

“New Market Tax Credit Transactions -- Tips in Using Delaware LLCs”

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I. Introduction

The entity of choice for tax credit investment funds, specifically in the new market tax credit (“NMTC”) area, is the limited liability company (the “LLC”). The choice of jurisdiction for LLCs is Delaware.

II. Formation and Purpose

An LLC must have a limited liability company agreement or operating agreement. Although such agreement in Delaware may be oral or implied, it is suggested that there be a short-form agreement at or about the time of the filing of the LLC’s certificate of formation. In this way, the LLC will have a written agreement in place prior to entering into any agreement, such as an allocation agreement, pre-investor member. Make sure to include in the operating agreement, as a purpose, the entry into allocation agreements or admission to lower-tier operating partnerships or LLCs, but be careful not to limit entry into any particular allocation agreement or operating entities so as to provide for greater flexibility. At the time the principal investor is admitted to the LLC, the agreement is expanded to reflect the parties’ business arrangement and tax credit matters.

III. Authority

Provide in the initial operating agreement for a manager or designate officers who may execute allocation agreements and operating entity documents without the need for member approval. This may avoid the need for resolutions by the member. However, even if you have authorizations in the operating agreement to enter into such agreements, be prepared to provide specific written resolutions by the member of the LLC.

IV. Flexibility

The hallmark of the Delaware LLC is its flexibility. Although the Delaware Limited Liability Company Act (the “LLC Act”) provides for default governance provisions in the event the operating agreement does not address certain matters, for the most part, the parties are free to address in the operating agreement the terms of investment, capital contribution and distribution, management and governance, allocation of profit and loss, voting and consent rights, information rights, liability, indemnification and dissolution.

V. Opinions

Be prepared to have a Delaware legal opinion in addition to any tax opinions regarding, among other matters, the formation of the fund, the enforceability of its operating agreement and the authority of the fund or its managing member to enter into transaction documents. In the case of NMTC allocation agreements with the CDFI Fund,* identify who will be the reviewer of documentation, including legal opinions, at the CDFI Fund and establish a contact early in the process. Reviewers may have varying comments on opinions and understanding the variations will avoid unanticipated delays.

VI. Summary

For the same reasons that the Delaware LLC is the choice generally for investment vehicles in connection with commercial and business transactions, it is also the choice of entity in the NMTC area. However, it is critical that counsel take advantage of the flexibility offered by the Delaware LLC and at the same time reflect the basic terms governing the entity in a written agreement at the time the LLC Certificate of Formation is filed.

This document is prepared for information purposes only. Please contact Ellisa Opstbaum Habbart at ehabbart@delawarecounselgroup.com or James C. Strum at jstrum@delawarecounselgroup.com if you have specific questions regarding this information. The Delaware Counsel Group LLP, Attorneys At Law, advises clients worldwide on Delaware corporate and alternative entity transactions. Their experience in complex Delaware transactional matters distinguishes The Delaware Counsel Group LLP as a leading Delaware-based law firm. The firm is recognized by Chambers USA as a leading law firm in Delaware Corporate/Mergers and Acquisitions law and founding partner Ellisa Opstbaum Habbart is listed as one of Delaware’s top alternative business entity lawyers. The firm is rated “AV” by Martindale Hubbell. Copyright © 2010.

* The CDFI Fund is short for Community Development Financial Institutions Fund.

