increased judicial recognition of the widespread use of interrelated corporate structures by subsidiary corporations operating under a parent entity’s corporate umbrella for tax and business planning purposes.”); *but see Nesbit v. Gears Unlimited, Inc.*, 347 F.3d 72, 86 n.7 (3d Cir. 2003) (arguing that *Vecco* failed to cite any authority for its “liberal trend”).

119. Widen, *supra* note 44, at 3. Widen’s study found that courts approved substantive consolidation in over half of the large public bankruptcies filed between the years 2000 and 2005. *Id.* at 4–6. For purposes of the study, substantive consolidation was deemed to occur “if (a) settlement of substantive consolidation litigation preceded approval of a reorganization plan or liquidation or (b) a plan of reorganization or liquidation proposed

C. Liability within SLLCs Must Be Predictable: Four Possible Standards

The current law defining the boundaries of corporate divisions and corporate groups in bankruptcy serves as a base for determining the boundaries within SLLCs. Courts can use this base to select the laws that best further predictable liability and the fair distribution of assets to creditors.¹²⁰ Part III.C. first explains the importance of predictable liability and then proposes four options for the treatment of series liability boundaries in bankruptcy. These options are placed along a continuum, from treating series boundaries as impenetrable to treating them as non-existent.

*1. The Importance of Predictable Liability**i. Liability Is Important*

Liability is vital to our legal system.¹²¹ Liability is one of the two principal means to enforce the law.¹²² Just as governments use imprisonment and fines to enforce criminal law, they use liability to enforce civil law.¹²³ A defendant is held liable when a court enters a money judgment against the defendant, and that judgment is collected by the judgment holder.¹²⁴ The ability to hold a defendant liable is crucial to upholding many civil rights.¹²⁵ Professor Lynn LoPucki explains that “[r]ights enforced through liability are among the most precious we hold. These include the civil rights of minorities, the rights of access of the disabled, and the right to be compensated for the infliction of injury to one’s person, property, or reputation.”¹²⁶

If a firm protects its assets from collection by creditors, it can reduce its liability—it can become “judgment-proof.”¹²⁷ Such asset protection, while beneficial to certain individuals and businesses, is detrimental to society if taken to the extreme.¹²⁸ Reducing liability subverts civil law by reducing or eliminating the ability of judgment creditors to collect remedies.¹²⁹ If a firm can avoid liability it has less incentive to avoid risky, liability-producing behavior.¹³⁰

Asset protection is most harmful to unsecured creditors.¹³¹ Contract creditors, such as banks, are able to contract around liability boundaries to secure the payment of their

substantive consolidation of two or more entities involved in related bankruptcy proceeding.” *Id.* Substantive consolidation included either the actual combination of two or more entities, voting on the plan as if two or more entities were a single entity, or distributing assets as if two or more entities were combined. *Id.* at 10–11.

120. See *supra* text accompanying notes 87–91 for a discussion of bankruptcy goals.

121. LoPucki, *supra* note 43, at 3–4.

122. *Id.*

123. *Id.*

124. *Id.* at 4.

125. *Id.* at 41.

126. LoPucki, *supra* note 43, at 41.

127. *Id.* at 4.

128. See *generally id.* at 3–5 (warning that if “judgment-proofing” goes too far, liability, a principal means of law and contract enforcement, will die).

129. *Id.* at 4.

130. *Id.* at 7.

131. See LoPucki, *supra* note 43, at 7 (noting that contract liability, unlike tort or statutorily imposed liability, can be preserved through private contracting).

debts.¹³² However, a judgment for civil liability is an unsecured debt.¹³³ In bankruptcy, unsecured creditors recover from a debtor only after secured creditors are paid in full and these unsecured creditors are lucky if they collect anything.¹³⁴ Creditors in bankruptcy are more likely to be unsecured than secured.¹³⁵ Therefore, protecting assets from unsecured creditors—from predictable, recurring, tort victims to those involving “unpredictable catastrophic liability” as faced by asbestos manufacturers—can provide a business with substantial savings.¹³⁶

The balance between creditors’ debt-collection rights and debtors’ ability to engage in innovative business transactions to avoid liability is a delicate one.¹³⁷ As one commentator indicated,

A system that is too pro-debtor will result in higher costs of borrowing for contract debtors, and a higher rate of uncompensated loss for tort victims. A system that is too pro-creditor will result in higher costs for social services as debtors become too destitute to afford the “necessities of life.”¹³⁸

When it comes to asset protection, the scales seem tipped toward the debtor.¹³⁹ “Strategies for defeating liability are readily available . . . individuals and small firms . . . already protect the vast bulk of all assets against liability.”¹⁴⁰

In our example, Julie hopes to protect Widgets, LLC from certain liabilities. She knows that Clunky widgets will likely cause some recurring tort liability because they break easily. Clunky widgets could force her business into bankruptcy if those tort claims become too great. Julie wants to avoid infecting her entire business with Clunky Widget liability risks. Therefore, she plans to limit all Clunky widget activity to Widgets LLC, Series C. She will hold her more valuable assets, including her Amazing and Boring widgets inventory, in other series. If Clunky widgets generate more tort liability than Julie can pay from Series C’s assets, Julie hopes to protect her remaining assets from creditors. She can do so if courts allow Series C to file for bankruptcy and limit creditors to Series C’s assets.

132. *Id.*

133. *Id.* at 10.

134. *Id.* at 11.

135. See BLUMBERG, *supra* note 78, at 452 (citing Jonathan M. Landers, *Another Word on Parents, Subsidiaries and Affiliates in Bankruptcy*, 43 U. CHI. L. REV. 527, 540 (1976)).

136. LoPucki, *supra* note 43, at 45–47 (adding that bankruptcy is the standard method of dealing with massive, unforeseen tort liability).

137. For example, “radical reform” preventing limited liability “could indiscriminately restrict the value creation—wealth, jobs, incomes, and new products for large numbers of people—that comes with business and financial innovation.” Schwarcz, *supra* note 53, at 53 (refuting claims that innovative business transactions will “kill” liability).

138. Thomas L. Flynn et al., *Self-Settled Spendthrift Trusts Move Close to Home*, 19-SEP AM. BANKR. INST. J. 10, n.18 (2000).

139. See generally LoPucki, *supra* note 43, at 8–9 (stating that most individuals and small firms already protect most of their assets against liability); *but see* Schwarcz, *supra* note 53, at 1, 28 (disagreeing with LoPucki, arguing that “an economic analysis . . . suggests that widespread use of . . . judgment-proofing techniques is unlikely,” especially in arms length transactions).

140. LoPucki, *supra* note 43, at 89.

ii. Liability Must Be Predictable

Bankruptcy law is designed to provide a remedy for collective creditors by furthering both efficiency and distributive justice.¹⁴¹ Regardless of whether a system is pro-creditor or pro-debtor, efficiency and distributive justice can only be achieved if liability is predictable.¹⁴² Therefore, in the case of Widgets, LLC, a bankruptcy court should allow Series C to have limited liability only if creditors could expect Series C to have limited liability.

Unpredictable liability leads to inefficiency and can harm all participants in the system.¹⁴³ To maximize efficiency, creditors, affiliates, and other participants must know whom they are doing business with and the extent of that firm's liabilities.¹⁴⁴ For example, investors must be able to know how much tort risk an entity can assume, and trade partners must be able to assess each other's financial conditions.¹⁴⁵ For debtors in a system of unpredictable liability, "liability would seem to strike out of nowhere, and there would be little they could do about it except to harden their own judgment-proof structures."¹⁴⁶ The possibility of liability will only deter debtors from engaging in risky activities or insure against such activities if debtors know they can be held liable.¹⁴⁷

In the context of asset segregation, predictable liability requires identifiable, stable boundaries among and within enterprises.¹⁴⁸ Conversely, the failure of the legal system to dictate clear standards for firm boundaries makes liability unpredictable. Therefore, liability of SLLCs can be fair and predictable only if the legal system clarifies the strength of liability shields within an SLLC.

2. Possible Standards for Liability Boundaries Within SLLCs

Most legal analysts who discuss possible liability boundaries of SLLCs have focused on entity law principles.¹⁴⁹ However, a focus on pure entity law analysis limits the possibilities that courts have in determining these boundaries. Legal scholars have increasingly recognized that "entity law [is] not the inevitable product of the corporate personality but a legal concept to serve certain objectives . . ." ¹⁵⁰ The strength of a firm's liability boundaries can be placed along a continuum that ranges from impenetrable boundaries to nonexistent boundaries. This Note identifies four general

141. Kale, *supra* note 46, at 315.

142. See LoPucki, *supra* note 43, at 67–68, 71 (discussing the importance of predictable liability).

143. See *id.* (noting that arbitrary assignment of liability would generate "probably intolerable uncertainty" for investors and that those who have liability "have to know they have it").

144. See *id.* at 67–68 (listing examples of how uncertain boundaries between enterprises could lead to inefficiencies).

145. *Id.*

146. *Id.* at 71.

147. LoPucki, *supra* note 43, at 71.

148. See *id.* at 67 (suggesting that a lack of clear boundaries creates "intolerable uncertainty" where judgment creditors must litigate the boundaries of the enterprise to know which assets they could enforce against).

149. See, e.g., Gattuso, *supra* note 2, at 33 (defining an SLLC as a "separate legal entity"); LARRY E. RIBSTEIN & ROBERT R. KEATINGE, 1 RIBSTEIN AND KEATINGE ON LTD. LIAB. COS. § 4.17 (2009) (suggesting that if SLLCs are "properly designed and drafted, they may provide a safe harbor against courts' piercing the veil and holding an entity or entities liable for debts incurred by sister entities or subsidiaries").

150. BLUMBERG, *supra* note 78, at 6.

points along this continuum, which represent the basic possibilities for boundaries within SLLCs in bankruptcy.¹⁵¹

The possibilities range from those upholding the strongest boundaries to those upholding no liability boundaries at all. The first two possibilities stem from entity law.¹⁵² The first of these possibilities establishes impenetrable boundaries, treating each series as a completely separate entity with separate liability in all circumstances.¹⁵³ The second of these possibilities is a rebuttable presumption of separate entity status.¹⁵⁴ To penetrate a boundary, a creditor would use enterprise law principles to show that the series did not maintain clear, distinct boundaries.¹⁵⁵ A third possibility is pure enterprise law, which determines whether the series of an SLLC are engaged in one “enterprise.”¹⁵⁶ If they are, creditors can collect from any series in the “enterprise” or from the SLLC as a whole.¹⁵⁷ The final possibility precludes liability boundaries in all circumstances.¹⁵⁸ Precluding liability boundaries would allow a creditor of one series to collect from eligible assets of other series.

i. Option 1: Impenetrable Boundaries Between Series

The first possibility is for bankruptcy courts to treat boundaries between series in an SLLC as impenetrable by creditors of sister series. This represents pure limited liability; it is entity law with no veil-piercing remedies.¹⁵⁹ No bankruptcy court would elect to uphold series boundaries in every situation. Even traditional corporations do not have impenetrable liability boundaries; corporate veils can be pierced, and corporations in a corporate group can face substantive consolidation.¹⁶⁰ SLLC laws themselves mandate that a series will lose its limited liability if it fails to follow statutory notice and separateness requirements.¹⁶¹

Some scholars advocate *nearly* impenetrable boundaries for certain entities.¹⁶² For example, Judge Richard Posner suggests that limited liability allows for the most efficient allocation of resources.¹⁶³ However, it is important that creditors be able to cross

151. I selected these points along the boundary continuum based on parallels to the entity and enterprise law principles that courts apply to corporations and corporate groups in bankruptcy. For a general discussion of the application of these principles, see generally *id.*

152. *See supra* Part III.B.1. (discussing entity law principles in bankruptcy).

153. This represents pure entity law with no veil-piercing remedies. *See supra* Part III.B.1 (discussing entity law).

154. This represents traditional entity law as courts apply it today. *See id.*

155. *See id.* (discussing veil-piercing in entity law).

156. I derived this option from scholars advocating the use of enterprise law in place of entity law for corporate groups in bankruptcy. *See supra* Part III.B.2 (discussing enterprise law).

157. *Id.*

158. This option stems from the treatment of corporate divisions in bankruptcy. *See supra* Part III.A (discussing unincorporated corporate divisions).

159. *See supra* Part III.B.1 (discussing entity law).

160. *See supra* notes 99–101, 113–19 (discussing veil piercing and substantive consolidation).

161. DEL. CODE ANN. tit. 6, § 18-215(b) (West Supp. 2010) (listing the statutory requirement of separate records).

162. BLUMBERG, *supra* note 78, at 447 (citing Judge Posner’s economic arguments supporting limited liability from Richard Posner, *The Rights of Creditors of Affiliated Corporations*, 43 U. CHI. L. REV. 499, 514–15, 524 (1976)).

163. BLUMBERG, *supra* note 78, at 447. *But see id.* at 450 (citing recent economic literature that “has

boundaries in certain situations.¹⁶⁴ Even Judge Posner, an advocate for limited liability, who eschews substantive consolidation even where a “truly unitary business” is involved, permits consolidation when a creditor reasonably relies on the appearance of greater capitalization than actually existed.¹⁶⁵

ii. Option 2: Entity Law with Exceptions

For corporate groups in bankruptcy, entity law is the general starting point.¹⁶⁶ Under entity law, courts assume that each corporation within a corporate group is an independent legal entity with liability separate from the other corporations in the group.¹⁶⁷ Courts respect this entity separateness absent compelling circumstances that call equity into play.¹⁶⁸

Given their familiarity with the entity formula, courts will be inclined to apply this entity law framework to SLLCs in bankruptcy as well.¹⁶⁹ If courts choose this route, they will assume that each series maintains limited liability in bankruptcy.¹⁷⁰ This assumption could be rebutted through the doctrines of enterprise liability and substantive consolidation.¹⁷¹ Courts would decide whether to apply these equitable remedies by analyzing the actual boundaries between series.¹⁷² Factors affecting actual boundaries could include the financial interdependence of series, the economic integration of the SLLC, the participation by the SLLC in its series’ decision-making processes, and whether the SLLC is held out to the public as a single integrated enterprise.¹⁷³ If an SLLC fails to maintain adequate boundaries, a court may permit a creditor to reach across the boundaries and collect from sister series or the SLLC as a whole.

SLLC statutes, which emphasize an entity-like separate treatment for series in

reservations about the validity” of Posner’s argument).

164. See generally *id.* at 6–7 (describing how traditional veil-piercing developed to address cases of fraud and cases where a subsidiary served only as a “sham” or “shell”).

165. *Id.* at 447 (citing Richard A. Posner, *The Rights of Creditors of Affiliated Corporations*, 43 U. CHI. L. REV. 499, 514–15, 524 (1976)).

166. BLUMBERG, *supra* note 78, at 703.

167. See *supra* Part III.B.1 (discussing bankruptcy and entity law as applied to corporate groups).

168. *In re Owens Corning*, 419 F.3d 195, 216 (3d Cir. 2005), *cert. denied* 2006 U.S. LEXIS 3492 (May 1, 2006).

169. See Mooney, *supra* note 13, at 392 n.6 (“Bankruptcy courts likely would look first to the degree of separateness conferred on a designated series by the law of the series LLC’s state of incorporation. The court may be inclined to presume rebuttably that a designated series of a series LLC is a separate corporation for purposes of the Bankruptcy Code and may rely on the bankruptcy doctrine of substantive consolidation if necessary to remedy abuse.”). See also Gattuso, *supra* note 2, at 37 (suggesting that SLLCs should consider practices that would minimize the risk of substantive consolidation in bankruptcy); RIBSTEIN & KEATINGE, *supra* note 149, at § 4.17 (“[O]ne justification for series LLC provisions is that, if properly designed and drafted, they may provide a safe harbor against courts’ piercing the veil and holding an entity or entities liable for debts incurred by sister entities or subsidiaries.”); SYMONDS & O’TOOLE, *supra* note 42, at § 5.22[B] (noting that “given the ‘entity-like’ features of a series, it may be expected that in an appropriate case principles similar to those that justify ‘piercing the veil’ of an entity may apply to impress liabilities of a series on members of that series. . .”).

170. For examples of scholars predicting this treatment of series in bankruptcy, see *supra* note 169.

171. See *supra* Part III.B.2 for an explanation of enterprise liability, including substantive consolidation.

172. *Id.*

173. BLUMBERG, *supra* note 78, at 696 (listing the factors courts consider when determining whether to apply substantive consolidation or enterprise liability to corporate groups in bankruptcy).

SLLCs, provide support for the use of entity law for SLLCs in bankruptcy.¹⁷⁴ For example, almost every SLLC statute provides that the debts, liabilities, obligations, and expenses of one series are not enforceable against the assets of another series.¹⁷⁵ As one commentator suggests, SLLC laws “make available with respect to a designated series . . . certain liability limitations and protections traditionally expected only at the entity level.”¹⁷⁶ Under this approach, if a series failed to follow SLLC statutory guidelines for series separateness, such as maintaining separate books and records, courts could disregard that series’s liability shields by applying substantive consolidation or enterprise liability principles.¹⁷⁷

Courts should choose a body of law that best reflects the reality of practices and creditor expectations surrounding SLLCs.¹⁷⁸ Generally, courts widely apply entity law, which is steeped in traditional views of the corporate structure and the benefits of limited liability.¹⁷⁹ However, the growing application of enterprise law suggests that entity law assumptions of separateness often do not reflect reality.¹⁸⁰ For example, courts now use substantive consolidation in the majority of large public bankruptcies.¹⁸¹ In the context of SLLCs, an entity-law assumption of series separateness would be inappropriate if it was consistently rebutted. A presumption that is rebutted in most cases is a poor presumption. Such a presumption fails to aid courts in difficult situations and undermines efficiency and predictability.¹⁸²

iii. Option 3: Enterprise Law

Some may argue that courts should apply enterprise law and its doctrine of substantive consolidation to SLLCs in bankruptcy.¹⁸³ Unlike entity law, enterprise law does not begin with the assumption of liability boundaries.¹⁸⁴ Rather, enterprise law looks at the situation as a whole and determines whether various firms are engaged in a joint enterprise.¹⁸⁵ If the firms are so engaged, creditors of that “enterprise” may collect from the assets of any constituent in that “enterprise.”¹⁸⁶

174. See Mooney, *supra* note 13, at 390 (suggesting that the series separateness that is mandated by most SLLC statutes may justify separate tax treatment).

175. *Id.*; see, e.g., DEL. CODE ANN. tit. 6 §§ 18-215(b) (West 2008).

176. SYMONDS & O'TOOLE, *supra* note 42, § 5.22[A].

177. Gattuso, *supra* note 2, at 37 (suggesting practices to reduce the risk of substantive consolidation in SLLCs, including: “maintaining separate books and records, by properly documenting asset transfers, by generally acting independently of the other series within the LLC, and by not commingling assets, preparing consolidated financial statements, obtaining joint financing, or entering into loan guarantees with other series”).

178. See *supra* Part III.C.1 (discussing the importance of predictable liability).

179. See *supra* Part III.B.1 (explaining the history and current dominance of entity law).

180. See *supra* Part III.B.2 for the discussion of the rise of substantive consolidation and enterprise liability as a way to better reflect the reality of corporate group practices.

181. Widen, *supra* note 44, at 3, 28.

182. See, e.g., BLUMBERG, *supra* note 78, at 7–8 (criticizing the “hundreds of irreconcilable cases” resulting from the indiscriminate and highly fact-based application of veil-piercing to rebut entity law presumptions in corporate group bankruptcies).

183. See Powell, *supra* note 1, at 17 (suggesting that courts may be willing to apply substantive consolidation to SLLCs).

184. See *supra* Part III.B.2 (discussing enterprise law principles).

185. *Id.*

186. See *supra* text accompanying note 105 (explaining that enterprise liability, if successfully invoked,

Pure enterprise law is rare; however, Phillip I. Blumberg advocates enterprise law “to respond to the changing business reality,” such as “the special problems presented by corporate groups.”¹⁸⁷ Another advocate of enterprise law, Professor Jonathan Landers, suggests substantive consolidation as a general rule when a parent and subsidiary are both bankrupt.¹⁸⁸ Landers provides only two exceptions where substantive consolidation would not be appropriate: (1) if consolidation would substantially prejudice a creditor who reasonably relied on the credit of one component of the group; or (2) if the parent “clearly had reason to treat the constituent corporations as separate entities,” the economic conduct of constituents is kept “rigidly separate,” assets and capital are not shuffled between constituents, and the constituents are not managed as a single enterprise.¹⁸⁹

The Maine court in *GxG Management* used an enterprise-like approach to determine whether an SLLC could sue on behalf of its series.¹⁹⁰ The court did not begin with an assumption that Series B had an identity separate from its SLLC.¹⁹¹ Instead, the court looked at the situation as a whole and determined that both Series B and its parent SLLC shared an interest in the boat that was the subject of litigation.¹⁹² The court concluded that Series B had its own special “interests” in the boat, but that it was not a separate legal entity.¹⁹³

The main criticism of enterprise liability is its potential unpredictability.¹⁹⁴ Enterprise law places a large amount of discretion in the hands of bankruptcy judges and, therefore, results can vary widely.¹⁹⁵ For example, “substantive consolidation presents an indeterminate risk to the ‘expectations’ parties have when entering into contracts, because it is becoming increasingly difficult to determine the doctrine’s applicability.”¹⁹⁶

Another criticism involves the harm that substantive consolidation can inflict on creditors of the debtor’s parent or sister entities.¹⁹⁷ If a court applies substantive consolidation to an SLLC’s series, secured creditors of one series might collect less due to substantive consolidation.¹⁹⁸ Through substantive consolidation, courts pool all assets

allows creditors to collect from the enterprise).

187. BLUMBERG, *supra* note 78, at 703.

188. Jonathan Landers, *A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy*, 42 U. CHI. L. REV. 589, 628–33 (1975); *see generally* Jonathan Landers, *Another Word on Parents, Subsidiaries, and Affiliates in Bankruptcy*, 43 U. CHI. L. REV. 527 (1976) (rebutting criticisms of substantive consolidation).

189. *Id.* (citing Jonathan Landers, *A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy*, 42 U. CHI. L. REV. 589, 633–34, 639–40 (1975)).

190. *GxG Mgmt. LLC v. Young Bros. and Co.*, Civil No. 05-162-B-K, 2007 WL 551761, at *7–8 (D. Me. 2007).

191. *Id.* at *7.

192. *Id.* at *7–8.

193. *See supra* notes 40–41 and accompanying text.

194. *See, e.g.*, LoPucki, *supra* note 43, at 69 (arguing against enterprise law, because it “will deprive the system of [entity law,] a fundamental concept for ordering and specifying liability”).

195. Kale, *supra* note 46, at 336–37.

196. *Id.* at 337 (quoting Christopher W. Frost, *Organization Form, Misappropriation Risk, and the Substantive Consolidation of Corporate Groups*, 44 HASTINGS L.J. 449, 460 (1993)); *see also* Widen, *supra* note 44, at 26 (“Uncertainty surrounds use of substantive consolidation doctrine in bankruptcy proceedings.”).

197. Kale, *supra* note 46, at 332–33.

198. *Id.* at 332.

2010]

Series LLCs: The Asset Protection Dream Machines?

819

and force creditors of different entities to collect from the single pool of assets.¹⁹⁹ The percentage recovery of each creditor changes, “for better or worse,” under substantive consolidation.²⁰⁰ The potential inequitable treatment of creditors is a key reason that courts have advised using substantive consolidation sparingly and as a last resort.²⁰¹

iv. Option 4: No Boundaries Between Series in Bankruptcy

The final option for courts is to not recognize any liability boundaries between series in bankruptcy. This option is similar to the treatment of unincorporated operating divisions within a corporation or within a traditional LLC.²⁰² Unincorporated operating divisions are not separate legal entities.²⁰³ They are merely part of the corporation or LLC as a whole.²⁰⁴ Therefore, a division enjoys no limited liability separate from the corporation or LLC to which it belongs.²⁰⁵

For SLLCs, a bankruptcy court could deny a series limited liability by refusing to recognize a series as a “person” within the meaning of the Bankruptcy Code. Refusing to recognize a series as a “person” would preclude a series from filing for bankruptcy independent of the master SLLC.²⁰⁶ Even though several state SLLC statutes define series as “persons,” bankruptcy courts are not bound by those definitions.²⁰⁷

In this scenario, an insolvent series could not file for bankruptcy on its own. It would have to turn to sister series or its master SLLC for financial assistance. If the SLLC lacked the assets necessary to remove its series from insolvency, the entire SLLC would have to file for bankruptcy. If the SLLC filed for bankruptcy, courts would not recognize series liability boundaries and would pool the assets of all the series in the bankruptcy estate. The same applies for unincorporated operating divisions: one division’s insolvency can force an entire corporation to file for bankruptcy, at which point the courts pool the assets of all the divisions in the bankruptcy estate.²⁰⁸

IV. RECOMMENDATION

Whether a series can file for bankruptcy, and if so, whether courts will grant it limited liability, depends on the goals of bankruptcy law. Bankruptcy goals include “protect[ing] . . . the interests of creditors and the equitable distribution of the assets of

199. *Id.*

200. Widen, *supra* note 44, at 1.

201. Kale, *supra* note 46, at 332–33; *see, e.g., In re Owens Corning*, 419 F.3d 195, 210 (3d Cir. 2005), *cert. denied* 2006 U.S. LEXIS 3492 (May 1, 2006) (“[B]ecause substantive consolidation is extreme (it may affect profoundly creditors’ rights and recoveries) and imprecise, this ‘rough justice’ remedy should be rare and, in any event, one of last resort after considering and rejecting other remedies . . .”).

202. *See supra* Part III.A (defining unincorporated corporate divisions and discussing their treatment in bankruptcy).

203. W. FLETCHER, CYCLOPEDIA OF THE LAW OF CORPORATIONS, § 4233.50 (West 2008).

204. *Id.*

205. *Id.*

206. *See supra* Part III.B.1.

207. *Id.*

208. Because a “division” is not recognized as a “person” within the Bankruptcy Code, it cannot file for bankruptcy on its own. *See supra* Part III.A.

the debtor's estate."²⁰⁹ This Part recommends that courts can best protect creditor interests and ensure equitable asset distribution by not allowing a series to file for bankruptcy. Alternatively, if a court does allow a series to file for bankruptcy, it should allow creditors to access the assets of related series and the SLLC as a whole.

A. Bankruptcy Courts Should Not Permit a Series to File for Bankruptcy Independently of Its SLLC

Bankruptcy courts should not allow a series to file for bankruptcy independently of its SLLC, because a series does not fit the definition of "person" under the Bankruptcy Code. The definition of a "person" in the Code lists individuals, partnerships, and corporations.²¹⁰ Although this definition is not exhaustive, its extension is limited.²¹¹ For example, bankruptcy courts consider LLCs to be "persons," even though LLCs are not listed in the Code's definition of "person."²¹² An LLC is a "person" because it shares so many similarities to a corporation that "there is no reason that [an LLC] is ineligible to be a debtor under the Code."²¹³ Unlike an LLC, an individual series shares few structural similarities with a corporation or a partnership.

Most importantly, the individuals, partnerships, and corporations listed as "persons" under the Code are all separate legal entities that can exist independently of other entities.²¹⁴ An LLC, like a corporation or a partnership, is also a legal entity that can exist on its own.²¹⁵ On the other hand, the only court to address the issue determined that the series in question was not a separate legal entity.²¹⁶ Additionally, a series cannot exist independently of its SLLC, and it only gains existence through its SLLC's charter.²¹⁷ Even under the Delaware, Illinois, and Iowa statutes, which define series as "persons" or separate "entities," a series derives its "personage" from the LLC that formed the series through the certificate of formation.²¹⁸ Therefore, "a 'series' does *not* appear to be [a

209. BLUMBERG, *supra* note 78, at 696; *see supra* text accompanying notes 87–91 (discussing the basics of bankruptcy law governing corporate groups).

210. 11 U.S.C. § 101(41) (2006).

211. *See supra* note 66 and accompanying text (citing the Bankruptcy Code's definition of "person").

212. *See* Wooster, *supra* note 67 and accompanying text (explaining that LLCs are not listed in the Bankruptcy Code's definition of "person," yet courts generally treat them as "persons").

213. *In re Midpoint Dev., L.L.C.*, 313 B.R. 486, 489 (Bankr. W.D. Okla. 2004) *rev'd on other grounds by In re Midpoint Dev., L.L.C.*, 466 F.3d 1201 (10th Cir. 2006).

214. *See* Powell, *supra* note 1, at 16 (suggesting that "series are something other than separate and distinct entities," because "series cannot exist absent the continued existence of a Series LLC," and because series "need not file anything with the Secretary of State"). At the same time that Powell rejects treating series as distinct entities, he notes that treating series as a single entity "would seem to frustrate a primary purpose of [the SLLC statutes]." *Id.* Ultimately, Powell rejects both a single-entity model and a multi-entity model for SLLCs in favor of his "Quasi-Trust Model." *Id.* Powell's "Quasi-Trust Model" focuses on the fact that "a Series LLC has no beneficial interest in assets held in series, nor does a series have a beneficial interest in assets held in a separate series, in each case unless otherwise provided in the [LLC] agreement." *Id.* at 16.

215. *See* Wooster, *supra* note 67 (explaining that LLCs are not listed in the Bankruptcy Code's definition of "person," yet courts generally treat them as "persons").

216. *GxG Mgmt. LLC v. Young Bros. and Co., Inc.*, Civil No. 05-162-B-K, 2007 WL 551761, at *7–8 (D. Me. Feb 21, 2007; *see supra* text accompanying notes 190–93).

217. *See supra* Part II.A.1 (outlining Delaware statutory requirements to form a series in an SLLC).

218. Conaway, *supra* note 16, at 700-01.

2010]

Series LLCs: The Asset Protection Dream Machines?

821

truly] independent ‘entity’ [under the state SLLC statutes].”²¹⁹ The state SLLC statutes that define a series as a “person” do so for convenience—to allow a series to contract and own assets in its own name, for example—not to establish a series as an “independent legal entity.”²²⁰

Refusing to allow series to file for bankruptcy is the best way to ensure the orderly, predictable, and reasonable management of debt. A series, unlike a corporation or LLC, does not present itself to the world as a separate legal entity.²²¹ Therefore, for reasons of fairness and predictability, courts should not treat a series as a separate legal entity in bankruptcy.

B. Bankruptcy Courts Should Not Permit Series Limited Liability

1. Eliminating Series Limited Liability Improves Predictability and Fairness

If a bankruptcy court allows a series to file for bankruptcy independently, or if an SLLC files for bankruptcy, courts should not limit liability between the series. Instead, courts should follow the fourth option in the liability continuum by disregarding series boundaries in bankruptcy.²²² Eliminating series boundaries in bankruptcy will increase predictability and decrease litigation; it is the most efficient, most logical, and fairest option on the liability continuum.²²³ This Part lists equitable considerations that courts consider when they disregard liability boundaries in corporate groups.²²⁴ These considerations include whether the group engages in essentially one business, the integration of the group’s external operations, and the integration of the group’s internal operations.²²⁵ This Part then demonstrates how courts can apply these equitable considerations to SLLCs to justify disregarding series liability boundaries within SLLCs.

i. Series Engaging in a Common Business

The first factor supporting consolidation is whether the debtor and affiliates in the debtor’s group engage in a similar nature of the business.²²⁶ The nature of the business of each series within a parent SLLC is likely substantially similar to that of the other series within the same parent SLLC. The multiple series of an SLLC generally all engage in a

219. *Id.* at 701 (emphasis in original).

220. *Id.*; see also SYMONDS & O’TOOLE, *supra* note 42, § 5.22 n.506 (explaining that the DLLCA 2006 amendment defining a series as a “person” was not intended to “signify a change in the nature of a series” but rather “to confirm that membership in a Delaware [LLC] . . . and the status, rights, and obligations attendant thereto, may be assets (and, as appropriate, liabilities, associated with a series of a series entity Such series is not a separate legal entity.”).

221. See *infra* notes 238–39 (discussing the likelihood that all series in an SLLC likely share common names, logos, etc.).

222. See *supra* Part III.C.2.iv for a discussion of this option.

223. See SYMONDS & O’TOOLE, *supra* note 42, § 5.22[A] (“The absence of clear or uniform legal authority regarding the treatment of series produces uncertainty and risk, especially when a series limited liability company becomes involved in litigation, or interacts with a governmental regulatory agency.”).

224. See BLUMBERG, *supra* note 78, at 696–99 (listing factors considered in applying substantive consolidation).

225. *Id.*

226. See *id.* at 699 (listing “the different nature of the business of the debtor and affiliates within a conglomerate group” as a miscellaneous factor in determining boundaries in corporate groups).

single business, much more so than most corporations in a corporate group do. For example, in financial-based SLLCs, a series may simply represent one of many accounts or investment pools.²²⁷ Other SLLCs use each series to hold one of many parcels of real estate.²²⁸ In the context of corporate groups, legal scholars have stated that “fragmentation of one economic enterprise into many corporations may be considered as an abuse of the corporate form”²²⁹ “[A] corporation should not be able to artificially carve up what is essentially one business in a way that prejudices creditors’ ability to have recourse against the assets of that one business.”²³⁰ Similarly, allowing an SLLC to split assets to avoid liabilities of a shared business is inequitable.

ii. Series External Integration

Series in an SLLC also display high external integration as compared to corporations in most corporate groups. First, whereas a corporation in a corporate group must present itself to the world as a separate legal entity—it must have its name on the door and maintain a recognizable separate identity—a series does not face these requirements.²³¹ By law, a series cannot exist independently of an SLLC.²³² A series’s right to exist stems from its inclusion in its SLLC; a series cannot be a stand-alone business entity.²³³ A series is created as a division within the master SLLC with little additional filing.²³⁴ Therefore, a series in an SLLC behaves much like a division within a corporation.²³⁵

Second, the external operations of a series and its SLLC are highly integrated, which weighs heavily against series limited liability in bankruptcy.²³⁶ Creditors and other constituents need to know whom they are dealing with in order to maximize business efficiency and equity.²³⁷ To determine the level of integration of external operations, courts might consider many of the factors that courts use in substantive consolidation cases: whether the series shares a name, a logo, trademarks, national advertising campaigns, and/or consolidated annual reports; and/or whether they represent themselves to the public as offices, branches, divisions, or other integral parts of the SLLC.²³⁸ These factors weigh heavily toward series integration.

227. *Choice of Business Entity*, *supra* note 5 (noting that series can compartmentalize funds or portfolios by placing each portfolio in its own series).

228. *Id.*; *see also* Gattuso, *supra* note 2, at 35–36 (“[R]eal estate investors frequently utilize Series LLCs to hold multiple parcels of real estate.”).

229. Kale, *supra* note 46, at 343 (quoting Mary Elisabeth Kors, *Altered Egos: Deciphering Substantive Consolidation*, 59 U. PITT. L. REV. 381, 435–36 (1998)).

230. *Id.*

231. DEL. CODE ANN. tit. 6, § 18-215 (West 2009).

232. *See supra* Part II.A.1 (outlining Delaware statutory requirements to form a series in an SLLC).

233. *Id.*

234. *Id.*

235. *See* Unincorporated Operating Division, 9 FLETCHER CYCLOPEDIA CORPORATIONS § 4233.50 (West 2008) (explaining that unincorporated corporate divisions are not legal entities and enjoy no limited liability).

236. *See* BLUMBERG, *supra* note 78, at 695–96, 698–99 (listing factors that would support a finding of integration).

237. *See supra* notes 144–45 and accompanying text (explaining that there is a need to know a firm’s liability and risks).

238. BLUMBERG, *supra* note 78, at 695–96, 698–99.

The law permits series' names to be nearly indistinguishable.²³⁹ Most series' names follow the same pattern—each series carries the name of the parent SLLC and a distinguishing number or letter.²⁴⁰ For example, the names of series in Widgets, LLC, might be “Widgets, LLC, Series A,” “Widgets, LLC, Series B,” and “Widgets, LLC, Series C.” Few third parties reading these names would assume each series was a separate entity with limited liability. The similarity of these names supports substantive consolidation, because similar names represent to the public that the series are offices, branches, divisions, or other integral parts of the SLLC.²⁴¹ The public may be further misled if a series shares a common logo, trademark, or advertising campaign with its SLLC.²⁴² Additionally, a series faces surprisingly few requirements to notify third parties of its limited liability. Proper notice requires only that the SLLC's certificate of formation filed with the Secretary of State contain a general “reference” to the limitation of liability of each series.²⁴³ The notice does not need to reference any specific series in the SLLC.²⁴⁴

iii. Series Internal Integration

Another factor supporting substantive consolidation is the “integration of internal operations of the debtor and the group.”²⁴⁵ While SLLC laws require series to separate certain internal operations from other series and the SLLC,²⁴⁶ many internal operations will likely remain integrated with the SLLC. Examples of integrated internal practices in SLLCs might include shared insurance coverage, participation in group employee training programs, exchange of information and reporting, group visitation and inspection programs, group auditing controls, and a series's reliance on other series or the SLLC for administrative support services, such as personnel, advertising, and legal services.²⁴⁷

Other factors affecting the interrelationship of corporations within a corporate group focus on specific internal practices rather than structure.²⁴⁸ Because specific practices can vary widely between SLLCs, these factors can be helpful but do not readily lend themselves to this generalized analysis. These factors include: (1) the financial structure of a series, including the adequacy of initial capitalization and the extent of intragroup loans and guarantees; (2) the commingling of accounts and shuttling of assets; (3) the behavior of series and the SLLC shortly prior to or after bankruptcy, including intragroup transfers; (4) the separateness of a series's books, accounts, and director and shareholder

239. The Delaware Code has no requirement that series names be readily distinguishable from sister series or the SLLC. DEL. CODE ANN. tit. 6, §§ 18-215 (West 2009). Illinois mandates that each series include the full name of the SLLC and be distinguishable from the names of other series. 805 ILL. COMP. STAT. ANN. 180/37-40(c) (West 2009).

240. This practice is basically mandated in Delaware. DEL. CODE ANN. tit. 6, §18-215 (b) (2008).

241. See BLUMBERG, *supra* note 78, at 699 (listing representations that a corporation is an office, branch, division, or integral part of the group as a factor supporting substantive consolidation in corporate groups).

242. *Id.*

243. DEL. CODE ANN. tit. 6, § 18-215(b), (c) (2009).

244. *Id.* § 18-215(b).

245. See BLUMBERG, *supra* note 78, at 698 (discussing substantive consolidation).

246. See *supra* note 19 and accompanying text for separate records requirements.

247. *Id.* (including these factors as variables affecting the integration of internal operations).

248. See BLUMBERG, *supra* note 78, at 696–99 (discussing the factors affecting the interrelationship of corporations within a corporate group).

meetings; (5) whether a series has separate directors, officers, employees, and offices; and (6) the extent of participation by the SLLC in a series's decision-making.²⁴⁹

2. Neither a Rebuttable Presumption of Limited Liability nor Enterprise Law Is Practical in SLLC Bankruptcies

Applying either a rebuttable presumption of limited liability or enterprise law is illogical for series in bankruptcy. Under either approach, the same factors supporting my recommendation²⁵⁰ would consistently lead courts to disregard series' boundaries. If bankruptcy courts began with the rebuttable presumption that each series had limited liability, more often than not creditors would rebut that presumption,²⁵¹ and courts would apply substantive consolidation. Even supporters of limited liability for series concede that "series LLCs may be at a greater risk for substantive consolidation than individual LLCs," especially because any internal liability boundaries dissipate if any statutory criteria for formation are not satisfied.²⁵²

Alternatively, if bankruptcy courts begin with enterprise law, more often than not creditors will show that the SLLC is one enterprise, and courts will not allow series limited liability.²⁵³ Both approaches lead to the same result as this Note's recommendation, but the approaches involve much greater uncertainty and much more litigation. Under either "assumption" approach, courts would have to analyze each of the factors listed in the prior Part in every case. Under either standard, the anomalous cases—where courts would uphold series boundaries—would not justify the expense and uncertainty of litigating boundaries in every SLLC bankruptcy case.

V. CONCLUSION

Bankruptcy courts can prevent a race to the judgment-proofing bottom by applying a fair and predictable standard to SLLC legal personhood and legal boundaries. First, courts should not recognize a series as a "person" under bankruptcy law.²⁵⁴ Refusing to recognize a series as a "person" will preclude a series from filing for bankruptcy in federal court.²⁵⁵ This predictable, efficient approach will prevent excessive judgment-proofing through SLLCs.²⁵⁶ Second, if a bankruptcy court allows a series to file

249. *Id.*

250. See *supra* Part IV.B.1.i–iv (recommending that bankruptcy courts should not permit series limited liability).

251. For example, "the first test of substantive consolidation allows consolidation when the debtor intentionally or inadvertently misleads creditors into believing multiple entities are one entity." *In re Owens Corning*, 419 F.3d 195, 211 (3d Cir. 2005), *amended by* 2005 U.S. App. LEXIS 18043 (3d Cir., Aug. 23, 2005). It takes no stretch of the imagination to see that creditors of a series easily could be misled into believing the series and the SLLC are one entity.

252. Gattuso, *supra* note 2, at 37.

253. See *supra* Part IV.B.1 for SLLC factors supporting substantive consolidation.

254. See *supra* Part II.D (discussing that an SLLC cannot file for bankruptcy unless an SLLC is defined as a "person" under the Bankruptcy Code and that no court has addressed the issue of whether an SLLC is a "person" under the Bankruptcy Code).

255. *Id.*

256. See *supra* Part IV.A (arguing that "for . . . predictability, courts should not treat a series as a separate legal entity in bankruptcy").

2010] *Series LLCs: The Asset Protection Dream Machines?* 825

independently, or if an SLLC files for bankruptcy, the court should not permit limited liability for each series.²⁵⁷ Unlike corporations, series do not present themselves to the world as separate legal entities. To avoid unjust results, courts should not shield liabilities and assets of one series from those of sister series or the master SLLC. If Julie wants to separate assets from liabilities, she can still use traditional asset-separation techniques, such as forming several separate LLCs, which involve less risk of leading creditors and debtors astray.

257. *See supra* Part IV.B (arguing that bankruptcy courts should not permit series limited liability).