



## Using LLCs for succession planning - by Thomas Kearns

March 19, 2019 - Front Section

The banks that give commercial mortgages and the institutions that invest equity into commercial real estate transactions always impose controls over the identity of the individuals who manage the borrower/joint venture. The controls include restrictions on transfers of controlling economic interests and on which individuals can exercise the management rights of the developer in the deal. So if Mary Developer convinces Big Hedge Fund Inc. to invest in a new deal and then obtains a loan from Bank, both the agreement with the Fund and the loan agreement will name Mary as the approved control person and place restrictions on what Mary can do with her economic interest in the deal and on whether Mary can quit and place her successor in charge.

Limited liability companies are typically the vehicle used for these investments. The LLC statutes in Delaware in particular, but also in New York and other states, generally permit the parties to create customized contractual rights in the agreement governing the LLC. In my example above, Mary could negotiate with the Fund in the LLC agreement governing the joint venture and with the Lender in the loan agreement to permit Mary Jr., her daughter who is active in the business, to replace her mother if Mary Sr. should become disabled or die.

The best way to address these issues is by creating an LLC to hold Mary's management rights. That LLC would:

- (i) Be the manager of the company formed with the Fund and be a party to the LLC agreement covering that company;
- (ii) Be owned by Mary alone or with her colleagues or family; and
- (iii) Be governed by its own LLC agreement containing the succession mechanism.

This structure avoids any need to formally substitute a new manager of the LLC with the Fund if Mary Sr. becomes disabled or dies. It also potentially limits Mary's exposure to personal liability by imposing an additional limited liability entity in the organization chart. This LLC structure also permits Mary to bring in investors at her level and share any profits or fees from the deal and, if the interest is small enough, to do so without obtaining the Fund's or the Bank's consent.

The succession provisions in LLC agreements can be elaborate—we did one for a multi-pronged family in its third generation complete with meeting and voting provisions and an arbitration mechanism with a pre-selected “rabbi”—or they can be as simple as in the following example:

“Mary Sr. shall have sole authority to manage this LLC provided that if Mary Sr. is unavailable due to illness, disability or death, Mary Jr. shall have full authority to manage this LLC during the period of Mary Sr.’s unavailability and shall have full authority to manage this LLC after Mary’s death or permanent disability.”

Thomas Kearns is a partner with Olshan Frome Wolosky LLP’s real estate department, New York, N.Y.

New York Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540