

The Emerging LLC and LLP Case Law: A
Survey of Cases Dealing With Registered
Limited Liability Partnerships and
Limited Liability Companies

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The Emerging LLC and LLP Case Law:
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Elizabeth S. Miller

I. Introduction

This paper summarizes cases that deal with limited liability company (LLC) and registered limited liability partnership (LLP) issues. Since these entities are of relatively recent origin, it will be some time before a substantial body of case law on these entities has developed. LLP cases number far fewer than LLC cases at this point. LLC cases have appeared with greater frequency and there is a growing number of cases in some significant areas such as veil piercing and fiduciary duties. Many of the opinions included below are unpublished and thus have limited precedential value. They are included, however, to illustrate the types of issues that have arisen and how the courts have dealt with them. Predictably, courts tend to analogize to corporations and partnerships when faced with LLC issues, and the results in the cases are generally not too surprising. In some cases, the courts do not appear to realize that they are dealing with an entity other than a corporation. In a few cases, the courts have not only recognized that an LLC is a distinct type of entity but have therefore refused to find corporate or partnership cases persuasive with respect to a particular issue.

One thing that becomes clear in reading the cases is that litigants, courts and headnote writers are struggling with the terminology and nature of LLCs and LLPs. Research of the case law is somewhat impeded by the fact that published LLC cases are digested under the "Corporations" (most often) or "Partnerships" (occasionally) topics of the West digest system, and the headnotes sometimes fail to indicate that the case involves an LLC. Mistaken references to limited partnerships as LLPs and vice versa, to LLCs as corporations (or "limited liability corporations"), to members as shareholders or partners, etc. appear with disturbing frequency. The development of a clear, well-reasoned body of case law dealing with the newer types of unincorporated entities will depend in large part on how effectively litigants educate courts as these cases arise.

II. Cases Involving Registered Limited Liability Partnerships

There are as of yet relatively few decisions dealing with limited liability partnership issues. Set forth below is a summary of cases that have appeared to date.

A. Suits By and Against Foreign LLPs: Personal Jurisdiction, Venue, etc.

Cadlerock Properties Joint Venture, L.P. v. Schilberg, 30 Conn. L. Rptr. 85, 2001 WL 950233 (Conn. Super. July 17, 2001)(holding that factual dispute regarding foreign LLP's transaction of business in Connecticut precluded summary judgment on ground that failure to register as foreign limited liability partnership precluded maintenance of suit).

Liberty Mutual Insurance Company v. Gardere & Wynne, L.L.P., Civ. A. No. 94-10609-MLW, 1994 WL 707133 (D. Mass. Dec. 6, 1994).

Issues discussed in this case include the capacity of an LLP to be sued, jurisdiction over partners of the LLP, the treatment and status of various partners of the LLP, and choice of law. The court addressed these issues as they related to the court's consideration of the defendants' motion to transfer venue from Massachusetts to Texas. The case was brought by Liberty Mutual Insurance Company ("Liberty Mutual") in federal district court in Massachusetts against a Dallas law firm, Gardere & Wynne, L.L.P. (Gardere & Wynne), a Texas registered limited liability partnership, and two Gardere & Wynne attorneys.

Gardere & Wynne frequently represented Liberty Mutual in litigation involving Liberty Mutual and its insureds. Two attorneys, Nabors and Woods, left another Texas law firm to join Gardere & Wynne (Nabors as a partner and Woods as an associate), bringing with them a client whose interests were adverse to Liberty Mutual in some pending litigation. Liberty Mutual sued Gardere & Wynne, Nabors, and Woods in Massachusetts for breach of fiduciary duty in connection with the handling of a conflict of interest. The defendants moved for dismissal or transfer of the case to

Texas. The court pointed out that a number of thorny issues would be avoided or best resolved if the case were litigated in Texas. Thus, the court concluded that the litigation should be transferred to Texas under 28 U.S.C. § 1404(a).

Under the rule governing suits against general partnerships in Massachusetts, Liberty Mutual would have had to name and serve each partner individually. In contrast, Texas law permits a partnership to sue and be sued in the partnership name (and service upon one partner will constitute service on the partnership). The court noted that a plaintiff may sue a limited partnership in Massachusetts by naming only the general partners and speculated that it might be possible to characterize an LLP as a limited partnership and bring suit by naming only those partners that would be personally liable for the claims Liberty Mutual was asserting. However, this would have required the court to determine whether a breach of fiduciary duty claim fell within the liability protection provided by the Texas statute at the time and, if so, whether some or all of the partners would nevertheless be liable under certain other provisions of the act. The court was reluctant to delve into these unsettled questions of Texas law, especially in the preliminary context of a motion to dismiss. Transfer of the suit to Texas, where suit could be maintained against the partnership in its common name and without joining all partners, obviated the need for such a determination as a threshold matter.

Nabors and Woods sought to dismiss the Massachusetts lawsuit brought by Liberty Mutual based upon lack of personal jurisdiction. Though there had been other partners of Gardere & Wynne who had visited Liberty Mutual at its Boston office over the years, the court observed that it would not have jurisdiction over either Nabors or Woods based solely on their own personal contacts with Massachusetts. Jurisdiction over them would have to be based upon the contacts by other partners, who, by operation of partnership law, were acting as agents of Nabors and Woods. The court noted that personal jurisdiction over a person may be based upon acts of the person's agent or business partner but noted a number of factors complicating the analysis in this case, including whether Woods had become a partner at all, whether jurisdictional contacts of partners could be used to maintain jurisdiction over other partners who were admitted after those contacts occurred, and whether jurisdiction could be predicated on contacts of partners of an LLP who may not be vicariously liable on the underlying claim. None of these questions had to be decided upon transfer of the case to Texas because the Texas district court would unquestionably have jurisdiction over all the defendants.

The court noted that there would ultimately be difficult issues of Texas law involved in litigation of the merits of the case, and a Texas court would be best suited to determine these. The court as well as the parties evidently assumed that the Texas LLP statute would be given effect and that Texas law would govern the extent to which damages and injunctive relief could be granted against partners other than those directly involved in the alleged wrongdoing. The court noted, however, that the issues involving Gardere & Wynne's conflicts of interest and compliance with rules of ethics might be governed by national standards.

UOP v. Andersen Consulting, No. CV 95014753S, 1995 WL 784971 (Conn. Super. 1995).

Defendant Andersen Consulting, L.L.P. ("AC LLP"), an Illinois registered limited liability partnership, argued that it was a foreign partnership within the meaning of the Connecticut long arm statute and that the long arm statute did not authorize personal jurisdiction over AC LLP because the suit did not arise out of the transaction of any business in Connecticut. The plaintiff argued that, because AC LLP had partners who resided in Connecticut, AC LLP was a citizen of Connecticut and not a "foreign partnership" under the long arm statute. Since the long arm statute did not define "foreign partnership," the court looked at other definitions. It looked at the definition of a foreign limited partnership and the definition of a foreign registered limited liability partnership in the partnership statutes and concluded that AC LLP was a foreign partnership under the long arm statute. However, the court concluded that the requirements of the long arm statute had been met.

B. Diversity Jurisdiction

In the following cases, the courts have held that the citizenship of an LLP for diversity jurisdiction purposes depends upon the citizenship of all of its partners. In other words, an LLP is a citizen of each state in which a partner resides. This rule follows from the United States Supreme Court case of *Carden v. Arkoma Associates*, 494 U.S. 185 (1990). In *Carden*, the Court reiterated the rule that the citizenship of an unincorporated association is determined based upon the citizenship of all of its members. Specifically, the Court held that a limited partnership is a citizen of every state in which a general or limited partner resides.

Conk v. Richards & O'Neil, LLP, 77 F. Supp.2d 956 (S.D. Ind. 1999).

Cohen v. Kurtzman, 45 F. Supp.2d 423 (D.C. N.J. 1999).

In this case, the presence of diversity jurisdiction turned upon whether the defendant law firm was a sole proprietorship or a limited liability partnership. The plaintiff argued that the law firm's registration as an LLP was a

fraud and that the firm was in fact and substance a sole proprietorship. However, the court found that the evidence overwhelmingly established that the firm was a New York LLP. Diversity was thus lacking because one of the partners was domiciled in the plaintiff's state of domicile, New Jersey. The court imposed Rule 11 sanctions against the plaintiff for failing to make a good faith effort to determine the status of the LLP law firm.

ALMS, Ltd., L.L.P. v. Barnes, No. Civ. A. 3:98-CV-1784-P, 1998 WL 907034 (N.D. Tex. Dec. 16, 1998).

ALMS, Ltd., L.L.P. v. Guzman, No. Civ. A. 3:98-CV-1798G, 1998 WL 684245 (N.D. Tex. Sept. 25, 1998).

Mudge Rose Guthrie Alexander & Ferdon v. Pickett, 11 F. Supp.2d 449 (S.D. N.Y. 1998).

After concluding that a registered limited liability partnership is a citizen of every state of which any of its partners is a citizen for diversity jurisdiction purposes, the court discussed the effect of the resignation of partners and dissolution of the partnership. The court concluded that, since a dissolved partnership continues to exist until winding up is completed, the partnership continues to exist and is a citizen of every state of which any of its partners was a citizen at the time the action was commenced. In the course of its discussion, the court commented by way of footnote that the New York "statute clearly enunciates that a general partnership that is registered as a RLLP is for all purposes the same entity that existed before registration and continues to be a general partnership under the laws of New York."

Reisman v. KPMG Peat Marwick LLP, 965 F. Supp. 165 (D. Mass. 1997).

Relying on *Carden v. Arkoma Associates*, the court rejected the plaintiff's argument that the citizenship of partners in an LLP who are not potentially liable should not be considered in determining the LLP's citizenship. The court stated that it was "particularly troubled that a Big Six accounting firm which operates offices within every state in the United States has effectively immunized itself from the reach of the diversity jurisdiction of the federal courts simply by organizing itself as a limited liability partnership rather than a corporation. Nevertheless, until Congress addresses the jurisdictional implications of this new class of business entities, this Court can reach no other result." The court noted by way of footnote that Peat Marwick might have "won" more than it bargained for because it would now be judicially estopped from advancing a contrary argument in any other court and "the doors of the federal courts ought now to be closed to Peat Marwick save in cases that involve a federal litigant or which pose a federal question." The court estimated that Peat Marwick was currently a litigant in approximately 93 diversity cases that ought not to be pending and stated that, if it had the database to determine all such cases, it would notify every court in which such a case was pending.

C. Pro Se Representation

Verizon Yellow Pages Co. v. Sims & Sims, P.C., No. 02-00961, 2003 WL 836087 (Mass.Super. Feb. 24, 2003) (concluding that lawyer partner in law firm LLP could not appear for partnership pro se because partner in LLP has limited liability and is legally distinct from LLP).

D. Limited Liability of Partners

Griffin v. Fowler, 579 S.E.2d 848 (Ga.App. 2003) (denying LLP partners' motion for summary judgment regarding liability for another partner's alleged malpractice and breach of fiduciary duty on the basis that there were legal services performed prior to the partnership's registration as an LLP and partners thus could not escape potential liability).

Verizon Yellow Pages Co. v. Sims & Sims, P.C., No. 02-00961, 2003 WL 836087 (Mass.Super. Feb. 24, 2003)(distinguishing partner in LLP from partner in traditional general partnership for purposes of pro se representation on basis that partner in LLP has limited liability and is legally separate and distinct from LLP).

Megadyne Information Systems v. Rosner, Owens & Nunziato, No. B213137, 2002 WL 31112563 (Cal. App. Sept. 21, 2002).

The plaintiff sued a law firm LLP and its partners for malpractice and breach of fiduciary duty. The court granted the defendants summary judgment on the malpractice claim but determined there were fact issues regarding a breach of fiduciary duty claim. The breach of fiduciary duty claim was premised on alleged misrepresentations by the firm to the plaintiff that the plaintiff had a viable claim against the Orange County Transportation Authority (OCTA) when the firm knew that limitations had run on the claim. The plaintiff also complained of the firm's continued representation and receipt of fees for worthless legal representation. The court determined that there were fact issues

relating to the personal liability of the partners. The court cited the California LLP provisions for the proposition that partners in an LLP do not have vicarious liability for the torts of another partner, and the court stated that the plaintiff could only hold a partner liable who was “involved in the handling of the matter.” All three partners claimed that one of them was the “sole attorney” who handled the matter and that the other two had no involvement. However, the court found there were fact issues as to the involvement of the other two. The fact issues were raised by the admittedly-involved attorney’s testimony that “there might have been discussions” with the other two partners that the plaintiff had a viable malpractice claim against the lawyers that had previously represented the plaintiff on their claim against OCTA. The court said these discussions could support an inference that the partners knew the plaintiff’s claim against OCTA was time-barred and that they participated in the decision not to tell the plaintiff while the firm continued its representation. In addition, the name of one of the partners who claimed he was not involved appeared on the caption page of the claim filed with OCTA, suggesting his involvement in the case.

Schaufler v. Mengel, Metzger, Barr & Company, LLP, 745 N.Y.S.2d 291 (N.Y. Sup. 2002) (apparently confusing LLP with limited partnership in stating that defendants had submitted insufficient evidence to establish that managing partner of accounting firm had no liability as a matter of law on buy-out agreement negotiated with plaintiff partner because the limited partnership act imposes joint and several personal liability on a general partner and on a limited partner who participates in the control of the business).

Foxchase, LLLP v. Cliatt, 562 S.E.2d 221 (Ga. App. 2002) (holding that partners in limited liability partnership could be held liable based on evidence of damages that occurred when individuals owned property prior to time it was conveyed to partnership).

Dow v. Donovan, 150 F. Supp.2d 249 (D. Mass. 2001).

The court held that an associate attorney who was terminated by her Massachusetts LLP law firm employer could not hold individual partners vicariously liable for Title VII gender discrimination claims, but would have to establish that an individual partner was negligent or committed some other kind of wrongful act, error or omission in order to hold the partner liable. The court refrained from deciding the “unsettled” questions regarding what proof would be required to hold individual partners liable if the plaintiff prevailed on her discrimination claim. The plaintiff was terminated after a meeting at which the partners considered and rejected admission of the plaintiff as a partner. The firm followed the statutory default rule that requires unanimity for admission of a partner. The firm claimed that no one spoke in favor of admitting the plaintiff. The plaintiff argued that each individual partner contributed to the decision to deny her partnership and that each partner’s negligence or wrongful act thus contributed to her injury. The court rejected this approach because it would “vastly expand the scope of relief beyond that provided in the statutes and precedents regarding Limited Liability Partnerships.” The defendants argued that, unless the plaintiff sued each partner for individual liability (which she might not be able to do under governing discrimination statutes), all of the partners were protected by the LLP statute and by the partnership’s “single vote” rule. (The firm argued that a single vote that was not discriminatory would preclude liability because there would be no damage resulting from any discriminatory intent on the part of any other partners.) The court balked at this approach as being too restrictive. The court stated that it need not decide the unsettled questions regarding the proof required of the plaintiff to reach individual partners’ assets because it would only be necessary if the plaintiff prevailed on her claims against the firm. The court, however, did go on to discuss the purpose of the LLP statute and its protection of partners from vicarious liability. The court recognized that individuals are not ordinarily liable under Title VII and state anti-discrimination statutes, the liability being, at least primarily, a partnership liability. The court recognized the protection from vicarious liability under the LLP statute but stated that the statute did not mean that partners in an LLP can never be liable in a discrimination suit. According to the court, the plaintiff must demonstrate some negligent or other wrongful act, error, or omission on the part of an individual partner that produced discrimination against the plaintiff. The court indicated that trial of these issues should be in a separate phase from the trial on the partnership’s liability because of the confusion and potential conflict of interest issues that would be likely to arise when dealing with individual partners’ liability. The court concluded that separate counsel was not necessary for each partner in a trial limited to the liability of the partnership. The court engaged in a lengthy discussion of professionalism and conflict of interest.

Lewis v. Rosenfeld, 138 F. Supp.2d 466 (S.D. N.Y. 2001), dismissed on other grounds on reconsideration, 145 F. Supp.2d 341 (S.D. N.Y. 2001).

The court acknowledged that two defendants who were partners in a New York LLP could not be held vicariously liable for the liabilities of the partnership when the plaintiff had not alleged that any of the tortious acts were committed by the defendants or any individual acting under their control. However, the plaintiff also asserted claims

arising out of the actions of a second partnership that was not registered as an LLP, and the defendants did have potential vicarious liability based upon their status as partners in that partnership. (On reconsideration, the court determined that the claims were time barred.)

Schuman v. Gallet, Dreyer & Berkey, L.L.P., 719 N.Y.S.2d 864 (N.Y. A.D. 1 Dept. 2001).

The court affirmed the decision of the lower court (*see Schuman v. Gallet, Dreyer and Berkey, L.L.P.*, 689 N.Y.S.2d 628 (N.Y. Sup. 1999)) determining that the plaintiff's general release of the defendant law firm and its partners did not release Berkey in his individual capacity because, under the New York LLP provisions, each partner is liable for any negligent or wrongful act committed by him or her or under his or her direct supervision or control. The complaint alleged claims against Berkey individually for negligence, breach of fiduciary duty, and legal malpractice in the supervision of the firm's escrow account. While the release was sufficient to release Berkey from his vicarious liability as a partner, it was not specific enough to release him for his own acts.

Kus v. Irving, 736 A.2d 946 (Conn. Super. 1999).

A client sought to hold the three partners of a law firm LLP liable in connection with the acts of one of the partners, Irving, in collecting a fee that exceeded that to which the client had agreed. The other two partners filed affidavits stating that they had no knowledge of Irving's dealings with the client until after the matter was concluded, that they did not have any supervision or control of Irving, and that Irving retained all fees from his activities and did not share them with the other partners. The Connecticut LLP statute protects partners from liability for any debts, obligations, or liabilities of the partnership except for the partner's own negligence, wrongful acts, or misconduct or that of any person under his direct supervision or control. The client claimed the other two partners were guilty of wrongful acts, negligence, and misconduct but produced no summary judgment evidence to that effect. The client also claimed that the other two partners violated provisions of Rule 5.1 of the rules of professional conduct. The court stated that even if there was evidence of a violation of Rule 5.1, the LLP statute supersedes the rule except where the other person is under the partners' "direct supervision and control." Since the other two partners shared no benefit, did not have supervision or control over Irving, and did not know of the matter until after it occurred, the court found that the other two partners were protected from liability.

Cruz v. Benine, 984 P.2d 1173 (Colo. 1999).

This case deals with issues of privity and claim preclusion in the context of a suit by a general partnership and its partners against Empire Enterprises Unlimited ("Empire"), two Empire partners, and an Empire employee. Throughout the opinion, the court referred to Empire as a limited partnership. In a prior suit, a partner in the general partnership plaintiff sued Empire and one of Empire's partners. The court held that the plaintiff in the prior suit was in privity with both the partnership in which she was a partner and her partner so as to bar them from suing Empire and the Empire partner who had settled the prior suit. However, the court held that suit against Empire's other partner and Empire's employee was not barred because they were not parties in the prior suit. At this juncture in the opinion, the court makes a point about the "different liability standards [that apply] to general partnerships. . . and to limited partnerships." Specifically, the court stated, "the UPL [Uniform Partnership Law] no longer provides for joint and several liability in a limited partnership." The court then quoted Section 7-60-115(2), the provision on registered limited liability partnerships. Thus, the court appeared to exhibit a type of confusion that has been reflected in a number of cases — that is, the distinction between a limited partnership and a limited liability partnership. Of course, it is possible under Colorado law for a limited partnership to register as a limited liability partnership, but it is certainly not clear that this was the situation to which the court was referring.

Middlemist v. BDO Seidman, LLP, 958 P.2d 486 (Colo. App. 1997).

The plaintiff, a CPA, sued her employer, BDO Seidman, LLP, and one of its partners for wrongful termination. The court, applying Colorado law, found that the partner was protected by the LLP shield. "A party seeking to hold a partner of a limited liability partnership personally liable for alleged improper actions of the partnership must proceed as if attempting to pierce the corporate veil," according to the court.

Liberty Mutual Insurance Company v. Gardere & Wynne, L.L.P., Civ.A. No. 94-10609-MLW, 1994 WL 707133 (D.Mass. Dec. 6, 1994) (noting unsettled questions about scope of coverage of Texas partial LLP shield and implying that Texas LLP statute would be given effect in Massachusetts litigation and that Texas law would govern extent to which damages and injunctive relief could be granted against partners other than those directly involved in the alleged wrongdoing).

E. Effect of Registration on Partnership

Institute of Physical Medicine & Rehabilitation, LLP v. Country-Wide Insurance, 752 N.Y.S.2d 232 (N.Y. City Civ. Ct. 2002) (stating that LLP may sue and be sued as if it were a partnership formed pursuant to the general provisions of the partnership law except for the limitation on liability of the partners because, under New York law, an LLP is a partnership even though the partners have limited liability).

Pytko v. Hannah LLP, 15 Mass.L.Rptr. 429 (Mass. Super. 2002) (noting that LLP status does not protect the partnership itself from liability for actions of its employees in the service of performance for the partnership).

Hager v. Amiri, No. 05-97-02046-CV, 2001 WL 533806 (Tex. App. May 21, 2001).

It appears that the court erroneously referred to an LLP as an LLC in this case. In reciting the facts of the case, the court stated that a judgment based on legal malpractice was entered against Hager, an individual attorney, and his former law firm Nichols, Jackson, Kirk and Dillard, as well as Nichols, Jackson, Dillard, Hager & Smith, L.L.P. The style of the case also refers to Nichols, Jackson, Dillard, Hager and Smith, L.L.P. On appeal, the court held that the malpractice occurred after the law firm “registered as a limited liability company.” The court sustained the contention that the trial court improperly held the “dissolved firm” of Nichols, Jackson, Kirk and Dillard liable. According to the court, since the firm had registered as a “limited liability company” prior to the time of the particular act that damaged the client, Hager “alone” was responsible for the damages. It is not clear whether the court was actually saying that the LLC or LLP law firm would not be liable. In reversing the judgment based upon various errors in the trial court, the court of appeals specifically decreed that the plaintiff take nothing against Nichols, Jackson, Kirk and Dillard but did not mention the judgment against Nichols, Jackson, Dillard, Hager & Smith, L.L.P.

Levine v. Bayne, Snell & Krause, Ltd., 92 S.W.3d 1 (Tex. App. 1999), rev’d on other grounds, 40 S.W.3d 92 (Tex. 2001).

A law firm sued to recover under a contingency fee contract with the Levines. The law firm was organized as a professional corporation when it was engaged by the Levines, and it subsequently reorganized as an LLP and then a limited partnership. The Levines argued the contract was a personal services contract that was not assignable without their consent and that Bayne, Snell & Krause, Ltd. was not a proper party. The court rejected the argument on the basis that attorneys can assign their accounts receivable and that the assignment involved the contractual right to payment.

Canada Life Assurance Company v. Estate of Lebowitz, 185 F.3d 231 (4th Cir. 1999).

In this case involving whether benefits were due the estate of a deceased partner of an LLP under an ERISA life insurance policy, the court noted in a footnote that the partnership is a limited liability partnership “incorporated” in Maryland. The court explained that, “[a]lthough WTP is a limited liability partnership, under Maryland law it is still liable for the representations of its agent partners.” The court went on to cite provisions of the Maryland RUPA applicable to the question of the partnership’s position on coverage under the policy in issue.

In re Metropolitan Metals, Inc., 228 B.R. 355 (M.D. Penn. 1998).

The issue in this case was whether the original order of the bankruptcy court appointing Main, Hurdman & Cranstoun as accountants for the Trustee was sufficient to authorize a final allowance to KPMG Peat Marwick LLP. Between the order appointing Main, Hurdman & Cranstoun and the application for allowance in issue the following events occurred: (i) Main, Hurdman & Cranstoun changed its name to Main Hurdman, (ii) Main Hurdman merged with Peat Marwick Mitchell & Co. to form a partnership known as Peat Marwick Main & Co., (iii) Peat Marwick Main & Co. changed its name to KPMG Peat Marwick, and (iv) KPMG Peat Marwick became a limited liability partnership and changed its name to KPMG Peat Marwick LLP. The court declined to see the transition from Main, Hurdman & Cranstoun to KPMG Peat Marwick LLP as merely an evolution of one entity from one era to another. “While the rules contemplate that partners and associates will come and go, the rules do not contemplate that entire entities can be gobbled up by other entities and retain their privilege to perform services to a bankrupt estate. . . . I see no alternative but that a new application be filed for the superseding entity.” The court concluded, under the circumstances, that it should grant retroactive relief and approve compensation for KPMG; however, the court stated that its “holding serves as fair warning of the need, in the future, for professionals to reapply for appointment should the character of their firm change in any but a nominal character.”

Mudge Rose Guthrie Alexander & Ferdon v. Pickett, 11 F.Supp.2d 449 (S.D. N.Y. 1998) (commenting in footnote that the New York LLP statute “clearly enunciates that a general partnership that is registered as a RLLP is for

all purposes the same entity that existed before registration and continues to be a general partnership under the laws of New York”).

Sasaki v. McKinnon, 707 N.E.2d 9 (Ohio App.1997).

This opinion addressed whether a shareholder derivative action that included claims against the corporation's outside auditor should be stayed based on an arbitration clause in a letter agreement between Ernst & Young, LLP and the corporation. In the course of its discussion, the court referred to Ernst & Young, LLP as Ernst & Young's "successor" and stated that "the two entities. . . are, but for the corporate change to a limited liability partnership designation, the same entities for all practical intents and purposes."

Howard v. Klynveld Peat Marwick Goerdeler, 977 F. Supp. 654 (S.D. N.Y. 1997), aff'd, 173 F.3d 844 (2nd Cir. 1999).

In this employment discrimination case, the court noted in passing that the defendant KPMG Peat Marwick became a limited liability partnership and amended its Articles of Partnership to add the suffix "LLP" to its name in August 1994. The court explained that the partnership "was not dissolved and continued without interruption with the same partners, principals, employees, assets, rights, obligations, liabilities and operations as maintained prior to the change." The court continued, "Peat Marwick LLP is in all respects the successor in interest to Peat Marwick."

UOP v. Andersen Consulting, No. CV 95014753, 1997 WL 219820 (Conn. Super. April 24, 1997).

Confusion regarding the nature of an LLP is apparent in the court's opinion on the defendant's motion to strike in this case. The defendant asked the court to strike a number of specific counts of the plaintiff's complaint on various grounds and to strike the entire complaint as to Andersen Consulting, the general partnership, on the grounds that the entity by that name did not exist. The defendant claimed that the plaintiff could not assert a cause of action against both Andersen Consulting, the general partnership, and Andersen Consulting, LLP, because the plaintiff alleged that Andersen Consulting, LLP, was the successor in interest to Andersen Consulting, the general partnership. The plaintiff argued that the defendant was "merely trying to absolve the liability of the general partners of Andersen Consulting by limiting the plaintiff's target to the limited liability company only." After this mistaken reference to Andersen Consulting, LLP, as a "limited liability company," the court rejected the defendant's motion to strike. The court gave as reasons the fact that Andersen Consulting, LLP, had not stated that it had assumed all of the liabilities of Andersen Consulting, the general partnership, and the fact that individual partners need not be named to commence a civil action against a general partnership.

Medical Designs, Inc. v. Shannon, Gracey, Ratliff & Miller, L.L.P., 922 S.W.2d 626 (Tex. App.--Fort Worth 1996).

The law firm of Shannon, Gracey, Ratliff & Miller, L.L.P. was sued for malpractice and obtained a summary judgment that was upheld on appeal on the basis that a "successor partnership" is *not liable* for the torts of a predecessor partnership. It is not clear from the opinion whether the partnership's registration as an LLP, which apparently took place after the malpractice suit was filed, was alone enough to make the partnership a "successor partnership" as that term was used by the court, but it seems unlikely. It is unfortunate, however, that the court did not provide greater insight into what it deemed a "successor partnership." The law firm involved had, subsequent to the time the alleged malpractice occurred, merged and unmerged with another law firm, and the plaintiff alleged that Shannon, Gracey, Ratliff & Miller, L.L.P. was liable as the successor partnership of the Shannon, Gracey, Ratliff & Miller firm that had represented the plaintiff in the matter giving rise to the malpractice claim. (The plaintiff's pleadings alleged that the firm was previously known as Reynolds, Shannon, Miller, Blinn, White & Cook, and, prior to that, as Shannon, Gracey, Ratliff, & Miller, and that the plaintiff's suit was against the firm in its current form and all of its predecessors.)

The court of appeals upheld the trial court's summary judgment on the basis that "even if Shannon, Gracey, Ratliff, & Miller, L.L.P. is a successor law firm, Texas does not recognize that successor partnerships are liable for the tortious conduct of predecessor partnerships." The court's opinion is brief and explores neither the factual background of the changes in the Shannon, Gracey firm nor the rationale for distinguishing between tort and contract claims when it comes to successor partnership liability. If the court's opinion stands for the proposition that registration as an LLP is enough to make the partnership a different "successor" partnership, and thus cut off the entity's liability for pre-registration tort claims, the opinion obviously has profound implications. It is unlikely, however, that this was the basis for the court's opinion. (Such a view is inconsistent, in this writer's opinion, with the underlying premise of the LLP statutes that an LLP is the *same* partnership as prior to registration.) Based upon the cases relied upon by the court, it appears that the court may have concluded that a dissolution results in a successor partnership which is not liable for the pre-dissolution torts of its predecessor. In view of the UPA approach to dissolution, under which any change in

membership results in a technical dissolution, this proposition itself has significant implications. Query whether this approach suggests that the departure of a partner in a UPA partnership would, in some states, require a new LLP registration to preserve the liability limitation of the partners in the "new" partnership? Such a result obviously seems absurd and points to the wisdom of the clearer entity approach under RUPA.

In a subsequent decision by another Texas court of appeals, the court addressed the possibility that a professional corporation might be liable for the malpractice of the predecessor partnership. The court pointed out in dicta that the lawyer who committed the malpractice in the *Shannon, Gracey* case was not employed by the successor law firms whereas a principal of both the earlier partnership and the successor professional corporation was alleged to have acted negligently in the case before the court. The court suggested, but did not decide, that this distinction might be outcome determinative. See *Andrews v. Diamond, Rash, Leslie & Smith*, 959 S.W.2d 646 (Tex. App.--El Paso 1997, writ denied).

F. Securities Laws

Toothman v. Freeborn & Peters, __ P.3d __, 2002 WL 31600861 (Colo.App. 2002).

The plaintiffs asserted various causes of action in connection with defendants' role in the sale of interests in fifty-three LLPs formed to sell pre-paid cellular phone services. The interests were sold by phone solicitation to approximately 5,000 investors. At issue for purposes of class certification was the analysis involved in determining whether the LLP interests were securities under the Colorado Securities Act. The trial court relied upon Colorado case law adopting the rationale of *Williamson v. Tucker* in concluding that common questions did not predominate over individual questions because whether the interests were securities would require analysis of each individual investor in relation to each partnership. The court of appeals held that the presumption of *Williamson v. Tucker* that a general partnership interest is not an investment contract security is not applicable to an LLP interest. The court discussed the rationale for presuming that the interest of a general partner (who has a legal right to participate in the management of the partnership and is personally liable for partnership obligations) is not an investment contract and for not applying such a presumption to the interest of a limited partner (who is a passive investor with no personal liability for the obligations of the business). The court concluded that an LLP interest cannot be analogized to either general partnership or limited partnership interests. The court was persuaded by cases in the LLC area that have declined to adopt a presumption that an LLC interest is not an investment contract. The court held that the relevant inquiry for the trial court was not to apply the *Williamson* examples related to general partnership interests but rather to determine whether the investors expected profits from the managerial efforts of someone else and whether the investors had a substantial power to affect the success of the enterprise.

G. Bankruptcy

In re Mahoney Hawkes, LLP, 289 B.R. 285 (Bankr. D. Mass. 2002) (analyzing proposed release of LLP debtor's partners under plan of reorganization providing for contribution of \$200,000 per partner and partners' relinquishment of claims for indemnity and defense under insurance policy and concluding that proposed release of partners was not proper under multi-factor test applied by court).

H. Status of LLP Partners Under Family Medical Leave Act

Siko v. Kassab, Archbold & O'Brien, L.L.P., 77 Fair Empl. Prac. Cas. (BNA) 1032, 4 Wage & Hour Cas. 2d (BNA) 1547, 1998 WL 464900 (E.D. Pa. Aug. 5, 1998).

The court refused to accept an LLP law firm's summary judgment argument that its partners were not employees for purposes of the Family Medical Leave Act (FMLA). Siko, an employee of an LLP law firm, brought an employment discrimination case alleging various violations of state law and Title VII, ERISA, and the FMLA. With respect to the FMLA claim, the firm argued that it was not subject to the FMLA because it did not have 50 employees. Siko argued that the firm's partners should be treated as employees under the FMLA, which would cause the firm to be subject to the statute. The court concluded that there was insufficient evidence to support the firm's claim that its partners were not employees. The court's analysis is somewhat confusing because it mixes corporate and partnership terminology, but the court apparently concluded that LLP partners are distinguishable from both shareholders of a professional corporation and general partners of a traditional general partnership. The court distinguished cases holding that partners are not employees under federal anti-discrimination statutes on the basis that those cases "are limited to general partnerships where the partner is either a shareholder or subject to unlimited liability." By footnote, the court noted that the cases cited by the firm "involve general partners who are subject to unlimited liability of the corporation. As such, those partners, unlike those at Defendant's law firm, are accountable for all the benefits and pitfalls attributable to the

corporation." The court went on to note that the "partners of Defendant's law firm are neither shareholders nor subject to unlimited liability, but, rather part of a limited liability partnership." Thus, the court concluded that the facts did not support the legal conclusion that the firm's partners were not employees.

III. Cases Involving Limited Liability Companies

Litigation involving limited liability companies is resulting in reported cases as well as unpublished opinions that are picked up by online legal research services. Such cases are appearing at a steadily increasing rate. Set forth below are brief synopses of LLC cases around the country to date.

A. Personal Jurisdiction Over Members or Managers

Cornerstone Technologies, LLC v. Conrad, No.Civ.A. 19712-NC, 2003 WL 1787959 (Del.Ch. March 31, 2003).

In this dispute regarding two Delaware LLCs operating in Pennsylvania, the two defendants, Unger and Conrad, moved to dismiss for lack of personal jurisdiction. The court granted Unger's motion because the court found that Unger did not transact any business in Delaware under § 3104(c)(1) of the Delaware long-arm statute. The plaintiffs argued that the formation of the LLCs in Delaware was the transaction of business in Delaware; however, Unger did not become a member (if he became a member at all) until well after the formation of the LLCs. The court rejected the argument that the acts of the original founders of the LLCs could be attributed to Unger when he later became a member of the LLCs. The court held that it had personal jurisdiction over Conrad (who was a founding member, manager, and high level officer of the LLCs) pursuant to 6 Del. C. §§ 18-109(a) and 18-110(a) and thus avoided analysis of whether the formation of the Delaware LLCs would constitute the transaction of business under § 3104(c)(1) and whether the claims would have a sufficient nexus to those acts. Section 18-110(a) sustained jurisdiction with respect to claims involving removal and replacement of Conrad as a manager, and § 18-109 provided a basis for jurisdiction with respect to all of the claims, including disputes related to a buy-out provision. Section 18-110 provides that service on the LLC constitutes service on "the person or persons whose right to serve as a manager is contested and upon the persons, if any, claiming to be a manager or claiming the right to be a manager." Although Conrad argued that the LLCs never had managers, the court noted that the plaintiffs had produced evidence that Conrad had previously claimed to be a manager, and the court concluded that the disputes over governance and management fell within the scope of § 18-110(a). The court went on to find that § 18-109 provided a basis for jurisdiction because it permits the exercise of personal jurisdiction over a manager "in all civil actions or proceedings brought in the State of Delaware involving or relating to the business of the limited liability company or a violation by the manager ... of a duty to the limited liability company, or any member of the limited liability company." The court also determined that the exercise of jurisdiction satisfied due process. Finally, the court determined that it should stay the litigation in Delaware pending the outcome of litigation between the parties in Pennsylvania.

Caldwell-Baker Co. v. Southern Illinois Co., 225 F.Supp.2d 1243 (D. Kan. 2002) (granting Illinois LLC's motion to dismiss for lack of jurisdiction where plaintiff failed to allege facts to indicate necessary minimum contacts, failed to address LLC's argument that it was not alter ego of corporate member as alleged by plaintiff, and failed to show any partnership agreement or other contract whereby LLC agreed to assume responsibilities of corporation in issue).

Stomar, Inc. v. Lucky Seven Riverboat Company, L.L.C., 821 So.2d 1183 (Fla. App. 2002)(upholding application of "corporate shield"doctrine to preclude exercise of personal jurisdiction over individuals acting in representative capacity for LLC in executing brokerage agreement, but remanding for reconsideration, in light of recent judicial development, the possibility of exercise of jurisdiction over individuals based on fraudulent inducement of the contract).

International Bancorp, L.L.C. v. Societe des Bains de Mer et du Cercle des Entrangers a Monaco, 192 F.Supp.2d 467 (E.D. Va. 2002)(holding that record did not support piercing LLC veil to subject member to court's personal jurisdiction under "stringent" Virginia veil piercing standard requiring "proof that the alleged alter ego used the corporation to disguise some legal wrong").

Chase Manhattan Bank v. Iridium Africa Corporation, No.00-0564-RRM(JJF)(MPT), 2002 WL 732070 (D. Del. April 5, 2002)(setting aside default judgment against Taiwanese corporation based upon reserve capital call obligations as member of Iridium LLC on showing that member presented potentially meritorious defense based upon

its alleged transfer of interest and its good faith belief that it was no longer a member of the LLC, beyond the jurisdiction of the court, and not properly served).

Palmer v. Moffatt, No. 01C-03-114-JEB, 2001 WL 1221749 (Del. Super. Oct. 10, 2001).

In this dispute between the members and managers of an LLC, several defendants moved for dismissal based upon lack of personal jurisdiction. The court interpreted the Delaware implied consent statute which establishes jurisdiction over (i) a manager designated as such in, or pursuant to, the LLC agreement or (ii) a person who materially participates in the management of the LLC though not designated as a manager. While the LLC agreement conferred broad authority to members, the court determined that it actually vested management in a management committee. The court held the defendants who did not serve on that committee were not subject to service under the implied consent statute. The court also determined that an individual who was a member of the committee when many of the disputed events occurred was subject to the implied consent statute.

Stauffacher v. Lone Star Mud, Inc., 54 S.W.3d 810 (Tex.App. 2001)(holding that individual failed to negate plaintiff's theory that individual was alter ego of a Wisconsin LLC for purposes of court's exercise of personal jurisdiction over individual).

777388 *Ontario Limited v. Lencore Acoustics Corp.*, 142 F. Supp.2d 309 (E.D. N.Y. 2001)(finding individuals who jointly owned and directed partnership and LLC were subject to personal jurisdiction based upon agency relationships).

Rubinbaum LLP v. Related Corporate Partners V, LP, 154 F. Supp.2d 481 (S.D. N.Y. 2001) (finding New York court had jurisdiction over managers and officers of Florida LLC).

Origins Natural Resources, Inc. v. Kotler, 133 F. Supp.2d 1232 (D. N.M. 2001).

The court in this trademark infringement action determined that it lacked jurisdiction over a nonresident LLC and its indirect owner who licensed the trademark to the LLC, the only contact with New Mexico being the fulfillment of an order placed over the Internet by an individual in New Mexico.

Hill v. Shell Oil Company, 140 F. Supp.2d 911 (N.D. Ill. 2001), order vacated in part on reconsideration, 149 F. Supp.3d 416 (concluding personal jurisdiction over a Delaware LLC with no direct presence in Illinois could not be sustained based upon jurisdiction over one of the LLC's members, but if a joint venture between the LLC and co-venturers over whom the court had jurisdiction could be established, the minimum contacts of the co-venturers would be attributed to the LLC).

M.G. Incentives v. J.J. Marchand, No. C6-00-962, 2001 WL 96223 (Minn. App. Feb. 6, 2001) (finding it unnecessary to decide whether the fiduciary shield doctrine should apply in Minnesota so as to protect an individual acting on behalf of an LLC where the plaintiff alleged facts sufficient to pierce the veil, the distinction between the individual and LLC was blurry, and the plaintiff alleged fraud against individual).

Royal Mortgage Corporation v. Montague, 41 S.W.3d 721 (Tex. App. 2001) (finding that an individual and corporation were acting as agents of a foreign LLC so as to support the exercise of personal jurisdiction over the LLC but concluding that there was no evidence the LLC was acting as alter ego of its members for purposes of personal jurisdiction over the members).

Assist Stock Management L.L.C. v. Rosheim, 753 A.2d 974 (Del. Ch. 2000).

In this case, the court interpreted and applied Delaware's implied consent statute for obtaining personal jurisdiction over managers of Delaware LLCs. The case involved a dispute between two members/managers of a Delaware LLC with its principal place of business in Florida. All parties agreed that the defendant Rosheim had no contact with Delaware beyond his involvement as a founder and manager of the LLC. The court discussed the precise statutory language of Section 18-109 and noted differences between it and the provision addressing jurisdiction over corporate directors. Ultimately, the court concluded that Section 18-109 supported the exercise of jurisdiction over Rosheim regardless of whether the claims against him alleged a breach of fiduciary duty because the claims involved disputes regarding the parties' rights under the LLC agreement and Delaware statutory and case law. The court concluded that Delaware has a compelling interest in the resolution of disagreements of this sort. Specifically, the court concluded that exercise of jurisdiction was proper in this case because: (1) the allegations against Rosheim centered on

his “rights, duties and obligations” as a manager of a Delaware LLC; (2) resolution of the matter was “inextricably bound up in Delaware law;” and (3) Delaware has a strong interest in providing a forum for disputes relating to the ability of managers of a Delaware LLC to discharge their respective managerial functions.

New England National LLC v. Kabro of East Lyme LLC, No. 550014, 2000 WL 254590 (Conn. Super. Feb. 23, 2000).

The plaintiffs sued Kabro of East Lyme, LLC (“East Lyme, LLC”), a New York LLC, for breach of a contract to purchase real estate from the defendants. Additionally, the plaintiffs sought to pierce the veil of the LLC and hold several other non-resident parties personally liable under veil piercing theories. The court’s opinion dealt with its jurisdiction over the parties. The court found that East Lyme, LLC had transacted business in Connecticut so as to justify the court’s exercise of specific personal jurisdiction over the LLC. The court also concluded it had jurisdiction over one LLC member who was instrumental in the negotiations of the real estate transaction in issue. The plaintiffs sought to obtain personal jurisdiction over the other non-resident parties by piercing the veil of East Lyme, LLC, but the court concluded that the plaintiffs had not alleged sufficient facts to pierce the veil to obtain jurisdiction over the other members of the LLC nor to obtain jurisdiction over another New York LLC that allegedly provided funds to East Lyme, LLC.

Solow v. Century Assets Corporation, 12 S.W.3d 512 (Tex. App. 1999).

Two members of an LLC argued that they were not subject to personal jurisdiction in Texas in an action against the members for breach of contract and breach of fiduciary duty. The members argued that their contacts with Texas were made in their official capacities on behalf of the LLC and were thus insufficient to support jurisdiction over them individually. The court equated an LLC to a corporation in this context, stating that “[j]urisdiction over an individual generally cannot be based on jurisdiction over a corporation with which he is associated unless the corporation is the alter ego of the individual.” The court examined the record, however, and found that the defendants’ purposefully established minimum contacts with Texas in their individual capacities by negotiating personal rights in certain transactions and by breaching their contractual and fiduciary duties. The court further concluded that assertion of personal jurisdiction would comport with fair play and substantial justice.

Lawson v. Tax Lien Resources Group, LLC, No. 98 C 245, 1998 WL 957331 (N.D. Ill. Dec. 15, 1998).

An LLC member sued two other members and the LLC in Illinois for an accounting of compensation and LLC profits allegedly owed. The plaintiff resided in Illinois, but the LLC was organized in Delaware and the two other members were citizens of Minnesota. The LLC agreement listed the LLC’s principal place of business as the address of one of the Minnesota members. The defendants moved to dismiss for lack of personal jurisdiction. The court reviewed the business of the LLC conducted in Illinois through the plaintiff and concluded that it had personal jurisdiction over the LLC and its members. The fiduciary shield doctrine did not avail the two Minnesota members inasmuch as they came to Illinois to meet with the plaintiff and discuss the formation of their business. The court also denied the defendants’ motion to transfer venue to a more convenient forum. (Interestingly, diversity jurisdiction was not questioned. If the plaintiff was indeed a member of the defendant LLC, diversity would be lacking under the line of cases noted below.)

MCNC Oil & Gas Company v. IBEX Resources Company, L.L.C., 23 F. Supp.2d 729 (E.D. Mich. 1998).

The court determined that the court had personal jurisdiction over three defendants who challenged the court’s jurisdiction. First, the court determined that it had jurisdiction over the defendant Oklahoma LLC. The court applied the Michigan long-arm statute regarding specific jurisdiction over unincorporated associations. Next, the court concluded that it had personal jurisdiction over the individual who signed various agreements on behalf of the LLC as its president. The court found that signing the agreements in his capacity as an officer rather than his individual capacity did not defeat the court’s jurisdiction because Michigan courts have not adopted the fiduciary shield doctrine. Finally, the court determined that it had personal jurisdiction over a corporation to which the LLC delegated its tasks under its contracts with the plaintiff. The court found that the individual who signed the agreements on behalf of the LLC represented the corporation in the pre-contract negotiations and at the last minute signed as president of the LLC.

ING (U.S.) Securities, Futures & Options, Inc. v. Bingham Investment Fund, L.L.C., 934 F. Supp. 987 (N.D. Ill. 1996).

A futures commission merchant sued an LLC and two of its members to collect the deficit balance in the LLC’s trading account. The court determined that it lacked personal jurisdiction over the LLC members based upon the fiduciary shield doctrine (described by the court as prohibiting the exercise of personal jurisdiction over a nonresident

whose only contacts with the forum state were "solely on behalf of his employer or other principal"). The plaintiff attempted to avoid the effect of the fiduciary shield doctrine by relying on the corporate alter ego doctrine. The defendants countered with an affidavit reciting that the LLC's assets were not treated as the assets of the individual defendants, that the LLC maintained necessary corporate records, that the LLC did not commingle its assets with those of the individual defendants, and that the LLC maintained a separate banking account. The affidavit was uncontradicted, and the court rejected the alter ego argument.

Worms v. WGB Partners, L.L.C., No. CV 950149182S, 1996 WL 571464 (Conn. Super. Sept. 26, 1996).

This case involved personal jurisdiction over nonresident individuals who were members of an LLC. The plaintiff was a fellow member of the LLC asserting various causes of action arising from an agreement to form and operate a partnership and LLC. The plaintiff and two defendants formed a Georgia LLC to provide investment banking services in both Atlanta and Greenwich, Connecticut, but never came to an agreement on the terms of the operating agreement. They subsequently terminated their relationship. (The plaintiff claimed that the parties actually formed a general partnership which they then changed to an LLC. The court referred to the business relationship in varied terms throughout the opinion, including a "partnership," "limited liability company," and "limited liability corporation"). The defendants apparently resided in Georgia and contended that their only dealings with the plaintiff consisted of negotiations by correspondence and telephone between Connecticut and Georgia about the operating agreement. The defendants argued that they did not transact business in Connecticut for purposes of a Connecticut statute granting personal jurisdiction. The court found that the defendants had transacted business in Connecticut and thus were subject to the court's jurisdiction. The court additionally concluded that the situation did not involve a claim against the LLC itself; the claim that the defendants breached their agreement to operate the business was a claim that could be asserted against them in their individual capacities.

Cornerstone Orthopedic Hospital v. Marquez, 944 F. Supp. 451 (W.D. N.C. 1996).

The defendant in this case was a doctor who was a limited partner in a limited partnership formed under North Carolina law to operate a hospital in McAllen, Texas. The limited partnership was formed as the result of a conversion from an LLC formed by the defendant and others. The parties involved in the creation of the LLC and limited partnership had a falling out, and the defendant was sued by the limited partnership in North Carolina. The defendant, who emphasized that he had never visited North Carolina, challenged the court's personal jurisdiction. The court found that the defendant had the requisite minimum contacts under North Carolina's long arm statute and the Constitution to warrant the exercise of jurisdiction. The court relied on the fact that the defendant played an active role in creating the limited partnership and assumed obligations to North Carolina business entities. In particular, the court stressed his participation in forming the LLC that was the predecessor to the limited partnership. The court pointed out that all of the business entities created by the parties were created under North Carolina law and that the defendant participated in the decisions regarding formation of the entities. (The court at one point mentioned that he signed the "articles of incorporation" of the LLC. This is in keeping with the court's later reference to another LLC as a "North Carolina corporation.") In connection with formation of the LLC, the defendant executed an operating agreement and a subscription agreement governed by North Carolina law. The defendant argued that status as a limited partner is not enough to create personal jurisdiction; however, the court distinguished the defendant from the type of passive investor that is a limited partner in a large limited partnership and is comparable to a shareholder in a large corporation. The defendant was more than a passive investor, according to the court, because he was one of the parties involved in forming the limited partnership and he undertook obligations that differed from those assumed by passive investors. The court concluded that the defendant was more akin to a general partner than a shareholder.

B. Diversity Jurisdiction

There is a growing body of case law adhering to the rule that the citizenship of an LLC is determined by the citizenship of each of its members for purposes of diversity jurisdiction. Under this rule, an LLC is a citizen of each state in which a member resides. This rule follows from the United States Supreme Court case of *Carden v. Arkoma Associates*, 494 U.S. 185 (1990). In *Carden*, the Supreme Court held that a limited partnership is a citizen of every state in which a general or limited partner resides based upon the rule that citizenship of an unincorporated association is determined by the citizenship of all of its members. In one of the first cases to address the issue of an LLC's citizenship, *Carlos v. Adamy*, No. 95 C 50264, 1996 WL 210019 (N.D. Ill. April 17, 1996), the court concluded that the corporate "nerve center" test would apply to an LLC, but the subsequent case law has embraced the *Carden* approach. The Second, Seventh, and Sixth Circuits have applied this rule to LLCs (see cases cited below). The district courts addressing the issue have overwhelmingly followed this approach; however, there are a few cases in which courts have applied the corporate

rule for determining citizenship (basing citizenship upon state of incorporation and principal place of business). This approach typically appears to result from a failure to recognize that an LLC is a type of entity distinct from a corporation.

Homfield II, L.L.C. v. Comair Holdings, Inc., 54 Fed.Appx. 731, 2003 WL 31780184 (6th Cir. 2003) (stating that LLC has the citizenship of its members, relying on *Cosgrove v. Bartolotta*).

Handelsman v. Bedford Village Associates, L.L.C., 213 F.3d 48 (2nd Cir. 2000) (applying *Carden* in concluding that LLC's citizenship is determined by citizenship of LLC's members).

Cosgrove v. Bartolotta, 150 F.3d 729 (7th Cir. 1998) (applying *Carden* in concluding that citizenship of single member LLC is citizenship of its sole member).

C. Service of Process

Stuyvesant Fuel Service Corp. v. 99-105 3rd Avenue Realty LLC, 745 N.Y.S.2d 680 (N.Y. City Civ. Ct. 2002)(service on LLC did not comply with New York statute because individual served was not a member or manager of the LLC and statute does not authorize service on a "managing agent").

Hovde Acquisition LLC v. Thomas, No. Civ.A. 19032, 2002 WL 1271681 (Del. Ch. June 5, 2002)(discussing improper and unsuccessful attempts to serve non-resident member and manager of Delaware LLC and allowing additional time to effectuate service that would relate back to the filing date of the lawsuit).

NCO Teleservices, Inc. v. Northeast Mortgage, L.L.C., 28 Conn. L. Rptr. 192, 2000 WL 1528900 (Conn. Super. Sept. 21, 2000)(discussing Connecticut statute providing for service of process on LLC).

Burse v. Black Rock Enterprises, No. CV98 035 65 18 S, 1999 WL 74026 (Conn. Super. Feb. 4, 1999).

The defendant LLC moved to dismiss for failure to serve the LLC's statutory agent. The plaintiff argued that the Connecticut statute providing for service on the statutory agent provides but one permissible method of service and that service on an LLC member fulfilled the requirements of the service statutes. The court agreed that the statute permitting service on the statutory agent was not exclusive and denied the motion to dismiss.

Scharmman's Inc. v. 388 West Broadway, LLC, 685 N.Y.S.2d 33 (N.Y. A.D. 1 Dept. 1999)(dismissing case due to improper service on LLC defendant).

Summit Bank v. Taylor, No. 96 Civ. 7229(BSJ), 1997 WL 811526 (S.D. N.Y. Nov. 12, 1997).

The LLC issue in this case was the effectiveness of an attempt to serve a subpoena on an LLC. The attempted service in this case was ineffective under the New York Limited Liability Company Act because service was attempted by delivery of the subpoena to an individual who was neither a manager nor a registered agent of the LLC.

D. Venue

Graziuso v. 2060 Hylan Blvd. Restaurant Corp., 753 N.Y.S.2d 103 (N.Y.A.D. 2 Dept. 2002) (transferring venue to county in which LLC's principal office was located as evidenced by articles of organization in absence of showing that articles had been amended to change principal office).

Hospicomm, Inc. v. International Senior Development, LLC, 2001 WL 1808026 (Pa. Com. Pl. Jan. 9, 2001)(concluding that LLC is "corporation or similar entity" rather than "partnership" or "association" for purposes of rules of civil procedure on venue).

Meterologic, Inc. v. Copier Solutions, Inc., 185 F.Supp.2d 1292 (S.D. Fla. 2002)(discussing piercing allegations in context of forum non conveniens motion).

ZPC 2000, Inc. v. The SCA Group, Inc., 86 F. Supp.2d 274 (S.D. N.Y. 2000) (concluding that venue of this case involving disputes between members of an Illinois LLC should be transferred to Illinois and rejecting argument that the forum selection clause of a non-disclosure agreement allegedly entered into between the members of the LLC should control).

E. Pro Se Representation

The cases thus far dealing with whether an LLC may appear *pro se* almost universally stand for the proposition that an LLC must appear through a licensed attorney. Some of the cases in this area are noted below.

Carlo, L.L.C. v. Yorro, No. SP1147/03, 2003 WL 32091320 (N.Y. Dist. Ct. April 30, 2003) (holding that an LLC must appear by an attorney like a corporation because an LLC has the attributes of a voluntary association with corporate limited liability protection).

Board of Education v. Franklin County Board of Revision, Nos. 01AP-878, 01AP-879, 2002 WL 416953 (Ohio App. March 19, 2002) (distinguishing LLC from partnership, an aggregate of individuals, and characterizing LLC as separate legal entity like corporation for purposes of requirement that it be represented by attorney in property tax valuation dispute, and holding statute permitting LLC member to file a complaint on behalf of LLC unconstitutional insofar as it permits persons who are not attorneys or owners of property to file a complaint before a board of revision on behalf of the owner).

In re ICLNDS Notes Acquisition, LLC, 259 B.R. 289 (Bankr. N.D. Ohio 2001) (holding that LLC may not file bankruptcy petition without being represented by counsel).

Strother v. Harte, 171 F.Supp.2d 203 (S.D. N.Y. 2001).

Paton v. Old Mill Builders, LLC, No. CV000339895S, 2000 WL 1912695 (Conn. Super. Dec. 14, 2000).

Valentine L.L.C. v. Flexible Business Solutions, L.L.C., 27 Conn.L.Rptr. 378, 2000 WL 960901 (Conn. Super. June 22, 2000).

Banco Popular North America v. Austin Bagel Company, L.L.C., No. 99 CIV. 11252 SAS, 2000 WL 669644 (S.D. N.Y. May 23, 2000).

International Association of Sheet Metal Workers Local 16 v. A J Mechanical, No. CIV. 99-451-FR, 1999 WL 447459 (D. Or. June 16, 1999).

Valiant Insurance Co. v. Nurse Network, LLC, No. CV 980578083, 1998 WL 712359 (Conn. Super. Sept. 25, 1998).

One member of a two-member LLC attempted to represent the LLC *pro se*. The court struck the appearance because only one of the members was before the court. The court stated that it would have jurisdiction if both members filed *pro se* appearances.

Poore v. Fox Hollow Enterprises, No. C.A. 93A-09-005, 1994 WL 150872 (Del. Super. March 29, 1994).

F. Standing/Authority to Sue

(See also certain cases under the heading “Derivative Suits.”)

Geysler v. Excel Legacy Corp., No. B159194, 2003 WL 21054762 (Cal.App. 2 Dist. May 12, 2003) (holding that trial court erred when it found individual was not a party to or third party beneficiary of LLC operating agreement and lacked standing to sue; fact issues existed with respect to whether operating agreement had been amended in connection with change in ownership of member of LLC, and individual’s tort claims were not dependent on existence of standing under the agreement).

Liker v. Ryder Systems, Inc., No. Civ.A. 01-3754, 2003 WL 1751462 (E.D. La. 2003) (holding that individuals were not proper plaintiffs to sue for breach of contract in name of LLC but that there were fact issues as to what entity was represented by LLC that entered contract).

Yew Prospect, LLC v. Szulman, 759 N.Y.S.2d 351(N.Y.A.D. 2 Dept. 2003) (holding that executor for deceased sole member of LLC plaintiff should be joined as plaintiff because executor of deceased sole member was authorized to wind up the affairs of the LLC pursuant to the New York LLC act and the terms of the LLC operating agreement).

In re Farmland Industries, Inc. (Farmland Industries, Inc. v. SF Phosphates Co.), __ B.R. __, 2003 WL 1950004 (Bankr. W.D. Mo. April 23, 2003) (stating that it was inappropriate for LLC to take sides in dispute between equal members over ownership and control).

Block v. Block, No. CV20078857S, 2002 WL 31888203 (Conn.Super. Dec. 10, 2002).

A fifty-percent member of an LLC brought suit, individually and on behalf of the LLC, against the other member of the LLC alleging that the defendant member breached his fiduciary duty and committed waste by mismanagement and theft. The defendant argued that the other member did not have authority to bring the suit on behalf of the LLC because the suit was not authorized by a majority in interest of the members. The court rejected the defendant's argument based on the Connecticut LLC act. The court pointed out that the Connecticut LLC statutes generally require a majority in interest of the members to authorize a suit in the name of the LLC but exclude the vote of any member who has an interest in the outcome of the suit that is adverse to the interest of the LLC. Based on that provision, the court found that the plaintiff was the only member with a voting interest and had authority to bring the suit on behalf of the LLC.

Kogut v. Church Homes, Inc., No. CV000436717S, 2002 WL 31662388 (Conn.Super. Nov. 6, 2002)(noting entity nature of LLC and concluding that member did not have standing to bring suit on LLC's contract in absence of any allegation that member was bringing action as third party beneficiary).

Starr v. Levin, No.02 C 2258, 2002 WL1941375 (N.D. Ill. Aug. 21, 2002)(staying fraud, breach of fiduciary duty, and breach of contract action by one LLC member against another pending resolution of concurrent derivative suit pending in Florida state court).

McGee v. Best, 2002 WL 1343225 (Tenn.Ct.App. June 18, 2002)(dismissing member's fraud claim against other members on the basis that the allegations stated a claim that was essentially derivative and thus member did not have standing to pursue it individually).

NSJ Investors, LLC v. TH/North San Jose, LLC, No. CIV. O1-1932PAMSRN, 2002 WL 1347588 (D. Minn. June 17, 2002)(finding subsequent action filed by LLC members in Southern District of New York alleging breach of fiduciary duty and breach of operating agreement did not violate court's injunction against instituting litigation involving interpleaded funds (as to which there was disagreement regarding distribution) in another forum).

Ward v. Hornik, No. 02.944, 2002 WL1199249 (E.D. Pa. June 3, 2002)(interpreting Pennsylvania LLC act and quorum and voting provisions of LLC operating agreement and concluding that suit brought on behalf of LLC was not authorized).

Giuliano v. Pastina, 793 A.2d 1035 (R.I. 2002)(dismissing plaintiff's claims that actions of defendant agent/employee of LLC damaged plaintiff's ownership interest in the LLC because such claims were derivative claims and plaintiff had not complied with procedural requirements for a derivative suit).

Holmes Development, LLC v. Cook, 48 P.3d 895 (Utah 2002)(stating in footnote that, although LLC claimant and related LLC may have the same management and be practically indistinguishable, they are legally separate entities, and court would not treat the LLCs as the same entity for purposes of standing to sue on a contract).

ME Corp., S.A. v. Cohen Brothers LLC, 739 N.Y.S.2d 133 (N.Y. A.D. 1 Dept. 2002)(holding that whether LLC had been dissolved and liquidated was disputed and thus it was premature to dismiss causes of action brought directly by individual members that were derivative in nature on basis that LLC had not been dissolved prior to commencement of the action).

Forum Financial Group v. President and Fellows of Harvard College, 173 F. Supp.2d 72 (D. Maine 2001)(questioning standing of individual member of LLC in case brought by LLC and member arising out of failed business transaction, but making no disposition on issue since it had not been raised).

Association of Merger Dealers, LLC v. Tosco Corporation, 167 F. Supp.2d 65 (D. D.C. 2001)(finding non-profit LLC formed to promote interests of Mobil retail service station dealers in Mobil-Exxon merger did not have standing to sue on its own behalf and lacked associational standing to sue as a representative under state law).

Dawson v. Atlanta Design Associates, Inc., 551 S.E.2d 877 (N.C. App. 2001).

A member of an LLC appealed an order to substitute the LLC as party plaintiff in a case arising out of the defendant's alleged breach of a contract with the plaintiff for the construction of a facility on property owned by the LLC. The court concluded that the individual member was a real party in interest because the claims did not allege injury to the LLC and, even assuming the LLC suffered injuries, the plaintiff's individual contract with the defendants created a "special duty" to the plaintiff.

Denley Rentals, LLC v. Etheridge, No. W2000-00189-COA-R3-CV, 2001 WL 792646 (Tenn. App. July 11, 2001).

Two LLCs and the individual who was the member and manager of both sued the defendants for breach of contract and fraud for failing to disclose a landfill on property bought by the LLC. The individual had entered the contract of sale but assigned his interest under the contract to an LLC. After the sale, the first LLC transferred the property to the second LLC, and the member made a "mental assignment" of the chose in action from the first LLC to the second. The court analyzed whether a single individual authorized on behalf of two separate entities may make a "mental assignment" of a chose in action from the first to the second. The court recognized the validity of the mental assignment because it said that mutual assent is undisputed where there is a "mental assignment" by a single individual, and the claims asserted were legally assignable.

Randolph Foundation v. Appeal from Probate Court of Westport, No. X05CV980167903S, 2001 WL 418059 (Conn. Super. April 3, 2001)(noting in dicta that an LLC is an entity with capacity to sue and be sued and that individual members may not bring LLC claims in their individual names).

St. Raymond v. City of New Orleans, 775 So.2d 31 (La. App. 2000)(permitting sole member of LLC that owned property that was subject matter of suit to amend petition filed in member's own name to make LLC a plaintiff in the case).

In re Heartland Food and Dairy Distributors, Inc. (Land-O-Sun Dairies, L.L.C. v. Heartland Food and Dairy Distributors, Inc.), 253 B.R. 32 (Bankr. S.D. Ill. 2000).

A suit was mistakenly filed in the name of a corporation rather than an affiliated LLC. The suit was dismissed due to the corporation's lack of capacity, and (after various missed opportunities to cure) the LLC ended up being barred by res judicata from pursuing the complaint refiled in its name because the LLC was in privity with the corporation that filed the initial complaint. In finding privity, the court relied in part upon the failure of the LLC and the corporation to comply with the formalities necessary to maintain separate existences. The court commented that the LLC's own counsel was confused about which entity was his client.

Crozier v. Gattoni, 28 Conn. L. Rptr. 320, 2000 WL 1682616 (Conn. Super. Oct. 5, 2000) (holding that LLC member did not have standing to bring suit for breach of contract and other claims arising out of LLC's contract).

Industrial Electronics Corp. of Wisconsin v. iPower Distribution Group, Inc., 215 F.3d 677 (7th Cir. 2000).

The plaintiff and seven other companies, including the defendant iPower Distribution Group, Inc. (iPower), formed an LLC to develop an integrated marketing and distribution consortium using iPower software. Once the LLC was formed, it entered a franchise agreement with iPower to allow the LLC to purchase, install, and use the iPower software. The franchise agreement contained an arbitration clause, but the LLC agreement did not. When the plaintiff later sued iPower alleging that iPower had made material misrepresentations to induce the plaintiff to join the LLC, iPower argued that the claim was subject to the arbitration clause in the franchise agreement. The court acknowledged that an LLC cannot bind its members or subject them to liability through contracts between the LLC and third parties but said that this principle did not resolve the case. The court explained that the plaintiff was like a corporate shareholder who would not have standing to sue or enforce a contract of the corporation; however, the court went on to address the possibility that the plaintiff was a third party beneficiary of the franchise agreement. The court did not have to resolve this issue because it determined that the injuries alleged did not arise under or relate to the franchise agreement. The alleged fraud related to the inducement of the plaintiff to join the LLC by entering the LLC agreement, and the arbitration provision in the franchise agreement did not affect disputes arising out of the LLC agreement.

Roger Boc, L.L.C. v. Weigel, RTG, Inc., 744 So.2d 731 (La. App. 1999).

Four individuals purchased some realty and one week later transferred ownership of the property to an LLC wholly owned by them. Later, the individuals and the LLC filed suit to rescind the purchase based upon fraudulent misrepresentations made during negotiations for the purchase of the property. The defendants argued that the individuals had no right to rescission because they transferred the property to the LLC. The court concluded that the individuals, but not the LLC, could maintain the action for fraud. According to the court, the legal effect of the fraud was to vitiate the formation of the contract of sale, and the domino effect rendered the transfer to the LLC a nullity. As for the LLC's standing, the court noted that the LLC was a "separate and distinct legal entity" that did not participate in the negotiations with the defendants leading to the sale of the property. Only the individual plaintiffs contracted with the defendants; the LLC, a legal entity that they owned, acquired the property by subsequent transfer. Thus, the court concluded the right of action arising out of the fraud was personal to the individuals.

Park Place Entertainment v. Simmons, No. Civ.A. 99-595, 1999 WL 1049828 (E.D. La. Nov. 18, 1999).

In this declaratory judgment action over a consulting agreement and an LLC operating agreement, the court held that a justiciable controversy did not exist and that, even if it did, the plaintiff would not have standing to bring the suit because the plaintiff was not a party to either agreement.

Ark Entertainment, L.L.C. v. C.J. Gayfer & Co., Inc., No. CIV.A. 99-1929, 1999 WL 717631 (E.D. La. Sept. 14, 1999).

An LLC and its two members filed suit alleging breach of a lease agreement. The court held that the members were not parties to the lease agreement and thus could not recover individually. The members' names appeared on the lease only on the signature page where they signed on behalf of the LLC, and they acknowledged that they negotiated the lease on behalf of the LLC. The court rejected the members' argument that they were entitled to recover individually on a detrimental reliance theory.

Midland Food Services, LLC v. Castle Holdings V, LLC, 792 A.2d 920 (Del. Ch. 1999).

Several LLCs sued their previous member and principal operating officer for breach of the fiduciary duties of care and loyalty, alleging that the member caused the LLC to enter leases on commercially unreasonable terms so as to advantage the member and other entities owned by him. Ownership of the LLCs had been transferred by the original member to certain creditors after the LLCs got into financial difficulty. The court held that the *Bangor Punta* doctrine barred the claims since the current owner of the LLCs acquired the LLCs after the alleged wrongdoing occurred. As explained by the court, "[t]he *Bangor Punta* doctrine ensures that a purchaser who obtains a controlling interest in a corporation after potential claims arose against those persons from whom the purchaser obtained his shares cannot use his control of the corporate machinery to cause the corporation to assert those claims directly." The purpose of the doctrine, according to the court, is to prevent persons from being able to re-trade arms-length transactions by using the corporation to sue the parties from whom they obtained their shares. The court found the doctrine applicable in this case. In a footnote, the court expressed doubt that the prior member could breach fiduciary duties owed to companies he wholly owned.

Matter of Roller, 689 N.Y.S.2d 897 (N.Y. A.D. 4th Dept. 1999).

The court stated that the petitioners owned membership interests in the LLCs that were the subject of a proceeding for judicial dissolution, thus they had standing to bring the proceeding under New York law.

McConnell v. Hunt Sport Enterprises, 725 N.E.2d 1193 (Ohio App. 1999)(finding member's breach of operating agreement by unilaterally bringing suit on behalf of LLC without requisite member approval was willful misconduct).

Cowboy Mouth L.L.C. v. Monkey Hill Productions, Inc., No. Civ. A. 98-2615, 1999 WL 35303 (E.D. La. Jan. 21, 1999).

The court in this case ordered the plaintiffs to file a Second Amended Complaint to address certain deficiencies in their pleadings. The case involved a dispute over proceeds from the sale of albums, but the facts of the case apparently were far from clear from the pleadings. The court noted that members of an LLC had sued in their individual capacities notwithstanding the Louisiana statutory provision that a member of an LLC is not a proper party in a case by or against an LLC except when the object is to enforce rights against or liability to the LLC. The court stated that it was unclear how the individuals had a cause of action for breach of contract, and the court admonished the parties to make clear, with respect to each claim, which party asserts liability and upon what basis of law. Apparently, the LLC was a successor to

an LLP which was a party to the contracts in issue, and the court also ordered the plaintiffs to provide a clear chronology of events, including how and when the LLP became an LLC.

Walker v. Virtual Packaging, LLC, 493 S.E.2d 551 (Ga. App. 1997).

Members of an LLC sued the LLC and other members asking for dissolution and damages for breach of fiduciary duty and violation of a non-competition agreement. The parties entered a consent order dissolving the company and reserving the issues involving breach of fiduciary duty and breach of the non-competition agreement. The trial court rendered summary judgment in favor of the defendants. The court first determined that the trial court had erred in implicitly rendering summary judgment on the breach of fiduciary duty claims because the claims were not properly raised in the summary judgment motions. The court next determined that the LLC's claim for breach of the non-competition agreement was not assigned to the members in the consent order dissolving the LLC. While the court agreed with the trial court that the members were not third party beneficiaries of the non-competition agreement, the court found that the members had standing to sue on the agreement because they were parties individually to the contract. Finally, the court found that the trial court had erred in ruling on the issue of whether the breach of non-competition agreement claim was derivative in nature because the parties had not had a full opportunity to be heard on the issue.

JM Avalon Investments, LLC v. Nischan, No. CV 960330010, 1997 WL 133939 (Conn. Super. March 7, 1997).

JM Avalon Investments, LLC and one of its members, Gaspero, sued Nischan, the other member of the LLC, and her husband for conversion, fraud, negligence, breach of contract, and unjust enrichment. Nischan sought to have the case dismissed on the basis that the LLC lacked standing to sue. Nischan argued first that the LLC was not authorized to bring the suit because Nischan, a fifty percent owner of the LLC, had not consented to the suit. The Connecticut LLC act provides that suit may be brought in the name of an LLC by any member or members who are authorized to sue by the vote of a majority in interest of the members. However, the court relied on another provision of the act that states that the vote of any member who has an interest in the outcome of the suit that is adverse to the LLC shall be excluded. Since the suit alleged wrongdoing by Nischan, the court determined that the remaining member, Gaspero, had authority to bring the suit in the name of the LLC without the vote of Nischan. Nischan next argued that her resignation as a member of the LLC dissolved the LLC and left it without standing to sue. The court relied on various provisions of the LLC act in concluding that the remaining member, Gaspero, had authority to wind up the LLC, which included bringing suit on its behalf.

Taurus Advisory Group, Inc. v. Sector Management, Inc., No. CV 960150830, 1996 WL 502187 (Conn. Super. Aug. 29, 1996).

The plaintiffs, Taurus Advisory Group, Inc. ("TAG") and Taurus Advisory Group, LLC ("Taurus LLC"), sued several parties for breach of contract, negligent misrepresentation, breach of the duty of good faith and fiduciary relationship, and other claims arising from an agreement among TAG and the defendants to form Taurus LLC. The defendants sought dismissal of the case on the grounds that the complaint asserted derivative claims that TAG attempted to bring individually and that TAG lacked the authority to commence an action in the name of Taurus LLC. The court first noted that Delaware law applied since the LLC was formed under Delaware law (citing Restatement (Second) of Conflict of Laws § 302). The court then accepted the parties' analogy of an LLC to a corporation, finding members to be similar to stockholders. The court accepted this analogy based on case law analogizing limited partners in a limited partnership (which the court referred to as a limited liability partnership) to corporate shareholders. The court determined that TAG's claims relating to the defendants' failure to make agreed contributions of capital and services alleged a direct injury and TAG could bring the suit on its own behalf. The court further decided that the complaint did not state an individual cause of action in favor of TAG for breach of fiduciary relationship because the only articulated harm was to the LLC (which the court mistakenly referred to at that point as a corporation), and because the complaint did not set out a relationship comparable to that involving a majority shareholder's duties toward the minority shareholders since the capital contributions were in equal amounts. Subsequent related decisions appear at 1997 WL 241153, 1998 WL 381883 and 1998 WL 199353.

G. Derivative Suits

VGS, Inc. v. Castiel, No. C.A. 17995, 2003 WL 723285 (Del.Ch. Feb. 28, 2003) (stating that case law governing corporate derivative suits is equally applicable to LLCs and concluding that breach of fiduciary duty claims (based on waste, mismanagement, and self-dealing) failed because they were derivative in nature and no demand had been made on LLC's board nor had plaintiff demonstrated futility of demand).

Sumlin Construction Co., L.L.C. v. Taylor, __ So.2d __, 2002 WL 31270292 (Ala. 2002) (holding that plaintiff, who was divested of member status by virtue of prior bankruptcy, did not have standing to bring derivative suit on behalf of LLC).

Excimer Associates, Inc. v. LCA Vision, Inc., 292 F.3d 134 (2nd Cir. 2002) (granting opportunity to amend to plead claims of direct injury with greater particularity where complaint could be construed to indicate existence of direct claim by LLC member based upon direct injury incurred as a result of additional contributions required after breach of operating agreement by other member).

McLeod v. Albanese, 815 So.2d 472 (Miss. App. 2002) (noting that statute determining who is proper plaintiff in LLC derivative suit requires that plaintiff be member at the time of the act or omission complained of (thus termination of member's membership by subsequent bankruptcy would not deprive member of standing to pursue derivative claim) and that fair and adequate representation requirement would likely be satisfied if all remaining members are alleged wrongdoers).

Giuliano v. Pastina, 793 A.2d 1035 (R.I. 2002) (dismissing plaintiff's claims that actions of defendant agent/employee of LLC damaged plaintiff's ownership interest in the LLC because such claims were derivative claims and plaintiff had not complied with procedural requirements for a derivative suit).

McGee v. Best, __ S.W.3d __, 2002 WL 1343225 (Tenn.Ct.App. 2002) (dismissing fraud claim because the allegations stated a claim that was essentially derivative and the plaintiff thus did not have standing to pursue it individually).

ME Corp., S.A. v. Cohen Brothers LLC, 739 N.Y.S.2d 133 (N.Y. A.D. 1 Dept. 2002)(holding that whether LLC had been dissolved and liquidated was disputed and thus it was premature to dismiss causes of action brought directly by individual members that were derivative in nature on basis that LLC had not been dissolved prior to commencement of the action).

Paclink Communications, Inc. v. Superior Court, 90 Cal. App. 4th 958, 109 Cal.Rptr.2d. 436 (Cal.App. 2 Dist. 2001).

Three members of an eight-member LLC sued in their individual capacities alleging various causes of action arising out of the transfer of the LLC's assets without their knowledge or consent and for no consideration. The court held that the claims belonged to the LLC and that the plaintiffs lacked standing to bring the claims in their individual capacities because the gravamen of the complaint was injury to the LLC based upon the fraudulent transfer of the LLC's assets. Thus, the claims must be brought by the LLC or derivatively by the members.

Halley v. Barnabe, 24 P.3d 140 (Kan. 2001).

In this consolidated appeal of three actions between two 50% members of an LLC, the Kansas Supreme Court held that the provisions of the new Kansas LLC act authorizing member derivative suits are procedural in nature and thus retroactive in effect such that they apply to litigation initiated prior to the effective date of the new act. The court noted the effective date provisions of the new Kansas LLC act, which took effect January 1, 2000, and provide that the new act is applicable to all LLCs whether formed before or after the effective date. The court also noted the Kansas Bar Association's commentary contrasting the effective date provisions of the new LLC act with the transition provisions of the Kansas Revised Uniform Partnership Act. Finding the provisions relating to derivative suits to be completely procedural in nature, the court concluded they applied to the actions pending in the three appealed cases. The court rejected the argument that the statutory provision in the old LLC act providing for limited liability of members and managers precludes derivative suits against members or managers. The court stated that the provision is not a shield from liability of a member or manager who commits actionable conduct against the LLC, but is a codification of the limited liability of managers and members for debts owed by the LLC. The court pointed out that the same limitation on liability was included in the new act along with the derivative suit provisions.

Safety Technologies, L.C. v. Biotronix 2000, Inc., 136 F. Supp.2d 1169 (D. Kan. 2001) (finding that Kansas precedent precluding corporate shareholders from suing in their individual capacities where the harm is derivative would apply to LLCs).

Harbor Hospital Services, Inc. v. GEM Laundry Services, L.L.C., Nos. 4830, 0207, 2001 WL 1808556 (Pa. Com. Pl. July 18, 2001)(stating that the court could treat as direct a derivative claim by the complaining member since they were the only two members of the LLC but concluding that the complaining member's principal was too far removed to bring a breach of fiduciary duty claim against the other member because the duty, if any, would be between the members of the LLC, not individual shareholders of the members).

Carson v. Lynch Multimedia Corporation, 123 F. Supp.2d 1254 (D. Kan. 2000).

The court concluded that a minority member's breach of fiduciary duty claim against the majority member, managers, and individual who allegedly controlled the managers was derivative and that the complaint must therefore address the demand requirement under Federal Rule 23.1 The court found that futility of demand was adequately reflected in the complaint.

Cabrini Development Council v. LCA Vision, Inc., 197 F.R.D. 90 (S.D. N.Y. 2000) judgment vacated, appeal dismissed, 292 F.3d 134 (2nd Cir. 2002) (following *Weber v. King* (E.D. N.Y. 2000) and concluding that members of a New York LLC have a common law right to bring a derivative action and that the LLC is an indispensable party in such a suit).

Weber v. King, 110 F. Supp.2d 124 (E.D. N.Y. 2000).

Two members of Kathleen's Bake Shop, LLC sued the third member alleging various acts of past and ongoing breach of contract, unfair competition, and interference with the LLC's business. The court concluded that the LLC was a necessary and indispensable party whose joinder was not feasible because it would destroy diversity jurisdiction. Additionally, the court recognized a common law right to bring a derivative action even though the New York LLC law does not include provisions expressly permitting derivative lawsuits. The court then concluded that many of the plaintiffs' claims were more appropriately characterized as claims of the LLC that should be brought derivatively. In the course of its analysis, the court discussed the nature of an LLC as a separate entity and the analogies that should be made to partnerships and corporations.

Walker v. Virtual Packaging, LLC, 493 S.E.2d 551 (Ga. App. 1997) (finding that the trial court erred in ruling on the issue of whether a claim based on the breach of a non-competition agreement was derivative in nature because the parties had not had a full opportunity to be heard on the issue).

Taurus Advisory Group, Inc. v. Sector Management, Inc., No. CV 960150830, 1996 WL 502187 (Conn. Super. Aug. 29, 1996).

The plaintiffs, Taurus Advisory Group, Inc. ("TAG") and Taurus Advisory Group, LLC ("Taurus LLC"), sued several parties for breach of contract, negligent misrepresentation, breach of the duty of good faith and fiduciary relationship, and other claims arising from an agreement among TAG and the defendants to form Taurus LLC. The defendants sought dismissal of the case on the grounds that the complaint asserted derivative claims that TAG attempted to bring individually and that TAG lacked the authority to commence an action in the name of Taurus LLC. The court first noted that Delaware law applied since the LLC was formed under Delaware law (citing Restatement (Second) of Conflict of Laws § 302). The court then accepted the parties' analogy of an LLC to a corporation, finding members to be similar to stockholders. The court accepted this analogy based on case law analogizing limited partners in a limited partnership (which the court referred to as a limited liability partnership) to corporate shareholders. The court determined that TAG's claims relating to the defendants' failure to make agreed contributions of capital and services alleged a direct injury and TAG could bring the suit on its own behalf. The court further decided that the complaint did not state an individual cause of action in favor of TAG for breach of fiduciary relationship because the only articulated harm was to the LLC (which the court mistakenly referred to at that point as a corporation), and because the complaint did not set out a relationship comparable to that involving a majority shareholder's duties toward the minority shareholders since the capital contributions were in equal amounts. Subsequent related decisions appear at 1997 WL 241153, 1998 WL 381883 and 1998 WL 199353.

H. Indispensable Parties

Holland v. Fahnestock & Co., Inc., 210 F.R.D. 487 (S.D. N.Y. 2002) (adopting magistrate's report (*see Holland v. Fahnestock & Co., Inc.*, No. 01CIV.2462RMB/JP, 2002 WL 1774230 (S.D. N.Y. Aug. 2, 2002) finding that LLC was not indispensable party because its interest was adequately represented by defendant and LLC was no more than co-obligor and joint tortfeasor with respect to pre-organization contract assigned to LLC by defendant).

Kennett v. The Carlyle Johnson Machine Co., No. CIV.A. 18690-NC, 2002 WL 1358755 (Del. Ch. June 17, 2002).

One of two founding members of an LLC alleged that the other member unilaterally caused membership interests to be transferred to two individuals, reducing the interests of the founding members and adding the two individuals as new members, without the approval required under the operating agreement. The plaintiff also complained of modifications of his employment relationship with the LLC. The court determined that the individuals to whom the membership interests were transferred, who were residents of Connecticut without any connection to Delaware other than their disputed ownership in a Delaware LLC, were necessary and indispensable parties with respect to the issue of their ownership in the LLC. The parties did not dispute the court's lack of personal jurisdiction over these parties. Most of the issues in the suit were dependent, directly or indirectly, on resolution of the dispute regarding ownership, and the court dismissed the claims involving these issues. The remaining two claims that did not turn on resolution of the ownership dispute were dismissed for other reasons.

Trademark Retail, Inc. v. Apple Glen Investors, LP, 196 F.R.D. 535 (N.D. Ind. 2000) (holding that LLC was an indispensable party in a suit by one member against another for breach of fiduciary duty and interference with contractual and business relations).

Cabrini Development Council v. LCA Vision, Inc., 197 F.R.D. 90 (S.D. N.Y. 2000), judgment vacated, appeal dismissed, 292 F.3d 134 (2nd Cir. 2002) (following *Weber v. King* (E.D. N.Y. 2000) in concluding that members of New York LLC have a common law right to bring a derivative action and that LLC is an indispensable party in such a suit).

Weber v. King, 110 F. Supp.2d 124 (E.D. N.Y. 2000).

Two members of Kathleen's Bake Shop, LLC sued the third member alleging various acts of past and ongoing breach of contract, unfair competition, and interference with the LLC's business. The court concluded that the LLC was a necessary and indispensable party whose joinder was not feasible because it would destroy diversity jurisdiction. Additionally, the court recognized a common law right to bring a derivative action even though the New York LLC law does not include provisions expressly permitting derivative lawsuits. The court then concluded that many of the plaintiffs' claims were more appropriately characterized as claims of the LLC that should be brought derivatively. In the course of its analysis, the court discussed the nature of an LLC as a separate entity and the analogies that should be made to partnerships and corporations.

I. Scope of Expert Testimony

Amster v. River Capital Int'l Group LLC, No. 00 Civ. 9708(DC), 2003 WL 1571593 (S.D.N.Y. March 26, 2003).

In this dispute related to an LLC dissolution, the court addressed the permitted scope of the testimony of the plaintiff's expert. The court said the expert would not be permitted to make "findings of fact," to opine as to the intent or credibility of the parties or witnesses, to opine as to what the law is, or to interpret provisions of the LLC agreement. The court said the expert would be allowed to explain the terms of the LLC agreement and to explain concepts applicable to partnerships and LLCs. The court said the expert would also be permitted to testify as to "indicia" or "badges" of fraud and as to tax matters.

J. Legal Notice Requirement

Barklee Realty Company LLC v. Pataki, No. 120546/99 (N.Y. Sup. Ct. Nov. 16, 2001).

The court struck down the New York law that requires LLCs to publish six weeks of consecutive notices in two newspapers in order to have the right to file lawsuits. The court held that the law violated constitutional due process rights.

K. Arbitration

In re Application of Donald J. Trump, 755 N.Y.S.2d 618 (N.Y.A.D. 1 Dept. 2003) (stating that "artificial distinction" sought to be drawn between individual petitioner and his wholly-owned LLC did not preclude arbitration under arbitration clause in agreement to which LLC was a party).

RiverLinks at Deer Creek, LLC v. Melz, No. M2002-00043-COA-R3-CV, 2002 WL 31890897 (Tenn.Ct.App. Dec. 31, 2002).

The appeals court held that the trial court should retain jurisdiction over an LLC issue of first impression notwithstanding the arbitration clause in the operating agreement. “An arbitrator dealing with the complex facts of this case would have no guidance on the proper interpretation of the Limited Liability Company Act, and would have to expend a great deal of time and energy to reach a well-considered conclusion, but his ultimate decision would have no precedential value.” It thus appeared reasonable to the court for the trial court to retain jurisdiction over the declaratory judgment claim relating to the retroactive effect of reinstatement after administrative dissolution of an LLC that was a member of another LLC.

Cambio Health Solutions, LLC v. Reardon, 228 F.Supp.2d 883 (M.D. Tenn. 2002)(holding that appeal of order, insofar as it denied motion to compel arbitration, divested district court of jurisdiction pending appeal in case where district court granted order compelling arbitration as to claims related to LLC agreement but declined to order arbitration of claims related to separate consulting agreement).

Prescott-Follett & Associates v. Delasa/Prescott Follett & Associates, No. Civ.A. 01-3178, 2002 WL 31528463 (E.D. La. Nov. 8, 2002)(compelling arbitration of dispute among LLC and its members under arbitration clauses contained in original and subsequent operating agreements, notwithstanding fraud in the inducement claim, where there was no assertion of fraud in the inducement relative to the arbitration clause alone).

MTS Communications Company, Inc. v. Mosaic Capital, No. B141818, 2002 WL 1788948 (Cal.App. 2 Dist. Aug. 5, 2002)(reviewing arbitration award based on sale of business opportunity by LLC that did not hold required license on basis that entire transaction was alleged to be illegal and therefore could not be sanctioned by court even in context of confirmation of arbitration award).

Addison v. Everest Connections Corporation, 37 Fed.Appx. 841 (8th Cir. June 20, 2002)(affirming denial of motion to compel arbitration in suit by former employees of LLC because employees were not parties to LLC agreement containing arbitration clause).

Mississippi Fleet Card, L.L.C. v. Bilstat, Inc., 175 F.Supp.2d 894 (S.D. Miss. 2001)(holding that members of LLC were bound by arbitration clause in processing agreement entered by LLC where members were third party beneficiaries of agreement and asserted claims arising under or related to the agreement).

Metro Riverboat Associates, Inc. v. Bally’s Louisiana, Inc., 817 So.2d 1275 (La. App. 2002)(affirming trial court’s grant of preliminary injunction where arbitration clause permitted one member to invoke arbitration without vote of membership in dispute over cash call and alleged transfer of interest inasmuch as penalty for refusal to arbitrate was forced sale of member’s interest, which would constitute irreparable injury).

Alternative Financial Solutions, LLC v. Colburn, 821 So.2d 981(Ala. 2001).

Two LLCs in the business of making payday loans were sued by borrowers who asserted that the loans violated state lending laws. The LLCs moved to enforce arbitration provisions in the contracts with the borrowers. The court did not find relevant the fact that the LLCs were organized under the law of another state or the fact that the LLC’s owners resided in another state for purposes of determining whether the payday loan transactions substantially affected interstate commerce under the Federal Arbitration Act.

Rice v. Piney Ridge Management, LLC, No. C8-01-763, 2001 WL 1569894 (Minn. App. Dec. 11, 2001).

Rice entered into a Subscription Agreement with an LLC that contained an arbitration clause. Rice also entered a Member Control Agreement that provided for repurchase of membership units under certain circumstances on specified terms. The Subscription Agreement incorporated by reference the Member Control Agreement. Rice filed suit seeking dissolution of the LLC as well as equitable relief against two LLC officers for misapplication of LLC assets and fraud. The officers demanded arbitration although they were not parties to the Subscription Agreement. The arbitrator awarded Rice an amount for his interest in the LLC, for which the LLC and one of the officers were made jointly and severally liable, and the arbitrator also awarded fees and expenses to Rice, for which he made the LLC and the two officers jointly and severally liable. The district court upheld the arbitrator’s award, and the two officers appealed, claiming that the arbitrator exceeded the scope of his authority. The court of appeals held that the arbitrator did not exceed his authority

based upon the broad language of the arbitration clause, Rice's allegations and claims, and the content of the officers' demand for arbitration.

Yazdani-Beioky v. Bhandara, No. 14-00-01509-CV, 2001 WL 1429414 (Tex. App. Nov. 15, 2001).

The court held that the arbitration clause in a two-member LLC's operating agreement did not require arbitration of claims against a separate corporation that contracted to manage the apartment complex owned by the LLC even though the corporation was owned by the members of the LLC and its only activity was managing the sole asset of the LLC.

Raspet v. Buck, 554 S.E.2d 676 (N.C. App. 2001).

The court held that the plaintiff's claims against the defendant were not within the scope of the arbitration clause in the operating agreement of an LLC they formed together because the plaintiff's claims related to the plaintiff's and defendant's employment in another investment firm.

Sordoni Skanska Construction Company, Inc. v. Swanson, 30 Conn.L.Rptr. 188, 2001 WL 985056 (Conn. Super. 2001)(holding that arbitration clause in construction management agreement between plaintiff and LLC required arbitration of claims against LLC and its members.)

Plinke v. PNE Media, LLC, No. Civ.A. 00-1817, 2001 WL 360788 (E.D. Penn. April 3, 2001).

The plaintiff sought to avoid arbitration required by an arbitration clause in an Amended and Restated LLC Agreement on the basis that the plaintiff did not intend a separate signature page that was subsequently attached to the Amended and Restated LLC Agreement to be an execution of that agreement. Various documents were involved in the acquisition of one LLC by another LLC. The plaintiff argued that he was misled into believing that the signature page referred to an earlier executed LLC agreement or to the operating agreement. The court rejected these arguments and found that the evidence indicated the plaintiff understood what he executed to be the signature page to the Amended and Restated LLC Agreement.

Industrial Electronics Corp. of Wisconsin v. iPower Distribution Group, Inc., 215 F.3d 677 (7th Cir. 2000).

The plaintiff and seven other companies, including the defendant iPower Distribution Group, Inc. (iPower), formed an LLC to develop an integrated marketing and distribution consortium using iPower software. Once the LLC was formed, it entered a franchise agreement with iPower to allow the LLC to purchase, install and use the iPower software. The franchise agreement contained an arbitration clause, but the LLC agreement did not. When the plaintiff later sued iPower alleging that iPower had made material misrepresentations to induce the plaintiff to join the LLC, iPower argued that the claim was subject to the arbitration clause in the franchise agreement. The court determined that the injuries alleged did not arise under or relate to the franchise agreement. The alleged fraud related to the inducement of the plaintiff to join the LLC by entering the LLC agreement, and the arbitration provision in the franchise agreement did not affect disputes arising out of the LLC agreement.

In the Matter of the Application of Proto, No. 99 Civ. 3056 (CBM), 2000 WL 1593350 (S.D. N.Y. Oct. 24, 2000)(refusing to vacate arbitration award upholding expulsion of LLC member and application of alleged oral no net deficit rule because misapplication of rules of contract interpretation does not arise to manifest disregard of law).

Staenberg v. Adams, 103 Wash. App. 1028, 2000 WL 1700132 (Wash. App. 2000)(granting LLC member trial de novo after arbitration between members pursuant to arbitration clause in LLC operating agreements and stipulation under certain provisions of Washington law).

Beaver Construction Company, Inc. v. Lakehouse, L.L.C., 742 So.2d 159 (Ala. 1999)(dealing with scope of arbitration clause in contract between LLC, members of LLC, and third party).

Maas Technologies, Inc. v. Henning, No. 98 01751, 1999 WL 269109 (La. App. 3 Cir. March 31, 1999).

The opinion in this case was originally available on Westlaw but was removed and is now only referenced in a table at 744 So.2d 238. Two members of an LLC sued the other two members and a third party alleging that a merger of the LLC into one of the defendant members and then into the third party constituted a conversion of the plaintiffs' assets. The LLC operating agreement had an arbitration clause that required "a dispute arising between the Members concerning the operation, management or buyout of the interest of the LLC" to be submitted to arbitration. The court held that the plaintiffs' claim fell within the scope of the arbitration clause. The court also found that the dispute must be arbitrated even though one of the defendants was not a party to the operating agreement. The court stated that the

plaintiffs' allegations were directed primarily against the member who controlled the entities with which the LLC merged. The court concluded that the first merger (between the LLC and one of its members) was certainly arbitrable and, if found improper, would make any complaint against the company involved in the second merger moot.

Mid-America Surgery Center, L.L.C. v. Schooler, 719 N.E.2d 1267 (Ind. App. 1999).

Two former members of an LLC sued the LLC to enforce the terms of the operating agreement entitling them to be bought out after they resigned as members, and the remaining members voted to continue the operation of the LLC. After the former members filed suit, the LLC sought to require the matter to be submitted to arbitration. The operating agreement had a clause requiring "any dispute, controversy or claim arising out of or in connection with or relating to" the operating agreement to be submitted to arbitration. The former members argued that the arbitration clause was unenforceable because of the LLC's breach of the agreement or, alternatively, because the LLC had waived its right to arbitration. The court rejected both arguments and held that the trial court erred in denying the application for arbitration.

Nuclear Medicine Consultants of Texas v. Bunick, No. 05-99-00570, 1999 WL 998041 (Tex. App. Nov. 4, 1999).

An LLC operating agreement contained an arbitration clause the validity of which was not disputed. The issue in the case was whether the right to arbitrate had been waived. The court held that it had not and ordered the trial court to compel arbitration.

Elf Atochem North America, Inc. v. Jaffari, 727 A.2d 286 (Del. 1999).

One member of a two-member LLC brought suit against the other member, individually and derivatively on behalf of the LLC, seeking equitable damages for breach of fiduciary duty and various other claims. The Chancery Court dismissed the case for lack of subject matter jurisdiction because the LLC agreement contained a choice of forum provision directing that disputes be arbitrated or litigated in California. The Delaware Supreme Court addressed the following questions: (1) whether the LLC, which did not itself execute the LLC agreement, was bound by the provisions of the agreement, and (2) whether contractual provisions requiring all disputes be resolved by arbitration or litigation in California were valid under the Delaware LLC act. The court held that the LLC agreement was binding upon the LLC as well as its members and that the contractual forum selection provisions were valid. The court's opinion goes into the background and policy of the Delaware LLC act and the principle of freedom of contract under the act. The court rejected the argument that, because the LLC itself had not signed the LLC agreement, the LLC was not bound by the provisions of the agreement. According to the court, "It is the members who are the real parties in interest. The LLC is simply their joint business vehicle." The court also held that the Delaware LLC act permits parties to agree to vest exclusive jurisdiction of disputes (including derivative claims) in courts outside Delaware. The act expressly permits LLC members or managers to consent to the nonexclusive jurisdiction of litigation or arbitration in a state other than Delaware, to the exclusive jurisdiction of litigation in Delaware, or to the exclusivity of arbitration in a state other than Delaware. The court noted that the act is silent with regard to agreements vesting exclusive jurisdiction of litigation in courts outside of Delaware and concluded that the General Assembly would have prohibited such provisions if it had desired to do so.

Simitar Entertainment, Inc. v. Silva Entertainment, Inc., 44 F. Supp.2d 986 (D. Minn. 1999).

Simitar Entertainment, Inc. ("Simitar") and Silva Entertainment, Inc. ("Silva Entertainment") formed a Minnesota LLC for the purpose of producing and promoting Tejano music. Simitar and the LLC sued Silva Entertainment and Silva, an individual, alleging breach of contract and numerous other causes of action such as RICO violations, deceptive trade practices, fraud, and breach of fiduciary duty. In a Member Control Agreement governing management of the LLC, an arbitration provision required "any controversy or claim arising out of this Agreement" to be resolved through arbitration. An Employment Agreement between the LLC and Silva also contained an arbitration clause. That clause required arbitration of disputes "of any nature" between Silva and the LLC that "may arise under" the Employment Agreement. The powers of the arbitrator differed under the two agreements in that the Employment Agreement empowered the arbitrator to offer the same degree of relief available through the courts while the Member Control Agreement did not apply to claims involving injunctive relief and only empowered the arbitrator to interpret and apply the provisions of the Member Control Agreement. The Employment Agreement stated that the Member Control Agreement would control any conflict between the two agreements. At the outset, the court noted that it addressed only the motion of Silva, the individual, to compel arbitration, because no motion had effectively been filed on behalf of Silva Entertainment. The court found the scope of the arbitration provisions was limited to damages for breach of contract claims. Thus, only the plaintiffs' breach of contract claim against Silva was referred to arbitration. The court did not

question whether the LLC itself was bound by the arbitration provisions in the Member Control Agreement, which was apparently executed by only the two members, Simitar and Silva Entertainment. The court did note in a footnote that the standing of Silva (an individual who was officer, director, and majority shareholder of Silva Entertainment) to enforce the Member Control Agreement was not entirely clear. The court concluded that Silva was entitled to enforce the Member Control Agreement arbitration provision because of his close relationship to Silva Entertainment and because the Complaint alleged that the misconduct of Silva and Silva Entertainment was not only intertwined but imputed from Silva to Silva Entertainment.

Metro Riverboat Associates, Inc. v. Bally's Louisiana, Inc., 706 So.2d 553 (La. App. 1998).

This case involved the interpretation of arbitration, change of control, and non-competition provisions of an LLC operating agreement. Two corporations, Metro Riverboat Associates, Inc. ("Metro") and Bally's Louisiana, Inc. ("Bally's"), were the members of an LLC formed to own and operate a gambling riverboat. Although Metro had a majority interest, the LLC operating agreement essentially required consent of both members for significant business decisions. When Bally's merged with Hilton Hotels Corporation, Metro claimed there was a "change of control" under the operating agreement that permitted most decisions to be made by a simple majority in interest. In addition, Metro claimed that Bally's was in violation of the non-competition provision of the operating agreement because Hilton Hotels had an ownership interest in another riverboat casino. Eventually, Bally's made demand on Metro for binding arbitration of their disputes, claiming that arbitration was required by the operating agreement. Metro filed suit asking for injunctive relief against Bally's. The court examined the arbitration provision of the operating agreement and concluded that the parties' disagreement was not within the scope of the arbitration clause covering "a dispute. . .with respect to the management and operation of the Company." Rather, their disagreement was over interpretation of contractual provisions that affected their respective management rights. The court next considered the meaning of the change in control and non-competition provisions and concluded that the limited evidence failed to meet the heightened burden of proof imposed on Metro to obtain injunctive relief.

Bubbles & Bleach, LLC v. Becker, No. 97 C 1320, 1997 WL 285938 (N.D. Ill. May 23, 1997).

The court determined that an arbitration clause in an LLC's operating agreement was not binding on the individual members of the LLC. Faye Becker ("Becker"), the managing member of Bubbles & Bleach, LLC ("B & B"), misappropriated funds of B & B. B & B brought suit in Illinois against Becker under the authority of one of its members for conversion, breach of fiduciary duty, and fraud. The Operating Agreement of B & B and the First Amended and Restated Limited Liability Company Agreement of B & B each contained an arbitration clause that required that arbitration of "any matters arising out of the terms and conditions of the underlying agreement" take place in Wisconsin and be governed by Wisconsin law. Becker moved for dismissal based upon the arbitration clause. The court concluded that neither the Operating Agreement nor the Amended and Restated Limited Liability Company Agreement of B & B was binding upon B & B. The agreements provided that they were binding upon the "parties" to such agreement; however, the term "parties" was not defined. The court noted that the LLC Agreement provided that it was by and among the members of the LLC and that the signatories to each agreement were the members. Further, it noted that the Wisconsin LLC statute defines the term "operating agreement" as a written agreement among the members. The court found that there was no indication that the legislature intended to bind LLCs as entities distinct from their constituent members. According to the court, the fact that B & B was a beneficiary of and subordinate to some of the terms of the agreements did not bind B & B under the arbitration clause. Rather, the arbitration clause was binding only upon the parties to the agreement.

L. Nature of LLC; Mischaracterization of LLC (What's In A Name?)

DeGeorge v. Warheit, No. 231953, 2003 WL 1879934 (Mich.App. April 15, 2003) (upholding sanctions imposed on plaintiff for asserting frivolous claims without reasonable basis to believe facts in complaint were true, citing as an example the drafting of the complaint as though "T & T Land Clearing, L.L.C., were a corporation, representing to the court the plaintiff and defendant Philip Warheit formed a corporation and filed its articles of incorporation with a state department, when in fact no such document exists for a limited liability company").

First National Bank of Chicago v. Maynard, 815 A.2d 1244 (Conn.App. 2003) (finding that issuance of bond for deed to LLC rather than individual member who was qualified bidder was irregularity in foreclosure sale because the LLC and its sole member are not the same legal entity, but concluding that irregularity did not cause any harm).

Locascio v. Erie Insurance Group, No. 2002CA00317, 2003 WL 746437 (Ohio App. March 3, 2003) (concluding that insurance policy insured LLC notwithstanding erroneous reference to LLC as partnership where it was clear policy was intended to insure LLC).

The Cafaro Company v. LaserLine Corporation, No. 01-CA-68, 2002 WL 31163738 (Ohio App. Sept. 26, 2002).

Fact issues regarding the type of business entity the parties to an agreement intended to form when they agreed to discharge a corporation's obligations by forming a "limited liability corporation" precluded summary judgment to recover on the corporation's obligations. The court found that the erroneous term did not render the agreement invalid or unenforceable, but it did create an ambiguity and a fact question.

Charpentier v. R&R Resort, Inc., 112 Wash. App. 1017, 2002 WL 1316232 (Wash. App. 2002).

The plaintiff sued her employer for hostile work environment and related claims. The complaint inaccurately identified the employer as a partnership rather than an LLC. The LLC's lawyer contacted the plaintiff's lawyer informing her of the mistake and offering to accept service of an amended complaint. The complaint was not amended, and the court dismissed it. A year and half later, an amended complaint was filed. In the new complaint, the plaintiff misidentified the LLC as a corporation. Two months later, after limitations had run, the defendant moved to dismiss the complaint, and the plaintiff moved to amend. The trial court denied the motion to amend and granted the motion to dismiss. The plaintiff appealed, arguing the trial court abused its discretion in finding inexcusable neglect on the part of the plaintiff. The plaintiff's lawyer explained that her files had been moved to off-site storage during the time the plaintiff was deciding whether to pursue a second lawsuit, and she did not have access to the documents showing the defendant was an LLC. The court took issue with this argument, stating that the plaintiff's lawyer chose not to access her files and to use the Washington Secretary of State's web site instead. The court acknowledged that the information in the web site is confusing in that LLC information is contained in the corporations database and refers to the "state of incorporation" and "date of incorporation." Under "category," the site indicated the defendant was a "limited liability regular." The plaintiff's lawyer assumed that LLC meant limited liability corporation. The court stated that the plaintiff's lawyer had no justification for assuming that the defendant was a corporation given the notice she received in the first lawsuit, the information obtained in the database search, and the availability of the LLC statute. The court concluded the failure to name the defendant as an LLC was inexcusable neglect and that the trial court's dismissal of the suit and award of attorney's fees to the defendant was proper.

Housing 21, L.L.C. v. Atlantic Home Builders Company, 289 F.3d 1050 (8th Cir. 2002)(holding that identities of LLC investors, among which were several charities, were irrelevant in suit where LLC, a distinct legal entity, was the sole plaintiff, and informing jurors of identities in response to inquiry from jury during deliberations was reversible error).

Board of Education v. Franklin County Board of Revision, Nos. 01AP-878, 01AP-879, 2002 WL 416953 (Ohio App. March 19, 2002)(distinguishing LLC from partnership, an aggregate of individuals, and characterizing LLC as separate legal entity like corporation for purposes of requirement that it be represented by attorney in property tax valuation dispute, and holding statute permitting LLC member to file a complaint on behalf of LLC unconstitutional insofar as it permits persons who are not attorneys or owners of property to file a complaint before a board of revision on behalf of the owner).

Cogniplex, Inc. v. Hubbard Ross, L.L.C., No. 00 C 7463, 00 C 7933, 2001 WL 436210 (N.D. Ill. April 27, 2001).

When the relationship between three members of an LLC soured, two of the members sued the third for various breaches of duty and violations of law. One of the claims was for breach of contract. The three members had failed to agree upon and execute an operating agreement, and the defendant argued that the relationship was thus not contractual. The court, however, determined that the claim withstood dismissal at the preliminary stage of the litigation based upon the permissive provisions of the Illinois Act regarding actions by members. The court cited the provision of the Illinois Act that authorizes members to bring an action against the LLC or other members to enforce their rights under the operating agreement or the Act or other rights and interests. The court noted that the statutory provision might not be directly on point but suggested that the breach of contract claim would not offend the spirit of the Act. The court indicated that whether the claim was ultimately viable would depend upon the specifics of how the LLC was structured, i.e., whether it was more like a corporation or a partnership. The court indicated that co-shareholders are not ordinarily

contractually bound to each other while partners are bound by a contract of mutual agency. The court stated that it did not have sufficient information regarding the organizational structure to determine which principle would apply.

General Electric Company v. County of Cook, No. 00 C 6587, 2001 WL 417321 (N.D. Ill. March 5, 2001).

The court found that a Delaware LLC falsely represented itself as a joint venture in a bid proposal submitted in connection with construction of a county hospital. The ordinances and the instructions to bidders apparently addressed partnerships and/or joint ventures and corporations but not LLCs. The LLC identified itself as a joint venture and submitted the execution form for a joint venture. The court found that the LLC was not a joint venture for purposes of meeting certain requirements regarding participation in minority and women's business enterprises and failed to meet certain other requirements. The court stated that the LLC, as a corporate entity, failed to comply with the requirements for corporate bidders. The court found that the LLC encouraged the county to believe that one of the LLC members would be personally responsible as a member of a joint venture when in fact the member would have no liability for the LLC's obligations.

Royal Mortgage Corporation v. Montague, 41 S.W.3d 721 (Tex. App. 2001) (rejecting the argument that an LLC's partnership returns established that the LLC was a partnership and pointing out that the K-1's as well as other documentation indicated the company was an LLC).

Morelli v. Morelli, No. 2:00-CV-988, 2001 WL 99859 (S.D. Ohio Feb. 1, 2001).

In this action between two brothers for dissolution of a partnership and partition, the spouse of the plaintiff brother was allowed to intervene for the purpose of asserting that the partnership was actually an LLC. The two brothers had purchased several parcels of real estate and conveyed title to Morelli Properties, LLC. Although the plaintiff's spouse produced evidence that articles of organization had been filed with the Ohio Secretary of State, her husband alleged that the articles of organization were never filed, that the LLC had never operated as an LLC, and that it had no separate existence apart from the brothers as an implied-in-fact partnership. The brothers argued that the plaintiff's spouse had at best a dower interest in the properties allegedly transferred to the LLC. The court concluded that the spouse had the right to intervene because she possessed a significantly protectable interest, a decision on the merits would impact her interest, and her interest would not be adequately protected by the existing parties. Additionally, the court concluded that the spouse met the standards governing permissive intervention.

Frontier Traylor Shea, LLC v. Metropolitan Airports Commission, 132 F. Supp.2d 1193 (D. Minn. 2000).

Three members of an LLC submitted a statement during the pre-qualification process associated with bidding on an airport construction project. In the statement, the members identified their entity as "Frontier/Traylor/Shea joint venture" and identified it as a "joint-and-several joint partnership." Subsequently, the LLC submitted the lowest bid, but the airport commission rejected the bid on the basis that the entity was not pre-qualified since it was an LLC rather than a joint venture partnership, the status indicated by the Frontier entity that was pre-qualified. The LLC sought injunctive relief and argued that it was a joint venture, citing a treatise and some cases referring to an LLC as a joint venture. The airport argued that a joint venture is a form of partnership and cannot take the form of an LLC. The court concluded that the airport commission's decision was not illegal, arbitrary, capricious, or unreasonable "[g]iven the lack of clarity in the status of when a limited liability corporation [sic] is legally a joint venture and the conflicting documents presented" to the airport commission.

All Comp Construction Company, LLC v. Ford, 999 P.2d 1122 (Okla. App. 2000) (stating that an LLC is a fictional "person" for legal purposes and, as such, is not entitled to recover damages for mental stress and anguish as a natural person would).

Abner Realty, Inc. v. Administrator of General Services Administration, No. 97 Civ. 3075(RWS), 1998 WL 410958 (S.D. N.Y. July 22, 1998).

An LLC defendant was awarded Rule 11 sanctions against the plaintiff and its lawyer based upon their failure to make the reasonable inquiry required under Rule 11. The plaintiff's repeated erroneous references to the LLC as a limited partnership were among numerous factors the court felt demonstrated the plaintiff's lack of reasonable inquiry. The court pointed out that certificates of formation and certificates of limited partnership are public records. Furthermore, the plaintiff continued to refer to the LLC as a limited partnership even after the LLC filed motions making it clear it was an LLC. The court gave various other examples of erroneous or unsubstantiated allegations and ordered both the plaintiff and the plaintiff's lawyers to pay monetary sanctions and write letters of apology.

M. Limited Liability of Members and Managers; Personal Liability Under Agency or Other Law

Evans v. Testa Development Assoc., No. CV010806425, 2003 WL 21101307 (Conn.Super. April 24, 2003) (holding that individual who acted only in his capacity as manager/member of LLC was not personally liable for LLC's wrongful prosecution of prior lawsuit and stating that elementary principle of corporate law that corporation and its stockholders are separate entities also applies to LLCs).

Hoang v. Arbess, __ P.2d __, 2003 WL 1842878 (Colo.App. 2003) (holding that LLC manager, like officer of a corporation, may be held personally liable for approving, directing, actively participating in, or cooperating in negligent conduct and that there was evidence sufficient to hold manager liable so that directed verdict in favor of manager was improper).

Black v. Bruner, No. 04-02-00733-CV, 2003 WL 724312 (Tex.App. March 5, 2003) (concluding that LLC member was not personally liable for LLC's contractual indemnity obligation in the absence of any evidence that the regulations provided that its members were individually liable for the LLC's debts).

Imperial Trading Co., Inc. v. Uter, 837 So.2d 663 (La.App. 2002) (affirming trial court's finding that supplier knew or reasonably should have known that LLC managers were acting in representative capacity and that members had refuted claim of undisclosed agency).

Rothstein v. Equity Ventures, LLC, 750 N.Y.S.2d 625 (N.Y. A.D. 2 Dept. 2002) (stating that LLC members may be held liable if they personally participate in the commission of a tort in furtherance of company business, but finding that allegations did not state viable claim because there were no allegations that defendants knowingly made any false representations inducing plaintiffs to purchase house and allegations regarding improper construction sounded in breach of contract rather than tort).

J. C. Compton Co. v. Brewster, 59 P.3d 1288 (Or.App. 2002) (finding evidence that LLC member contracted to pay debts of LLC and its predecessor).

Lexington Land Company, LLC v. Howell, 567 S.E.2d 654 (W. Va. 2002)(referring to LLC and its member interchangeably, but acknowledging in footnote that LLC is separate from its members and that creation of LLC offers its members liability protection).

Cooper v. Creative Homes of Distinction, L.L.C., No. COA01-1138, 2002 WL 2004298 (N.C. App. Sept. 3, 2002).

The plaintiffs, employees of an LLC, sued the LLC, its manager, and certain transferees of the LLC's property for unpaid wages and losses from unlawful distributions. The plaintiffs obtained a judgment holding the manager liable on these claims. The court of appeals cited the statutory provisions regarding the limited liability of members and managers and reversed the judgment because the manager was merely an agent of the LLC and not a party to the employment contracts with the plaintiffs. The trial court made no findings that the manager itself had agreed to be bound by the employment contracts with the plaintiffs or that the manager employed, terminated, failed to make wage payments to, or was indebted to the plaintiffs. Rather, it was the LLC that employed, failed to pay wages to, and was indebted to the plaintiffs. The trial court also made no findings that the manager was involved in the unlawful distribution of assets so as to support imposing liability based on the distributions.

Stuyvesant Fuel Service Corp. v. 99-105 3rd Avenue Realty LLC, 745 N.Y.S.2d 680 (N.Y. City Civ. Ct. 2002).

Members of an LLC who were sued individually moved to dismiss on the basis that the building in question was owned by the LLC, that any contracts with the plaintiff were with the LLC, that the members did not sign any contracts in their individual capacity or guarantee any of the LLC's debts to plaintiff, and the New York LLC law provides that members are not personally liable for LLC debts. The court denied the motion to dismiss because the statute provides that the articles of organization may provide for personal liability of members, and the members failed to provide a certified copy of the articles organization from which the court could ascertain whether the members had personal liability.

Warren Supply Company v. Lyle's Plumbing, L.L.C., 74 S.W.3d 816 (Mo. App. 2002).

A member of an LLC appealed a judgment holding him personally liable for the LLC's debt. The basis of the judgment against the member was that he had signed a credit application in the guaranty portion with the designation "member" after the signature. The member argued that the guaranty was ambiguous for various reasons, including the fact that the document was only signed in one place (the credit application portion itself was not signed) and the signature was qualified with the notation "member." The court held that the document was not ambiguous because the member did not disclose his principal, and the court upheld the trial court's imposition of personal liability without considering parol evidence.

Neato, LLC v. Soundview Partners, 32 Conn.L.Rptr. 219, 2002 WL 145579 (Conn.Super.2002)(construing complaint as alleging fraudulent conduct on part of member individually (for which member would have personal liability regardless of liability protection provided by LLC) rather than an attempt to pierce the veil).

Fleet One, LLC v. Cook, No. 4618, 2002 WL 1189559 (Tenn. Ct. App. June 5, 2002)(analyzing agency principles and language of contract in concluding that individual who signed credit application as "operations manager" of LLC did not have personal liability as guarantor).

Way v. Andries, 819 So.2d 465 (La. App. 2002)(holding that statutes did not impose personal liability on LLC members or managers for parish taxes).

Alexander Company, Inc. v. Bensaid, No. 01-1309, 2002 WL 1034037 (Wis. App. May 23, 2002)(affirming judgment imposing personal liability on member of two-member LLC on basis that members were partnership by estoppel where LLC members did not disclose form of their business to creditor, members used phrases such as "we are going to do this" and "we are going to do that" in meeting with creditor, payment required by creditor before beginning work was check drawn on personal account of member, and letter regarding financial capability from bank indicated that individual member had been approved for loan).

Christensen v. Rostand Associates, No.CV010075818S, 2002 WL 1042149 (Conn. Super. May 2, 2002)(denying summary judgment in favor of LLC members with regard to injury occurring on premises owned by LLC because material fact of members' possession, maintenance, or control of property was disputed).

Kline v. Keystar One. L.L.C., No. 99-1649, 2002 WL 681237 (Iowa App. April 24, 2002)(affirming judgment imposing personal liability on LLC member because issue was not preserved for review).

Quantum Color Graphics, LLC v. The Fan Association Event Photo GmbH, 185 F.Supp.2d 897 (N.D. Ill. 2002)(holding that allegations were sufficient to state claim for personal liability of individual owner of German companies and California LLC on basis that individual acted for partially disclosed principals).

Ehle v. Williams & Boshea, L.L.C., No. Civ.A. 01-3757, 2002 WL 373271 (E.D. La. March 7, 2002)(finding joinder of individual who claimed he could not be liable because he was member of LLC was not fraudulent where there was evidence LLC was never formed and plaintiff asserted claims based upon negotiations to form LLC).

Curole v. Ochsner Clinic, LLC, 811 So.2d 92 (La. App. 2002).

The plaintiff, a doctor employed by an LLC clinic, sued the LLC and several doctors affiliated with the clinic after the plaintiff was terminated, alleging various claims based on tortious interference with business relationship, unfair competition, and defamation. The plaintiff argued that the CEO of the LLC was personally liable for these acts. The court found the CEO was protected under the statutory provision protecting an LLC member, manager, employee, or agent from personal liability. The plaintiff argued that liability could be premised on the language of the statute preserving liability for any negligent or wrongful act of a member, manager, employee, or agent. The court stated that, to give the statute meaning, the phrase would have to refer to acts done outside one's capacity as a member, manager, employee, or agent, and the allegations did not set forth facts showing the CEO acted outside his capacity as an LLC officer.

First Fairfield Funding, LLC v. SSMLN, LLC, No. X06CV000167489S, 2002 WL 194538 (Conn. Super. Jan. 15, 2002)(seeking to hold LLC manager and member liable based on individual's own participation in commission of tort rather than status as a member or manager).

F & G Investments, L.L.C. v. 1313 Hickory, Ltd., 807 So.2d 1004 (La. App. 2002).

The lessor of premises occupied by an LLC sought to hold the individual who signed the lease on behalf of an LLC personally liable on the lease, arguing that the individual signed the lease in his personal capacity. Though the signature form was somewhat ambiguous, the court found the lease as a whole did not indicate that the individual was signing in his personal capacity. The lease stated that it was between two LLCs, a space for the individual to sign as surety was left blank, and the court construed the ambiguity against the plaintiff since the words under the signature lines were provided by the plaintiff.

Wirthman-Tag Construction Company, L.L.C. v. Hotard, 804 So.2d 856 (La. App. 2001).

Two individuals signed a construction contract on behalf of a business that was not designated as an LLC. The individuals claimed that the other parties knew of the agency relationship and understood the individuals were signing in a representative capacity. The court found that there was a triable issue of fact in this regard.

Magara v. Pepitone, No. CV000441504S, 2001 WL 1420664 (Conn. Super. Oct. 26, 2001) (refusing to allow collateral attack on default judgment against individuals who claimed that they were members of an LLC and not personally liable to the plaintiff).

Baumstein v. Myklebust, No. 01-0614, 2001 WL 869506 (Wis.App. Aug. 2, 2001).

An LLC member appealed a judgment against him personally in the amount of the plaintiff's earnest money down payment on the purchase of a lot. The court stated that the judgment was proper because the defendant had signed documents relating to the sale without indicating that he was acting as an agent of the LLC.

Harold Cohn & Co., Inc. v. Harco International, LLC, No. CV990089169, 2001 WL 523540 (Conn. Super. May 2, 2001) (relying upon cases in the corporate context holding that an officer or shareholder who commits a tort is liable regardless of whether the corporation is liable and stating that it was unnecessary to pierce the veil of the LLC because the individual himself committed the fraud).

Matjasich v. State of Kansas Dept. of Human Resources, 21 P.3d 985 (Kan. 2001).

The Kansas Supreme Court held that a member of a Utah LLC was personally liable for unpaid wages under Utah's wage payment laws, which provided for such personal liability. The court analyzed the Kansas Wage Payment Law and concluded that it did not provide for personal liability of LLC members because the definition of employer had not been amended to include LLCs along with corporations, partnerships, etc.; however, the court concluded that the Utah wage payment law rather than the Kansas law governed the liability of the members of the Utah LLC for unpaid wages arising out of its business in Kansas. With respect to the interpretation of Kansas law, the court acknowledged that a corporate officer who knowingly permits the corporation to violate the wage payment law would have personal liability under the Kansas Wage Payment Law, but the court pointed out that the wage payment law did not address LLCs, and the Kansas LLC Act not only provided for limited liability of members and managers but specifically provided that an LLC was not to be construed as a corporation. The court concluded, however, that the Utah wage payment law (which is more broadly drafted and under which the LLC member would have liability for unpaid wages) applied even though the LLC was an employer in Kansas because the Kansas LLC Act provides that the laws of the jurisdiction of organization govern the internal affairs and the liability of members. The court construed these provisions to include not only the LLC act but other laws bearing on member liability.

Rodale Press, Inc. v. Salm, No. CV000374983S, 2001 WL 496895 (Conn. Super. April 25, 2001) (holding that a member of an LLC was personally liable on the basis that the LLC did business under a trade name without filing a trade name certificate as required by Connecticut law).

Dornfried v. Granquist, No. CV000502628S, 2001 WL 306851 (Conn. Super. March 13, 2001).

The plaintiff sought to hold the individual owner and manager of an LLC liable for breach of contract, but the court determined that the plaintiff's contract was with the LLC and that the contract adequately disclosed the representative capacity of the individual who signed as "manager." The court emphasized that the LLC statutes give the term "manager" a special connotation and protect managers from liability to third parties. The court rejected the plaintiff's arguments that the court should disregard the liability shield of the LLC under the instrumentality or identity rule because the plaintiff failed to plead either theory.

450 West 14th St. Corp. v. 40-56 Tenth Ave. L.L.C., 724 N.Y.S.2d 273 (N.Y. Sup. 2001) (dismissing executrix of the deceased sole member of the LLC on the basis that a member of an LLC is not a proper party to an action against the LLC).

Harmon Building Associates v. Weinmann, No. 23021, 2000 WL 33146961 (Va. Cir. Ct. Sept. 27, 2000).

Two individuals who signed a lease on behalf of an LLC argued that the lessor should not recover against them personally because the name of the LLC was incorrect. It is unclear why the defendants thought that the discrepancy in the name protected them from personal liability. It is also unclear whether the discrepancy in the name turned out to be the basis on which they were held liable. In any event, the court refused to modify the lease and entered judgment in the amount of the balance due on the lease.

Whitmore v. Hawkins, No. 99-1443, 2000 WL 828285 (4th Cir. June 27, 2000).

Whitmore was employed to be the chief operating officer of an LLC. Hawkins, an individual, recruited Whitmore and signed the employment agreement on behalf of the LLC. Hawkins did not sign in an individual capacity, but the employment agreement's initial paragraph recited that the parties were the LLC, Whitmore and Hawkins. When Whitmore was later terminated, he sought to hold Hawkins personally liable for the severance pay to which he was entitled under the contract. The court found that the agreement was ambiguous with respect to the liability of Hawkins since he did not sign in an individual capacity but was referred to as a party in the contract. The court examined the extrinsic evidence and concluded it was sufficient to create an issue for the jury as to personal liability of Hawkins under the contract. Thus, the court reversed the trial court's dismissal of Hawkins from the case.

United States v. Washington Mint, L.L.C., 115 F. Supp.2d 1089 (D. Minn. 2000).

Referring to an LLC member as a controlling shareholder of the LLC's stock, the court concluded that such status was not alone sufficient to impose liability on the LLC member for the LLC's copyright or trademark infringement. The court also found that ownership of a significant interest in the controlling member and a position on what the court referred to as the board of directors of the LLC did not amount to a showing of any direct participation and control over the LLC's activities sufficient to impose liability for the copyright and trademark violations. A corporation that leased employees to the LLC and certain individual officers of the corporation as well as the CEO of the LLC were found to have sufficient involvement in the LLC's activities to be liable for some or all of the violations.

ABC, LLC v. State Ethics Commission, No. CV 00-0504071S, 2000 WL 1701226 (Conn. Super. Oct. 11, 2000)(mentioning Commission ruling that individual members of an LLC can be subjected to civil penalties with respect to prohibited contingent fee lobbying agreements entered by the LLC).

Addy v. Myers, 616 N.W.2d 359 (N.D. 2000).

The court rejected the plaintiffs' claim that a member of an LLC agreed to assume personal liability for the LLC's debt. The LLC involved had four members, consisting of two individuals and two entities. Informally, the group consisted of four families. When the LLC experienced financial difficulties, two individuals in the group personally signed for several lines of credit over a period of months. These individuals argued that the defendant member of the LLC and her husband agreed to assume personal liability for a portion of the debt. The court concluded that the defendant was not liable as a guarantor because she did not sign a written guaranty (as required by the North Dakota Statute of Frauds to enforce a guaranty). The plaintiffs argued that the defendant was liable as a member of the LLC because a majority of the members voted to borrow the funds for the LLC and to assume equally the debt. The court discussed the principle that an LLC is a separate legal entity whose members are not liable for its debts and obligations and concluded that the defendant member was not liable because she did not agree to be liable for any part of the loan. The court of appeals also upheld the trial court's dismissal of the member's husband because there was no evidence that he was a named owner or manager of the LLC or had done anything to personally obligate himself on the borrowing in issue.

The Color Bar Printing Company v. Litt, No. 76715, 2000 WL 193251 (Ohio App. Feb. 17, 2000).

The plaintiff sued two individuals for breach of contract, and the individuals asserted that they were not personally liable because they were "limited liability partners in an entity known as Windstar Publications, Ltd." Later in the opinion, Windstar Publications, Ltd. is identified as an Ohio limited liability company. The court noted that the plaintiff had named the individuals as parties, not the LLC, and that the complaint alleged that the individuals had breached their contract with the plaintiff. The court concluded that the complaint stated a claim against the individuals.

Harris v. Guetersloh, No. 07-99-0046-CV, 2000 WL 12523 (Tex. App. Jan. 6, 2000).

The defendants, three individuals, were held personally liable on a contract executed on behalf of “Reo Harvest” without any language or abbreviation indicating that Reo Harvest was an LLC. On appeal, the defendant complained of the trial court’s exclusion of evidence that Reo Harvest was a New Mexico LLC and that the plaintiff had notice of that fact prior to the signing of the contract. The appeals court held that it was not error to exclude the evidence because the defendants had failed to properly plead the defenses that would support their claim of non-liability as members of an LLC. The applicable defenses required verified pleas which the defendants failed to present.

Hosale v. Warren, No. 01A01-9810-CV-00523, 1999 WL 548538 (Tenn. App. July 29, 1999).

A creditor sued a member of an LLC construction company for payment on a project, and the trial court found in the creditor’s favor. On appeal, the court held that the defendant’s statement of the issues was inadequate, but the court went on to note that the evidence did not preponderate against the trial judge’s findings. The opinion gives little insight into the facts but does note the creditor’s contentions that the creditor was never told of the LLC, that the defendant represented the entity as a joint venture, and that the defendant told the creditor that he and the other LLC member were involved in a partnership.

Anthony v. Blum, No. CV 960336878S, 1999 WL 259726 (Conn. Super. April 23, 1999).

The plaintiff sought to hold a member of an LLC law firm liable on a promissory note executed by the LLC. The promissory note was executed to repay the plaintiff for negligent legal services provided by the member. The court acknowledged statutory provisions making clear that a member is liable for his own negligent or wrongful acts; however the member in this case was not liable since the action was a breach of contract action for payment of the note and not a malpractice action against the member. The member signed the note as a member of the LLC and on behalf of the LLC, and the contractual obligation represented by the note was an LLC debt from which the member was protected by the statutory limitation of liability of members.

Creative Resource Management, Inc. v. Soskin, No. 01A01-9808-CH-00016, 1998 WL 813420 (Tenn. App. Nov. 25, 1998).

An individual signed a contract as president of an LLC. The court recognized that personal liability of LLC officers, members, and other agents is limited by the Tennessee LLC act and that ordinarily a signature of a corporate officer preceded by the corporation’s name and followed by a designation of corporate capacity is a signature in a representative rather than individual capacity. However, the contract in question contained personal guarantee language, and the court concluded that the language could not refer to the LLC. According to the court, the language had to reflect the personal guarantee of the individual who signed the agreement.

Michaud v. Quinn, No. CVNH 97108476, 1998 WL 667162 (Conn. Super. July 9, 1998).

The plaintiff sued the defendant, an individual, for past due rent the plaintiff claimed was owed under an oral agreement for the sublease of office space from the plaintiff. The same month the defendant arranged for the use of the office space and moved into the space, the defendant formed an LLC. The defendant gave the plaintiff business cards for the LLC and showed the plaintiff his new stationery. The defendant denied that any rent was owed and argued that, if any rent was owed, it was owed by the LLC. The court stated that whether the agreement was entered into by the defendant in his individual or representative capacity was a question of fact, and the court found that the agreement was entered by the defendant individually. The court noted the defendant’s testimony that he did not specifically say he would be renting as an LLC. That the plaintiff may have known the defendant was forming an LLC was insufficient to charge the plaintiff with knowledge that he was dealing with an LLC. As an aside, the court indicated that an LLC could become liable for pre-formation debts just as a corporation may become liable for pre-incorporation debts by acceptance of the benefits of a transaction.

Page v. Roscoe, LLC, 497 S.E.2d 422 (N.C. App. 1998).

In this case, the court found that the plaintiff’s naming of an individual member of an LLC in a nuisance suit was improper and was a basis for sanctions under Rule 11 of the North Carolina Rules of Civil Procedure. The plaintiffs brought a nuisance action against an LLC and a member of the LLC based upon the LLC’s plan to build a gas storage facility. The plaintiffs eventually dismissed all of their claims, and the LLC and its member sought Rule 11 sanctions. The court found that the plaintiffs’ allegations against the LLC were sufficient to avoid Rule 11 sanctions; however, the court found that the allegations against the individual member were not well-grounded in law and violated Rule 11. The court cited provisions of the North Carolina LLC act providing that an LLC member is not liable for the obligations of the LLC solely by reason of being a member and that a member is not a proper party to a proceeding against an LLC.

Since the plaintiffs' complaint did not allege any acts on the part of the member individually, the naming of the individual member was not well-grounded in law and violated Rule 11.

Water, Waste & Land, Inc. v. Lanham, 955 P.2d 997 (Colo.1998).

In this case, two individuals who were members and managers of an LLC were held personally liable on a contract with a third party under the partially-disclosed principal doctrine. Under well established common law agency principles, if an agent contracts for a partially-disclosed principal (i.e., the third party knows of the existence of the principal but does not know the principal's identity), the agent is personally liable on the contract as a general rule. In this case, Preferred Income Investors, L.L.C. was identified only as P.I.I. to the third party. The court rejected the argument that the constructive notice provisions of the Colorado LLC act protected the individuals from liability since they failed to adequately identify the LLC principal.

In re National Credit Management Group, L.L.C., 21 F. Supp.2d 424 (D. N.J. 1998).

The FTC and State of New Jersey brought an action against an LLC and its member/officers for violation of federal and state consumer protection laws. The court found that the individual defendants were liable under provisions of the Federal Trade Commission Act that make individuals liable for acts of a corporation where the individuals exercise certain control or authority related to the violations. The court concluded that the same standard should apply to determine the liability of LLC members.

Bayside Tire & Exhaust LLC v. Alabama Dept. of Revenue, Ala. Admin. Law Division, No. 98-272 (Oct. 13, 1998) (noted in BNA Business Law Advisor Vol. 1, No. 6).

An administrative law judge decided that a member of an LLC had personal liability for the tax liability of the LLC, but the Alabama Department of Revenue was not entitled to collect the LLC's outstanding tax assessment from the member because the member was not assessed in his individual capacity. The Department had twice contacted the LLC about outstanding W-2 forms. When the LLC failed to respond, the Department issued a penalty assessment for each missing W-2. The judge stated that an LLC is treated as a partnership for tax purposes in Alabama, and a member is thus individually liable for the tax (citing the partnership act provision on partner joint and several liability). However, the member was not liable because he was not assessed in his individual capacity (citing the partnership act provision that a judgment against a partnership is not itself a judgment against a partner).

Zaugg & Zaugg Architects v. Wagner, No. 96-CA-117-2, 1997 Ohio App. LEXIS 3987 (Ohio App. Aug. 8, 1997).

Six parties agreed to enter a venture to build a residential golf course development. Two of the parties, John Zaugg and Marion Zaugg, had an architectural partnership. At the initial meeting of the group, the Zauggs were employed to do architectural work for the project. Part of their payment was to be in the form of an ownership interest in the venture, but no written agreement was entered, and details regarding the arrangement were left unresolved. Ultimately, about a year after the Zauggs began working on the venture, the parties formed an LLC. When the Zauggs submitted their bill to the LLC a few months later, it was a source of contention. The Zauggs and two other members of the LLC signed a statement of understanding in which they agreed that the Zauggs would accept a specified amount in payment for their services. The court upheld the trial court's judgment imposing personal liability for the Zauggs' architectural fees upon the other two members who signed the statement of understanding. The court noted that the document did not indicate that the debt was owed by the LLC, and the members signed the document without indicating representative capacity.

N. Veil Piercing

1. Piercing to Impose Liability

KLM Industries, Inc. v. Tylutki, 815 A.2d 688 (Conn.App. 2003) (noting that trial court's reference to corporate defendant as LLC was incorrect and disagreeing with trial court's decision to pierce the corporate veil, but agreeing with trial court that the determination of whether to pierce the corporate veil of a stock corporation or to disregard the LLC requires the same analysis).

Advanced Telephone Systems Inc. v. Com-Net Professional Mobile Radio LLC, 59 Pa. D & C.4th 286 (Pa.Ct.Com.Pl. May 15, 2003) (concluding that plaintiff in breach of contract action was not entitled to pierce the veil

of an LLC where plaintiff (which was run by sophisticated businessmen) knew it was dealing with an LLC and sought no guaranties).

Dornfried v. Granquist, No. CV000502628, 2003 WL 1996024 (Conn.Super. March 27, 2003) (holding that evidence was not sufficient to pierce veil of single-member LLC and hold member liable for LLC's breach of contract).

Imperial Trading Co., Inc. v. Uter, 837 So.2d 663 (La.App. 2002) (affirming trial court's finding that plaintiff failed to prove LLCs were disregarded to extent that they were indistinguishable from their members under corporate veil-piercing standards, and noting that such ruling did not constitute any opinion as to whether veil piercing is available in the case of LLCs as it is in the case of corporations).

Warburton/Buttner v. Superior Court (Tunica-Biloxi Tribe of Louisiana, real party in interest), 127 Cal.Rptr.2d 706 (Cal.App. 2002).

The plaintiff, a casino developer, contracted with a Delaware LLC controlled by the Tunica-Biloxi Tribe. The Tribe was a 51% member of the LLC when the suit was filed and subsequently became 100% member. The plaintiff sued the LLC for breach of contract and alleged that the Tribe was the LLC's alter ego. Whether the Tribe had waived its sovereign immunity was in dispute in the case. The trial court denied the plaintiff's motion to compel discovery and granted the Tribe's motion for summary judgment on the basis of Tribal sovereign immunity. The appellate court granted the plaintiff's petition for mandamus, finding that the plaintiff was entitled to proceed with discovery on matters bearing on subject matter jurisdiction/Tribal sovereign immunity. In setting forth the rules regarding liability of LLC members, the court relied upon California law, noting that it had not been provided with any references to how Delaware law may differ from California law in this respect. The court cited the provisions of the California LLC act that provide for limited liability of members and that adopt the common law of alter ego liability. The court appeared to accept the possibility that alter ego liability might be established in reaching its conclusion that discovery should be allowed to proceed. The court referred to allegations of commingling of funds, lack of corporate formalities, and undercapitalization of the corporate entity.

J. C. Compton Co. v. Brewster, 59 P.3d 1288 (Or.App. 2002).

The plaintiff sought to hold an LLC's member liable for attorney's fees for breach of a contract between the plaintiff and the LLC. While the jury found that improper undercapitalization of the LLC caused the LLC to breach its contract, the jury found no damages from the undercapitalization. According to the court, the damages resulted from the member's own breach of its separate contract with the plaintiff (under which the member assumed payment of the LLC's debts) not from a breach of contract by the LLC for which it might be responsible as an alter ego.

Hunter v. Youthstream Media Networks, Inc., 241 F.Supp.2d 52 (D. Mass. 2002).

The plaintiff moved for pre-trial equitable attachment of the assets of an LLC member, alleging that the LLC member was liable for the LLC's breach of contract based on veil-piercing principles. The court denied the motion. The court found that the plaintiff failed to establish he was likely to prevail on the piercing claim. The court cited corporate veil-piercing cases and set forth the following factors considered in a corporate veil-piercing case: insufficient capitalization, non-observance of corporate formalities, nonpayment of dividends, insolvency of the corporation at the time of the litigated transactions, siphoning of corporate funds by dominant shareholders, non-functioning officers and directors other than shareholders, absence of corporate records, use of the corporation for transactions of dominant shareholders, and use of the corporation in promoting fraud. The court acknowledged that the plaintiff's evidence portended some indicia of control by the member over the LLC but pointed to a dearth of evidence with respect to most of the factors listed above.

Emma Rosina, LLC v. Bilides Building & Excavating, LLC, No. CV020462976S, 2002 WL 31898066 (Conn.Super. Dec. 10, 2002)(striking conclusory allegations of unity of interest, lack of separateness, alter ego, and instrumentality because complaint did not set forth factual basis to support such allegations where plaintiff sought to pierce LLC veil and hold member personally liable).

Iron Workers Local 58 v. Citizens Bank, No. Civ.A. 02-1848, 2002 WL 31427329 (E.D. La. Oct. 25, 2002)(holding allegations that LLC was formed to evade paying plaintiffs moneys owed under collective bargaining agreement, when liberally construed, were sufficient to avoid motion Rule 12(b)(6) motion to dismiss, and individual organizer of LLC might have personal liability under alter ego or successor liability theories).

Mowles v. Predictive Control Systems, LLC, Nos. Civ.A. CV-02-355, CV 02-356, 2002 WL 31546164 (Me.Super. Oct. 22, 2002)(finding veil-piercing allegations were sufficient to state a cause of action against LLC's 75% member where plaintiff alleged that member "dominates the managerial and financial affairs of [the LLC] in such a way that makes it unjust for him to benefit from [the LLC's] limited liability").

Westmoreland Associates, LLC v. Kispert, No. 082774/99, 2002 WL 50474 (N.Y.City Civ.Ct. Sept. 20, 2002)(stating that formation of LLC to avoid personal liability is perfectly legal, and refusing to pierce veil of LLC landlord and hold members liable for overcharge because corporate status or nature of the business organization must be used to perpetrate fraud, and LLC status of landlord was irrelevant to tenant's payment of rent).

Leber v. Universal Music and Video Distribution, Inc., 225 F.Supp.2d 928 (S.D. Ill. 2002).

The plaintiffs sued for breach of a collective bargaining agreement of Universal Music and Video Distribution, Inc. ("Universal") and sought to hold an LLC in which Universal was a member and the LLC's other corporate member ("Panasonic") liable under various theories, including alter ego. The court applied the alter ego doctrine as it has developed in the labor law context and concluded that neither the LLC nor Panasonic were the alter egos of Universal.

United Automobile, Aerospace & Agricultural Implement Workers of America Local v. OEM/Erie Westland, LLC, 203 F.Supp.2d 825 (E.D. Mich. 2002)(applying DOL five-factor list and factors from case law regarding corporate "sameness" to determine genuine issues of fact existed with respect to whether LLC and member constituted "single employer" for purposes of WARN Act and breach of collective bargaining agreement claims).

Pinebrook Properties, LTD. v. Brookhaven Lake Property Owners Association, 77 S.W.3d 487 (Tex.App. 2002).

This was a dispute regarding land use, and Pinebrook Properties, Ltd., a Texas limited partnership, owned the lake, dam, roadways, and recreational areas at issue in the case. Pinebrook Properties Management, L.L.C., a Texas limited liability company, was the general partner. The court identified Musgrave, an individual, as the "president and general managing partner" of the LLC. The trial court found that the LLC and the partnership were alter egos of Musgrave and entered judgment against Musgrave individually. The court held that the alter ego doctrine is inapplicable to a partnership, stating that "there is no veil that needs piercing, even when dealing with a limited partnership, because the general partner is always liable for the debts and obligations of the partnership to third parties." With regard to the finding that the LLC was the alter ego of Musgrave, the court acknowledged that an LLC is a legal entity separate from its members and managers, who are by statute protected from personal liability for the liabilities of the LLC. However, the court did not question the application of the alter ego doctrine to the LLC. The court cited a Texas corporate veil-piercing case in declaring that it would examine the evidence to see if there is such unity between Musgrave and the LLC that separateness had ceased to exist and holding only the LLC as the general partner liable would result in injustice. The evidence of alter ego presented was that the LLC had no checking account, had not filed a tax return, and that Musgrave had sent a letter under his own signature without designating that he signed it in any other capacity. A second letter signed without any designation of a representative capacity was also argued to show lack of regard for the "corporate" structure. However, the court cited the Texas Business Corporation Act and Texas corporate veil-piercing cases for the principle that failure to follow corporate formalities is no longer a factor in determining alter ego under Texas law. The court concluded that there was no evidence of alter ego, pointing to the fact that there was no evidence of commingling of funds or that Musgrave disregarded the corporate structure. The court noted that the evidence revealed that Musgrave was not the sole manager of the LLC (there being two other managers involved) and that there was no evidence that Musgrave used the LLC for personal purposes.

Kaycee Land and Livestock v. Flahive, 46 P.3d 323 (Wyo. 2002).

The Wyoming Supreme Court addressed a certified question from the district court in an LLC veil piercing case asking if, in the absence of fraud, the remedy of piercing the LLC veil is available in the same manner as piercing the corporate veil under Wyoming law. The court first reviewed the circumstances under which the corporate veil may be pierced under Wyoming law. The court then turned to the Wyoming LLC act, which states that the members and managers of an LLC do not have liability for the LLC's debts, obligations, or liabilities, but is silent as to veil piercing. The court concluded that applying veil-piercing principles would not run counter to legislative intent. The court could discern no policy or legal reason to treat LLCs differently from corporations in this regard although the court did note that the various factors which would justify piercing an LLC veil would not be identical to the corporate situation for the "obvious reason that many of the organizational formalities applicable to corporations do not apply to LLCs." The court found it inadvisable in the absence of a complete factual context to articulate all possible factors to be applied to

Wyoming LLCs in the future. The court concluded by clarifying that fraud or an intent to defraud is not required to disregard a corporate or LLC entity.

In re Securities Investor Protection Corporation v. R.D. Kushnir & Co. (R.D. Kushnir & Co. v. Adler Drobny Fischer LLC), 274 B.R. 768 (Bankr. N.D. Ill. 2002)(concluding that, while Illinois LLC act precludes piercing LLC veil to hold members and managers liable based on failure to observe formalities, nothing in statute bars piercing the LLC veil on other grounds applicable to corporations).

Collins v. E-magine, LLC, 739 N.Y.S.2d 15 (N.Y. A.D. 1 Dept. 2002)(recognizing statutory liability protection of LLC members and managers and holding plaintiff failed to raise triable issue on alter ego theory in view of “heavy burden to be met if the corporate veil is to be pierced”).

Curole v. Ochsner Clinic, LLC, 811 So.2d 92 (La. App. 2002)(finding allegations insufficient to require an inquiry into whether LLC veil should be pierced to hold CEO of LLC personally liable).

Jackson v. Carlos Supermarket, LLC, No. CV000599734, 2002 WL 378317 (Conn. Super. Feb. 14, 2002)(finding insufficient evidence to hold LLC member liable under either instrumentality or identity rule for LLC supermarket’s false imprisonment of customer).

Hesni v. Williams & Boshea, L.L.C., No. Civ.A. 01-3745, 2002 WL 373273 (E.D. La. March 7, 2002)(in context of considering fraudulent joinder assertion, court could not conclude that there was no possibility of personal liability of LLC member given evidence of commingling of funds and failure to follow statutory formalities required for formation).

ABC, LLC v. State Ethics Commission, No. CV 00-0504071S, 2001 WL 1669371 (Conn. Super. Dec. 12, 2001)(acknowledging that there are circumstances under which Connecticut law allows disregard of the separate identity of a corporation or LLC but finding no evidence that would permit disregard of the separate LLC existence in this case).

Andrews v. Kerr McGee Corp., No. 1:00CV158-D-A, 2001 WL 1704144 (N.D. Miss. Dec. 5, 2001).

The plaintiffs in this environmental tort action sought to pierce the veil of a Delaware LLC wholly owned by a Delaware corporation. The court looked to the Delaware law on veil piercing because the Mississippi LLC act provides that liability of an LLC member is governed by the law of the state of organization. The court stated that two elements were required under Delaware law to disregard the separate legal existence of the LLC: (1) complete domination and control by the member such that the LLC and its parent operated as a single economic entity, and (2) deliberate and purposeful misuse of the corporate form that results in unfairness, injustice, and injury to the plaintiff. The court found that the plaintiffs had made no allegations regarding the second element. The court stated that intentional undercapitalization is one of the primary ways to satisfy the second element and noted that the plaintiffs had not raised any issue in this regard. Thus, the court granted the defendant’s motion for summary judgment on the veil-piercing claim.

Wisconsin Gas Company v. Bauer, No. 01-0369, 2001 WL 1510625 (Wis. App. Nov. 20, 2001)(rejecting argument that LLC and corporation were actually one company on basis of several common owners and alleged fraudulent concealment of relationship between companies).

Peinado v. Barnett, No. A093923, 2001 WL 1380441 (Cal. App. Nov. 6, 2001).

The court affirmed an administrative law judge’s conclusion that the alter ego doctrine applied to a single member LLC that acted as a contractor without the required license. The evidence relied upon by the court to establish alter ego included the fact that the California LLC was required to have at least two members and only had one. The court stated that the LLC was thus not legally constituted when it was formed. In addition, the court characterized the LLC’s failure to file the required statement of information with the Secretary of State as a disregard of legal formalities and a failure to maintain adequate records. The court pointed to a unity of interest based upon the sole ownership and control of the member. Finally, the court noted that the member and LLC used the same address.

NetTech Solutions, LLC v. Zippark.com, No. 01 CIV. 2683(SAS), 2001 WL 1111966 (S.D. N.Y. Sept. 20, 2001).

The plaintiff brought breach of contract, copyright infringement, and unfair competition claims against an LLC and the individual who was president and a member of the LLC. The plaintiff sought to pierce the LLC's veil to hold the individual personally liable, and the individual sought to have these claims dismissed. The court discussed the corporate alter ego doctrine under New York law and concluded that there were facts to suggest that the individual exercised complete domination and control over all matters concerning the LLC and that such domination was used to commit a wrong. The court noted that the other members of the LLC were the individual's wife and two daughters, and there were no employees. The LLC's sole business was to invest the proceeds from business with one of the plaintiffs. The court stated that if the LLC did breach the agreement it had with the plaintiff by misappropriating confidential and proprietary information, there was little doubt that the individual used his control over the LLC to commit the wrong. Thus, the court declined to dismiss the breach of contract claim against the individual. With respect to the copyright infringement and unfair competition claims, the court stated that the test was whether a corporate officer is a moving, active, conscious force behind the infringement. Characterizing the individual as a corporate officer of the LLC, the court found the plaintiffs had alleged sufficient facts to avoid dismissal of the copyright infringement and unfair competition claims against the individual.

Bastan v. RJM & Associates, LLC, 29 Conn. L. Rptr. 646, 2001 WL 1006661 (Conn. Super. June 4, 2001).

The individual sole member of an LLC argued that there can be no equitable piercing in the context of a member-managed LLC. The defendant relied on the statutory authorization of member-managed LLCs and several law review articles stating that it would be difficult to pierce member-managed LLCs. The court rejected the defendant's argument, stating that the argument overlooked the "considerable structure" required in the formation and operation of LLCs. The court concluded that the plaintiff had alleged facts that would support a conclusion that the limitation on a member's liability would not apply in this case.

Stone v. Frederick Hobby Associates II, No. CV000181620S, 2001 WL 861822 (Conn. Super. July 10, 2001).

The court found that there was sufficient evidence to allow the plaintiffs to pursue their alter ego and instrumentality veil-piercing claims against the members of an LLC and a commonly owned LLC. The court discussed various examples of failure to follow corporate formalities and concluded that the standard under Connecticut law did not require any actual fraud to pierce the veil of the LLC on a breach of contract claim. One piece of evidence the court noted in support of the contention that the LLC form was improperly used as a shield to avoid responsibility for contractual obligations was the statement of an attorney for the defendants during a meeting between the parties in which the attorney told the plaintiffs to "go ahead and sue [the LLC]. There is no money in [the LLC]. Why do you think we set it up as an LLC in the first place?"

Jordan v. Commonwealth, 549 S.E.2d 621(Va. App. 2001).

The members of an LLC that owned property that created a public nuisance were convicted of maintaining a public nuisance. The Commonwealth acknowledged that title to the property was held in the LLC but argued that the defendants should be deemed the owners of the property because they were the sole members in the LLC, shared its profits, and represented themselves to be the owners. The court of appeals recognized the status of the LLC as a separate legal entity and found that the public nuisance offense, placed in its ancient common law context, only authorizes prosecution of the person or entity that holds actual title to the property on which a nuisance continues. Since the evidence established that the LLC and not the individual members were the owners of the property, the convictions were reversed.

Berwyn Capital Investments, Inc. v. Shore Venture Group, LLC, No. CIV.A. A. 01-691, 2001 WL 883278 (E.D. Pa. June 14, 2001).

The plaintiff sued two LLCs and individuals who were "officers and directors" for breach of contract and conversion. The individual defendants alleged that they were not liable because they executed the contracts as officers and directors of the LLCs. The plaintiff claimed that it would be able to prove that the "corporate" veils should be pierced. The court held that the individual defendants were probably correct in their contention that the complaint failed to allege enough facts to warrant veil piercing, but that the complaints contained adequate allegations that the individuals breached the contracts and had personal liability for conversion, which the court characterized as a possible predicate to veil piercing.

Rafferty v. Noto Brothers Construction, L.L.C., No. CV000082596, 2001 WL 459073 (Conn. Super. April 17, 2001).

The court stated that the protection afforded by the LLC is not absolute and may be disregarded, as in the case of a corporation, when the LLC is the alter ego or business conduit of individuals. The defendants' motion to strike on the basis that the action could not be maintained against individuals who were not parties to the contract in issue was denied because the plaintiffs had pleaded alter ego.

Dornfried v. Granquist, No. CV000502628S, 2001 WL 306851 (Conn. Super. March 13, 2001) (rejecting plaintiff's argument that court should disregard LLC liability shield under instrumentality or identity rule because plaintiff failed to plead either theory).

Hollowell v. Orleans Regional Hospital LLC, 217 F.3d 379 (5th Cir. 2000).

The district court's opinion denying summary judgment in this case is summarized *infra*. In this WARN Act case, the plaintiffs sued an LLC and various other individuals and entities seeking to pierce the veil of the LLC as well as two corporate members of the LLC on alter ego grounds. The plaintiffs also sought to establish that the LLC and various related entities constituted a single business enterprise. The jury found for the plaintiffs on both the alter ego and single business enterprise issues. On appeal, the defendants argued that there was insufficient evidence to support these findings. The court of appeals noted that neither party challenged the district court's conclusion that Louisiana would treat an LLC in the same manner as a corporation for veil-piercing purposes. (In an earlier footnote, the court described LLCs as "essentially corporations which the Louisiana tax code taxes as partnerships.") The court rejected the defendants' attack on the jury's findings. With respect to the alter ego finding, the defendants' challenged the jury's findings of undercapitalization of the LLC and commingling of funds. The court stated that, even if the court were to accept the defendants' arguments, the defendants had failed to present a challenge to the jury's finding of alter ego based upon the "totality of the circumstances." The court of appeals also rejected a challenge to the jury's finding of single business enterprise, citing evidence of common ownership, common management, a unified employment policy, and disregard for corporate separateness of the entities.

Leisure Resort Technology, Inc. v. Trading Cove Associates, No. CV000091180, 2000 WL 1682535 (Conn. Super. Oct. 13, 2000).

The court granted a motion to strike allegations that two LLC members and two individuals referred to as directors of the LLC were personally liable under veil-piercing alter ego theories because the allegations were mere conclusions of law rather than facts that would demonstrate the veil should be pierced if proven true.

Hamilton v. AAI Ventures, L.L.C., 768 So.2d 298 (La. App. 2000) (applying corporate veil-piercing principles and upholding the trial court's piercing of the LLC veil to impose personal liability on an LLC member for breach of the LLC's contract).

Bass v. Lifecare Holdings, Inc., No. Civ.A. 99-1864, 2000 WL 377815 (E.D. La. April 12, 2000).

In this employment discrimination case, the plaintiffs sued their employer, a Louisiana LLC. The plaintiffs also sought to hold liable the sole owner of the LLC, a corporation, and an affiliated LLC that served as the manager of the employer LLC. The plaintiffs argued that the three entities satisfied the "single employer" test for Title VII purposes. The court concluded that the plaintiffs failed to demonstrate a sufficient departure from the ordinary relationship between a parent and subsidiary to meet the "single employer" standard. The court listed a number of factors it deemed relevant and concluded that the plaintiffs had not demonstrated that the three entities were "so interrelated, without observing ordinary formalities" or that the LLC was "so dominated, particularly as to its employment decisions" as to justify treating either or both of the affiliates as a single employer with the LLC employer. The court specifically went on to conclude that performance of administrative services and duties by the LLC that served as manager of the employer LLC was not irregular and did not evidence single employer status by the manager LLC.

Trustees of the Village of Arden v. Unity Construction Company, No. C.A. 15025, 2000 WL 130627 (Del. Ch. Jan. 26, 2000) (discussing the possibility of piercing the "corporate" veils of an LLC and related corporation on alter ego grounds and finding that similar ownership was insufficient to justify disregarding the business forms).

GMAC Commercial Mortgage Corp. v. Gleichman, 84 F. Supp.2d 127 (D. Me. 1999).

GMAC sued a real estate development LLC and its sole member for breach of a loan contract. GMAC sought to hold the individual member liable under corporate veil piercing theories. The court referred to the LLC and its

member in corporate terms throughout most of the opinion and applied corporate veil piercing principles. The court concluded that GMAC's pleadings were sufficient to allege a "misuse of corporate form" and an "inequitable outcome if the Court recognizes [the LLC's] corporate form." Thus, GMAC survived the member's Rule 12(c) motion to dismiss the claim. The alleged misuse of "corporate form" was the member's announced intent to dissolve the LLC after repudiation of the contract. GMAC alleged that a dissolution would deprive it of its ability to recover damages, which the court found to satisfy the requirement that GMAC allege that an "inequitable result" would flow from recognition of the "corporate form." GMAC also survived the member's motion for summary judgment. The court said that some of the evidence GMAC produced to show the member's improper use of the LLC's "corporate form" included: undercapitalization of the LLC on formation, payment of a deposit by a related company controlled by the member, and methods by which the LLC distributed funds.

People v. Garban, LLC f/k/a Garban Ltd., 80 Fair Empl. Prac. Cas. (BNA) 351, 1999 WL 496182 (N. Y. Sup. June 17, 1999).

In this sexual harassment case against two LLC stock brokerage firms, the plaintiff sought to hold two corporations alleged to be controlling members of the LLCs as well as the ultimate parent and another affiliate liable for the conduct of the LLCs. The court discussed corporate veil-piercing principles and concluded that the plaintiff had failed to plead facts warranting a "piercing of the corporate shield." The court thus dismissed the action as to the defendants other than the LLCs.

Masinter v. Salem Road Assoc., L.L.C., 522 S.E.2d 562 (Ga. App. 1999).

The court held that the plaintiff failed to establish a breach of contract, thus arguments regarding veil piercing to make the members of the LLC personally liable were moot.

New Horizons Supply Cooperative v. Haack, No. 98-1865, 1999 WL 33499 (Wis. App. Jan. 28, 1999).

The trial court in this case held a member of an LLC personally liable for a debt of the LLC. On appeal, the court reversed. The trial court's comments are worth noting. The judge started out by stating that it was a problem that no one had filed any documents to show what the LLC agreement stated. The court went on to note that "the rules of dissolution apparently were not followed" because creditors were not notified and articles of dissolution were not filed. In awarding the plaintiff judgment on its claim, the judge stated:

Haack signed . . . an agreement for Kickapoo Valley Freight LLC, but it would appear to me that the corporation was just a shell around which there were no real intentions to operate like a corporation because there was no intent even to dissolve the corporation, and the court's going to find that the corporate veil is pierced by the fact that the people were acting like a partnership, being taxed like a partnership, and haven't even dissolved the-

. . . I'm treating this as a partnership and assessing liability to the remaining partner. . . That's the evidence that's before me, and unless I would have some other evidence that was not presented, I have to treat this matter as a partnership and assume that the limited liability agreement did not alter the normal partnership liability situation.

(The opinion refers to the judgment as a "small claims judgment," and presumably the individual was not represented by counsel at the trial.) On appeal, the court first noted that the Wisconsin LLC act imports corporate veil-piercing principles. However, the appeals court found that there was insufficient evidence to pierce the veil of the LLC. The appeals court stated that the trial court's comments implied that it "erroneously deemed Kickapoo Valley's treatment as a partnership for tax purposes to be conclusive." The court noted the lack of evidence to support a conclusion that the member dominated the LLC such that it had no separate existence or was an instrumentality for injustice. The court of appeals upheld the judgment against the member, however, on the basis that she did not take appropriate steps to shield herself from liability upon dissolution and distribution of the LLC's assets. The court noted that filing articles of dissolution and notifying creditors are apparently optional under the Wisconsin statute, but the rules for distribution of assets on dissolution and the priority of creditors are fixed by statute. LLC creditors whose claims are not otherwise barred under the statute may pursue LLC members to the extent of the member's proportionate share of the claim or the assets of the LLC distributed to the member in liquidation. Since the member did not prove that the plaintiff's claim exceeded the value of any assets she received, the court affirmed the judgment.

Tom Thumb Food Markets, Inc. v. TLH Properties, LLC, No. C9-98-1277, 1999 WL 31168 (Minn. App. Jan. 26, 1999).

The plaintiff sued its LLC landlord and sought to pierce the LLC veil to hold liable the member who signed the lease on behalf of the LLC. The trial court concluded that the member was personally liable. The court of appeals reversed. The court of appeals first noted that the Minnesota LLC act makes the corporate veil-piercing cases applicable to LLCs. After reciting the conditions under which Minnesota courts will pierce the corporate veil, the court concluded that the record did not establish the injustice or fundamental unfairness required to pierce the veil. The member did not intentionally mislead the plaintiff, and the plaintiff did not come with clean hands because its own conduct contributed to the breach of the lease.

In re Sanner (Birdsell v. Fort McDowell Sand and Gravel), 218 B.R. 941 (D.Ariz. 1998).

The bankruptcy court cited Arizona corporate veil-piercing cases in concluding that the founder and manager of the LLC defendant had no personal liability on the claims against the LLC. The bankruptcy trustee argued that it was not necessary to pierce the veil of the LLC because the individual was a party to a plan to engage in collusive bidding under Section 363(n) and was liable for his own conduct. However, the court characterized this argument as “an attempt to make an end run around the protections afforded shareholders, directors, and officers by the corporate form” and as unsupported by the evidence. In addition, the agreement in question was signed on behalf of the LLC in a representative capacity rather than an individual capacity.

Marina, LLC v. Burton, No. CA 97-1013, 1998 WL 240364 (Ark. App. May 6, 1998).

In this breach of contract action by Burton against an LLC and its sole member, the appeals court upheld the trial court's refusal to pierce the LLC veil. The appeals court also found no error in the trial court's refusal to hold the member liable for misrepresenting that a number of other individuals were also members of the LLC. Burton argued that the LLC's veil should be pierced because the LLC was undercapitalized and inadequately financed. However, the court noted that Burton was aware the LLC was a new entity and that the financing of the project was to be accomplished through a bank loan. The court was not convinced under these facts that it should disturb the trial court's ruling. The court found that Burton's misrepresentation claim against the member failed because there was evidence to support the trial court's finding that Burton had not reasonably relied on the member's misrepresentations regarding membership in the LLC. In this regard, the court pointed out that Burton acknowledged that he was aware LLCs were designed to limit an investor's liability. Further, apparently satisfied with having a mortgage on the land that was the subject of the contract, Burton testified that the financial capability of the individuals listed as members was none of his business.

Hollowell v. Orleans Regional Hospital, 14 IER Cases 225, 1998 WL 283298 (E.D. La. May 29, 1998).

In this WARN Act class action against various individuals and health care organizations, the court discussed veil piercing under Louisiana limited liability company law. After discussing corporate veil piercing and citing numerous commentators on LLC veil piercing, the court concluded that the veil of the defendant LLC could be pierced if the LLC acted as the "alter ego" of its members or if the LLC's members committed fraud or deceit on third parties through the LLC. The court concluded that there were fact issues precluding summary judgment on the veil-piercing claims. The court also discussed the application of the WARN Act single business enterprise doctrine to the LLC and related co-defendants. The court recognized that the analysis overlapped somewhat with that involved in veil piercing and concluded that summary judgment was inappropriate on this claim as well.

United States v. Johnston, 13 F. Supp.2d 1316 (M.D. Fla. 1998).

The court considered the United States' “Motion to Set Aside as Fraudulent Conveyance Forfeited Property or in the Alternative a Determination That K & J Limited Liability Company is the Alter Ego of the Defendant Beryle Johnston.” The court concluded that a transfer of certain real property from a partnership to an LLC was fraudulent and thus did not reach the alter ego question.

Ditty v. Checkrite, Ltd., Inc., 973 F. Supp. 1320 (D. Utah 1997).

In this Fair Debt Collection Practices Act suit, the plaintiffs attempted to hold Mr. Deloney, who was apparently the sole member and manager of an LLC law firm (the plaintiff alleged that Deloney was the "sole shareholder, sole director and president"), personally liable for the actions of his firm on the basis that he was the alter ego of the LLC. The court noted that most commentators assume that veil-piercing theories apply to LLCs, and the court analyzed the claim applying the traditional corporate alter ego doctrine. The court concluded that the plaintiffs had not produced sufficient evidence at the summary judgment stage to pierce the LLC veil and hold Deloney liable as a matter of law.

In re Multimedia Communications Group Wireless Assocs. of Liberty County (Mills v. Webster), 212 B.R. 1006 (Bankr. M.D. Fla. 1997).

Two individuals formed a corporation and an LLC to offer Direct TV services to rural areas. Later, the LLC filed a Chapter 7 bankruptcy petition. The trustee filed a complaint against the individuals and several related corporations and LLCs, seeking a declaratory judgment that the affiliated companies were alter egos and instrumentalities of one another. The court discussed and applied corporate veil piercing principles but concluded that the circumstances did not warrant piercing the veil in this case.

Northern Tankers (Cyprus) Ltd. v. Backstrom, 967 F. Supp. 1391 (D. Conn. 1997).

In this federal maritime veil piercing case, the court pierced the veil of a number of entities, but it is unclear whether the LLCs mentioned in the case were among these entities. The plaintiff in the case sought to hold two individuals, Backstrom and Lindholm, and various related entities liable for a judgment the plaintiff had obtained against a shipping company controlled by Backstrom and Lindholm. The court identified "53 individual, corporate, partnership and trust defendants." In fact, two of the defendants were Colorado LLCs. The court applied federal common law to pierce the corporate veil of numerous shipping and real estate corporations, holding that these corporations were merely alter egos of Backstrom and Lindholm. Additionally, the court stated that it was piercing the "corporate veil of various other entities" that were fraudulently created for Lindholm personally. This is an apparent reference to part or all of a group of entities that owned substantial real and personal property in Colorado. This group consisted of a grantor trust, two corporations, a limited partnership and two LLCs. These entities were not directly part of the shipping and real estate enterprise operated by Backstrom and Lindholm but were personal investment vehicles of Lindholm. Although the two LLC defendants were identified by the court as part of this latter group of entities, it is unclear from the opinion whether the LLC veils were actually pierced. The court specifically found that the limited partnership and its corporate general partner were alter egos of Lindholm and expressly disregarded their "corporate" existence. The court did not specifically address the LLCs in this way. The opinion does not indicate the basis for exercising jurisdiction over the LLCs, but it appears that jurisdiction may have been premised upon the fact that the LLCs were alter egos of Lindholm. The court noted that the LLCs were among defendants that had contested jurisdiction, and the court adopted a special master's recommended ruling that jurisdiction was present. In an earlier reported decision, the court had postponed deciding whether the LLCs and certain other defendants were subject to jurisdiction based upon their alter ego status to provide the plaintiff an opportunity to engage in discovery on the alter ego issue. See *Northern Tankers (Cyprus), Ltd. v. Backstrom*, 901 F. Supp. 72 (D. Conn. 1995).

2. Reverse Piercing

Devan Lowe, Inc. v. Stephens, __ So.2d __, 2002 WL 1301670 (Ala.Civ.App. June 14, 2002)(permitting garnishment of payments to LLC to satisfy judgment against member on basis that LLC was sham established for fraudulent and illegal purpose of evading judgment creditor).

Litchfield Asset Management Corporation v. Howell, 799 A.2d 298 (Conn. App. 2002).

The court upheld the trial court's reverse piercing of the LLC veil of two LLCs under the instrumentality and identity theories. After a default judgment was taken against Mary Ann Howell, she reorganized her business into two new LLCs. Howell's husband and daughters had small interests in the parent LLC, but the evidence showed that only Howell was active in the business. The evidence also showed that Howell never drew a salary or regular distributions, but she used LLC funds to pay personal expenses and provide substantial, interest-free loans to family members. The court reviewed policy arguments for and against reverse piercing and concluded that reverse piercing to allow the judgment creditor to reach the assets of the LLCs was appropriate. The court rejected the argument that the plaintiff was required to prove fraud to pierce the LLC veil. The court found that Howell had used her control of the LLCs to unjustly avoid her personal debt to the plaintiff because the LLC's payment of her personal expenses directly rather than paying salary or regular distributions deprived the plaintiff of any means of collecting the judgment against Howell.

Great Neck Plaza, L.P. v. Le Peep Restaurants, LLC, 37 P.3d 485 (Colo. App. 2001).

A judgment creditor garnished the bank account of an LLC after obtaining a judgment against two corporations affiliated with the LLC. The LLC was formed after the creditor initiated its lawsuit against the corporations. The LLC was funded by all of the assets of one of the corporations, which became the sole member of the LLC, and the revenues from the business that had been operated by the corporation thereafter went to the LLC. The court found that the LLC and related corporations were alter egos of one another, that fraudulent conveyances had occurred, and that the judgment debtors and related parties had acted in concert to insulate assets from the judgment. The entities were set up in a tiered

structure, but one individual was the ultimate owner and was the president or manager of all the entities. The court noted that assets were moved “gymnastically” among the entities for what were claimed to be tax reasons unsupported by the evidence. Since the LLC was the alter ego of an entity named in the garnishment, the court held that the garnishment of the LLC’s account was proper.

Trans Union LLC v. Credit Research Inc., No. 00 C 3885, 2001 WL 648953 (N.D. Ill. June 4, 2001).

The defendants filed several counterclaims against Trans Union LLC and Acxiom Corporation. The defendants sought to hold Acxiom liable for the acts of Trans Union, Acxiom’s largest shareholder, on the basis that Acxiom was Trans Union’s alter ego. The court noted that recovering from a subsidiary for a parent’s wrong is somewhat unorthodox, but, because the court ultimately found that alter ego was not sufficiently pled, the court stated that it expressed no opinion on whether such a reverse-piercing is tenable. The court discussed and applied corporate veil piercing principles, equating an LLC to a corporation for these purposes. (After stating that both Acxiom and Trans Union were Delaware corporations, the court explained in a footnote that “Trans Union is technically a limited liability company, not a corporation, but the corporate form is still defined by Delaware law.”) The only allegations to support the conclusory allegation of alter ego in the complaint were that Trans Union was the largest shareholder of Acxiom and that Trans Union placed two directors on Acxiom’s board. The court stated that these allegations were insufficient to support a veil piercing claim. The court pointed to the absence of any allegations about corporate formalities, capitalization, solvency, or how there was any facade.

3. Piercing to Enable LLC to Enforce Contract of Member or Another

Holmes Development, LLC v. Cook, 48 P.3d 895 (Utah 2002) 553541 (Utah 2002)(stating in footnote that, although LLC claimant and related LLC may have the same management and be practically indistinguishable, they are legally separate entities, and court would not treat the LLCs as the same entity for purposes of standing to sue on a contract).

C & J Builders & Remodelers, LLC v. Geisenheimer, No. CV 97-040555S, 1998 WL 203400 (Conn. Super. April 17, 1998), *aff’d*, 733 A.2d 193 (Conn. 1999).

In this case, a construction contractor operating as a sole proprietor entered a construction contract with an arbitration clause. During the course of the construction work, the sole proprietor reorganized as an LLC. The contract contained a clause prohibiting assignment of any monies due under the contract without consent of the owner. The court held that the LLC could enforce the arbitration clause of the contract because the individual sole proprietor and the LLC were “practically identical.” The court began its discussion of the “identity rule” with references to the concept of piercing the corporate veil. The court recognized that the rule “is more often applied in cases where an individual attempts to hide behind the corporate veil to avoid his legal obligations;” however, the court then stated that “there is no conceptual reason not to apply the rule to avoid injustice here.” (The Connecticut Supreme Court affirmed the result in this case but did so by treating the organization of the LLC as a conversion rather than relying on veil piercing principles.)

4. Piercing to Obtain Jurisdiction Over Members or LLC

Yukon Partners, Inc. v. The Lodge Keeper Group, Inc., 572 S.E.2d 647 (Ga. App. 2002)(holding, in context of challenge to personal jurisdiction, that existence of unspecified affiliation was insufficient to pierce veil of numerous hotel LLCs in absence of showing that entities were sham or used to defeat public convenience, justify wrong, protect fraud, defend crime or any other reason which would in equity or good conscience justify disregard of entities).

International Bancorp, L.L.C. v. Societe des Bains de Mer et du Cercle des Etrangers a Monaco, 192F.Supp.2d 467, 2002 WL 334745 (E.D. Va. 2002)(holding that record did not support piercing LLC veil to subject member to court’s personal jurisdiction under “stringent” Virginia veil piercing standard requiring “proof that the alleged alter ego used the corporation to disguise some legal wrong”).

Quantum Color Graphics, LLC v. The Fan Association Event Photo GmbH, 185 F.Supp.2d 897 (N.D. Ill. 2002)(holding that claims against two German companies and California LLC may be aggregated for jurisdictional purposes, and contacts could be imputed among defendants, on basis of allegations that companies were all alter egos of one another and individual defendant owner).

Stauffer v. Lone Star Mud, Inc., 54 S.W.3d 810 (Tex.App. 2001)(holding that individual failed to negate plaintiff's theory that individual was alter ego of a Wisconsin LLC for purposes of court's exercise of personal jurisdiction over individual).

M.G. Incentives v. J.J. Marchand, No. C6-00-962, 2001 WL 96223 (Minn. App. Feb. 6, 2001).

The court stated it need not decide whether the fiduciary shield doctrine should apply in Minnesota so as to protect the sole owner and president of an LLC from the court's exercise of personal jurisdiction because the actions of the individual fell outside the protections of the doctrine. In this regard, the court concluded that the plaintiff alleged facts sufficient to pierce the veil of the LLC.

Royal Mortgage Corporation v. Montague, 41 S.W.3d 721 (Tex. App. 2001)(concluding there was no evidence that LLC was acting as alter ego of its members for purposes of personal jurisdiction over members).

Oliver v. Boston University, No. 16570, 2000 WL 1038197 (Del. Ch. July 18, 2000)(concluding that LLC was Boston University's alter ego for purposes of personal jurisdiction assuming truth of allegations that LLC was formed by BU solely to serve its interest and was completely dominated by BU).

New England National LLC v. Kabro of East Lyme LLC, No. 550014, 2000 WL 254590 (Conn. Super. Feb. 23, 2000).

The plaintiffs sued Kabro of East Lyme, LLC ("East Lyme, LLC"), a New York LLC, for breach of a contract to purchase real estate from the defendants. Additionally, the plaintiffs sought to pierce the veil of East Lyme, LLC and hold several other non-resident parties personally liable under veil piercing theories. Initially, the plaintiffs relied upon veil-piercing principles to give the court personal jurisdiction over the other non-resident parties. The court concluded it had jurisdiction over one LLC member who was instrumental in the negotiations of the real estate transaction in issue but found that the plaintiffs had not alleged sufficient facts to pierce the veil to obtain jurisdiction over the other members of the LLC under either the instrumentality or identity test. The plaintiffs also failed to convince the court that it had jurisdiction over another New York LLC that allegedly provided funds to East Lyme, LLC.

Sinopac International Co. v. Southwestern Bell Telecommunications, Inc., No. 14-98-00116-CV, 1999 WL 418365 (Tex. App. June 24, 1999).

The court described the defendants as limited liability companies organized under the laws of Hong Kong and the People's Republic of China. The court found the companies lacked sufficient contacts with the State of Texas to support general or specific jurisdiction. The court also rejected the plaintiff's argument that the companies were alter egos of one another and of a Texas corporation such that the Texas corporation's contacts should be imputed to the foreign companies. The court noted both a lack of evidence and a lack of cited authority for the alter ego argument.

ING (U.S.) Securities, Futures & Options, Inc. v. Bingham Investment Fund, L.L.C., 934 F. Supp. 987 (N.D. Ill. 1996).

The court determined that it lacked personal jurisdiction over LLC members based upon the fiduciary shield doctrine (described by the court as prohibiting the exercise of personal jurisdiction over a nonresident whose only contacts with the forum state were "solely on behalf of his employer or other principal"). The plaintiff attempted to avoid the effect of the fiduciary shield doctrine by relying on the corporate alter ego doctrine. The defendants countered with an affidavit reciting that the LLC's assets were not treated as the assets of the individual defendants, that the LLC maintained necessary corporate records, that the LLC did not commingle its assets with those of the individual defendants, and that the LLC maintained a separate banking account. The affidavit was uncontradicted, and the court rejected the alter ego argument.

5. Piercing in Other Contexts

In re Application of Donald J. Trump, 755 N.Y.S.2d 618 (N.Y.A.D. 1 Dept. 2003) (stating that "artificial distinction" sought to be drawn between individual petitioner and his wholly-owned LLC did not preclude arbitration under arbitration clause in agreement to which LLC was a party).

Somerville S Trust v. USV Partners, LLC, No. Civ.A. 19446-NC, 2002 WL1832830 (Del. Ch. Aug. 2, 2002) (finding credible evidence of mismanagement of LLC in action to inspect books and records of LLC based in part on evidence that individual who was sole member of LLC's manager used LLC as his alter ego).

UCA, L.L.C. v. Landsdowne Community Development, 215 F.Supp.2d 742 (E.D. Va. 2002)(refusing to disregard separate existence of LLC for purposes of easement issue under federal Pole Act).

Abraham & Sons Enterprises v. Equilon Enterprises, LLC, 292 F.3d 958 (9th Cir. 2002)(rejecting argument of franchisors that LLC jointly owned by franchisors was not separate entity for purposes of California franchise law that gives right of first refusal to franchisees before franchisor may sell or transfer to another person premises leased to franchisee).

Egle v. Egle, 817 So.2d 136 (La. App. 2002) (finding ex-wife raised possibility that defendants were solidarily liable with ex-husband so as to interrupt prescription in case where ex-wife alleged ex-husband hid community assets and diverted them to a number of corporations and LLCs owned and controlled by him as a single business enterprise).

Robinson v. Geo Licensing Company, LLC, 173 F. Supp.2d 419 (D. Md. 2001) (rejecting attempt to treat majority member and LLC as a single entity and recognizing member's ability to sue LLC on contract made with LLC).

In re Kaplan Breslaw Ash, LLC, 264 B.R. 309 (Bankr. S.D. N.Y. 2001).

In this Chapter 11 case in which a mortgageholder sought relief from the automatic stay to foreclose a mortgage, the court found as facts the mortgageholder's unchallenged assertions that the debtor LLC and a related corporation were "for all intents and purposes one entity."

In re Lake Country Investments, L.L.C. (Agnicourt, L.L.C. v. Stewart), Nos. 99-20287, 00-6064, 2001 WL 267475 (Bankr. D. Idaho March 19, 2001) (stating that there were fact issues regarding whether the managing and majority member of an LLC was the alter ego of the LLC in the context of an equitable subordination claim).

Holden v. Connex-Metalna, No. Civ.A. 98-3326, 2000 WL 1801844 (E.D. La. Dec. 6, 2000) (relying on Louisiana state law to recognize the separate legal existence of two related LLCs for purposes of applying the Robins Dry Dock doctrine in federal maritime context).

In re Heartland Food and Dairy Distributors, Inc. (Land-O-Sun Dairies, L.L.C. v. Heartland Food and Dairy Distributors, Inc.), 253 B.R. 32 (Bankr. S.D. Ill. 2000).

A suit was mistakenly filed in the name of a corporation rather than an affiliated LLC. The suit was dismissed due to the corporation's lack of capacity, and (after various missed opportunities to cure) the LLC ended up being barred by res judicata from pursuing the complaint refiled in its name because the LLC was in privity with the corporation that filed the initial complaint. In finding privity, the court relied in part upon the failure of the LLC and the corporation to comply with the formalities necessary to maintain separate existences. The court commented that the LLC's own counsel was confused about which entity was his client.

In re Fawell (Davis, Mannix & McGrath v. Fawell), Nos. 98 B 01274, Adv. 98 A 01306, 1999 WL 569449 (Bankr. N. D. Ill. July 26, 1999).

In the course of responding to a creditor's complaint regarding the debtor's valuation of stocks and interests in incorporated and unincorporated businesses, the court noted that there was no evidence to pierce the respective "corporate veils" of the separate corporate, partnership, and limited liability company entities involved.

O. Formation of (or Failure to Form) LLC

Compton v. Kirby, 577 S.E.2d 905 (N.C.App. 2003).

Three individuals agreed that the business they were forming would be an LLC but never finalized a draft operating agreement and never signed any written agreement. One of the individuals wrote a letter confirming the terms of the partnership agreement that he alleged existed among them, and the defendant called this individual the same day and expressly recognized the terms of the partnership agreement set out in the letter were correct. There was other evidence that the parties carried on the business as a partnership. The defendant claimed, however, that he was the sole owner of the business. The jury found that a partnership existed between the two plaintiffs and that the defendant's failure to acknowledge the partnership was a breach of fiduciary duty. The trial court entered judgment for the plaintiffs, and the court of appeals affirmed the judgment.

Lester Associates v. Commonwealth, 816 A.2d 394 (Pa.Cmwlth.Ct. 2003) (concluding that there was no legal transfer of title on which transfer tax could be imposed based on deeds into and out of LLC where LLC did not exist at the time of the purported conveyance to it).

Ehle v. Williams & Boshea, L.L.C., No. Civ.A. 01-3757, 2002 WL 373271 (E.D. La. March 7, 2002)(finding that joinder of individual who claimed he could not be liable because he was member of LLC was not fraudulent where there was evidence the LLC was never formed and plaintiff stated claims based upon negotiations to form LLC).

Flores v. Gutschow, No. 13-00-556-CV, 2001 WL 1590510 (Tex. App. Dec. 13, 2001).

Two parties signed a “Pre Organization Agreement” in which they agreed to form an LLC and then to form an S corporation or LLP within 60 days of the contract. The contract stated that the LLC would pay specified sums to the S corporation or LLP, and the sums were set out by the names of each party and referred to as “contributions.” Each party was to be issued a certificate to reflect a specified percentage of ownership in the new S corporation or LLP. The contract had a “pullout” clause allowing any member to withdraw and be reimbursed his initial capital contribution. The contract also provided for reorganization of the S corporation or LLP to reflect equal ownership when all initial capital contributions were refunded. The court held that this contract unambiguously obligated the parties to contribute the sums specified to the LLC.

Chimble v. Hutter, No. X01CV990162957, 2001 WL 357919 (Conn. Super. March 29, 2001).

This dispute arose out of an agreement between the parties to refinance, renovate, sell, and divide the proceeds of the residence of one of the parties. The original agreement contemplated that an LLC would be formed to hold the property, with ownership of the LLC equally divided between the parties in “shares of stock.” Title to the property was transferred to the party who obtained the financing but was not transferred to an LLC. The court found that the failure to transfer title to the property to the LLC did not involve any fraud or unjust enrichment. The court found that the party who took title and obtained the financing had intended to convey title to an LLC, but the parties abandoned this plan when they discovered that the transfer would involve another transfer tax. The court went on to find that the parties owed each other only limited fiduciary duties in connection with their partnership or joint venture arrangement.

Harvey v. Covington, No. M2000-01184-COA-R3-CV, 2001 WL 120733 (Tenn. App. Feb. 14, 2001).

Two individuals signed a letter of intent to create an LLC. Each of them took certain steps toward operating the business such as applying for a credit card, requesting an employer identification number, and opening a bank account, but the LLC was never formed. The court concluded that the business was a partnership and that the defendant’s fraud in failing to organize the LLC as promised, converting business funds, and defrauding the plaintiff out of the funds entitled the plaintiff to rescission of the partnership.

Nystrom v. Servus Robots, L.L.C., No. LF-1517-3, 2000 WL 249246 (Va. Cir. Ct. March 2, 2000).

According to the plaintiff Nystrom, in February 1998, Nystrom and Ward agreed to form an LLC to which Nystrom would devote 75% of his time acting as “President” and in which Nystrom would receive in exchange for his services a 25% ownership interest. In October 1998, articles of organization were prepared (and apparently filed). An operating agreement was also prepared, but Ward repudiated the agreement and denied promising a 25% interest to Nystrom. In December 1998, Ward, acting as “chairman” of the LLC, fired Nystrom as president. The court concluded that the facts as pled by Nystrom stated a cause of action for fraud in the inducement, breach of contract, and quantum meruit.

Marrett v. Scott, No. CIV.A. 299cv244-D-B, 2000 WL 491857 (N.D. Miss. April 10, 2000).

The issue in this case was whether the court should grant injunctive relief requiring removal of a lis pendens obtained by the plaintiff in the case. The underlying dispute involved breach of contract, breach of fiduciary, and related claims based upon the plaintiff’s contention that the defendants refused to sign a proposed operating agreement that would have formed an LLC to develop certain real property. The court did not address the plaintiff’s contention that the parties had a joint venture agreement that was violated when the defendants refused to sign the operating agreement. The court only examined whether the standard for the preliminary injunctive relief sought by the defendants had been met, and the court determined that it had.

Holmes v. Lerner, 74 Cal.App.4th 442, 88 Cal. Rptr. 2d 130 (Cal. App. 1 Dist. 1999).

Two individuals, Holmes and Lerner, came up with a novel idea for cosmetics and agreed to go into business together to develop and market their “Urban Decay” line of cosmetics. Without informing Holmes or including her in

the ownership, however, Lerner and her business consultant, Soward, formed an LLC to produce and market Urban Decay. Holmes was included in periodic "board meetings" of the business both before and after formation of the LLC, and she worked in the business on a day to day basis, but her inquiries regarding her role in the business were met with vague answers. Eventually, Holmes learned that the business was being conducted as an LLC. She continued to participate in the business for a few months after learning of the LLC, but the relationship finally went completely sour, and Soward told her she was no longer welcome. The case was tried and decided under partnership law, and the court only mentions the LLC in the course of discussing the facts. Holmes sued Lerner and Soward and prevailed on various causes of action including breach of an oral partnership agreement between Holmes and Lerner. The appeals court upheld the trial court's determination that a partnership was formed between Lerner and Soward. The court discussed the Uniform Partnership Act and case law relevant to formation of partnerships and concluded that no express agreement to share profits is necessary to form a partnership. According to the court, an understanding to share in profits and losses was implicit in the Holmes-Lerner agreement. The court also found that the agreement was sufficiently definite. Soward was found liable for conspiracy and aiding and abetting fraud and breach of fiduciary duty. Holmes was awarded compensatory damages for the loss of her partnership interest. In this regard, the jury was instructed that the appropriate measure of damages was half the value of Urban Decay at the date of the breach of the agreement. The case was apparently tried under the theory that the date of the breach was the date on which Holmes was told she was no longer welcome. The jury also awarded punitive damages.

Lloyd v. Horn, Inc., No. 97-3074, 1998 WL 939493 (10th Cir. Aug. 21, 1998).

The court of appeals affirmed the decision of the district court rescinding an operating agreement on the basis of unilateral mistake and constructive fraud. A partnership converted to an LLC, but the managing partner did not inform the others that he did not intend to continue in his management role after the conversion. The LLC operating agreement did not appoint the individual as managing member, but the other members assumed he would take on the position consistent with his role in the partnership. The court found the concealment amounted to constructive fraud because it breached the fiduciary duty of the managing partner to disclose material information. Thus, the court upheld the trial court's rescission of the LLC operating agreement. (The district court's opinion is available at 1997 WL 150052 (D. Kan. Jan. 29, 1997)).

Medical Waste Technologies, L.L.C. v. Alexian Brothers Medical Center, Inc., No. 97 C 3805, 1998 WL 387705 (N.D. Ill. June 24, 1998).

In litigation involving an alleged breach of a joint venture agreement, the court held that the attorney-client privilege as to documents relevant to the formation of an LLC had been waived when the client injected as a new issue in the case the argument that formation of the LLC was a condition precedent to formation of the joint venture. Two businesses allegedly agreed to enter into a joint venture agreement which involved formation of a new LLC. One of the prospective members brought suit. The LLC was never created, and the other prospective member argued that formation of the LLC was a condition precedent to the formation of the joint venture. Ruling on a discovery dispute, the court held that documents relevant to formation of the LLC were not protected by the attorney-client privilege and must be produced. Because it had already ordered the documents produced, the court did not find it necessary to address the plaintiff's argument that the law firm which undertook the responsibility of filing the articles of organization (referred to by the court as "articles of incorporation") owed the plaintiff, as a prospective one-half owner, a duty of full disclosure of all instructions and communications relating to the endeavor.

Advanced Orthopedics, L.L.C. v. Moon, 656 So.2d 1103 (La. App. 1995).

Two individuals, Heath and Moon, established a business called "Advanced Orthopedics, L.L.C." Heath filed LLC articles of organization and an initial report with the Secretary of State's office, and a certificate of organization for Advanced Orthopedics, L.L.C. ("Advanced") was issued. Heath and Moon had a falling out. Moon established his own competitive business and then resigned from Advanced. Litigation ensued. The specific issues addressed by the court in this opinion were essentially (1) whether Advanced constituted a legally formed LLC and (2) whether Moon had made a capital contribution which should be returned.

Moon argued that he did not have the subjective intent to form an LLC, that he did not adequately understand the concept of an LLC and that, because he did not sign an operating agreement, he rejected the formation of an LLC. The court rejected these arguments. The court noted that Moon did not question the viability of the LLC during the year of its operation and observed that the statute provides that a certificate of organization is conclusive evidence that an LLC has been duly organized. The court stated that "[a]ttaining a certain level of understanding regarding L.L.C.s is not a prerequisite to the formation of and participation in one." Further, the court stated that it was aware of no requirement in the law that an LLC have an operating agreement to be viable.

Moon also argued that he was entitled to reimbursement for a capital contribution. Moon contended that he made his agreed upon \$10,000 capital contribution in the form of past experience, good will, services rendered, and equipment. While the court acknowledged that capital contributions do not have to be in cash, it concluded that there was no evidence that Moon made a non-cash capital contribution.

P. Pre-Formation Contracts or Dealings

Urda v. Sahl, No. CV020468800S, 2003 WL 21007160 (Conn.Super. April 17, 2003) (concluding that the defendant promised to convey a 50% interest in real estate, rather than an interest in an LLC later formed to hold the real estate, in exchange for the plaintiff's management of the real estate, and thus the oral agreement was subject to the Statute of Frauds).

Schawk, Inc. v. City Brewing Co., LLC, No. 02-1833, 2003 WL 1563767 (Wis.App. March 27, 2003) (questioning the import of an alleged offer made on behalf of an as-yet-unformed LLC).

Holland v. Fahnestock & Co., Inc., 210 F.R.D. 487 (S.D. N.Y. 2002) (adopting magistrate's report finding LLC was not indispensable party because its interest was adequately represented by defendant, and LLC was no more than co-obligor and joint tortfeasor with respect to pre-organization contract assigned to LLC by defendant).

Holland v. Fahnestock & Co., Inc., No. 01CIV.2462RMBBJP, 2002 WL 1774230 (S.D. N.Y. Aug. 2, 2002)(finding that individual sole proprietor was not discharged from liability when LLC was formed and succeeded to liability on pre-formation contract and that individual and LLC were thereafter joint obligors on the contract).

Johnson v. King Media, Inc., No. Civ.A. 01-2311, 2002 WL 1372363 (E.D. Pa. June 24, 2002).

King Media sued on a contract with Zebra Marketing.com. King Media alleged that Zebra Marketing.com was a partnership, and it sued the partnership and its three alleged partners. One of the alleged partners sought dismissal on the basis that Zebra Marketing.com was an LLC, and the contract was not with the individual personally. The court denied the motion to dismiss, stating that the contract was entered four months prior to formation of the LLC and the subsequent formation of the LLC could not protect the partners from personal liability arising out of the contract with the partnership.

In re Rickel & Associates, Inc. (Rickel & Associates, Inc. v. Smith), 272 B.R. 74 (Bankr. S.D. N.Y. 2002)(holding that pre-formation securities fraud was ratified by LLC after its formation).

Ehle v. Williams & Boshea, L.L.C., No. Civ.A. 01-3757, 2002 WL 373271 (E.D. La. March 7, 2002)(finding that joinder of individual who claimed he could not be liable because he was member of LLC was not fraudulent when there was evidence the LLC was never formed and plaintiff stated claims based upon negotiations to form LLC).

Shampton v. City of Springboro, No. CA2000-08-080, CA2000-09-081, 2001 WL 1403051 (Ohio App. Nov. 13, 2001).

A short-term lease was signed by an individual on behalf of an LLC shortly after the LLC was formed. The LLC asserted promissory estoppel claims based upon promises made before the LLC was formed. The defendant argued that the LLC was a third party to the lease and without standing to assert promissory estoppel. The court applied principles applied to corporate promoters to conclude that the LLC could assert promissory estoppel even though it did not exist at the time of the promises.

Breka v. Falcon Electric Corporation, No. C8-00-1434, 2001 WL 641524 (Minn. App. June 12, 2001).

Four individuals formed a business (ADA Engineering, L.L.C. or "ADA") they intended to be an LLC. Their attorney failed to file the articles of organization, and the failure was not discovered until after a corporation agreed to acquire ADA. A memo written on the acquiring corporation's stationery stated that because the secretary of state had no record of ADA as an LLC, the corporation would treat ADA as a partnership and purchase its assets and assume its liabilities as a partnership. One of the owners of ADA was an officer and major shareholder of the acquiring corporation. Although the assets of ADA were transferred and its business assumed by the acquiring corporation, the terms of the acquisition were never finalized, no consideration was paid, and litigation against the acquiring corporation and the majority shareholder who was also an owner of ADA ensued. Among the issues addressed in this appeal was whether the trial court erred in finding that ADA was a partnership and not a de facto LLC. The court of appeals relied upon case

law dealing with defective incorporation as well as the common law and statutory definition of a partnership to conclude that ADA was a partnership. The court also held that the other owners were not estopped to deny ADA's status as an LLC.

The Pepsi-Cola Bottling Company of Salisbury, Maryland v. Handy, No. 1973-S, 2000 WL 364199 (Del. Ch. March 15, 2000).

The court determined that the members of an LLC were not protected from liability by the Delaware LLC act because the claims against the members were based upon fraudulent acts committed by the members before the LLC was formed. The court phrased the issue as follows: "if a person makes material misrepresentations to induce a purchaser to purchase a parcel of land at a price far above the fair market value, and thereafter forms an LLC to purchase and hold the land, can that person later claim that his status as an LLC member protects him from liability to the purchaser under § 18-303 [of the Delaware LLC Act]?" Not surprisingly, the court answered the question in the negative. The court did not find it necessary to reach the argument that veil piercing is the only way to hold an LLC member liable other than a claim based upon an improper distribution under § 18-607 of the Delaware LLC Act since the members were being sued for conduct that occurred before the formation of the LLC and thus were not being sued in their capacities as members of an LLC.

Ruggio v. Vining, 755 So.2d 792 (Fla. App. 2000).

Prior to the filing of articles of organization for an LLC, Ruggio signed a \$100,000 promissory note on behalf of the LLC payable to Vining. Ruggio claimed that Vining knew the LLC had not yet been formed, but Vining claimed that Ruggio represented the LLC had already been formed. The note was somewhat unusual in that it provided for the issuance of a 1% ownership interest in the LLC (referred to as "1% of all shares of stock authorized to be issued by the articles of incorporation filed in the State of Florida by the obligor") in lieu of payment at the election of the holder. At the time the note was executed, the Florida LLC act provided that "[a]ll persons who assume to act as a limited liability company without authority to do so shall be jointly and severally liable for all debts and liabilities." (Later the act was amended to add an exception for any liability to a person who also had actual knowledge that there was no organization of an LLC.) The act also provides that an LLC shall not transact business or incur indebtedness, except that which is incidental to its organization or to obtaining subscriptions for or payment of contributions, until the articles of organization have been filed. The court explained the purpose of provisions like this as protection of innocent third parties who have dealings with an entity that does not exist and never becomes adequately capitalized. The court ultimately determined that fact issues remained. The court questioned whether Vining himself might have been assuming to act as the LLC. The court stated that the record did not establish whether the unusual note was "incidental" to the LLC's organization or a "subscription" or a "contribution." In a footnote the court chastised Ruggio's counsel for continued reliance on provisions from the corporation statute and limited argument regarding the applicable provision in the LLC act.

In re Bernstein (Bernstein Ranch, LLC v. U.S.), 230 B.R. 144 (Bankr. D. N.D. 1999).

An LLC claimed an agricultural lien on cattle proceeds by virtue of feed and care provided the cattle. Two brothers who owned the cattle executed a bill of sale to the LLC, in which they were members, and the LLC later reconveyed the cattle to the brothers. The lien was challenged with respect to the period of time during which title to the cattle was held by the LLC on the basis that, under North Dakota law, an owner of crops or livestock cannot claim a supplier's lien for inputs the owner himself provides to the crop or livestock. The court compared the transfer to the LLC to a case in which a family created a partnership for the purpose of raising potatoes. A company owned by the mother provided services and claimed a lien, but it was disallowed on the basis that the mother, as a participant in the joint venture, had an interest in the crops themselves, and the expenses for which she claimed a lien constituted a contribution to the common undertaking of the joint venture. The court stated that the circumstances surrounding the LLC were similar to those in that case. If the cattle were owned by the LLC during the time in question, said the court, the logic of that case would preclude recognition of the lien. The court analyzed the circumstances of the transfer to the LLC and determined that the sale was absolute and effective upon the signing of the bill of sale. Since the cattle were owned by the LLC, it could not claim a lien for its expenses for feed and services.

Heritage National Associates Limited Partnership v. 21 St Investment Group L.L.C., No. 05-99-00317-CV, 2000 WL 426437 (Tex. App. April 19, 2000).

An LLC sought to enforce an agreement to purchase and sell property that was executed on behalf of the LLC prior to the filing of articles of organization with the Oklahoma Secretary of State. The court applied an Oklahoma statute that provided that a person or corporation may not deny the validity of a contract relating to real property if the

person or corporation has knowingly received and accepted benefits under the contract. The court concluded that the seller was estopped under this provision to assert the LLC's lack of capacity. In a subsequent opinion on rehearing, the court concluded that there had been no fraud on the part of the individual who represented that the LLC was in existence.

P.D.2000, L.L.C. v. First Financial Planners, Inc., 998 S.W.2d 108 (Mo. App. 1999).

The plaintiff LLC sought to bring suit on a contract entered on the LLC's behalf prior to the LLC's formation, and the defendant defended on the basis that the LLC lacked capacity to enter and enforce the contract. The contract was signed by the organizer as president of the LLC and, upon its formation, the LLC ratified or adopted the organizer's pre-formation activities. In the contract, the defendant acknowledged that the LLC was in the process of being formed as a Nevada LLC. The defendant argued that it was not bound because it withdrew prior to the LLC's ratification of the contract. The court held, however, that under the circumstances in this case the defendant was estopped to deny the existence of the LLC.

Q. Fraudulent Inducement in Formation of LLC

VGS, Inc. v. Castiel, No. C.A. 17995, 2003 WL 723285 (Del.Ch. Feb. 28, 2003) (applying New York law pursuant to choice of law clauses in agreements and rejecting claim of misrepresentation and fraudulent inducement relating to investment in LLC where the transaction was a multi-million dollar transaction executed following negotiations among sophisticated parties and the complaining party had the opportunity to discover information making reliance unwarranted).

Lloyd v. Horn, Inc., No. Civ.A. 95-2549-KHV, 1997 WL 150052 (D. Kan. Jan. 29, 1997), *aff'd*, 1998 WL 939493 (10th Cir. Aug. 21, 1998).

The court rescinded an operating agreement of an LLC on the grounds that Lloyd, one of the members, committed fraud in the formation of the LLC, and the court concluded that Lloyd's rights were governed by the partnership agreement under which the parties had operated before organizing as an LLC. However, the court concluded that it could not determine Lloyd's rights under the partnership agreement by summary judgment and scheduled the matter for trial. The court referred to confusion between the terms "capital account" and "capital contribution" and as to whether Lloyd should be treated as a withdrawing or expelled partner under the provisions of the partnership agreement.

Gee v. Bullock, 1996 R.I. Super. 941, 1996 WL 937009 (R.I. Super. Nov. 16, 1996).

Two members of an LLC sued the third member, Bullock, seeking injunctive relief barring Bullock from operating the LLC and permitting them to carry on the business. Bullock sought dissolution and an accounting. The court found that Bullock made fraudulent representations when she claimed to have sole ownership of an existing business into which she induced the plaintiffs to invest and when she promised to sign an operating agreement giving the plaintiffs a fifty-one percent controlling interest in their newly formed LLC. In fact, another individual had a substantial interest in the business Bullock claimed to own, and Bullock later refused to sign the operating agreement for the new LLC. Ultimately, Bullock locked the other two members out of the business premises and transferred the assets of the LLC to a new corporation formed by Bullock and yet another investor. The court concluded that the LLC dissolved when Bullock wrongfully excluded/expelled the other two members from the business and that the LLC could only continue for winding up purposes. Thus, the court denied the plaintiffs' requested injunctive relief. The court went on to discuss the fraudulent nature of the transfer of the LLC's assets to Bullock's new corporation under Rhode Island's Uniform Fraudulent Transfer Act. Finally, the court appointed an attorney to conduct the winding up of the LLC because Bullock, having wrongfully caused the dissolution of the LLC, was not entitled to participate in the winding up of the LLC's affairs.

R. LLC Property and Interest of Members

Parking Deck LLC v. Anvil Corp., 576 S.E.2d 24 (Ga.App. 2002) (imputing sole member's knowledge of easement to LLC notwithstanding subsequent sale of member's interest because property owner was LLC, not the members of the LLC).

First Union National Bank v. Clark, No. Civ. 02-05-P-H, 2002 WL 1585529 (D. Me. July 17, 2002).

A judgment creditor argued that the bank account of an LLC was subject to attachment to satisfy the judgment against the individuals who were members of the LLC. The court cited the provisions of the Maine LLC act that specify that property transferred to or acquired by an LLC becomes LLC property and that a member has no specific interest in

LLC property. The judgment creditor argued that the account was a joint account because it was used for personal expenses and the bank treated the account as a joint account. The court rejected this argument, pointing out that the account was in the name of the LLC only and that various aspects of the documentation indicated the account was a commercial or business account.

Hutson v. Young, 564 S.E.2d 780 (Ga. App. 2002)(stating that an action to compel specific performance of two LLCs which own land involves the sale of personalty, and such a suit indirectly involving land does not permit the filing of a lis pendens).

Brown Wood Products, Inc. v. Interlab Robotics, Inc., No. H22232, 2002 WL 660452 (Cal. App. April 22, 2002).

The plaintiff obtained a default judgment against the defendant (Interlab Robotics, Inc.), and pursued money in a bank account in the name of H-Square Engraving Systems, which was allegedly a fictitious name under which the defendant and its president did business as a joint venture. The plaintiff obtained the funds after obtaining a partnership charging order and an order freezing the bank account of H-Square Engraving Systems (“H-Square”) followed by appointment of a receiver who was directed to seize the assets of H-Square, determine the interest of the defendant in the assets, and distribute the assets. H-Square then apparently argued (the court characterized its briefing as “less than clear”) that it was an LLC and it was not liable for the judgment because it was not the judgment debtor. The court acknowledged that, if H-Square was an LLC, it was “arguably correct” that it was not the judgment debtor and could not be charged with the defendant’s debt to the plaintiff. However, the court stated that if H-Square was a joint venture, its argument was to no avail because the defendant’s interest in it could be charged to satisfy the defendant’s debt to the plaintiff. (The court cited the charging order provisions of the partnership statute and equated a joint venture to a partnership, but did not explain how these provisions would entitle the receiver to directly reach the assets of the alleged joint venture.) The court cited conflicting evidence as to whether H-Square was an LLC, a joint venture, or a fictitious name. Ultimately, the court found that the evidence supported the receiver’s implicit conclusions that H-Square was a fictitious business name for the defendant and no allocation of the money in the bank account was necessary.

Premier Van Schaack Realty, Inc. v. Sieg, 51 P.3d 24 (Utah App. 2002).

A real estate listing agent sought to collect its commission under its brokerage agreement when the owner of the property conveyed the property to a newly formed LLC in which the owner of the property and three other individuals were the members. The member who contributed the property received a 40% membership interest and a 9% preferential return on the future profits from the property. Further, the property could not be encumbered without the consent of the member who contributed the property to the LLC. The court determined that the contribution of the property was not a sale or exchange under the brokerage agreement. The court reasoned that the owner of the property retained an ownership interest in the property that caused him to assume the risks of an investor rather than the risks of a seller. The court stated that whether a sale or exchange for consideration occurred is a fact-intensive inquiry that requires more than a mere showing that an owner transferred his property to a separate legal entity. “Where the owner retains essentially the same ownership interest in the property as he had prior to the conveyance, with plans to develop the property by improving it with the possibility of future gains or losses, and can prevent the record owner from encumbering the property without his permission, such a transaction is not a sale or exchange,” said the court. Under this test, the court concluded that the conveyance to the LLC was not a sale or exchange.

In re Rodio (Associates Commercial Corp. v. Rodio), 257 B.R. 699 (Bankr. D. Conn. 2001).

The debtor in this bankruptcy proceeding claimed that he had equitable rights in a tractor owned by an LLC of which he was a member. The court rejected this argument, finding it clear that the debtor’s membership interest was property of the estate but the LLC’s property was not. Thus, the holder of a security interest in the tractor was allowed to foreclose its interest.

Gebhardt Family Investment, L.L.C. v. Nations Title Insurance of New York, Inc., 752 A.2d 1222 (Md.App. 2000).

The issue in this case was whether a title insurance policy continued in effect for property transferred by a husband and wife to their wholly owned LLC. The court held that the transfer terminated the policy. The Gebhardts conveyed the real property to a Virginia LLC of which they were the only members. The deed recited that the LLC paid \$160,990 for the property, but Mr. Gebhardt testified that this recitation was for transfer tax purposes and that the LLC did not pay anything for the property. The Gebhardts argued that the conveyance was in effect a conveyance to themselves because they were the sole members of the LLC. The court, however, stressed that an LLC is a separate

entity and that there was indeed a transfer from one entity or person to another. The court stated that there was a real conveyance even if no money changed hands because the Gebhardts obtained benefits conferred by a Virginia LLC, including limited liability and estate planning benefits. Finally, the court rejected the argument that, because they had already reported the cloud on the title before the transfer to the LLC, the Gebhardts should be able to recover under the title policy. The court rejected this argument on the basis that any loss suffered by virtue of the cloud on the title would be suffered by the LLC, not the Gebhardts, because the Gebhardts successfully conveyed the entire property under a special warranty deed.

Warren Davis Properties V, L.L.C. v. United Fire and Casualty Co., 4 S.W.3d 167 (Mo. App. 1999).

The court held that the manager of an LLC is competent to testify as to the value of LLC property even though the manager is not an expert so long as the manager is in fact familiar with the value of the realty. The court reached this conclusion based upon Missouri case law recognizing that a managing officer of a corporation is competent to testify on the value of corporate property.

Jennette v. Jennette, No. 01-A-01-9810-CH-00549, 1999 WL 732519 (Tenn. App. Sept. 21, 1999).

In this divorce action, Mr. Jennette claimed that he had no interest in an LLC he formed, but the court found that he did have an interest. Although Mr. Jennette was the organizer of the LLC, chose the lawyers and accountants for the company, and signed the operating agreement as one of the members, Mr. Jennette claimed that he was only an employee of the LLC. The LLC did not withhold taxes on the money he drew, however, and the court pointed out, as “the most telling piece of circumstantial evidence,” that Mr. Jennette had listed a 49% interest in the LLC, valued at \$450,000, in a financial statement he provided a bank. The trial court concluded that Mr. Jennette’s testimony was not truthful and viewed the paper trail as indicating that Mr. Jennette owned a valuable interest in the LLC. The court of appeals upheld the trial court’s conclusion.

March Trading, Inc. v. Sloan, 25 Conn.L.Rptr. 339, 1999 WL 732955 (Conn. Super. Aug. 30, 1999).

The plaintiff brought a bill of discovery action against a member of an LLC seeking sworn copies of the member’s membership certificate giving notice of a pledge of the membership interest. Under an agreement between the member and the plaintiff, the member was to pledge a 20% LLC interest as partial security for a promissory note. The agreement also required the member to place a legend on the certificate indicating that the interest had been pledged. When the member refused to provide the plaintiff proof that the language had been placed on the certificate, the plaintiff brought this action. The court found that the plaintiff was entitled to maintain the bill of discovery seeking proof of compliance with the agreement.

Graves v. Graves, 967 S.W.2d 632 (Mo. App. 1998).

This divorce action included an issue as to the propriety of the trial court’s order that one spouse, who was awarded all interest in the couple’s LLC, execute a lease on behalf of the LLC. Mr. and Mrs. Graves owned an LLC which operated on a tract of land it leased from the Graves. The trial court awarded Mr. Graves all right, title and interest in the LLC and awarded Mrs. Graves the land on which the LLC operated. The court also ordered Mr. and Mrs. Graves to sign a twelve month lease of the land to the LLC at a specified rent. The lease included a signature line for the LLC to be signed by Mr. Graves as president. Mr. Graves complained that the court did not have jurisdiction over the LLC and that the order to execute the lease was thus improper. The court acknowledged the difference between a member’s interest in an LLC and property of the LLC itself, but analogized the situation to that of a sole shareholder corporation where a court may order the shareholder spouse to cause the corporation to undertake certain acts. The court concluded that the trial court was within its authority to cause the LLC to lease the property from Mrs. Graves since it did not order the LLC to distribute any property and did not directly order the LLC to sign the lease.

In re Welty, 217 B.R. 907 (Bankr. D. Wyo. 1998).

The debtor in this bankruptcy case claimed that his interest in an LLC was exempt because it was held in a tenancy by the entirety. The court noted that an ownership interest in an LLC is intangible personal property. The court stated that there must be a clear manifestation of intent on the face of the instrument of conveyance to support the existence of a tenancy by the entirety. The court concluded that the articles of organization, the only evidence of the ownership interests of the debtor and his spouse, did not demonstrate an intent to hold ownership in the LLC in a tenancy by the entirety.

Hagan v. Adams Property Associates, Inc., 482 S.E.2d 805 (Va. 1997).

In this case, the plaintiffs, Ralph and Maureen Hagan (the Hagans), executed an agreement with the defendant, Adams Property Associates, Inc. (Adams), giving Adams the exclusive right to sell the Hagans' apartment complex for \$1,600,000. The agreement provided that if the property was "sold or exchanged" within one year, with or without Adams' assistance, the Hagans would pay Adams a fee of six percent of the "gross sales amount." Before the year had expired, the Hagans and two other parties formed an LLC, and Hagan transferred the property to the LLC in exchange for an interest in the LLC, the LLC's assumption of debt on the property, and a promissory note from the LLC secured by a second deed of trust on the property. Adams sought its commission on the basis that the transfer of property to the LLC constituted a sale of the property. The Hagans argued that transfer of legal title to the property represented their contribution to the capitalization of a new company, and not a sale of the property. The Hagans added that they did not receive any present valuable consideration for the contribution. The Virginia Supreme Court found that the benefits received by the Hagans by virtue of the transfer of the property constituted valid consideration. It further distinguished the cases cited by the Hagans for the proposition that the transfer was capitalization on the basis that those cases involved the capitalization of a partnership rather than an LLC. The court stated that a partnership is not an entity separate from its partners, thus a partner's transfer of property to the partnership is "only a change in the form of ownership." The court characterized an LLC as an entity separate from its members and concluded that the member's transfer of the property to the LLC thus amounted to a sale.

Gattoni v. Zaccaro, No. CV 970396081, 1997 WL 139410 (Conn. Super. March 13, 1997).

This proceeding arose out of a dispute between Gattoni and Zaccaro, 49% and 51% members, respectively, of an LLC. Gattoni alleged various misdeeds and breaches of contract by Zaccaro and sought an accounting and judicial dissolution of the LLC. The specific matter before the court was the request of Zaccaro and the LLC for discharge of a *lis pendens* filed by Gattoni on real property owned by the LLC. The court granted the request inasmuch as the claims did not involve the real property within the meaning of the relevant Connecticut statute. The court pointed out that Gattoni did not have an interest in specific LLC property. Rather, Gattoni had a membership interest in the LLC, and the membership interest was personal property. The court rejected the argument that his claim for dissolution involved a claim for partition of the real property owned by the LLC. The court also addressed a request by Gattoni for a preliminary injunction that would essentially order preservation of the real property and prohibit its transfer. The court denied the request for injunctive relief based upon its conclusions that Gattoni failed to establish likelihood of success on the merits of his claims and did not show that Zaccaro was likely to dispose of the property in a way that would thwart winding up and dissolution of the LLC. A subsequent related opinion is published at 727 A.2d 706 (Conn. App. 1999).

Reid v. Town of Hebron, No. CV 9354384S, 1996 WL 634254 (Conn. Super. Oct. 22, 1996).

The plaintiff was denied a building permit to build a house on a lot he owned. He appealed the decision of the Hebron Conservation Commission, claiming that the decision deprived him of any reasonable use or practical value of his property and amounted to a taking of the property without just compensation. During the course of the appeal, the plaintiff transferred his interest in the lot to an LLC in which he owned a fifty percent interest. The defendant argued that the plaintiff was not a party aggrieved by the denial of the permit and thus could not pursue the appeal because he did not sustain his interest in the property at issue throughout the course of the proceedings. The plaintiff relied on his ownership in the LLC to establish his aggrievement. The court quoted the LLC statute to the effect that property transferred to or otherwise acquired by an LLC is property of the LLC and not of the members individually. The court held that, because the property was transferred to another party who was not a party before the Commission and not a party to the appeal, the plaintiff was not aggrieved and had no standing to appeal. (Had the plaintiff been the sole member of the LLC, it appears the court would have treated him as the beneficial owner of the property based upon a prior case in which the court treated the sole stockholder of a corporation as beneficial owner of land owned by the corporation.)

Diaz v. Fernandez, 910 P.2d 96 (Colo. App. 1995).

This case involved the application of Colorado receivership law in the context of an LLC. The court allowed an LLC member to pursue appointment of a receiver for the LLC because an LLC member has a personal property interest in the LLC and thus may satisfy the Colorado rule which provides for the appointment of a receiver when the moving party establishes "a prima facie right to the property, or to an interest therein, which is the subject of the action and is in possession of an adverse party and such property, or its. . . profits are in danger of being lost. . . or materially injured or impaired."

S. Authority of Members and Managers

Apple Glen Crossing, LLC v. Trademark Retail, Inc., 784 N.E.2d 484 (Ind. 2003) (stating that a principal who honors an obligation wrongfully incurred by its agent may nevertheless enforce its remedies against the agent for the wrongful action, but holding that “change orders” approved by LLC manager did not constitute “Major Decisions” requiring unanimous consent of members under LLC operating agreement and thus change orders were not a basis for the majority member to remove the minority member as manager).

Connecticut Car Rental, Inc. v. Prime One Capital Co., LLC, 247 F.Supp.2d 158 (D.Conn. 2003) (holding that member had actual authority to assign car lease agreements pursuant to the LLC formation agreement (under which the assignments were not “major decisions”), and that, alternatively, even assuming actual authority was lacking, the assignments were binding under the Washington LLC act (as acts of a member of a member-managed LLC apparently acting in the usual way of business) and common law apparent authority).

TIC Holdings, LLC v. HR Software Acquisitions Group, Inc., 750 N.Y.S.2d 425 (N.Y. Sup. 2002), *aff'd*, 2003 WL 116115 (N.Y. A.D. 1 Dept., Jan. 13, 2003) (concluding LLC manager did not have authority under New York LLC act or operating agreement to execute agreement obligating LLC to transfer assets that constituted all or substantially all of the LLC’s assets inasmuch as operating agreement’s broad grant of authority was “subject ... to the requirements of applicable law” and the failure of the other members to object did not satisfy the requisite “affirmative vote” of a majority in interest of the members).

Cooper v. Creative Homes of Distinction, L.L.C., No. COA01-1138, 2002 WL 2004298 (N.C. App. Sept. 3, 2002).

After the individual who was manager of an LLC was terminated as manager, the LLC designated a new manager, but the individual continued to operate the LLC with the knowledge of the members, who took no steps to stop the individual from doing so. The court held under these circumstances that the terminated manager was acting with apparent authority.

EZ Auto, L.L.C. v. H.M. Jr. Auto Sales, No. 04-01-00820-CV, 2002 WL 1758315 (Tex.App. July 31, 2002).

The plaintiff sought to hold an LLC liable on a transaction by the manager (Marks) on the LLC’s behalf. The LLC argued that Marks had been removed as manager at a meeting of the members and lacked authority to bind the LLC. The LLC was designated as manager-managed in its articles of organization and Marks was named the initial manager in the articles of organization. The court reviewed the statutory provisions dealing with actual and apparent authority of managers of manager-managed LLCs as well as the provisions of the articles of organization and regulations of the LLC and concluded that the evidence conclusively established that Marks was the initial manager with actual authority to act for the LLC. The question was whether Marks continued to have actual authority at the time in question. The court noted that there was evidence that proper notice required under the regulations had not been given to all members of the meeting at which Marks was removed. The court stated that the plaintiff did not have standing to directly challenge the irregularity in the meeting, but the failure to give notice of the meeting to Marks, who was also a member of the LLC, did impact the analysis of his authority. The court stated that an agent has actual authority where a principal intentionally confers it or intentionally or negligently allows the agent to believe he has authority. Since the evidence did not show that Marks was dispossessed of the belief that he was authorized to continue to act on the LLC’s behalf, he continued to have actual authority to bind the LLC.

Taghipour v. Jerez, 52 P.3d 1252 (Utah 2002).

The Utah Supreme Court affirmed the holding of the court of appeals that a loan agreement signed by the manager of an LLC was binding on the LLC under the provisions of the Utah LLC act in effect at the time. Although the loan agreement was signed by the manager without approval of the members as required by the operating agreement, the court held that the loan agreement was binding on the LLC because the Utah act provided: “Instruments and documents providing for the acquisition, mortgage, or disposition of property of the limited liability company shall be valid and binding upon the limited liability company if they are executed by one or more managers.” The court concluded this specific provision controlled over a more general statutory provision stating that a manager has authority to bind the LLC unless otherwise provided in the articles of organization or operating agreement. The manager was identified as such in the articles of organization, and, though the operating agreement limited his authority, the lender did not have a due diligence obligation to determine the manager’s authority and was not responsible for the fact that the manager absconded with the funds.

Ward v. Hornik, No. 02.944, 2002 WL 1199249 (E.D. Pa. June 3, 2002)(interpreting Pennsylvania LLC act and quorum and voting provisions of LLC operating agreement and concluding that suit brought on behalf of LLC was not authorized).

Construction and Environmental Management, LLC v. R & R Landholding, LLC, 746 So.2d 817 (La.App. 1999).

This case involved a dispute as to the authority of Stephen Bandi to obligate R & R Landholding, LLC (“R & R”) on certain transactions. Michael and Darlene Reed owned 50% of R & R. The other 50% of R & R was owned by another LLC, Regatta Investment Group, LLC (“Regatta”). Bandi was the managing member of Regatta. Regatta also owned a 50% interest in Construction and Environmental Management, LLC (“CEM”), which was the general contractor for R & R’s project to renovate an apartment complex. The dispute involved Bandi’s authority to approve change orders and borrowing on behalf of R & R. The Reeds claimed that Bandi was not the managing member of R & R and that, in any event, all decisions required an oral or written vote of a majority of all members. The court found that there were no such votes taken at any time, no meetings held, and no minutes recorded. Michael Reed testified that he left decisions regarding the construction project to Bandi. The Reeds did not object to the work performed. Based on such evidence, the court refused to disturb the trial court’s finding that Bandi had actual or apparent authority to approve the change orders. In the course of reaching this conclusion, the appeals court dismissed R & R’s argument that the Louisiana LLC statute’s interested member/manager provision nullified Bandi’s execution of the change orders to CEM. While the trial court found that Bandi had authority to obligate R & R on the change orders, it concluded that Bandi did not have authority to obligate R & R on a \$32,000 loan. There was no testimony that decisions regarding financial obligations were delegated to Bandi; thus, the appeals court upheld this finding as well.

J.M. Equipment and Transportation, Inc. v. Gemstone, L.L.C., No. CV9662031, 1998 WL 573255 (Conn. Super. Aug. 25, 1998).

The plaintiff relied upon the agency power of an LLC member to bind the LLC to the plaintiff for parts and labor in connection with the repair of a bulldozer. The charges in question were incurred at the request of one member of a two member LLC. The court relied upon the provisions of the Connecticut LLC act that make members of an LLC agents of the LLC for any act apparently carrying on in the usual way the business of the LLC absent a lack of authority known to the third party. The court examined the facts surrounding the transaction and concluded that the member had apparent authority to bind the LLC.

In re D&B Countryside, L.L.C. (D&B Countryside, L.L.C. v. Newell), Case No. 95-11946-SSM, Adv. Proceeding No. 96-1110 (February 24, 1997).

This opinion is unpublished and is not available on Westlaw or Lexis. The issue in the proceeding was the authority or apparent authority of LLC managers to execute deeds of trust against the LLC’s assets and obligate the LLC for repayment of certain loans to the managers. Robert and Marilyn DeLuca were members and managers of D&B Countryside, L.L.C., a Virginia LLC. Newell loaned the DeLucas substantial amounts of money secured by various deeds of trust on property owned by the LLC. Eventually, the DeLucas also executed a note on behalf of the LLC. The deeds of trust and note were executed by the DeLucas without the consent of the other members of the LLC. The court examined the operating agreement of the LLC and concluded that it did not confer actual authority on the DeLucas to execute the deeds of trust or the note. The court then considered whether the DeLucas had apparent authority to bind the LLC. Relying on common law principles and provisions of the Virginia LLC act, the court concluded that the DeLucas did not have apparent authority to execute the deeds of trust or the note.

T. Admission of Members

Sosa v. Shearform Manufacturing, 784 So.2d 609(Fla. App. 2001).

Sosa agreed to loan money to an LLC in two installments in exchange for a 1/3 membership in the LLC. Sosa made an initial advance to the LLC but did not make the second advance. The trial court concluded that Sosa first breached the agreement by failing to pay the second installment, but the court of appeals held that it was the other parties to the agreement who first breached by failing to take immediate action to admit Sosa as a member in accordance with the agreement.

McDonald v. Miller, No. 00AP-994, 2001 WL 300736 (Ohio App. March 29, 2001).

Four individuals entered an operating agreement for an LLC that listed them as members and required that each of them contribute \$5,000 as an initial capital contribution. One of the individuals did not make the required

contribution. The issue addressed by the court was whether the individual who failed to make the contribution was a member, and the court held that he was. The other members argued that he never became a member because of his failure to make the required contribution. The court, however, found that he was a member under the clear and unambiguous language of the operating agreement. The court pointed out that the operating agreement listed the individual as a member and presupposed that the person required to make the capital contribution was a member when it provided that “each Member shall contribute \$5,000 as the initial Capital Contribution.”

Prefer v. Pharmnetrx, LLC, 18 P.3d 844 (Colo. App. Oct. 12, 2000).

In this suit by a member to challenge the member’s termination as employee and manager of the LLC, the court refused to disturb the finding that the member’s written consent to admission of new members required by the Colorado LLC Act was established by various writings, taken together, including a proxy request sent to investors by the member.

U. Fiduciary Duties of Members and Managers

Kronemyer v. Philadelphia Indemnity Insurance Co., No. B161586, 2003 WL 21213243 (Cal.App. May 27, 2003).

In the context of a dispute over the coverage provided by an “Executive Safeguard” insurance policy providing “Directors and Officers Liability & Company Reimbursement Insurance,” the president of two South Dakota LLCs argued that South Dakota and California law, as well as the LLC operating agreement, required the LLCs to indemnify him. The court stated that South Dakota law permits South Dakota LLCs to indemnify officers and agents but does not mandate indemnification. Similarly, the court said California law permits, but does not require, LLCs to indemnify officers. The court pointed out that California law prohibits LLCs from indemnifying officers for breach of fiduciary duty. The court also determined that the terms of the operating agreement did not require indemnity because the LLC was required to do so only on advice of counsel and only after approving such an action.

Weissberg v. Peinado, Nos. A097102, A097232, 2003 WL 1849243 (Cal.App. April 10, 2003) (discussing proper measure of damages in context of LLC member’s liability for conversion, breach of fiduciary duty, fraud, breach of contract, and breach of the duty of good faith and fair dealing).

Pinnacle Data Services, Inc. v. Gillen, 104 S.W.3d 188 (Tex.App. 2003).

Four individuals formed a Texas LLC designated as member-managed by its articles of organization. Two of the individuals, Gillen and Baldrige, each owned a 25% interest, and an entity owned and operated by the other two individuals (Max and Morris Horton) owned the other 50% of the LLC. (The court noted in a footnote that the Hortons were apparently under the impression that they had the right to participate in management although they were not technically members of the LLC.) Disagreements over management developed, and Gillen proposed amending the LLC’s articles of organization to change it to a manager-managed LLC and electing Gillen as manager. The regulations (the Texas equivalent of an operating agreement) provided that amendment of the articles of organization required the affirmative vote of at least 66 2/3% of the ownership interest while the articles of organization provided for amendment by the affirmative vote of two-thirds of the members. Gillen and Baldrige voted for the proposed changes and relieved the Hortons of their duties with the LLC. The entity member brought suit for declaratory relief, unjust enrichment, and member oppression. The trial court granted summary judgment to Gillen, Baldrige, and the LLC. The declaratory relief hinged on the determination of whether the voting provisions of the articles of organization or the regulations controlled. Under the Texas LLC act, the regulations may contain any provisions for the regulation or management of the LLC not inconsistent with law or the articles of organization. Thus, the court determined that the articles of organization controlled, and the amendment received the requisite vote. The entity member claimed that it was not given a copy of the articles until two years after the regulations were signed, but the court stated that there was no evidence that it sought to obtain a copy (even though it signed regulations that were expressly subordinate to the articles of organization), and the articles were on file with the Secretary of State. The court stated that the regulations, the articles of organization, and the Texas LLC act are not rendered inoperative by the failure to exercise diligence in obtaining a copy of the articles before agreeing to their terms. The court also found that the entity member had not set forth any evidence that Gillen, Baldrige, or the LLC obtained any benefit through fraud, duress, or taking undue advantage of the entity, and thus the trial court did not err in granting summary judgment on the unjust enrichment claim. The court cited shareholder oppression cases for the definition of “member oppression,” but held that the entity did not set forth any evidence in support of its member oppression claim. The court found the determination that the articles of organization control disposed of the breach of contract claim but not the remaining reformation and breach of fiduciary duty-based claims. The defendants claimed that the claim for breach of fiduciary duty was without merit because the action taken complied

with the articles of organization, but the court concluded that compliance with the articles was not dispositive of such claims. The court's opinion implies that the duties of the LLC members equate to those of corporate officers and directors, but the opinion is not entirely clear in this regard.

In re Brentwood Lexford Partners, L.L.C., 292 B.R. 255 (Bankr. N.D. Tex. 2003).

The Chapter 7 trustee brought an adversary proceeding to set aside alleged fraudulent transfers. The court held that certain distributions to the members were fraudulent transfers. The court also addressed breach of fiduciary duty claims against members of the LLC who were officers. The court discussed the fiduciary duties of the LLC's officers as if they were officers of a corporation. The court stated that the officers of a corporation owe a fiduciary duty to the corporation and its shareholders. Further, the court stated that the officers owe a fiduciary duty to the creditors of the corporation when the corporation is insolvent. According to the court, "[o]fficers of an insolvent corporation breach their fiduciary duty by transferring funds to themselves, in effect, as equity holders, to the detriment of the corporation's creditors." The court determined, however, that the trustee and the LLC's major creditor were estopped from pursuing the breach of fiduciary duty claim. The noteholder was a "sophisticated player" and understood companies in the LLC's business. It conducted its own assessment of the LLC's assets and concluded that the LLC's assets supported its debt structure. The excess cash distributions were permitted under the terms of the note. The court thus applied the equitable estoppel doctrine to the fiduciary duty claim related to the excess cash distributions. The court also concluded that the officers of the LLC did not breach a fiduciary duty when they resigned from the LLC, formed another LLC, and transferred some business to the new LLC. The court stressed that the officers did not have a non-competition or non-solicitation agreement. Additionally, the agreement under which the LLC was acquired from the noteholder recognized that the officers had fiduciary duties to other interest holders in the real estate they controlled and permitted the officers to exercise discretion regarding property management contracts when their fiduciary duty to other interest holders required. (This case is further summarized below under the headings "Distributions" and "Fraudulent Transfer.")

VGS, Inc. v. Castiel, No. C.A. 17995, 2003 WL 723285 (Del.Ch. Feb. 28, 2003) (applying "law of the case" doctrine and entering summary judgment on breach of fiduciary duty claim against two managers who orchestrated clandestine written consent to merger for purpose of eliminating majority control by third manager inasmuch as prior trial on corporate governance issue had already determined that the two managers owed a duty of loyalty to majority member and fellow manager and that attempted merger constituted a breach of that duty).

Jundt v. Jurassic Resources Development, North America, L.L.C., 656 N.W.2d 15 (N.D. 2003).

An LLC member asserted that other members breached their fiduciary duty to the LLC by diverting an LLC business opportunity to an entity owned by the defendant members. The court noted that it had not previously ruled on the corporate opportunity doctrine but identified four tests established as standards for identifying a corporate opportunity: the "line of business" test, the "interest or expectancy test," the "fairness" test, and the "ALI" test. The court concluded that the plaintiff failed to meet his burden under any of the theories because the defendants owned two-thirds of the LLC membership interests and controlled business decisions under the operating agreement. According to the court, "[t]he majority owners impliedly disclosed to themselves and to [the LLC] all of the relevant facts about [the LLC's] asserted corporate opportunity ... and elected to forego the opportunity." The court also stated that financial inability justifies a corporation in rejecting an opportunity. The court found the plaintiff had made no showing that the LLC had the financial ability to take advantage of the opportunity and that there was evidence supporting the trial court's finding that the LLC's debts exceeded the appraised value of its assets.

Bio-Septic Systems, LLC v. Weiss, 60 P.3d 943 (Mont. 2002).

Weiss, Cullinan, and others formed an LLC to market a device invented by Weiss. Acrimonious relations developed between Cullinan and the other members. The LLC eventually collapsed, and Weiss ultimately assumed management. Weiss informed Cullinan that he intended to dissolve the LLC and disburse the assets as required by law. Cullinan accused Weiss of wrongdoing in connection with certain payments and Weiss's commencing work for a company with which the LLC had previously contracted for marketing of the device. Cullinan brought suit for dissolution of the LLC and accused Weiss of breach of fiduciary duty. Weiss counterclaimed and joined in the request for dissolution. Cullinan filed an amended complaint alleging sole ownership of the LLC and waiving any further winding up. The court upheld the lower court's finding that Cullinan acted arbitrarily, vexatiously or not in good faith on the basis of various actions disruptive to the LLC's business. The court also upheld the lower court's determination that Weiss did not breach his fiduciary duties to the LLC. Cullinan offered no evidence that Weiss's handling of payments was improper, and the court held that a resolution authorizing Weiss to make certain disbursements that was allegedly signed by one of the members after his withdrawal from the LLC was not deceptive and indicated a good faith

attempt to formalize an arrangement in the midst of confusing circumstances. Finally, the court did not agree with Cullinan that Weiss had breached his fiduciary duty by forming a sole proprietorship and competing with the LLC. The court said the LLC was breaking up and the contract between the LLC and the company with whom Weiss subsequently contracted had expired. Weiss contracted with the company as an independent contractor after disclosing his intentions to the other members of the LLC. The court concluded that payments to Weiss were payments to him as an independent contractor, and Weiss did not convert property of the LLC. The court also upheld the accounting made by Weiss to the members in connection with the winding up of the LLC.

Credentials Plus, LLC v. Calderone, 230 F.Supp.2d 890 (N.D. Ind. 2002).

Calderone was a member and the sole officer and operating employee of an Indiana LLC providing physician credentialing services. Prior to her departure from the LLC, she registered a domain name for a competing company. After her departure, while she was still a member in the LLC, she incorporated her new business and solicited customers. A few months later she sold her interest in the LLC to her father. The court addressed the LLC's breach of fiduciary duty claims under both contract and common law principles. The court determined that Calderone violated a covenant not to compete contained in a letter agreement between the members. The agreement prohibited a "shareholder" from competing with the business of the LLC without approval of the other "shareholders." The court concluded that Calderone's activities before she sold her "shares" to her father violated the agreement. The court also concluded that Calderone's conduct violated common law fiduciary duties. The court discussed fiduciary duties in partnerships and close corporations and concluded that "Indiana LLCs, being similar to Indiana partnerships and corporations, impose a common law fiduciary duty on their officers and members in the absence of contrary provisions in LLC operating agreements." The court found that Calderone owed a fiduciary duty even though she herself was not a member but owned her interest in the LLC through a single-member LLC. The court said she would nevertheless owe a duty not to seize business opportunities as the LLC's sole officer and operating employee and she had admitted in responses filed with the court that she owed a duty to the other members "to deal fairly, honestly and openly with them."

Blue Chip Emerald LLC v. Allied Partners Inc., 750 N.Y.S.2d 291 (N.Y.A.D. 1 Dept. Nov. 26, 2002).

The plaintiff sold its 50% interest in a venture (the sole asset of which was a building) to the defendants, who controlled the managing member/remaining 50% owner, based on an \$80 million valuation of the venture's property. Two weeks later, the defendants contracted to sell the property to a third party for \$200 million. The "venture" involved in this case was apparently an LLC (it is identified in the case as Ceppetto Enterprises, LLC), but the court refers to it throughout as a venture or joint venture. The court notes that the venture was organized under Delaware law but does not refer to a specific statute. The court relies on case law on the fiduciary duties of "venturers" and "managing co-venturers" (including *Meinhard v. Salmon*) and concludes that the contractual disclaimers relied upon would be voidable as the fruit of the fiduciary's breach of its obligation to make full disclosure in the context of a buy-out. The court stated: "Defendants have not brought to our attention any authority, from either New York or Delaware (the state under whose law the Venture was organized), that would give effect to a waiver of a fiduciary's duty of full disclosure that the fiduciary obtained by means of its breach of that very duty, even where the party that gave the waiver was ... commercially sophisticated and advised by its own counsel." The provisions in issue were provisions of the buy-out agreement in which the plaintiff acknowledged that it had been afforded an opportunity to conduct its own due diligence and was satisfied with the information made available to it in conducting the due diligence and provisions in which the plaintiff disclaimed any profits realized by the defendants on the future sale of the venture property and any claim for fraud, breach of loyalty, or fiduciary duty arising out of the venture with one specific exception. The court stated that "a fiduciary cannot by contract relieve itself of the fiduciary obligation of full disclosure by withholding the very information the beneficiary needs in order to make a reasoned judgment whether to agree to the proposed contract." The court refused to dismiss the claim

TIC Holdings, LLC v. HR Software Acquisitions Group, Inc., 750 N.Y.S.2d 425 (N.Y. Sup. 2002), *aff'd*, 2003 WL 116115 (N.Y.A.D. 1 Dept. Jan. 14, 2003).

The manager of a New York LLC executed an agreement obligating the LLC to transfer the LLC's assets to a new company being formed by one of the LLC's members. After rejecting the argument that the manager was authorized to take the action under the operating agreement, the court addressed the claims of the manager and member that they were entitled to summary judgment under release and indemnification provisions of the operating agreement. The member relied upon a release relating to actions involving conflict of interests and breach of fiduciary duty. The court found, however, that the language indicated the scope of the release was confined to matters related to actions taken in connection with the member's dual involvement in the LLC and a specified company in which the LLC invested. Further, the court found the release would be ineffective if it was intended to release the member from *all* actions taken

in his self-interest. For example, the court said, a release cannot reach willful and intentional misconduct. The court noted that certain alleged misconduct of the member might fall within this realm, e.g., alleged breaches of fiduciary duty, intentional interference with the LLC's ability to obtain financing, and attempted misappropriation of an LLC business opportunity. With respect to the manager's release claim, the court found that the complaint alleged liability based on actions outside the scope of the operating agreement's release of the manager because it involved conduct not properly within the capacity of manager (e.g., his attempt to bind the LLC to transfer its assets without authority). Further, the New York LLC act provides that an operating agreement may not eliminate or limit liability if a judgment establishes bad faith, intentional misconduct, or a knowing violation of law, which the allegations indicated. The court stated that the manager's alleged breaches of fiduciary duty involved misconduct that might result in a judgment based on bad faith, intentional misconduct, or knowing violations of the LLC act. The manager's summary judgment claim for indemnification was rejected for similar reasons. The operating agreement provided for indemnification of the manager to the fullest extent permitted by law, but the New York LLC act precludes indemnification if a judgment establishes bad faith or deliberate dishonesty. The member's claim for indemnification was rejected because he cited no provision of the operating agreement providing for his indemnification.

In re Woods (Cundy v. Woods), 284 B.R. 282 (D. Colo. 2001).

The plaintiffs and the debtor were investors who entered a joint venture agreement and formed an LLC to secure financing and manage a real estate project. The debtor was also the attorney for the LLC (referred to in the case as the joint venture) and a member of the management committee. The plaintiffs alleged that the debtor owed them a fiduciary duty as a co-venturer, management committee member, and attorney for the venture, and that his liability for the venture's debt was non-dischargeable because it arose from a defalcation of fiduciary duty when he obligated the venture to loan amounts in excess of borrowing authorizations. The court found that there must be an express or technical trust, not merely a general fiduciary relationship like that arising out of an attorney-client, joint venture, or partnership relationship in order for a fiduciary relationship to exist under section 523(a)(4) (the dischargeability exception for defalcation in a fiduciary capacity). Additionally, the court found that the bankruptcy court was in error in concluding a defalcation had occurred.

Anest v. Audino, 773 N.E.2d 202 (Ill. App. 2002).

Through a series of transactions, Anest invested in an insolvent LLC and became a member. At the time of his investment, the management structure was changed from manager-management to member-management. The LLC sold a beer line cleaning device called the BLM 2000. The LLC exhausted its capital infusion, and an emergency meeting of the LLC's members was called, the stated purpose of which was "to discuss changing the business relationship of the company from a non-exclusive distributor to an importer and the ramifications thereof." The notice was faxed three days before the meeting. The operating agreement required five days' notice of a meeting and did not address facsimile notice. Four of the five members attended the meeting. Audino, a 5% member, did not attend. At the meeting, the members discussed an offer for a five-year exclusive distributorship of the BLM 2000 from the patent holder of the device. The members at the meeting voted not to make the substantial capital contributions that would be required to secure the exclusive distributorship offer. After the meeting, these four members formed a new LLC to obtain the exclusive distributorship offer. When Anest, one of these four members, sued Audino to recover on another debt, Audino counterclaimed against Anest for breach of fiduciary duty and tortious interference with Audino's business expectancy. The trial court granted Anest's motion for directed findings. The trial court held that Anest did not owe Audino a fiduciary duty because Anest did not have control over the daily operations of the LLC or otherwise have management-like responsibilities. The trial court also held that, even if there was a duty owed, Anest did not breach it because the LLC did not have the financial ability to act upon the business opportunity in issue. The appeals court reversed. The appeals court held that the Illinois LLC act in effect at the time required the court to look to the law of corporations to determine the existence of any fiduciary duties. The court cited *Hagshenas v. Gaylord*, which held that shareholders in a closely held Illinois corporation owe one another partner-type fiduciary duties. The court stated that Anest's capacity as a 12% member in a member-managed LLC made him more than a minority shareholder; rather, he was akin to an officer or director of a corporation who owes fiduciary duties to shareholders and the corporation. The court found that the BLM 2000 distributorship opportunity was a business opportunity of the LLC and that the financial inability of the LLC was not controlling since the assets of the LLC were used to develop it. The court also noted that the opportunity was not properly disclosed and tendered to the LLC because the notice violated the requirements of the operating agreement.

McGee v. Best, ___ S.W.3d ___, 2002 WL 1343225 (Tenn.Ct.App. 2002).

The plaintiff was a one-third member and the Chief Manager of a Tennessee LLC. After disagreements arose, the members of the LLC other than the plaintiff took action by written consent to terminate the employment of the plaintiff and to exercise a buy-out right on the part of the LLC triggered by the termination of employment of a member. The plaintiff brought suit alleging various causes of action, including breach of fiduciary duty, fraud, breach of the operating agreement, and breach of the duty of good faith and fair dealing. The court of appeals upheld the trial court's conclusion that members of a member-managed LLC do not owe one another fiduciary duties under the Tennessee LLC act. The Tennessee act provides that members of a member-managed LLC must account to the LLC for any benefit, and hold as trustee for it any profits derived by the member without consent of the other members, from any transaction connected with the formation, conduct, or liquidation of the LLC or any use of its property. The act goes on to provide that a member's duties must be discharged in good faith, with the care of an ordinarily prudent person in a like position under similar circumstances, and in a manner the member reasonably believes to be in the best interest of the LLC. The court stated that the statute defines the fiduciary duty of a member of a member-managed LLC as one owing to the LLC, not to individual members. The court stated that it could not "contravene the intent of the Legislature." The court also dismissed the fraud claim on the basis that the allegations stated a claim that was essentially derivative, and thus the plaintiff did not have standing to pursue it individually. The court stated that the general rule of at-will employment in Tennessee was not altered by the operating agreement and that there is no implied covenant of good faith and fair dealing in an employment at will contract. (The trial court based its dismissal of the good faith and fair dealing claim on its conclusion that "performance of a contract by its terms cannot be characterized as bad faith" and its assessment that the operating agreement allowed the very actions taken in terminating the plaintiff's employment.) The court found that the plaintiff waived his argument that there had been a breach of contract based upon a conflict of interest in violation of the operating agreement. The court did conclude that there was a fact issue as to whether there was "cause" to terminate the employment of the plaintiff under the operating agreement, an issue that was relevant to the valuation of the plaintiff's membership interest under the terms of the operating agreement.

Ault v. Brady, 37 Fed.Appx. 222, 2002 WL 1301520 (8th Cir. 2002).

In this dispute between the members of an Arkansas LLC, a member whose employment was terminated alleged that the managing member breached his fiduciary duty in terminating the member and attempting to force the terminated member to sell his units back to the LLC under a repurchase provision in the operating agreement. The managing member terminated the member "for cause" and notified the member that the LLC would exercise its option to buy the member's units. Under the operating agreement, a member terminated for cause was entitled only to the value of the member's capital account. Ultimately, the district court found that the managing member was within his authority to terminate the member's services but that the termination was without cause. Thus, the member was entitled to the fair market value of his units rather than the value of his capital account. The terminated member argued that the repurchase provision in the operating agreement did not apply to his situation, but the district court and the court of appeals determined that the repurchase provision was applicable. In response to the terminated member's argument that the managing member breached his fiduciary duty, the court of appeals stated that, under Arkansas law, a manager of an LLC is not liable to the LLC or another member unless he engages in gross negligence or willful misconduct. The court stated that the operating agreement gave the managing member broad authority to make all decisions regarding the management of the LLC and responsibility for all administrative matters; thus, the managing member acted well within his authority in terminating Ault. Moreover, said the court, the managing member's conduct in attempting to reacquire the terminated member's units was permissible under the operating agreement.

Disola Development, LLC v. Mancuso, 291 F.3d 83 (1st Cir. 2002)(construing Massachusetts prejudgment interest statute in context of judgment against former members of LLC for conversion, breach of fiduciary duty, and wrongful distribution).

Solar Cells, Inc. v. True North Partners, LLC, No. Civ.A. 19477, 2002 WL 749163 (Del. Ch. April 25, 2002).

A member of an LLC whose interest would decrease from 50% of the voting units to 5% of the voting units in a proposed merger of the LLC sought a preliminary injunction on the basis that the other member and managers appointed by it acted in bad faith in approving the proposed merger and that the defendants would be unable to prove the entire fairness of the merger. First Solar, LLC (the "LLC"), a Delaware LLC, was formed by True North Partners, LLC ("True North") and Solar Cells, Inc. ("Solar Cells") to commercialize solar power technology. Solar Cell contributed the technology, and True North contributed and loaned money to the LLC. Solar Cells and True North each received 50% of the voting membership units, and True North received 100% of the non-voting units. True North had the right to elect three of the five managers, and Solar Cells had the right to elect the other two. The LLC's initial

funding was depleted, and the members unsuccessfully negotiated various alternatives for financing and restructuring. Without notice to Solar Cells, the True North managers executed a written consent approving the proposed merger of the LLC into an LLC wholly owned by True North. Solar Cells received notice of the proposed merger four days before it was to close. Under the terms of the merger, the balance of True North's loan to the LLC would be converted into equity, and Solar Cells would end up with 5% of the voting units in the surviving LLC. The court found that there was a reasonable likelihood that Solar Cells would prevail on the merits, that is, that True North would be required to establish the entire fairness of the merger and would be unable to do so. True North argued that the actions taken to authorize the merger were clearly authorized by the operating agreement and that the operating agreement limited fiduciary duties owed by the True North managers. The court noted that the provisions of the operating agreement limited liability stemming from a conflict of interest but that the limitation on the managers' liability did not bear on the request for injunctive relief. Further, the provisions of the operating agreement protected the managers so long as they acted in good faith. With respect to fair dealing, the court was critical of the lack of an independent bargaining mechanism and failure to give Solar Cells advance notice. ("[I]t is not an unassailable defense to say that what was done was in technical compliance with the law. . . . The fact that the Operating Agreement permits action by written consent of a majority of the Managers and permits interested transactions free from personal liability does not give a fiduciary free reign to approve any transaction he sees fit regardless of the impact on those to whom he owes a fiduciary duty.") The court also found that the valuation used to establish the price was likely not fair because it was irreconcilable with valuations only a few months before True North decided to proceed with the merger. Finally, the court found that irreparable harm was threatened because of the dilution of the equity and voting position of Solar Cells, the difficulty in valuing the LLC, and the limitation of True North's liability for conflicts arising from its fiduciary obligations.

In re Bigmar, Inc., Section 225 Litigation, No. Civ.A. 19289-NC, 2002 WL 550469 (Del. Ch. April 5, 2002).

The Chancery Court addressed the fiduciary duties of members of a Michigan LLC in order to determine the validity of the actions of one of the members in voting the LLC's shares of stock in a Delaware corporation. Citing the Michigan LLC act, the court stated that members of the LLC owed the LLC and one another fiduciary duties. More specifically, the court referred to a duty of complete candor and an obligation to provide full and fair disclosure of all material facts relating to any matter involving the LLC. With respect to the delegation of authority to vote the shares of stock in issue, the court stated the member seeking to enforce her rights must show all material facts relating to its execution were disclosed. The court cited two Delaware cases involving corporations, *Malone v. Brincat* and *Rosenblatt v. Getty Oil Co.*, in support of the duty of full candor and disclosure. The court concluded that the member had obtained the delegation of authority to vote the shares by a breach of her fiduciary duty, if not outright fraud, and that the delegation was thus invalid.

RT Gilbane Corp. v. Neighborhood House, LLC, No. 00-1973, 2002 WL774992 (Mass. Super. Feb. 15, 2002)(granting summary judgment in favor of members of LLC who were not active in LLC's management on breach of fiduciary duty claim by non-member project manager who claimed that the LLC and project manager were "joint venturers" and sought to characterize the individual LLC members as partners/fiduciaries of the project manager)

Fine v. Bork, No. CV010808586, 2002 WL 207538 (Conn. Super. Jan. 16, 2002).

The court held that the obligations of LLC members and managers are clearly established by the Connecticut LLC act, citing a provision requiring a member or manager to discharge his duties in good faith, with the care of an ordinarily prudent person under similar circumstances, and in a manner he reasonably believes to be in the best interests of the LLC. The court also cited provisions requiring a member or manager to account for any benefit received without disinterested manager or member approval. The court concluded that the defendant breached his fiduciary duties when the defendant unilaterally amended the LLC operating agreement of Tower Business Center, LLC ("Center") to permit it to have only one member, and dissolved Associates, LLC ("Associates"), Center's 99% member. The defendant owned the other 1% of Center and was the majority member of Associates. The plaintiff was the minority member of Associates. At the time Center was formed, Connecticut law required an LLC to have two or more members, and the operating agreement required Center to have two members. The court stated that by dissolving Associates and empowering Center to have only one member, the defendant averted dissolution of Center by dissociation of Associates and became the sole member of Center, a single purpose LLC owning a parcel of commercial real estate. The court characterized the defendant's conduct as a "scheme to obtain sole ownership of the subject property to the exclusion of the plaintiff."

In re C.R. Amusements, LLC (Acropolis Enterprises, Inc. v. C.R. Amusements, LLC), 259 B.R. 523 (Bankr. D. R.I. 2001).

The minority interest holders of an LLC claimed that the 51% interest holder (“Moneta”) breached its fiduciary duty to the minority by scheming to financially cripple the LLC so that the LLC would default on its loan and its assets could be acquired and developed by Moneta. Although provisions of the operating agreement quoted in one footnote of the opinion indicate that it was a manager-managed LLC and that Moneta was the manager, the court couched the fiduciary duty of Moneta in terms of its majority ownership. The court referred to Moneta as the “Majority Shareholder” and the minority members as the “Minority Shareholders” and stated that Moneta, as a majority shareholder, owed a duty to the minority under Rhode Island law. The court quoted a Rhode Island Supreme Court opinion in which the court held that shareholders in a closely held (“less-than-thirty-shareholder”) corporation assume fiduciary duties to one another and the corporation when they act as partners, noting that this duty was imposed on the basis of the small number of shareholders, active participation of shareholders in management, close and intimate working relations, and the fact that the shareholders acted as if they were partners. When the court analyzed the evidence regarding the conduct of Moneta, however, it concluded that the minority owners had failed to prove their allegations that Moneta breached its fiduciary duty.

Harbor Hospital Services, Inc. v. GEM Laundry Services, L.L.C., Nos. 4830, 0207, 2001 WL 1808556 (Pa. Com. Pl. July 18, 2001).

The dispute in this case related to the affairs of a Pennsylvania LLC formed to provide laundry services to the hospital customers of one of the members of the LLC. The parties to the litigation included the LLC, its two members, and various individuals and entities affiliated with the members. The court interpreted various provisions of the Pennsylvania LLC law as authorizing the court to look to principles of partnership and/or corporate law in analyzing fiduciary duties of LLC members. The operating agreement of the LLC in issue provided for management of the LLC to be vested in the members. Therefore, the court concluded that it should treat the members like partners and that a member who failed to properly run the daily operations of the LLC may ultimately be liable for breach of fiduciary duty as a co-member of the LLC. In the course of its decision, the court quoted from commentary to the Pennsylvania LLC law stating that members who do not act as managers, like corporate shareholders or limited partners, would not have the fiduciary duty of managers. The quoted comment went on to note, however, that a non-managing member would have no right to appropriate LLC property for personal use, and that courts should fashion rules in appropriate circumstances by analogy to corporate or partnership law principles to deal with situations such as oppression of minority members, actions taken in bad faith, etc. With respect to standing, the court stated that if the complaining member’s claim against the other member were construed as a derivative claim, the court could treat it as direct since they were the only two members of the LLC. However, the court concluded that the complaining member’s principal was too far removed to bring a breach of fiduciary duty claim against the other member. The duty, if any, said the court, would be between the members of the LLC, not individual shareholders of the members. Similarly, the shareholders of the allegedly breaching member could not be held liable for breach of fiduciary duty.

In re McKnew (KMK Factoring, L.L.C. v. McKnew), 270 B.R. 593 (Bankr. E.D. Va. 2001).

The issue in this adversary proceeding was whether, for purposes of § 523(a)(4) of the Bankruptcy Code, the debtor was acting in a fiduciary capacity in his role as manager of a Virginia LLC. The court recognized that an LLC manager has a fiduciary duty to the LLC based upon statutory provisions obligating the manager to exercise good faith business judgment, but found that an LLC manager is not a fiduciary for purposes of § 523(a)(4). The court ultimately determined that the manager’s excess withdrawals from the LLC amounted to a non-dischargeable claim for embezzlement. The court concluded that this conduct was “willful misconduct” such that the Virginia \$100,000 liability cap was not applicable. The case is further discussed below under the heading “Bankruptcy.”

VGS, Inc. v. Castiel, No. CIV.A. 17995, 2001 WL 1154430 (Del. Ch. Sept. 25, 2001).

The court found that the breach of fiduciary duty by two managers to Castiel in pursuing a merger eliminating Castiel’s control without prior notice to Castiel (the subject of a prior opinion summarized below) was not so egregious as to justify awarding Castiel attorney’s fees. The court noted that the process followed by the two managers (which was held to be a breach of the managers’ duty of loyalty in the prior opinion) complied with the LLC’s operating agreement and the Delaware LLC act. Further, the court noted that the prior opinion did not reflect any conclusion that the two managers were not motivated by an honestly held view that Castiel’s continued control threatened the interests of the LLC. (The court went on to find that the repeated failure of one of the managers to appear for deposition justified a partial award of expenses and attorney’s fees.)

Coady v. Martin, 784 A.2d 897 (Conn. App. 2001).

The court in this case held that there were no fiduciary duties owed by one member of an LLC to the other member, and the court of appeals upheld this conclusion because the LLC agreement on which the plaintiff based the breach of fiduciary duty argument was found to be unenforceable due to lack of an essential term. On appeal, the court noted that the plaintiff had relied solely on the terms of the written agreement in asserting his breach of fiduciary duty claims. Although the plaintiff attempted to raise a joint venture theory on appeal to argue that fiduciary duties were owed independently of the written agreement, the court restricted its review to the theory relied upon by the plaintiff at trial. The court of appeals found no error in the trial court's conclusion that the membership agreement was unenforceable for lack of an essential term.

Robinson v. Geo Licensing Company, LLC, 173 F. Supp.2d 419 (D. Md. 2001).

In this case involving a Delaware LLC, breach of fiduciary duty was not an issue, but the court made the passing comment that the majority interest holder of an LLC owes a fiduciary duty to the LLC's minority interest holder. The court cited *Froelich v. Erickson* (a case summarized below) In *Froelich v. Erickson*, the governing documents of the LLC used corporate terms and expressly incorporated Maryland law regarding corporate fiduciary duties.

Flippo v. CSC Associates III, L.L.C., 547 S.E.2d 216 (Va. 2001).

The Virginia Supreme Court affirmed a trial court judgment holding the manager of Flippo Land & Timber Co., LLC, a family-owned LLC (Flippo LLC) liable for breach of fiduciary duty to the LLC and barring the manager and his brother from serving as managers. Flippo LLC held timberlands and had three members: Carter Flippo, who was also manager, Carter's brother Arthur Flippo, and CSC Associates III, L.L.C. ("CSC"), an LLC owned by the three children of Carter's and Arthur's sister. In response to the refusal of CSC to allow Carter and Arthur to transfer their interests in Flippo LLC to individual LLCs for estate planning purposes, Carter consulted a law firm and chose a course of action suggested by the law firm that would allow Carter and Arthur to satisfy their estate planning goals by holding their interests in the timberland business in LLCs. Pursuant to the advice received by Carter from his lawyers, Carter, as manager of Flippo LLC, caused the LLC to transfer all of its non-cash assets to a new LLC. The transfer of Flippo LLC's assets dissolved Flippo LLC under the operating agreement, and CSC was given the option of joining the new LLC if it agreed to the terms of its operating agreement, under which Carter and Arthur could hold their interests through LLCs. (Prior to trial, the new LLC dissolved and returned the assets to Flippo LLC, rendering claims against the new LLC moot.) Carter was found liable for breach of fiduciary duty based upon his orchestration of the transfer of Flippo LLC's assets to the new LLC. He appealed, arguing that he was entitled to a defense based upon his reliance on the law firm's advice. His defense was based upon a provision of the Virginia LLC act protecting a manager who acts in good faith reliance on legal counsel or other professionals. The court found that this provision was not applicable in the instant case. The court pointed out that a manager, like a corporate director, is required by statute to discharge his duties in accordance with his good faith business judgment in the best interests of the LLC. Additionally, the LLC and corporate statutes contain nearly identical provisions protecting managers and corporate directors from liability in the exercise of that judgment under certain circumstances. The court found, however, that Carter was receiving advice in his personal capacity for his own personal interests when he consulted with the law firm, and he was therefore not protected by these provisions. Further, the court rejected the argument that reliance on advice of counsel was a defense to punitive damages, and the award of punitive damages was upheld. The court also upheld the removal of Carter as manager and the prohibition of his brother Arthur's serving as manager on the basis that this point was not properly preserved for appeal. The court finally rejected the claims of Carter and Arthur for dissolution of Flippo LLC and for rescission of the operating agreement based on fraud and mutual mistake, and the court upheld sanctions against Carter and Arthur based upon their allegations of mutual mistake and fraud.

International Paper Company v. Androscoggin Energy LLC, No. 00C 6215, 2001 WL 503058 (N.D. Ill. May 10, 2001).

The plaintiff, the parent company of a member of an LLC with two other entity members, sued the LLC and its other two members for breach of contract and negligent misrepresentation based upon certain representations and warranties in the LLC operating agreement and an energy services agreement between the LLC and the plaintiff. The court had occasion to briefly address fiduciary duties between the plaintiff and the two defendant members of the LLC in connection with the negligent misrepresentation claim. The plaintiff's allegations relating to fiduciary duties were vague, but the court made the point that fiduciary duties generally are owed by LLC members to one another. The plaintiff had not relied upon this principle, but the court noted that this principle alone would not have been enough because the plaintiff was not itself a member of the LLC. It was not at all apparent to the court that fiduciary duties

would flow from the defendant members of the LLC to the parent of the other member, and the plaintiff failed to pursue the argument.

In re Larry's Apartment, L.L.C. (Galam v. Carmel), 249 F.3d 832 (9th Cir. 2001).

An LLC member was found liable for breach of fiduciary duty to the LLC for his actions in purchasing a parking lot adjacent to the LLC's business and refusing to allow the LLC to continue its use of the lot. The court imposed a constructive trust on the lot for the benefit of the LLC without compensation to the member because the member had improperly caused the LLC to pay personal expenses exceeding the amount he paid for the land. The issue was whether an award of attorney's fees, based upon an Arizona statute providing for recovery of attorney's fees in an action arising out of a contract, was proper. The court concluded that this action did not arise out of a contract. The only contract the court identified as being related to the action was the peripheral contract the LLC member entered into with the seller of the land. The relationship of that contract to the action was insufficient to support the fee award.

In re Lake Country Investments, L.L.C. (Agincourt, L.L.C. v. Stewart), Nos. 99-20287, 00-6064, 2001 WL 267475 (Bankr. D. Idaho March 19, 2001).

The court rejected the argument that a 50% member of an LLC breached its fiduciary duties by purchasing a note and secured position on real estate of the LLC rather than making an additional capital contribution to the LLC so the LLC could discharge the obligation. The Chapter 11 debtor in this case was Lake Country Investments, LLC ("Lake Country, LLC"). Agincourt, LLC was one of two 50% members of Lake Country, LLC. The managing and majority member of Agincourt, LLC was West Wood Investments, Inc. ("West Wood"). Noyes, a creditor of Lake Country, LLC, argued that West Wood and Agincourt, LLC were alter egos so that the conduct of West Wood was attributable to Agincourt, LLC. Noyes claimed that West Wood's secured claim against Lake Country, LLC should be equitably subordinated because the failure of Agincourt, LLC to advance funds to Lake Country, LLC and the purchase of the note and secured position by West Wood breached the fiduciary duties of West Wood/Agincourt, LLC. The court stated there were genuine issues of material fact on the alter ego contention, but the breach of fiduciary duty allegation was rejected as a matter of law, thus the court granted summary judgment dismissing the equitable subordination claim. The court noted that, under the operating agreement, neither member was obligated to contribute additional capital or make loans to the LLC. The court said that Noyes did not show how a member of an LLC breaches a fiduciary duty by acting (or not acting) in a manner specifically permitted by the operating agreement. Further, the court rejected the argument that statutory law created a fiduciary duty between the members. Noyes relied upon the provision of the Idaho LLC act requiring a member to account to an LLC for any benefit received without consent of a majority of disinterested members or managers. The court stated that an LLC is distinct from a corporation or partnership and viewed the case law applicable to partnerships as having "limited utility." Further, the court noted that the Idaho LLC act recognizes the primacy of the structural and organizational documents and concluded that nothing in the statutory provision relied upon by Noyes required that the court ignore the limits the parties themselves structured in the operating agreement. In a footnote, the court indicated that it considered significant the fact that the dispute involved "a close quarters fight among those who were most intimately involved with the LLC" rather than the interests of the LLC or its unsecured creditors. The court noted that the parties were all sophisticated and assisted by expert counsel and that the causes of action sought to recharacterize or alter the effect of prior transactions.

Cimarron Feeders v. Bolle, 17 P.3d 957 (Kan. App. 2001).

A trial court used the language of Section 404 of the Kansas Revised Uniform Partnership Act to define for the jury the fiduciary duties of LLC members. The court of appeals concluded that the trial court's use of language from the partnership statute was not error. The court stated that the trial court did not apply the partnership act but merely utilized the language for guidance on the breach of fiduciary duty issue.

Carson v. Lynch Multimedia Corporation, 123 F. Supp.2d 1254 (D. Kan. 2000).

The Robert C. Carson Revocable Trust (the "Carson Trust") owned a 20% interest in an LLC, and Robert C. Carson was the president and general manager of the LLC. The LLC was retained under a management agreement to manage Carson Communications. After a dispute over whether Carson took a business opportunity without first offering it to the LLC, the LLC's board of managers voted to terminate Robert Carson as president and general manager. The new president and general manager then terminated the management agreement between the LLC and Carson Communications. Carson and the Carson Trust sued the majority member, the three individual managers appointed by the majority member, and an individual who allegedly influenced and controlled the managers for breach of fiduciary duty in terminating Carson and the management agreement. The defendants moved to dismiss on the basis that the plaintiffs failed to state a claim. The court refused to dismiss the breach of fiduciary duty claim against Gabelli, the

individual who allegedly influenced and controlled a majority of the managers, concluding that the allegations of influence and control over a majority of the LLC managers was sufficient to permit the plaintiffs to go forward in their attempt to prove an implied or imputed fiduciary duty. The court also rejected the defendants' argument that the business judgment rule required dismissal. The court stated that the business judgment rule presupposes that directors act on an informed basis and in the honest belief that their actions are in the best interest of the company, and the court pointed out that the complaint alleged that the actions were taken for reasons wholly unrelated to the business of the LLC. The court also rejected the defendant's argument that the LLC act protected the defendants from liability for breach of fiduciary duty or minority oppression because of the provision that no member or manager is liable for the debts and obligations of the LLC. Contrary to the defendants' assertion that the operating agreement must provide for any remedy for breach of fiduciary duty, the court stated that the act recognizes that a manager or member may owe fiduciary duties and allows the operating agreement to expand or restrict those duties. The court distinguished liability for the debts and obligations of the LLC from liability for breach of fiduciary duty.

VGS, Inc. v. Castiel, No. C.A. 17995, 2000 WL 1277372 (Del. Ch. Aug. 31, 2000) aff'd, 781 A.2d 696 (Del. 2001).

An LLC with three entities as members and three individuals as managers entered a merger approved by two of the three managers pursuant to the operating agreement. In the merger, two members with a combined 75% in the LLC were relegated to a 37.5% minority interest in the surviving corporation, and Castiel, the individual who controlled the two members with the 75% interest, was excluded from management. Castiel appointed two of the three managers of the LLC (these managers consisted of Castiel and another appointee), but the third manager (the owner of the 25% member) convinced Castiel's appointee to join him in a written consent to merge the LLC without notice to Castiel. The court determined that the LLC agreement permitted a merger to be approved by a vote of a majority of the managers and that Section 18-404(d) of the Delaware LLC act literally permits written majority consents without notice to other managers, but the court concluded that the two managers breached their duty of loyalty to Castiel by failing to give him notice. The following comment by the court regarding the application of Section 18-404(d) is representative of the court's tone throughout the opinion: "The General Assembly never intended, I am quite confident, to enable two managers to deprive, clandestinely and surreptitiously, a third manager representing the majority interest in the LLC of an opportunity to protect that interest by taking an action that the third manager's member would surely have opposed if he had knowledge of it. My reading of Section 18-404(d) is grounded in a classic maxim of equity -- 'Equity looks to the intent rather than to the form.'" The court stated that the two managers who took the action to merge owed a duty of loyalty to the LLC, its investors and Castiel, their fellow manager. The court observed that the LLC agreement allowed the action to merge to be taken by a simple majority of managers (rather than following the default member approval requirement) because all parties understood that Castiel had the right to appoint and remove a majority of the managers. Had notice been given, Castiel of course would have attempted to remove his appointee and block the action. The court rejected the argument that the managers were protected by the business judgment rule. The court said the managers owed Castiel a duty to give him prior notice even if he would have interfered with a plan that they conscientiously believed to be in the best interest of the LLC. If Castiel was not suited to run the company, as claimed by the other two managers, this was an issue to be determined in board meetings with all managers present or in future litigation, if necessary.

Walker v. Resource Development Company Limited, L.L.C., 791 A.2d 799 (Del. Ch. 2000).

Walker, a first cousin of former President Bush, was brought in as a member of a Delaware LLC in order to utilize his connections and reputation to help the LLC secure needed financing. After Walker failed to secure financing and the other members became concerned about Walker's drinking problem, financial irresponsibility, and other matters, he was relieved of his official duties for a period of time. He was later given his job back, and the members entered into a formal operating agreement designating Walker as an 18% member. Ultimately, however, the relationship soured completely, and the other members purported to remove him as a member and terminate his ownership interest. The members referred to Walker's poor performance and misconduct in the written notice of his removal, but there was also a dispute over whether Walker had a side deal that constituted a conflict of interest. The court concluded that the other members had no authority to remove Walker as a member either under the Delaware LLC act or the operating agreement. The court rejected the argument that the members had the inherent power to remove Walker and deprive him of his ownership interest based upon his alleged breach of fiduciary duty. Although the court recognized that there was a relationship of sufficient trust and confidence to impose on Walker a duty to disclose a material fact such as a conflict of interest, the court concluded that the members did not rely on any understanding that Walker was independent in entering into the operating agreement. Thus, the court rejected the members' misrepresentation claim against Walker. The court also rejected the members' claim that they were protected from liability for their effort to appropriate Walker's

interest based upon a good faith reliance on the operating agreement. After purporting to remove Walker, a series of financing transactions led to the exchange of the members' membership interests in the LLC into shares of a Canadian corporation. Walker failed to prove the value of his 18% interest in the LLC, thus there was no basis for an award of damages; however, the court imposed a constructive trust in Walker's favor upon 18% of the shares the other members had received in the Canadian corporation.

In re Garrison-Ashburn, L.C., 253 B.R. 700 (Bankr. E.D. Va. 2000).

In the course of discussing whether the operating agreement of an LLC was an executory contract for purposes of the Bankruptcy Code provisions preventing enforcement of certain ipso facto clauses, the court made some observations about fiduciary duties. The court described the provisions of the operating agreement regarding management and noted that a member was not obligated to participate in management or provide any personal expertise or service to the LLC, and a member was permitted to resign from all offices and committee positions without breaching the operating agreement. In such a case, the court said, the member would be analogous to a shareholder in a corporation. In a footnote, the court stated that, unlike partnerships, there are no fiduciary obligations among members of an LLC. The court noted that the Virginia LLC act imposes a duty of good faith business judgment on managers but is silent as to members. (In fact, the Virginia LLC act imposes this duty on any member who is participating in management.) The court went on to cite the provision of the Virginia LLC act permitting a member to transact business with the LLC on the same basis as a non-member. The court found the absence of statutory provisions imposing fiduciary obligations on one member to another or the LLC significant, noting that LLCs are statutory creations, not common law creations like partnerships, and pointing to the express provisions on fiduciary duties in the Virginia partnership statutes.

Suntech Processing Systems, L.L.C. v. Sun Communications, Inc., No. 05-99-00213-CV, 2000 WL 1780236 (Tex.App. Dec. 5, 2000).

The minority member of a Texas LLC claimed that the majority member owed it a fiduciary duty as a matter of law. The case does not state whether the LLC was member-managed or manager-managed, but the articles of organization provided as follows: "Members of this Company have a duty of undivided loyalty to this Company in all matters affecting this Company's interest." The Texas LLC act provides: "To the extent that at law or in equity, a member, manager, officer, or other person has duties (including fiduciary duties) and liabilities relating thereto to a limited liability company or to another member or manager, such duties and liabilities may be expanded or restricted by provisions in the regulations." The court noted the absence of Texas case law on fiduciary duties of LLC members and looked to case law regarding fiduciary duties of shareholders of a closely held corporation. In prior cases, the court had held that co-shareholders of closely held corporations are not necessarily in a fiduciary relationship. Rather, the existence of a fiduciary relationship is a question of fact. The court applied the same reasoning and stated that its conclusion was not affected by the fact that the defendant was the majority member. The court pointed out the provision in the LLC's articles of organization provided for a duty of loyalty to the LLC rather than between the members. The court said that neither the statute nor the provision in the articles authorized the court to find that there was a fiduciary relationship between the members as a matter of law, and the issue was remanded for determination by the factfinder.

Lynch Multimedia Corp. v. Carson Communications, L.L.C., 102 F. Supp.2d 1261 (D. Kan. 2000).

One of the members of a Kansas LLC sued another member and the member's owners and agent for breach of the operating agreement and breach of fiduciary duty when they acquired other cable franchises rather than securing them for the LLC. The LLC operated a television cable system, and the operating agreement specified that if an opportunity to purchase certain cable television systems came to the attention of a member, the opportunity must first be offered to the LLC. Another provision in the operating agreement stated that any member or manager was permitted to engage in other business ventures, and the LLC would have no rights in such regard. Robert Carson was trustee of the Robert Carson Trust, a 20% member of the LLC, as well as president and a manager of the LLC. In 1997, Carson informed representatives of Lynch Multimedia Corporation (Lynch), a 60% owner of the LLC, of the potential availability of certain cable systems. Lynch was receptive to exploring the opportunities. Over the next year, discussions and negotiations continued. At one point, a Lynch representative rejected the acquisition of the cable systems, but a couple of proposals were made a few months later in the fall of 1998. In the spring of 1999, Carson acquired the cable systems through his own entity. Lynch sued for breach of the operating agreement and breach of fiduciary duty. The court held that the operating agreement's requirement that certain opportunities be "offered" to the LLC contemplated only that the LLC be made aware of such opportunities, not that a formal offer be presented. The court concluded that Carson satisfied this requirement by making Lynch aware of the opportunities. The court rejected Lynch's claims that a formal meeting was required, noting that the LLC at all times operated on an informal basis with Lynch's acquiescence. The

court also stated that the operating agreement's requirement that certain opportunities be offered to the LLC must be read in conjunction with the provision permitting members to engage in other ventures; therefore, it plainly was directed at permitting members to enter separate and additional business relations in the cable TV industry. The court thus granted summary judgment in favor of the defendants on both the breach of operating agreement and breach of fiduciary duty claims. The court said that Lynch had not articulated how the breach of fiduciary duty claims were distinguishable from the breach of operating agreement claims. The court cited the provision of the Kansas LLC act that permits members of an LLC to expand or restrict their duties and liabilities by agreement. Lynch argued this provision did not apply because it was passed after the LLC in this case was formed, but the court held otherwise, citing the legislature's intent that from January 1, 2000, the act shall apply to all LLCs formed in Kansas, whether formed before or after that date.

Froelich v. Erickson, 96 F. Supp.2d 507 (D. Md. 2000), aff'd, 5 Fed.Appx. 287 (4th Cir. 2001).

The factual background of this case is rather complicated, but the claims involved assertions of fraud, breach of fiduciary duty, and breach of contract by Froelich, an ousted CEO and board member of a Maryland LLC. Froelich was also a member of the LLC who, along with other minority members, was cashed out in a squeeze-out merger following a reclassification of interests of the LLC approved by all members except Froelich. Two documents primarily governed the LLC's operations as an LLC. These documents were an Operating Agreement, which the court characterized as the LLC equivalent of a corporate charter, and a Members Agreement, which the court described as the equivalent of a stockholders' agreement. The operating agreement defined classes of preferred and common interests, the role and responsibility of the board, and the rights and duties of the members. The member agreement supplemented the operating agreement by specifically defining rights of members and restrictions on alienation of interests. The court summed up Froelich's claims as a challenge to "a handful of corporate actions taken by [the LLC's] Board and its Members." The court summed up the key issues in the case as follows: "(i) Did the corporate documents or Maryland corporate law authorize the Board to take the actions that Froelich challenges? (ii) If the Board or the Members had the power to act, by what standard (e.g., business judgment rule or fiduciary duty) should the Court review the Board's exercise of that power? and (iii) Did the Board meet the appropriate standard?" The court characterized the case as arising in the context of corporate decisions by the LLC's board of directors and applied the business judgment rule. The court noted that the LLC's operating agreement stated that the LLC's directors "are subject to the duties of a corporate fiduciary as defined by Maryland law;" thus, the court continued, the LLC board's decisions are measured against the business judgment rule "just as if [the LLC] were a traditional corporation, rather than an LLC." The court found no evidence that the board had acted in bad faith and concluded that the board's actions were protected by the business judgment rule. The court also concluded as follows: the LLC and majority member did not breach a duty of good faith and fair dealing (noting uncertainty under Maryland law as to whether there is a separate cause of action in this regard and stating that the duty in any event only prohibits a party from preventing the other party from performing under the contract); the majority member did not breach a fiduciary duty to Froelich by usurping a business opportunity (stating that a majority interest holder clearly owes the minority a fiduciary duty but finding no breach in view of the board's independent approval of the transaction); the reclassification did not breach the operating agreement or the member agreement (finding that the transaction fell outside a provision in the member agreement restricting redemptions and was governed by the operating agreement, which was amended in accordance with its terms to permit the reclassification). In Froelich's favor, the court found that the LLC owed Froelich severance pay under an employment agreement between the LLC and Froelich and that the reclassification and squeeze-out were related parts of a transaction in which Froelich had properly preserved his statutory right to an appraisal. The court explained that the Maryland LLC statute grants a member the same appraisal rights as an objecting stockholder under corporate law. Maryland corporate law provides appraisal rights in connection with a parent-subsidary merger, and Froelich properly objected to the squeeze-out merger. The court viewed the reclassification and subsequent squeeze-out merger as a single transaction rather than separate events such that Froelich was entitled to appraisal of his interests immediately prior to the reclassification rather than appraisal of his reclassified interests immediately prior to the merger that occurred five months later.

McConnell v. Hunt Sports Enterprises, 725 N.E.2d 1193 (Ohio App. 1999).

This was the first case to address the fiduciary duties of members of an LLC to any significant degree. In this case, the court stated that members of an LLC are in a fiduciary relationship that would generally prohibit competition with the business of the LLC. (The court did not directly address the management structure, but it appears that the LLC was member-managed. The opinion notes at one point that the operating agreement did not name any person or entity the operating or managing member of the LLC.) The court concluded, however, that members may contractually limit or define the scope of the fiduciary duties. Specifically, the court recognized the validity of a provision in the operating agreement of an Ohio LLC that permitted members to compete with the LLC. When some of the members of an LLC

formed to obtain a hockey franchise objected to the terms of a lease that was necessary to obtain the franchise, other members formed a separate group that agreed to the lease and obtained the franchise. The court found the operating agreement clearly and unambiguously permitted members to compete against the LLC and thus obtaining the franchise did not breach a fiduciary duty. The court indicated that “the method of competing” might constitute a breach of fiduciary duty if it amounted to “dirty pool” but found no willful misconduct, misrepresentation, or concealment by the members who formed the other group. Further, the court found that the non-competing member breached the operating agreement by unilaterally undertaking litigation on behalf of the LLC without the requisite approval of the members. The member argued his actions did not constitute willful misconduct and that his actions were protected under the exculpation and indemnity provisions of the operating agreement. The court, however, found that the exculpation and indemnity provisions applied in the context of members’ carrying out their duties under the operating agreement and that there was no duty to unilaterally bring the litigation. The court concluded that the member engaged in willful misconduct in filing the suit without asking even one other member for permission when the agreement required a majority vote. The member argued that the litigation was undertaken upon advice of counsel and therefore in good faith. The court stated that the evidence did not show that the member relied upon advice that the member was acting within the scope of authority conferred by the agreement. The evidence showed only that the member caused the suit to be filed and that the member’s general counsel had responsibility for the litigation.

V. Inspection Rights and Access to Information

Somerville S Trust v. USV Partners, LLC, No. Civ.A. 19446-NC, 2002 WL1832830 (Del. Ch. Aug. 2, 2002)(concluding that member’s stated purposes (to investigate allegations of wrongdoing and mismanagement of the LLC and to value its membership interest) were proper purposes for books and records inspection, that plaintiff proffered credible evidence of mismanagement that would adversely affect the member’s interest, and that various specified documents and records were subject to inspection).

Arbor Place, L.P. v. Encore Opportunity Fund, L.L.C., No. Civ.A. 18928, 2002 WL 205681 (Del. Ch. Jan. 29, 2002).

A member of two Delaware LLCs sought to inspect the books and records of the LLCs, and the managing member of the LLC argued it need only produce the LLC’s general ledger accounts transactions histories, continuity schedules, annual reports, bank account ledger cards, and trial balances. The court interpreted the Delaware LLC act and LLC agreements (which gave access to “all books and records” of the LLCs) and concluded that the member also had the right to inspect the tax returns and member lists of the LLC. The court rejected the argument that disclosure of the member lists would violate the privacy provisions of the Gramm-Leach-Bliley Act because there is an exception to the prohibition on disclosure where disclosure is necessary to comply with other laws and legal requirements, and the court found disclosure was required to comply with Delaware law and other legal requirements. The LLC members also sought access to records of two Cayman Island corporations that were investment funds in which the LLCs invested member funds, but the court rejected this request on the basis that the members were not shareholders in the corporations and there was no basis to disregard the separate existence of the entities.

Degennaro v. Midtown Bridge, LLC, No. A-6209-99T2 (N.J. App. Oct. 26, 2001).

A member of a New Jersey LLC sought to inspect the LLC’s financial records. The LLC’s operating agreement contained provisions requiring the LLC to maintain books and records and permitting members to visit the properties of the LLC and discuss the business and affairs of the LLC with the managers. The operating agreement also required the managers to prepare and provide to LLC members certain financial reports. The operating agreement did not recite that the members had any right to inspect the LLC’s financial records. The court found that furnishing the reports was all that was required (and thus the member did not have the right to inspect the LLC’s financial records) since the New Jersey LLC act states that a member may obtain “true and full information regarding the status of the business and financial condition” of the LLC “subject to such reasonable standards ... as may be set forth in an operating agreement.”

W. Interpretation of Operating Agreement, Articles of Organization

Radding v. Freedom Choice Mortgage, LLC, 820 A.2d 317 (Conn.App. 2003).

An LLC established a production bonus and profit-sharing program for certain of its employees including the plaintiff. The plaintiff executed certain documents in connection with the program and was provided copies of the LLC operating agreement and an amendment to the operating agreement listing the plaintiff and five other new members. The operating agreement stated that no member would be entitled to receive income from the production bonus or profit-

sharing programs until the member had been a member for one full calendar year. The amendment to the operating agreement listing the plaintiff as a member was dated December 12, 1995, and the plaintiff signed other related documents in late December, 1995. On December 13, 1996, the plaintiff and the LLC's principal owner had an argument that resulted in plaintiff's termination of employment. The plaintiff's right to remuneration under the bonus and profit-sharing program hinged on the effective date of the plaintiff's admission as a member. The court analyzed the statutory provisions regarding admission of LLC members, the terms of the operating agreement, and the documents signed by the plaintiff and rejected the argument that the plaintiff's admission was not effective until the plaintiff signed the documents related to his admission. The court held that the plaintiff became a member as of the date of the amendment to the operating agreement reflecting plaintiff's admission as a member. The court also concluded that the plaintiff did not cease to be a member when his employment was terminated. The court examined the operating agreement and the statutory provisions regarding cessation of membership and concluded that the majority member's removal of the plaintiff's name from the operating agreement schedule of members did not constitute a vote by the majority member because it was not done in accordance with the voting procedures set forth in the operating agreement.

KSI Rockville, LLC v. Eichengrun, __ N.Y.S.2d __, 2003 WL 21223849 (N.Y.A.D. 2 Dept. 2003).

In an action for an accounting and dissolution of an LLC, the court determined that the managing member, who contributed only services rather than cash to the LLC, had no proprietary or financial interest in the LLC because the operating agreement required the members' initial contributions to be made in the form of cash. The court construed ambiguities in the agreement regarding contributions against the managing member because he drafted the agreement. The managing member argued that he was to be compensated for his services and that such amount would be credited to his initial capital contribution; however, the operating agreement stated that the managing member was to be compensated in an amount to be determined from time to time by the members, and the record contained no evidence that the members consented to compensation at any time or in any amount.

Pinnacle Data Services, Inc. v. Gillen, 104 S.W.3d 188 (Tex.App. 2003).

The articles of organization of a Texas LLC provided that the articles of organization (which provided for member-management) could be amended by the vote of two-thirds of the members while the regulations (operating agreement) provided that amendment of the articles of organization required the vote of 66 2/3% in interest. Two of the three members (constituting 50% in interest) voted to amend the articles of organization to change the LLC to a manager-managed LLC. The court held that the provision in the articles of organization controlled because the Texas LLC act provides that the regulations may contain any provisions for the regulation or management of the LLC not inconsistent with law or the articles of organization.

Fillmore LLC v. Fillmore Machine & Tool Co., 783 N.E.2d 1169 (Ind.App. 2003) (concluding that there was no agreement that member transfer equipment and other assets to LLC, even though accountant prepared tax returns reflecting such transfer, where terms of written agreements, including operating agreement, made no mention of such transfer and reflected contributions of members consisting only of cash and accounts receivable).

Cunningham Group Development Services, L.L.C. v. Richardson, No. Civ. 03-2233 MJD/JGL, 2003 WL 1572010 (D.Minn. March 19, 2003) (concluding that plaintiffs had shown reasonable probability that they would prevail on merits of claims involving struggle for control of LLC and buy-out of interests of defaulting members under terms of operating agreement, but that plaintiffs had not shown imminent and irreparable harm so as to satisfy standard for injunctive relief).

Apple Glen Crossing, LLC v. Trademark Retail, Inc., 784 N.E.2d 484 (Ind. 2003) (holding that "change orders" approved by LLC manager did not constitute "Major Decisions" requiring unanimous consent of members under LLC operating agreement).

Connecticut Car Rental, Inc. v. Prime One Capital Co., LLC, 247 F.Supp.2d 158 (D.Conn. 2003) (holding that member had actual authority to assign car lease agreements pursuant to the LLC formation agreement because the assignments did not fall within types of decisions requiring governing board approval).

Jundt v. Jurassic Resources Development, North America, L.L.C., 656 N.W.2d 15 (N.D. 2003) (concluding that trial court erred in interpreting member control agreement when it found that member who invested no money in LLC was not entitled to any tax write-offs and that money investors were entitled to all the tax write-offs).

Seed v. Astra Genstar Partnership, No. C2-02-1143, 2003 WL 178790 (Minn.App. Jan. 28, 2003) (holding that change in ownership of 100% of membership interests in LLC which was member of second LLC was not “change in direct ownership of 50% or more of the voting and equity interests” of second LLC so as to trigger option under change in control clause of agreement because the owner of the membership interest in the second LLC did not change).

Dover Place, LLC v. Coffey, No. A098399, 2003 WL 178832 (Cal.App. Jan. 28, 2003) (concluding that member was not required to return distribution because it did not violate statutory restrictions and operating agreement could not reasonably be interpreted to impose greater restrictions than statute).

Chase Manhattan Bank v. Iridium Africa Corp., 239 F.Supp.2d 402 (D. Del. 2002) (holding that lender could not sue members of an LLC on the basis that there were implied-in-fact contracts between the members and the LLC to make additional capital contributions upon lender’s demand when there was an express contract in the LLC agreement between the LLC and the members allegedly imposing the same obligation on the members).

Imprimis Investors, LLC v. Insight Venture Management, Inc., 752 N.Y.S.2d 26 (N.Y.A.D. 1 Dept. 2002) (concluding that denial of summary judgment was proper because there were fact issues as to whether member’s right to profits under LLC agreement was dependent upon compliance by related entity (which was alleged to be alter ego of member) with consulting agreement).

Hopson v. Bank of North Georgia, 574 S.E.2d 411 (Ga.App. 2002).

A member of a Georgia LLC pledged all of his interest as an LLC member to secure a bank loan. When the bank attempted to foreclose its security interest, the member argued that the operating agreement required consent of the other members for transfer of an interest in the LLC and that the bank had no security interest because of the bank’s failure to obtain consent of the other members. The operating agreement was quoted by the court as follows:

11.01 *General*. Except as otherwise provided herein, neither a Member nor an Economic Interest Owner shall have a right to:

(a) sell, assign, pledge, hypothecate, transfer, exchange or otherwise transfer for consideration, (collectively, “Sale”) ...

11.02 *Transferee Not Member in Absence of Unanimous Consent*.

(a) Notwithstanding anything contained herein to the contrary, if all of the remaining Members do not approve by unanimous written consent the proposed Sale or Gift of the Transferring Member’s Membership Interest or Economic Interest to a transferee or donee which is not a Member immediately prior to the Sale or Gift, then the proposed transferee or donee shall no right to participate in the management of the business and affairs of the Company or to become a Member. The transferee or donee shall be merely an Economic Interest Owner. No transfer of a Member’s interest in the Company (including any transfer of an Economic Interest or any other transfer which has not been approved by unanimous written consent of the Members) shall be effective unless and until written notice ... has been provided to the Company and the non-transferring Member.

The court concluded that the operating agreement permitted the transfer of the economic interest and that the bank obtained a security interest in the member’s economic interest which it was entitled to foreclose.

TIC Holdings, LLC v. HR Software Acquisitions Group, Inc., 750 N.Y.S.2d 425 (N.Y. Sup. 2002), aff’d, 2003 WL 116115 (N.Y.A.D. 1 Dept. Jan. 14, 2003).

The manager of a New York LLC executed an agreement obligating the LLC to transfer the LLC’s assets to a new company being formed by one of the LLC’s members. The manager took the position that he was authorized to execute the agreement based on the authority conferred in the operating agreement and the fact that he had e-mailed the members of the LLC that he would execute such an agreement if the members did not object in writing by a specified date. (The e-mail was sent on December 22, 2000, the Friday before a Christmas holiday weekend, and the deadline for objecting was December 28, 2000. The 87% member had advised the manager that he would be away on a family vacation and could not be reached between December 20th and 30th.) The court rejected the argument that the broad authority conferred in the operating agreement authorized the manager to transfer the assets because the manager’s authority under the operating agreement was “subject in all cases to ... the requirements of applicable law.” The New York LLC act requires a majority in interest of the members to approve a transfer of all or substantially all of an LLC’s assets unless otherwise provided in the operating agreement. The only specific authority to transfer assets under the operating agreement was to dispose of assets in the ordinary course of business, and the transfer agreement in question was not in the ordinary course. The court rejected the argument that the manager was authorized to act by virtue of the failure of the members to object to the transfer. The court said the members’ failure to object did not satisfy the

provision of the operating agreement that approval for any matter coming before the members required the “affirmative vote” of a majority in interest of the members. Finally, the court rejected the argument of the manager and the member who sought to acquire the LLC assets through a new company that the operating agreement released them from any liability related to their action as a matter of law. The member relied upon a release relating to actions involving conflict of interests and breach of fiduciary duty. The court found, however, that the language indicated the scope of the release was confined to matters related to actions taken in connection with the member’s dual involvement in the LLC and a specified company in which the LLC invested. Further, the court found the release would be ineffective if it was intended to release the member from all actions taken in his self-interest. For example, the court said, a release cannot reach willful and intentional misconduct. With respect to the manager’s release claim, the court found that the manager’s alleged misconduct fell outside the scope of the operating agreement’s release of the manager because it involved conduct not properly within the capacity of manager (e.g., his attempt to bind the LLC to transfer its assets without authority). Further, the New York LLC act provides that an operating agreement may not eliminate or limit liability if a judgment establishes bad faith, intentional misconduct, or a knowing violation of law, which the allegations indicated. The manager’s summary judgment claim for indemnification was rejected for similar reasons. The member’s claim for indemnification was rejected because he cited no provision of the operating agreement providing for indemnification.

Zanker Group, LLC v. Summerville at South Windsor, No. CV00044637S, 2002 WL 31303566 (Conn.Super. Sept. 19, 2002).

Zanker sought to enforce rights under the operating agreements of two LLCs formed to develop and operate managed care facilities. The court first found that LLC common units issued to Zanker subject to forfeiture in the event additional projects were not identified by Zanker became fully vested because Zanker identified such projects or was excused from doing so by the other member’s repudiation of its agreement with Zanker. The court next determined that Zanker was entitled to a placement distribution based on the number of its vested common units. The operating agreement provided for the distribution “through an appropriate withdrawal from the funds of the Facility,” and the facilities had operated at a loss. The court stated that Zanker was not entitled to payment if there were no available funds but would be entitled to a distribution based on its vested units when funds were available. Finally, the court interpreted a provision of the operating and development agreements that entitled Zanker to a distribution of 1% of the gross revenues in return for the provision of consulting services. The other member argued that a sentence describing consulting services as “professional consultation, marketing, and other clinical and administrative services, *as requested* by [the other member]” limited payment to requested services. The court disagreed and found that the fee was owed whether services were requested or not.

Valinote v. Ballis, 295 F.3d 666 (7th Cir. 2002).

The Seventh Circuit Court of Appeals affirmed the district court’s interpretation of the buy-sell provisions of an LLC’s operating agreement. (The district court’s opinion is found at 2001 WL 1135871.) In brief, Valinote exited the LLC pursuant to a push-pull buy-sell provision under which Ballis, the other member of the LLC, set the price of the 50% interest that each held at a negative \$79,064. At the time, the LLC owed Valinote exactly that amount so that no money changed hands, and Ballis became the sole member of the LLC. When a bank pursued Valinote on his guaranty of LLC indebtedness, Valinote argued that he should be indemnified by Ballis. The court cited and discussed at length the terms of the operating agreement, contrasting the push-pull buy-sell provisions with provisions dealing with buy-out upon resignation of a member, and concluded that Valinote had no implied right of indemnification against Ballis. Valinote had a right against the LLC, but not against the other member. The court concluded that Valinote, as a former member, was not covered by a clause in the operating agreement that imposed cross-indemnity obligations between the members (interpreting “members” to include only current members). The court explained the negative price in terms of the increased risk each took by giving up the right of indemnification against the other.

McGee v. Best, __ S.W.3d __, 2002 WL 1343225 (Tenn.Ct.App.2002).

The plaintiff was a one-third member and the Chief Manager of a Tennessee LLC. After disagreements arose, the members of the LLC other than the plaintiff took action by written consent to terminate the employment of the plaintiff and to exercise a buy-out right on the part of the LLC triggered by the termination of employment of a member. The members relied on a provision of the operating agreement under which a member’s employment could be terminated for “cause” (as defined in the agreement) and asserted the LLC’s right to repurchase the member’s interest under a valuation that applied when employment was terminated for cause. The plaintiff brought suit alleging various causes of action, including breach of fiduciary duty, fraud, breach of the operating agreement, and breach of the duty of good faith and fair dealing. The plaintiff alleged that the other members breached the operating agreement and the covenant of good faith and fair dealing by purporting to terminate him for cause when no cause existed and by attempting to

acquire his membership interest. The court examined provisions of the LLC operating agreement and an employment agreement between the plaintiff and the LLC and concluded that these agreements did not alter the general rule of at-will employment in Tennessee. The court also noted that there is no implied covenant of good faith and fair dealing in an at-will employment contract in Tennessee. Thus, the court granted the defendants summary judgment on these claims. (The trial court based its dismissal of the good faith and fair dealing claim on its conclusion that “performance of a contract by its terms cannot be characterized as bad faith” and its assessment that the operating agreement allowed the very actions taken in terminating the plaintiff’s employment.) The court found that the plaintiff waived his argument that there had been a breach of contract based upon a conflict of interest in violation of the operating agreement. The court did conclude that there was a fact issue as to whether there was “cause” to terminate the employment of the plaintiff under the operating agreement, an issue that was relevant to the valuation of the plaintiff’s membership interest under the terms of the operating agreement.

Ault v. Brady, 37 Fed.Appx. 222, 2002 WL 1301520 (8th Cir. 2002).

In this dispute between the members of an Arkansas LLC, the court interpreted provisions of the operating agreement regarding transfer of units and buy-out in connection with the termination of employment of the member. The three members of the LLC were Brady, Pierce, Ault, and an entity owned by Brady and Pierce. In the course of a power struggle between Brady and Pierce, Pierce transferred his units to Ault. Subsequent to the transfer, Brady notified Pierce that he was terminated and the LLC would exercise its option to purchase his units. When Ault revealed to Brady that he now owned Pierce’s units, Brady demanded Ault turn the units over to the LLC. Ault refused, and Brady terminated Ault and informed him that the LLC would buy back his units pursuant to the operating agreement. Ault took the position that the repurchase provision in the operating agreement did not apply to him because he was an independent contractor rather than an employee. The operating agreement provided that the LLC had the option to purchase a member’s units “upon the termination of employment” of a member. Ault also argued that the transfer of Pierce’s units to Ault was not subject to a provision of the operating agreement that restricted transfer and provided that a transferee who received units in violation of the restriction was not a “substituted member” and had only economic rights. Ault argued that, since he was already a member, the provision was inapplicable. The court of appeals held that the provision applied to any transfer, and the term “substituted member” could only logically be viewed in terms of units, i.e., a substituted member with respect to particular units. The court of appeals also rejected Ault’s interpretation of the repurchase provision. The court stated that whether Ault was an independent contractor rather than an employee was irrelevant to the application of the provision. In either case, he was “employed” by the LLC, and the provision applied whenever the “employment” of a member was terminated. Finally, the court rejected Ault’s challenge to the valuation of his units. Following the district court’s decision that the LLC had the right to purchase Ault’s units, the parties stipulated to a procedure for valuation. The procedure specified that each party would select a CPA, and the two CPAs chosen by the parties would select a third. The appraisal most different from the other two would be disregarded, and the value would be an average of the remaining two. Two of the CPAs valued Ault’s units at zero, and the CPA chosen by Ault valued his units at \$2 million. Ault conceded that he was bound by the stipulation but argued the agreement carried with it an implied duty of good faith and fair dealing, which included the duty to follow customary and usual accounting standards. The court characterized Ault’s argument as nothing more than an attack on the CPAs’ methodology and concluded that Ault was bound by the stipulation under both contract and estoppel principles.

Ward v. Hornik, No. 02.944, 2002 WL 1199249 (E.D. Pa. June 3, 2002) (interpreting Pennsylvania LLC act and quorum and voting provisions of LLC operating agreement and concluding that suit brought on behalf of LLC was not authorized).

Metro Riverboat Associates, Inc. v. Bally’s Louisiana, Inc., 817 So.2d 1275 (La. App. 2002) (affirming trial court’s grant of preliminary injunction where arbitration clause permitted one member to invoke arbitration without vote of membership in dispute over cash call and alleged transfer of interest inasmuch as penalty for refusal to arbitrate was forced sale of member’s interest, which would constitute irreparable injury).

Chase Manhattan Bank v. Iridium Africa Corporation, 197 F.Supp.2d 120 (D. Del. 2002) (finding fact questions precluding summary judgment regarding the validity of amendment to and assignment of rights under reserve capital call provisions of Iridium LLC agreement).

Estate of Murray, No. 2000-T-0152, 2002 WL 550071 (Ohio App. April 12, 2002) (interpreting provisions of operating agreement governing buy-out of deceased member’s interest and concluding that date of withdrawal was date of personal representative’s distribution of the estate’s interest in the LLC and that valuation of interest as recorded

in “last regular accounting period” should be based on last monthly record preceding withdrawal, as phrase was ambiguous and extrinsic evidence indicated books were kept on monthly basis).

Chase Manhattan Bank v. Iridium Africa Corporation, No. 00-564-RRM(JJF)(MPT), 2002 WL 732070 (D. Del. April 5, 2002) (discussing reserve capital call provisions and provisions waiving objections to jurisdiction contained in Iridium LLC agreement in context of member’s motion to set aside default judgment).

Weinmann v. Duhon, 818 So.2d 206 (La. App. 2002) (finding nothing unlawful in provision admitting persons as members on condition that they not vote to expel original members, provision that transfer of interest to spouse automatically conveys membership in LLC, provision requiring unanimous vote for expulsion, or provisions that effectively permitted one faction of members to fire general manager while other faction could re-hire him, but concluding that impasse created by such provisions justified judicial dissolution).

NSJ Investors, LLC v. TH/North San Jose, LLC, No. CIV. 01-1932PAMSRN, 2002 WL 334413 (D. Minn. Feb. 22, 2002) (interpreting provisions of operating agreement regarding approval required for commencement of litigation and employment of counsel and concluding that interpleader action to determine how to make distributions was in “ordinary course of business” thus not requiring approval of non-managing members to hire lawyer to pursue suit even though employment of counsel generally required approval of non-managing members under agreement).

Concrete Company, Inc. v. MMC Holdings, Inc., 201 F.Supp.2d 1192 (M.D. Ala. 2001) (denying LLC member’s requested stay of judgment pending appeal of court’s interpretation of buy/sell provision, finding no indication that refusal to stay judgment would inflict irreparable harm on member).

Coady v. Martin, 784 A.2d 897 (Conn. App. 2001).

The court held that the membership agreement on which the plaintiff based his claims was unenforceable due to lack of an essential term. The defendant (Martin) filed documentation with the Connecticut Secretary of State to establish an LLC, and the plaintiff (Coady) and Martin entered a written membership and subscription agreement. Under the agreement, Coady received a 50% interest in the LLC from Martin, but the agreement acknowledged that two other individuals involved in the project would receive interests in a lesser proportion at a later date. Prior to the agreement, discussions had been held, but the parties had been unable to agree on the precise percentages to which the other two individuals were entitled based upon their prior role in the project. The trial court held that the membership agreement was unenforceable because there had been no meeting of the minds and there was a lack of consideration. The court of appeals upheld the trial court’s conclusion that the membership agreement was unenforceable for lack of an essential term, that is, delineation of the percentage of ownership interests of all of the parties. (Having upheld this conclusion, the court of appeals did not reach the issue of lack of consideration.)

Pine Creek, LLC v. Pine Mount, LLC, 558 S.E.2d 44 (Ga. App. 2001).

In this dissent and appraisal proceeding, the court examined the transfer restrictions in an LLC operating agreement and concluded that there were fact issues as to whether the operating agreement was violated.

ESCA of Baltimore, LLC v. Colkitt, 164 F. Supp.2d 584 (D. Md. 2001) (finding that there were fact issues as to whether an LLC member made a transfer of his membership interest for consideration in violation of transfer restrictions contained in the operating agreement).

Stark v. Fuchs, 764 N.E.2d 446 (Ohio App. 2001).

Members representing 60% of the interests in an LLC attempted to remove the member who was serving as manager and appoint a new manager. The operating agreement (and Ohio LLC act) did not address the vote required to remove the manager. The incumbent manager argued that his removal required a unanimous vote of the members because the operating agreement appointed him as manager. The incumbent manager based his position on contract principles, arguing that the operating agreement was a contract that could only be modified with unanimous assent. The members who were trying to remove the manager argued that interpreting the agreement to require unanimous consent would defeat the provisions of the operating agreement that contemplated and referred to removal and election of managers and officers. The agreement had a provision that required the doctrine of cy pres to be applied to give effect as near as possible to the intent of the parties, and the court concluded that the only reasonable voting method that would give effect to the provisions on removal and election was a simple majority vote rule. The court also construed the agreement against the manager because he was the drafter.

In re Utilimax.com, Inc., 265 B.R. 63 (Bankr. E.D. Pa. 2001).

The debtor was one of approximately 180 members of an LLC that operated as a conduit for its members and was responsible for the bulk electric power system in a multi-state area. The LLC filed an involuntary petition of bankruptcy against the debtor based upon an unpaid obligation for goods sold and delivered. Issues included whether the claim asserted by the LLC was subject to a bona fide dispute and whether fellow members of the LLC could qualify as holders of claims against the debtor. The court discussed provisions of the LLC operating agreement regarding enforcement of obligations and concluded that the joining petitioners did not have “claims” and that conversations at a members committee meeting did not amount to a de facto amendment of the operating agreement.

Flippo v. CSC Associates III, L.L.C., 547 S.E.2d 216 (Va. 2001).

In addition to addressing breach of fiduciary duty and other issues in this case, the Virginia Supreme Court examined the meaning of two provisions in an LLC operating agreement relating to dissolution, continuation, and purchase of a member’s interest. Article 13 of the operating agreement provided for dissolution on the death, resignation, bankruptcy, or dissolution of a member unless the procedures of Article 9 were followed resulting in an election to continue the LLC. Article 9 provided that, on the death of a member, the remaining members could elect to purchase the interest of the deceased member or elect to continue the LLC. If the remaining members did not make “either of these elections” the LLC was dissolved. The court rejected the defendants’ argument that the “election” referred to in Article 13 referred only to the election to continue and did not include the election to buy the departed member’s interest. The supreme court rejected this argument and agreed with the trial court that either of the two elections referred to in Article 9 resulted in continuation of the LLC. The court relied upon general rules of contract construction and considered the purposes of the parties and the circumstances surrounding execution of the operating agreement, including the terms of a restated partnership agreement drafted for the partnership that was the predecessor to the LLC. (The court went on to uphold sanctions imposed upon the parties who alleged fraud and mutual mistake with respect to the inclusion of these terms in the operating agreement. The sanctions were based upon the fact that the parties who claimed they were misled had the assistance of “experienced” and “sophisticated” attorneys who specialize in this type of work. According to the trial court, it was “ridiculous” to say that the plaintiff could mislead such attorneys.)

International Paper Company v. Androscoggin Energy LLC, No. 00C 6215, 2001 WL 503058 (N.D. Ill. May 10, 2001).

The plaintiff contracted with the defendant LLC for the defendant to provide an electric power facility at plaintiff’s mill, and the plaintiff argued that certain representations and warranties contained in the LLC operating agreement as well as a separate energy services agreement between the plaintiff and the LLC were false. The plaintiff, which was the parent company of one of three entity members of the LLC, sought to hold the other two members of the LLC liable for the alleged misrepresentations. The representations and warranties related to pending and threatened legal proceedings and compliance with laws and contracts. The court concluded that the representations and warranties in the operating agreement were not false, and the plaintiff could not rely on the LLC’s representations and obligations under the separate agreement to hold the other two members of the LLC liable under the operating agreement.

Baker v. Jones & Henry Engineers, LTD, No. L-00-1198, 2001 WL 304088 (Ohio App. March 30, 2001).

A member of an engineering firm LLC sued for wrongful termination after the other members voted to terminate his employment and demanded he resell his membership interest. The plaintiff argued that termination of his employment was wrongful because the operating agreement and membership interest subscription agreement contractually obligated the LLC to retain him. The member based this argument on the inclusion of the phrase “long-term investment” in each of these agreements, which the member asserted was evidence that a member was entitled to employment until he voluntarily left the firm or retired. The court concluded that there was no evidence of an express or implied contract in this regard. The court also rejected other arguments based upon promissory estoppel, public policy and fraud.

McDonald v. Miller, No. 00AP-994, 2001 WL 300736 (Ohio App. March 29, 2001).

Four individuals entered an operating agreement for an LLC that listed them as members and required that each of them contribute \$5,000 as an initial capital contribution. One of the individuals did not make the required contribution. The issue addressed by the court was whether the individual who failed to make the contribution was a member, and the court held that he was. The other members argued that he never became a member because of his failure to make the required contribution. The court, however, found that he was a member under the clear and unambiguous language of the operating agreement. The court pointed out that the operating agreement listed the

individual as a member and presupposed that the person required to make the capital contribution was a member when it provided that “each Member shall contribute \$5,000 as the initial Capital Contribution.”

Lieberman v. Wyoming.com LLC, 11 P.3d 353 (Wyo. 2000).

The court interpreted the Wyoming LLC act and the operating agreement of a Wyoming LLC to determine the rights of Lieberman, a dissociated member. Lieberman’s contribution upon formation of the LLC was documented at \$20,000, consisting of services rendered and to be rendered. When Lieberman was terminated as vice-president of the LLC, he served a notice of withdrawal and demand for the return of his share of the current value of the company, which he estimated at \$400,000. The remaining members avoided dissolution of the LLC by electing to continue the LLC and approved the return of Lieberman’s \$20,000 capital contribution. The court discussed a provision of the Wyoming LLC act that entitles a member to demand the return of the member’s capital contribution if the operating agreement does not prohibit or restrict the right. Since the LLC operating agreement did not restrict this right, Lieberman was entitled to the return of his \$20,000 contribution. The question remained whether he was entitled to receive any further distribution. A provision permitting a member to compel dissolution upon an unsuccessful demand for the return of the member’s contribution was not applicable since the LLC agreed to return Lieberman’s contribution. Noting the absence of a provision in the Wyoming LLC act governing dissociation, the court turned to various provisions of the operating agreement dealing with membership certificates, transfer of interest, quorum and voting and concluded that it remained unclear what became of Lieberman’s ownership interest beyond his capital contribution. Thus, the court remanded for a further determination in this regard.

Suntech Processing Systems, L.L.C. v. Sun Communications, Inc., No. 05-99-00213-CV, 2000 WL 1780236 (Tex.App. Dec. 5, 2000).

The minority member of a Texas LLC claimed that the majority member owed it a fiduciary duty as a matter of law. The case does not state whether the LLC was member-managed or manager-managed, but the articles of organization provided as follows: “Members of this Company have a duty of undivided loyalty to this Company in all matters affecting this Company’s interest.” The Texas LLC act provides: “To the extent that at law or in equity, a member, manager, officer, or other person has duties (including fiduciary duties) and liabilities relating thereto to a limited liability company or to another member or manager, such duties and liabilities may be expanded or restricted by provisions in the regulations.” The court noted the absence of Texas case law on fiduciary duties of LLC members and looked to case law regarding fiduciary duties of shareholders of a closely held corporation. In prior cases, the court had held that co-shareholders of closely held corporations are not necessarily in a fiduciary relationship. Rather, the existence of a fiduciary relationship is a question of fact. The court applied the same reasoning and stated that it made no difference that the defendant was the majority member. The court pointed out the provision in the LLC’s articles of organization provided for a duty of loyalty to the LLC rather than between the members. The court said that neither the statute nor the provision in the articles authorized the court to find that there was a fiduciary relationship between the members as a matter of law, and the issue was remanded for determination by the factfinder.

Lynch Multimedia Corp. v. Carson Communications, L.L.C., 102 F. Supp.2d 1261 (D. Kan. 2000).

One of the members of a Kansas LLC sued another member and the member’s owners and agent for breach of the operating agreement and breach of fiduciary duty when they acquired other cable franchises rather than securing them for the LLC. The LLC operated a television cable system, and the operating agreement specified that if an opportunity to purchase certain cable television systems came to the attention of a member, the opportunity must first be offered to the LLC. Another provision in the operating agreement stated that any member or manager was permitted to engage in other business ventures, and the LLC would have no rights in such regard. Robert Carson was trustee of the Robert Carson Trust, a 20% member of the LLC, as well as president and a manager of the LLC. In 1997, Carson informed representatives of Lynch Multimedia Corporation (Lynch), a 60% owner of the LLC, of the potential availability of certain cable systems. Lynch was receptive to exploring the opportunities. Over the next year, discussions and negotiations continued. At one point, a Lynch representative rejected the acquisition of the cable systems, but a couple of proposals were made a few months later in the fall of 1998. In the spring of 1999, Carson acquired the cable systems through his own entity. Lynch sued for breach of the operating agreement and breach of fiduciary duty. The court held that the operating agreement’s requirement that certain opportunities be “offered” to the LLC contemplated only that the LLC be made aware of such opportunities, not that a formal offer be presented. The court concluded that Carson satisfied this requirement by making Lynch aware of the opportunities. The court rejected Lynch’s claims that a formal meeting was required, noting that the LLC at all times operated on an informal basis with Lynch’s acquiescence. The court also stated that the operating agreement’s requirement that certain opportunities be offered to the LLC must be read in conjunction with the provision permitting members to engage in other ventures; therefore, it plainly was directed at

permitting members to enter separate and additional business relations in the cable TV industry. The court thus granted summary judgment in favor of the defendants on both the breach of operating agreement and breach of fiduciary duty claims. The court said that Lynch had not articulated how the breach of fiduciary duty claims were distinguishable from the breach of operating agreement claims. The court cited the provision of the Kansas LLC act that permits members of an LLC to expand or restrict their duties and liabilities by agreement. Lynch argued this provision did not apply because it was passed after the LLC in this case was formed, but the court held otherwise, citing the legislature's intent that from January 1, 2000, the act shall apply to all LLCs formed in Kansas, whether formed before or after that date.

Froelich v. Erickson, 96 F. Supp.2d 507 (D. Md. 2000), aff'd, 5 Fed.Appx. 287 (4th Cir. 2001).

The factual background of this case is rather complicated, but the claims involved assertions of fraud, breach of fiduciary duty, and breach of contract by Froelich, an ousted CEO and board member of a Maryland LLC. Froelich was also a member of the LLC who, along with other minority members, was cashed out in a squeeze-out merger following a reclassification of interests of the LLC approved by all members except Froelich. Two documents primarily governed the LLC's operations as an LLC. These documents were an Operating Agreement, which the court characterized as the LLC equivalent of a corporate charter, and a Members Agreement, which the court described as the equivalent of a stockholders' agreement. The operating agreement defined classes of preferred and common interests, the role and responsibility of the board, and the rights and duties of the members. The member agreement supplemented the operating agreement by specifically defining rights of members and restrictions on alienation of interests. The court summed up Froelich's claims as a challenge to "a handful of corporate actions taken by [the LLC's] Board and its Members." The court summed up the key issues in the case as follows: "(i) Did the corporate documents or Maryland corporate law authorize the Board to take the actions that Froelich challenges? (ii) If the Board or the Members had the power to act, by what standard (e.g., business judgment rule or fiduciary duty) should the Court review the Board's exercise of that power? and (iii) Did the Board meet the appropriate standard?" The court characterized the case as arising in the context of corporate decisions by the LLC's board of directors and applied the business judgment rule. The court noted that the LLC's operating agreement stated that the LLC's directors "are subject to the duties of a corporate fiduciary as defined by Maryland law;" thus, the court continued, the LLC board's decisions are measured against the business judgment rule "just as if [the LLC] were a traditional corporation, rather than an LLC." The court found no evidence that the board had acted in bad faith and concluded that the board's actions were protected by the business judgment rule. The court also concluded as follows: the LLC and majority member did not breach a duty of good faith and fair dealing (noting uncertainty under Maryland law as to whether there is a separate cause of action in this regard and stating that the duty in any event only prohibits a party from preventing the other party from performing under the contract); the majority member did not breach a fiduciary duty to Froelich by usurping a business opportunity (stating that a majority interest holder clearly owes the minority a fiduciary duty but finding no breach in view of the board's independent approval of the transaction); the reclassification did not breach the operating agreement or the member agreement (finding that the transaction fell outside a provision in the member agreement restricting redemptions and was governed by the operating agreement, which was amended in accordance with its terms to permit the reclassification). In Froelich's favor, the court found that the LLC owed Froelich severance pay under an employment agreement between the LLC and Froelich and that the reclassification and squeeze-out were related parts of a transaction in which Froelich had properly preserved his statutory right to an appraisal.

VGS, Inc. v. Castiel, No. C.A. 17995, 2000 WL 1277372 (Del. Ch. Aug. 31, 2000), aff'd, 781 A.2d 696 (Del. 2001).

The court interpreted the provisions of an LLC agreement to determine what vote of the managers was required to authorize a merger. The LLC agreement did not expressly state whether the managers must act unanimously or by majority vote. Under the LLC agreement the initial board of managers consisted of three managers, one of which the minority member had the right to appoint. The individual controlling the members owning a majority of the membership units had the right to appoint the other two managers. The agreement had language addressing how many managers the minority member could appoint if the size of the board was increased. The court noted that, if unanimity were required, the number of managers appointed by the minority member would be irrelevant because just one would suffice to veto any action. Further, the court noted that the agreement contained provisions requiring the consent of the minority member for certain transactions, a provision that would be unnecessary if unanimity of managers were required. The court also considered a provision permitting dissolution by vote of the managers or members holding 2/3 of the units. The court said it seemed unlikely the members designed the LLC agreement to permit members holding 2/3 of the units to dissolve the LLC but denied their appointed managers the power to reach the same result unless the minority manager agreed. The court rejected the argument that the members could generally act by majority vote while unanimity of managers was required. The practical effect of such an arrangement would have been that any matter on which the

minority member disagreed would then be approved by a vote of the members. The court was confident such a result was not intended. Ultimately, the court determined, however, that the merger approved by a majority of managers should be rescinded because, while the merger was approved in accordance with the procedures required by the LLC agreement, it was in breach of the managers' fiduciary duties.

Whitmore v. Hawkins, No. 99-1443, 2000 WL 828285 (4th Cir. June 27, 2000).

Whitmore was hired as chief operating officer of an LLC that operated fast food restaurants. He also received a 5% membership interest in the LLC and a 5% interest in a second LLC that was being formed to acquire additional fast food franchises. When Whitmore's employment was terminated, he claimed that he was entitled to receive the value of his membership interests under provisions of the Maryland LLC act in effect at the time. The court pointed out that the statutory provisions relied upon by Whitmore were default provisions and that the operating agreements of the two LLCs had provisions addressing withdrawal and buy-out. The court concluded that the termination of Whitmore's employment did not amount to a withdrawal or entitle Whitmore to receive the value of his interest under either of the operating agreements, thus Whitmore was not entitled to be bought out.

Signal Capital Corporation v. Signal One, LLC, No. E2000-00140-COA-R3-CV, 2000 WL 1281322 (Tenn. App. Sept. 7, 2000) (construing Acquisition Agreement, Employment Agreement, and LLC Agreement of Delaware LLC as interrelated and enforcing North Carolina forum selection clause in the Acquisition Agreement with respect to all the plaintiff's claims).

Oil and Grease on Wheels, Inc. v. Medicare Supply Co. of New England, No. C.A. 96-1789, 2000 WL 622584 (R.I. Super. April 26, 2000).

A receiver was appointed for Medicare Supply Co. of New England ("Medicare"), a member of a Rhode Island LLC. Medicare argued that appointment of the receiver constituted an event of dissociation under the LLC agreement which in turn entitled Medicare to be bought out under the agreement. Events of dissociation included a change in control of a member of the LLC. Control was defined under the agreement as an ownership interest sufficient to carry any motion, the right to elect or appoint directors or managers, or the right to manage. The court concluded that a change in control had occurred because the shareholders, directors, and officers of Medicare no longer controlled Medicare. The court stated that control did not have to shift to the receiver for a change in control to occur; it was sufficient that those formerly in control no longer had control. The court rejected the argument that the receiver was an assignee but did accept that the receiver was analogous to a judgment or lien creditor of Medicare. As a type of lien creditor, the court said the receiver succeeded to the rights of the dissociated member to be bought out.

Lindsay, Marcel, Harris & Pugh, L.L.C. v. Harris, 752 So.2d 335 (La. App. 2000).

Harris and Pugh gave notice of their withdrawal from their four-member law firm LLC and formed their own law firm. When the LLC filed suit against the withdrawn members, the withdrawn members answered and sought dissolution. The court of appeals determined that the withdrawn members had no right to seek judicial dissolution because the statute conferred no such right on former members. In addition, the court found no basis in the operating agreement for the withdrawn members to obtain dissolution. Included among the causes of dissolution listed in the operating agreement was "reduction in the number of Members to 1," but the court pointed out that two members remained after the withdrawal of the other members.

McConnell v. Hunt Sports Enterprises, 725 N.E.2d 1193 (Ohio App. 1999).

This was the first case to address the fiduciary duties of members of an LLC to any significant degree. In this case, the court stated that members of an LLC are in a fiduciary relationship that would generally prohibit competition with the business of the LLC. (The court did not directly address the management structure, but it appears that the LLC was member-managed. The opinion notes at one point that the operating agreement did not name any person or entity the operating or managing member of the LLC.) The court concluded, however, that members may contractually limit or define the scope of the fiduciary duties. Specifically, the court recognized the validity of a provision in the operating agreement of an Ohio LLC that permitted members to compete with the LLC. The court found support for its conclusion in the case law regarding partnerships and close corporations. The case involved a dispute between members of an LLC formed to pursue a professional hockey franchise for Columbus, Ohio. When some of the members objected to the proposed terms of a lease that was necessary to obtain ownership of the franchise, other members formed a separate ownership group that agreed to the lease and obtained the franchise. The court found the operating agreement clearly and unambiguously allowed the members to compete against the LLC and obtain the hockey franchise. The court rejected the argument that the provision in issue only allowed members to engage in other types of businesses. The court

did indicate at a couple of points that action related to obtaining the franchise or “the method of competing” could constitute a breach of fiduciary duty if it amounted to “dirty pool,” but the court noted the trial court’s finding that the competing members had not engaged in any kind of willful misconduct, misrepresentation, or concealment. The court discussed several other provisions of the operating agreement as noted below.

The court concluded that the competing member’s conduct did not breach a provision of the operating agreement requiring unanimous consent of the members to do any act “that would make it impossible to carry on the ordinary business of the Company” because the provision only applied to actions taken “on behalf of the Company.” Forming the competing ownership group was not an action taken on behalf of the LLC.

The court also addressed provisions of the operating agreement regarding additional capital contributions. The operating agreement required consent of all members to call for additional capital and stated that members would have the opportunity, but not the obligation, to contribute if the members determined that additional capital was required to preserve and maintain the business. The court found that the competing member’s actions, including allegedly stating that he would attempt to block an effort to raise additional capital, did not breach the agreement.

The court found that the non-competing member breached the operating agreement by unilaterally undertaking litigation on behalf of the LLC without the requisite approval of the members. The member argued that his actions did not constitute willful misconduct and that the exculpation and indemnity provisions of the LLC protected him. However, the court found that the exculpation and indemnity provisions applied in the context of members carrying out their duties under the operating agreement and that there was no duty on the member’s part to unilaterally file the actions at issue. Furthermore, the court found the evidence indicated willful misconduct on the member’s part.

Finally, the court determined that the judicial dissolution of the LLC on the basis that it was no longer reasonably practicable to carry on the business in conformity with the LLC’s articles of organization and operating agreement was not “wrongfully caused” by the member who acted wrongfully in breaching the operating agreement and usurping control of the LLC. The reason it was no longer practicable to carry on the business was the LLC’s failure to obtain the hockey franchise rather than the wrongful conduct of a member. Thus, no member was precluded from participating in the winding up by the terms of the operating agreement that allowed only members who have not wrongfully caused dissolution to participate in winding up. The issue was moot, however, because there was a liquidating trustee appointed by the court.

Fausel v. JRJ Enterprises, Inc., 603 N.W.2d 612 (Iowa 1999).

JRJ Enterprises, Inc. (“JRJ”), a member of a Wyoming LLC involved in a Colorado casino operation, sued for anticipatory breach of a contract for the sale of JRJ’s membership interest in the LLC. The contract for the sale of the membership interest was captioned “Agreement for Sale of Stock” (“Stock Agreement”), and it contained a provision wherein JRJ warranted its membership units were not subject to any restrictions on transfer other than those set forth in the operating agreement or articles of organization of the LLC. This, the court concluded, incorporated by reference the provisions of the operating agreement restricting transfer of JRJ’s membership interest. Thus, interpretation of the Stock Agreement required the court to interpret restrictions on transfer in the LLC operating agreement as well. At issue were timing requirements of right of first refusal provisions in the operating agreement and requirements in the Stock Agreement regarding approval of the Colorado Gaming Division and closing of the sale. The court concluded that the deadline for closing the sale under the right of first refusal provisions did not constitute a deadline for purposes of the Stock Agreement because failure to close by that date would simply require that the membership interest would have to be offered to the LLC and remaining members again under the right of first refusal provision. Since the trial court had viewed the deadline under the right of first refusal provisions as the final deadline for performance of the sale under the Stock Agreement, the court remanded for further determinations relating to the anticipatory breach claim.

Donnelly v. Brown, Winick, Graves, Gross, Baskerville, Schoenbaum and Walker, P.L.C., 599 N.W.2d 677 (Iowa 1999).

A lawyer left his firm (a professional LLC) and went to another firm, and there was a dispute over the provision of the operating agreement dealing with benefits to be paid to a retiring member. The specific issue on appeal was whether the “continuation payments” under the operating agreement qualified as “retirement benefits” under Iowa DR 2-108(A). The payments were conditioned on the lawyer’s termination of the private practice of law in Iowa. The lawyer argued that this was an impermissible covenant not to compete. The court concluded that the provisions in this case (requiring ten years of service and sixty years of age or twenty-five years of service) clearly constituted a retirement plan, and the restriction on future practice was therefore valid, even though the plan applied to situations involving less than full retirement.

Lusk v. Elliott, No. Civ. A. 16326, 1999 WL 644739 (Del. Ch. Aug. 13, 1999).

An LLC member (“Elliott”) assigned his 99% interest in the LLC to a family trust, and the 1% member (“Lusk”) claimed that he was the sole remaining member and manager on the basis that the assignment was not effective to transfer membership rights. The court determined that the assignment transferred Elliott’s membership along with his 99% financial interest. The operating agreement prohibited assignment of a member’s interest other than to another member; however, both members signed a consent to the transfer of Elliott’s 99% membership interest and agreed that the assignment would not constitute a prohibited assignment under the operating agreement. The parties agreed that the consent amended the prohibition on transfer in the operating agreement but disagreed as to whether the consent authorized the conveyance of Elliott’s membership along with the financial interest. Lusk relied upon the Delaware LLC act provisions that characterize an assignment as carrying only the financial interest of the member. Since the operating agreement did not define “assignment,” Lusk argued the court should look to the Delaware act for the effect of an assignment. The court disagreed. The court said that the consent and assignment indicated what was meant by the term “assignment” since the instruments referred to assignment of Elliott’s “entire undivided membership interest.” The court concluded that this language encompassed Elliott’s membership as well as his 99% ownership interest.

Sherrets v. The Lund Company, No. A-97-1350, 1999 WL 502138 (Neb. App. July 6, 1999).

An LLC member who was bought out pursuant to a push-pull provision in the LLC operating agreement claimed that he was entitled to a portion of net rental income held by a third party under a property management agreement at the time of the closing of the sale of the member’s interest. The court examined the provisions of the operating agreement and the property management agreement and agreed that the member was entitled to recover a portion of the net rental. The court viewed the member as a third party beneficiary of the property management contract executed by the LLC and disagreed with the defendant’s argument that the member assigned his interest in the disputed funds when he sold his interest in the LLC.

Clark v. Kelly, No. C.A. 16780, 1999 WL 458625 (Del. Ch. June 24, 1999).

This case was a dispute over who were the managers of a Delaware LLC, and the determinative issue was whether the transfer of all of the shares of a corporate member of the LLC to a trust was a “transfer” of an LLC interest within the meaning of the operating agreement. Plaintiff Clark, the sole shareholder of one of the members of the LLC claimed to be the sole manager of the LLC. The other member of the LLC was La Empresa De La Mar D’Oro, Inc. (“La Empresa”), a California corporation. The stock of La Empresa was titled in Danis at the time La Empresa became a member of the LLC. After formation of the LLC, Danis transferred the stock of La Empresa to a living trust of which Danis and his wife were the trustors and co-trustees. The issue was whether the transfer of the shares to the trust triggered a provision of the operating agreement requiring consent. If the transfer requiring consent occurred without such consent, the transferee’s status was that of a mere assignee. The definition of “transfer” under the operating agreement included a transaction whereby the equity owners of a member as of the date of the member’s admission to the LLC own less than 90% of the equity securities of the member after the transaction. The court determined that the transfer of the shares of La Empresa to the trust did not fall within the definition of a transfer under the operating agreement because the shares were community property under California law and Danis’s wife therefore had a 50% equitable interest in the shares before the transfer to the trust. The court rejected the plaintiff’s argument that the Delaware choice of law clause in the operating agreement, together with the internal affairs doctrine, required Delaware law to apply to the determination of ownership of the shares of La Empresa. According to the court, “Even if the choice of law provision in the Operating Agreement were found to govern, the internal affairs doctrine – which is a well-established principle of Delaware substantive law – requires this Court to look to the law of the state of incorporation to determine the relationships between the corporate entity and its directors, officers, and stockholders. . . . Because La Empresa is a California corporation, . . . this Court would be required to look to California law in all events to determine who are the equity owners of La Empresa.”

Investcorp, LP v. Simpson Investment Company, L.C., 983 P.2d 265 (Kan. 1999).

The members of a family-held Kansas LLC deadlocked on important management issues, and several members withdrew to effect a dissolution of the LLC. The withdrawing members claimed that they were entitled to participate in the LLC’s winding up under the operating agreement. The LLC’s remaining members argued that the withdrawing members were no longer members and thus had no right to participate in the LLC’s winding up. Both factions relied on the operating agreement, which provided for the “members” to wind up and liquidate the LLC and defined “members” as “those persons who are members of the Company from time to time, including any Substitute Members.” The district court found that the withdrawing members were not entitled to participate in the dissolution process. The Kansas Supreme Court, however, examined the use of the term “member” and “remaining member” in other provisions of the

operating agreement and concluded that “[t]he many references to ‘member’ in the Act when coupled with the operating agreement suggest that the better view is that, in dissolution, ‘member’ includes a withdrawing member having a financial interest in the Company’s assets.” The court went on to state that control of the dissolution process resided in the managers of the LLC under the operating agreement and the Kansas act.

Elf Atochem North America, Inc. v. Jaffari, 727 A.2d 286 (Del. 1999).

One member of a two-member LLC brought suit against the other member, individually and derivatively on behalf of the LLC, seeking equitable damages for breach of fiduciary duty and various other claims. The Chancery Court dismissed the case for lack of subject matter jurisdiction because the LLC agreement contained a choice of forum provision directing that disputes be arbitrated or litigated in California. The Delaware Supreme Court addressed the following questions: (1) whether the LLC, which did not itself execute the LLC agreement, is bound by the provisions of the agreement, and (2) whether contractual provisions requiring all disputes be resolved by arbitration or litigation in California are valid under the Delaware LLC act. The court held that the LLC agreement was binding upon the LLC as well as its members and that the contractual forum selection provisions were valid. The court’s opinion goes into the background and policy of the Delaware LLC act and the principle of freedom of contract under the act. The court rejected the argument that, because the LLC itself had not signed the LLC agreement, the LLC was not bound by the provisions of the agreement. According to the court, “It is the members who are the real parties in interest. The LLC is simply their joint business vehicle.” The court also held that the Delaware LLC act permits parties to agree to vest exclusive jurisdiction of disputes (including derivative claims) in courts outside Delaware. The act expressly permits LLC members or managers to consent to the nonexclusive jurisdiction of litigation or arbitration in a state other than Delaware, to the exclusive jurisdiction of litigation in Delaware, or to the exclusivity of arbitration in a state other than Delaware. The court noted that the act is silent with regard to agreements vesting exclusive jurisdiction of litigation in courts outside of Delaware and concluded that the General Assembly would have prohibited such provisions if it had desired to do so.

American Teletronics Long Distance, Inc. v. Equalnet Corporation, No. 97 C 2842, 1999 WL 35787 (N.D. Ill. Jan. 13, 1999).

Several parties entered various agreements concerning the sale and marketing of long distance services. It was contemplated that two of the parties would enter a purchase and sale agreement, but one of the parties decided against consummating the acquisition. The parties had executed an LLC operating agreement that referred to a letter of intent regarding the purchase and sale agreement. The issue was whether the plaintiff had alleged a valid and enforceable contract in order to state a valid claim for breach of contract. The answer essentially depended upon whether the LLC agreement incorporated by reference the purchase and sale agreement or was at least ambiguous in such respect. Considering the pleadings at an early stage in the proceedings, the court concluded that it was possible that the LLC agreement incorporated by reference the purchase and sale agreement or was ambiguous regarding the scope of the parties’ contractual relationship; therefore, the court denied the defendant’s motion to dismiss for failure to state a claim.

Metro Riverboat Associates, Inc. v. Bally’s Louisiana, Inc., 706 So.2d 553 (La. App. 1998).

This case involved the interpretation of arbitration, change of control, and non-competition provisions of an LLC operating agreement. Two corporations, Metro Riverboat Associates, Inc. (“Metro”) and Bally’s Louisiana, Inc. (“Bally’s”), were the members of an LLC formed to own and operate a gambling riverboat. Although Metro had a majority interest, the LLC operating agreement essentially required consent of both members for significant business decisions. When Bally’s merged with Hilton Hotels Corporation, Metro claimed there was a “change of control” under the operating agreement that permitted most decisions to be made by a simple majority in interest. In addition, Metro claimed that Bally’s was in violation of the non-competition provision of the operating agreement because Hilton Hotels had an ownership interest in another riverboat casino. Eventually, Bally’s made demand on Metro for binding arbitration of their disputes, claiming that arbitration was required by the operating agreement. Metro filed suit asking for injunctive relief against Bally’s. The court examined the arbitration provision of the operating agreement and concluded that the parties’ disagreement was not within the scope of the arbitration clause covering “a dispute. . .with respect to the management and operation of the Company.” Rather, their disagreement was over interpretation of contractual provisions that affected their respective management rights. The court next considered the meaning of the change in control and non-competition provisions and concluded that the limited evidence failed to meet the heightened burden of proof imposed on Metro to obtain injunctive relief. On appeal after remand, the court of appeals upheld the trial court’s grant of preliminary injunctive relief. *Metro Riverboat Associates, Inc. v. Bally’s Louisiana, Inc.*, 777 So.2d 578 (La. App. 2000). The Louisiana Supreme Court reversed, holding that Metro had failed to establish its injury could not

be compensated by money damages. *Metro Riverboat Associates, Inc. v. Bally's Louisiana, Inc.*, 789 So.2d 565 (La. 2001).

Five Star Concrete, L.L.C. v. Klink, 693 N.E.2d 583 (Ind. App. 1998).

The court in this case determined that a dissociating member of an LLC had no right under the LLC's operating agreement or the Indiana LLC act to receive a distribution of income allocated to the member for tax purposes, but the court refused to render summary judgment on the issue of whether the buy-out of the dissociating member divested the member of its entire economic interest in the LLC, in part because the meaning of the term "units" was not clear under the operating agreement. Klink, Inc. ("Klink") and four other corporations formed an LLC. Klink withdrew from the LLC, and the remaining members decided to purchase Klink's ownership units and continue the business. The members agreed that Klink would receive \$61,047.22 for the value of Klink's "units." After the end of Klink's fiscal year, Klink was allocated its share of the LLC's income for the portion of the year that Klink was a member. Klink asserted that it was entitled to a distribution in this amount. The court concluded that neither Indiana law nor the operating agreement gave a member a right to a distribution of income allocated to the member for income tax purposes. The remaining issue involved the meaning of the term "units" inasmuch as Klink's units were bought out on its withdrawal. The LLC contended that Klink divested itself of its entire interest when it sold its units to the LLC. Klink argued that it sold less than all of its economic rights. Klink pointed to the operating agreement reference to a unit as "an interest in the Company representing a contribution to capital." The LLC pointed out, however, that the operating agreement generally entitled each unit to a vote and a proportionate share of the LLC's net income, gains, losses, deductions, and credits. The court concluded that fact issues precluded resolution of this issue by summary judgment. The court addressed as a separate issue the valuation method and whether it represented the fair market value of Klink's entire interest. The court concluded that summary judgment was not appropriate on this issue either.

Child Care of Irvine, L.L.C. v. Facchina, No. Civ. A. 16227, 1998 WL 409363 (Del. Ch. July 15, 1998).

This case involved a dispute between LLC members in which it was unclear whether the parties' rights were governed by the shareholder agreement of the predecessor corporation, the default provisions of the Delaware LLC act, the merger agreement by which the predecessor corporation was converted to an LLC, or a draft LLC agreement never signed by the members. The plaintiff members of the LLC sought to remove the defendant member, Facchina, as manager of the LLC. The parties had originally formed the business as a Delaware corporation. The corporation was subsequently converted into an LLC by virtue of a merger of the corporation into a newly formed Delaware LLC which survived the merger. An LLC agreement for the new LLC was never signed. The plaintiffs claimed that the shareholder agreement of the predecessor corporation reflected the terms of the members' agreement for the operation of the LLC. Alternatively, the plaintiffs relied upon the default right to remove a manager under the Delaware LLC act. Facchina claimed that a draft LLC agreement never signed by the members governed their relationship. Alternatively, Facchina claimed that the merger agreement itself was the LLC agreement. The court concluded that summary judgment for either side was inappropriate because there were sharply disputed facts and insufficient undisputed facts to support a legal ruling on the issues before the court. The court noted that both the shareholder agreement and the draft LLC agreement contained arbitration provisions and encouraged the parties to pursue arbitration in California.

Goldstein and Price, L.C. v. Tonkin & Mondl, L.C., 974 S.W.2d 543 (Mo. App. 1998).

This case involved interpretation of an LLC law firm's operating agreement in order to resolve a dispute over the effective date of a member's withdrawal and the withdrawn member's rights with respect to certain fees received by the firm after the member's withdrawal. The LLC in this case converted from a partnership in January 1994 and adopted the partnership agreement as the operating agreement until a new operating agreement could be prepared. In November 1994, before a new operating agreement was adopted, one of the members, Tonkin, advised other members of the firm that he intended to withdraw. He provided a written notice of withdrawal stating an effective date of December 31, 1994. The managing members concluded that the partnership agreement that served as the LLC's operating agreement required Tonkin's withdrawal on November 30, 1994. The agreement stated that "withdrawal shall become effective on the last day of the calendar month after service of the withdrawal notice. . ." The court found this language by itself to be ambiguous but interpreted it with reference to other parts of the agreement and concluded that withdrawal was effective November 30, 1994. The parties also had a disagreement as to the withdrawn member's share of certain fees received by the firm after Tonkin's withdrawal. The court looked to the operating agreement as controlling but found no provision addressing work in progress in the withdrawal context. Thus, under the terms of the written agreement, Tonkin was not entitled to any portion of the disputed fee. However, the court concluded that the parties orally modified the operating agreement regarding the fee in question by agreeing to treat the fee as an account receivable. The agreement provided for allocation of accounts receivable, and Tonkin was awarded his share under the agreement. The court rejected

Tonkin's claims against the firm for breach of fiduciary duty. The court stated that the record supported the trial court's findings that the firm did not conceal assets, interfere with client relationships, defame members of the withdrawing member's new firm, or "act in other ways that would warrant a finding of breach of fiduciary duty."

Zaugg & Zaugg Architects v. Wagner, No. 96-CA-117-2, 1997 Ohio App. LEXIS 3987 (Ohio App. Aug. 8, 1997).

Six parties embarked on a venture to build a residential golf course development. Two of the parties, John Zaugg and Marion Zaugg, had an architectural partnership and rendered substantial architectural services toward development of the project. About a year after the Zauggs began working on the venture, the group decided to form an LLC, and articles of organization were filed. A draft operating agreement was circulated among the members but was not signed. A few months later, the parties met to sign the latest draft of the operating agreement, but only three members signed it. The Zauggs' bill for architectural services became a source of contention, and the Zauggs withdrew from the LLC. The LLC claimed that the withdrawal was wrongful under the terms of the operating agreement. The Zauggs were among the members who signed the operating agreement, thus the LLC argued the Zauggs were bound. The court found, however, that the agreement was not a final, binding agreement since all of the members had not agreed to its terms. Thus, the Zauggs were permitted to withdraw by the default provisions of the Ohio LLC act.

Bubbles & Bleach, LLC v. Becker, No. 97 C 1320, 1997 WL 285938 (N.D. Ill. May 23, 1997).

The court determined that an arbitration clause in an LLC's operating agreement was not binding on the individual members of the LLC. Faye Becker ("Becker"), the managing member of Bubbles & Bleach, LLC ("B & B"), misappropriated funds of B & B. B & B brought suit in Illinois against Becker under the authority of one of its members for conversion, breach of fiduciary duty, and fraud. The Operating Agreement of B & B and the First Amended and Restated Limited Liability Company Agreement of B & B each contained an arbitration clause that required that arbitration of "any matters arising out of the terms and conditions of the underlying agreement" take place in Wisconsin and be governed by Wisconsin law. Becker moved for dismissal based upon the arbitration clause. The court concluded that neither the Operating Agreement nor the Amended and Restated Limited Liability Company Agreement of B & B was binding upon B & B. The agreements provided that they were binding upon the "parties" to such agreement; however, the term "parties" was not defined. The court noted that the LLC Agreement provided that it was by and among the members of the LLC and that the signatories to each agreement were the members. Further, it noted that the Wisconsin LLC act defines the term "operating agreement" as a written agreement among the members. The court found that there was no indication that the legislature intended to bind LLCs as entities distinct from their constituent members. According to the court, the fact that B & B was a beneficiary of and subordinate to some of the terms of the agreements did not bind B & B under the arbitration clause. Rather, the arbitration clause was binding only upon the parties to the agreement.

MHM/LLC, Inc. v. Horizon Mental Health Management, Inc., No. 14465, 1996 WL 592719 (Del. Ch. Oct. 3, 1996), aff'd, 694 A.2d 844 (Del. 1997).

The plaintiff sold its interest in an LLC to the parent company of the other member of the LLC. The plaintiff claimed that the terms of the LLC agreement and another agreement regarding the LLC entitled it to a pro rata payment of LLC funds for the portion of the month before the close of the sale of its interest in the LLC. The defendant claimed that the terms of the agreements precluded such a distribution. The court examined various provisions of the agreements and concluded that one of the provisions required a distribution to be made to the plaintiff for its pro rata share of the LLC's net cash flow for the month at issue.

X. Transfer of Interest; Buy-Out of Member

Eikon Street Manager, L.L.C. v. LSF King Street Manager, L.L.C., ___ S.W.3d ___, 2003 WL 21223299 (Tex.App 2003).

Two groups of entities, Lone Star and Eikon, were members of an LLC with a push-pull buy-sell provision. Either party could invoke the provision by notice to the other member in which the invoking member set forth an amount (the "Stated Amount") which represented the price at which the invoking member would be willing to purchase all the assets of the LLC as if the invoking member were a hypothetical third party proposing to purchase the assets of the LLC. The agreement set forth a formula for calculating the value of each member's interest based on the Stated Amount. After the invoking member gave notice to the other member, the other member could elect to buy the invoking member's interest or sell its own interest to the invoking member. Eikon invoked the buy-sell provision, and Lone Star accepted the Stated Amount proffered by Eikon but believed that Eikon had miscalculated the price. Lone Star agreed to buy

Eikon's interest and tendered a check for the full amount claimed by Eikon for its interest, but reserved its right to contest the amount. While the LLC agreement required Lone Star to provide a 10% cash deposit on acceptance of the offer, Lone Star placed a cashier's check in escrow for a portion of the deposit and a letter of credit for the remainder of the deposit. Eikon brought suit alleging that Lone Star had breached the agreement by failing to deliver the cash deposit and seeking liquidated damages under the agreement and attorney's fees. Lone Star counterclaimed for declaratory judgment requiring Eikon to sell its interest pursuant to the agreement. The court concluded that Lone Star's interpretation of the purchase price provisions of the agreement was correct and that Lone Star had the right to accept the offer and reserve its rights as it had done. The court concluded that Eikon did not have the right to liquidated damages. With respect to the deposit requirement, the court determined that questions regarding compliance with this requirement were only relevant in the event that the purchase of the interest did not close. Since the closing occurred, the question did not need to be addressed.

Seed v. Astra Genstar Partnership, No. C2-02-1143, 2003 WL 178790 (Minn.App. Jan. 28, 2003) (holding that change in ownership of 100% of membership interests in LLC which was member of second LLC was not "change in direct ownership of 50% or more of the voting and equity interests" of second LLC so as to trigger option under change in control clause of agreement because the owner of the membership interest in the second LLC did not change).

Jundt v. Jurassic Resources Development, North America, L.L.C., 656 N.W.2d 15 (N.D. 2003).

In the context of certain disputes among the members of an LLC the members told the trial court that they wanted to sever their relationship. At a hearing, an attorney for one of the defendants stated that the members did not want the LLC liquidated because it would cause tax problems for all the members. The trial court found that the members could no longer work together and that liquidation and partition were not appropriate equitable remedies. The court concluded that cancellation of the plaintiff's minority interest in the LLC in exchange for payment of \$300,000 by the defendant members was the appropriate equitable remedy. The defendants appealed the judgment requiring them to buy out the plaintiff. The court of appeals reversed, holding that none of the statutory grounds for equitable relief or court-ordered sale of membership interests had been established and the trial court was thus without authority to grant such relief.

Cogniplex, Inc. v. Hubbard Ross, L.L.C., No. 00 C 7463, 2002 WL 31834895 (N.D. Ill. Dec. 17, 2002) (finding disputed facts precluded summary judgment on parties' claims relating to dissociation and buyout agreement).

Sage v. Radiology and Diagnostic Services, L.L.C., 831 So.2d 1053 (La.App. 2002).

Three radiologists who had been practicing together formed a Louisiana LLC and apparently continued their practice in the LLC. The court stated that the LLC adopted no operating agreement, and the members paid nothing for their interests. The members received monthly distributions based on a number of factors. Several years later, one of the members withdrew and demanded a distribution in the amount of the fair market value of his interest, which was the default statutory measure of the distribution owed a withdrawing member at the time of the member's withdrawal. However, on the date the LLC was formed, the LLC act provided that a withdrawing member was entitled to a distribution in the amount of the "fair market value as of the date contributed of the member's capital contribution." The LLC argued that the law in effect at the time the LLC was formed governed the amount of the withdrawing member's distribution and that the member was not entitled to any distribution because his contribution was zero. The court agreed that the law in effect at the time of the formation of the LLC controlled. The court reasoned that the amendment was a substantive change that should be given prospective effect only because it changed the existing rights and interests of a withdrawing member. Further, the court concluded that application of the amended law would impair the obligations created under the contract entered by the members when they formed the LLC, and the Louisiana LLC act provides that amendments will not impair the obligations of any contract existing when the amendment goes into effect.

Hopson v. Bank of North Georgia, 574 S.E.2d 411 (Ga.App. 2002).

A member of a Georgia LLC pledged all of his interest as an LLC member to secure a bank loan. When the bank attempted to foreclose its security interest, the member argued that the operating agreement required consent of the other members for transfer of an interest in the LLC and that the bank had no security interest because of the bank's failure to obtain consent of the other members. The operating agreement was quoted by the court as follows:

11.01 *General*. Except as otherwise provided herein, neither a Member nor an Economic Interest Owner shall have a right to:

(a) sell, assign, pledge, hypothecate, transfer, exchange or otherwise transfer for consideration, (collectively, "Sale") ...

11.02 *Transferee Not Member in Absence of Unanimous Consent.*

(a) Notwithstanding anything contained herein to the contrary, if all of the remaining Members do not approve by unanimous written consent the proposed Sale or Gift of the Transferring Member's Membership Interest or Economic Interest to a transferee or donee which is not a Member immediately prior to the Sale or Gift, then the proposed transferee or donee shall have no right to participate in the management of the business and affairs of the Company or to become a Member. The transferee or donee shall be merely an Economic Interest Owner. No transfer of a Member's interest in the Company (including any transfer of an Economic Interest or any other transfer which has not been approved by unanimous written consent of the Members) shall be effective unless and until written notice ... has been provided to the Company and the non-transferring Member.

The court found that the operating agreement permitted the transfer of the economic interest and concluded that the bank obtained a security interest in the member's economic interest which it was entitled to foreclose.

Schwegman v. Howard, 2002 WL 31247084 (Tenn.Ct.App. Oct. 8, 2002).

Schwegman sued Howard for breach of an agreement to assign 10% of Howard's interest in an Indiana LLC to Schwegman. Howard executed an assignment of 10% of his interest in the LLC to Schwegman, and Schwegman received a copy of the LLC operating agreement and a consent to membership. The consent to membership was signed by Howard but not the other two members of the LLC. The operating agreement did not alter the Indiana default rule requiring unanimous consent to admit an assignee as a member. Howard argued that the contemporaneous documents rule required the assignment and consent be read together and that unanimous consent of the members was a condition precedent for Schwegman to receive an interest in the LLC. Schwegman argued that there is a difference between assignment (pursuant to which an assignee is entitled only to receive distributions) and transfer of an LLC interest (pursuant to which the transferee is admitted as a member) and that assignment is allowed under the Indiana LLC act unless prohibited by the operating agreement. The court concluded that whether the agreement was an assignment or transfer could only be determined after a hearing on the merits.

Kosoy v. Kieselstein-Cord, No. 01 CIV. 7102(HB), 2002 WL 24313 (S.D. N.Y. Jan. 9, 2002).

An LLC member (Kosoy) sued a third party (Keiselstein-Cord) who allegedly orally agreed that he would purchase a membership interest from Kosoy and assume responsibility for managing the LLC's business. The LLC operating agreement had a push-pull buy-sell provision, and Keiselstein-Cord allegedly agreed that if Kosoy would buy the membership interest of the other member, Keiselstein-Cord would then purchase the interest from Kosoy. The court concluded the agreement lacked essential terms, in particular, a purchase price or a mechanism for its determination. (As put by the court, the agreement was no more than an offer to purchase what was formerly the other member's interest "at an unspecified time, in an unspecified manner, and for an unspecified price, and then at an unspecified time, assume responsibility for operating the boutique" operated by the LLC.)

Pettit v. HFP, LLC, No. 231078, 2002 WL 31188479 (Mich. App. Oct. 1, 2002).

Pettit worked at Burns Clinic Medical Center, P.C. (the "P.C.") and was a member of an LLC that owned the real property where the clinic operated. Pettit sued the LLC for amounts he claimed were owed for the buy-back of his interest in the LLC and compensation for the discounting of his interest in the LLC's predecessor partnership. The court upheld summary judgment in favor of Pettit. First, the court determined that, while there was evidence of financial difficulties of the LLC at a later date, there was no evidence that the buy-out payment would have violated the statutory restriction on distributions at the time it was owed. Next the court interpreted an arrangement whereby the P.C. made two of three payments recommended by the LLC to compensate physicians who had bought into the LLC at a greater price than physicians who were subsequently admitted. The court interpreted this arrangement to involve a legal obligation on the part of the LLC to make the payments.

Ault v. Brady, 37 Fed.Appx. 222, 2002 WL 1301520 (8th Cir. 2002).

In this dispute between the members of an Arkansas LLC, the court interpreted provisions of the operating agreement regarding transfer of units and buy-out in connection with the termination of employment of the member. The three members of the LLC were Brady, Pierce, Ault, and an entity owned by Brady and Pierce. In the course of a power struggle between Brady and Pierce, Pierce transferred his units to Ault. Subsequent to the transfer, Brady notified Pierce that he was terminated and that the LLC would exercise its option to purchase his units. When Ault revealed to Brady that he now owned Pierce's units, Brady demanded Ault turn the units over to the LLC. Ault refused, and Brady terminated Ault and informed him that the LLC would buy back his units pursuant to the operating agreement. Ault took the position that the repurchase provision in the operating agreement did not apply to him because he was an independent contractor rather than an employee. The operating agreement provided that the LLC had the option to purchase a

member's units "upon the termination of employment" of a member. Ault also argued that the transfer of Pierce's units to Ault was not subject to a provision of the operating agreement that restricted transfer and provided that a transferee who received units in violation of the restriction was not a "substituted member" and had only economic rights. Ault argued that, since he was already a member, the provision was inapplicable. The court of appeals held that the provision applied to any transfer, and the term "substituted member" could only logically be viewed in terms of units, i.e., a substituted member with respect to particular units. The court of appeals also rejected Ault's interpretation of the repurchase provision. The court stated that whether Ault was an independent contractor rather than an employee was irrelevant to the application of the provision. In either case, he was "employed" by the LLC, and the provision applied whenever the "employment" of a member was terminated. Finally, the court rejected Ault's challenge to the valuation of his units. Following the district court's decision that the LLC had the right to purchase Ault's units, the parties stipulated to a procedure for valuation. The procedure specified that each party would select a CPA, and the two CPAs chosen by the parties would select a third. The appraisal most different from the other two would be disregarded, and the value would be an average of the remaining two. Two of the CPAs valued Ault's units at zero, and the CPA chosen by Ault valued his units at \$2 million. Ault conceded that he was bound by the stipulation but argued the agreement carried with it an implied duty of good faith and fair dealing, which included the duty to follow customary and usual accounting standards. The court characterized Ault's argument as nothing more than an attack on the CPAs' methodology and concluded that Ault was bound by the stipulation under both contract and estoppel principles.

Valinote v. Ballis, 295 F.3d 666 (7th Cir. 2002).

The Seventh Circuit Court of Appeals affirmed the district court's interpretation of the buy-sell provisions of an LLC's operating agreement. In brief, Valinote exited the LLC pursuant to a push-pull buy-sell provision under which Ballis, the other member of the LLC, set the price of the 50% interest that each held at a negative \$79,064. At the time, the LLC owed Valinote exactly that amount so that no money changed hands, and Ballis became the sole member of the LLC. When a bank pursued Valinote on his guaranty of LLC indebtedness, Valinote argued that he should be indemnified by Ballis. The court cited and discussed at length the terms of the operating agreement, contrasting the push-pull buy-sell provisions with provisions dealing with buy-out upon resignation of a member, and concluded that Valinote had no implied right of indemnification against Ballis. Valinote had a right against the LLC, but not against the other member. The court concluded that Valinote, as a former member, was not covered by a clause in the operating agreement that imposed cross-indemnity obligations between the members (interpreting "members" to include only current members). The court explained the negative price in terms of the increased risk each took by giving up the right of indemnification against the other.

Pine Creek, LLC v. Pine Mount, LLC, 558 S.E.2d 44 (Ga. App. 2001).

In this dissent and appraisal proceeding, the court examined the transfer restrictions in an LLC operating agreement and concluded that there were fact issues as to whether the operating agreement was violated.

ESCA of Baltimore, LLC v. Colkitt, 164 F. Supp.2d 584 (D. Md. 2001) (finding that there were fact issues as to whether an LLC member made a transfer of his membership interest for consideration in violation of transfer restrictions contained in the operating agreement).

Flippo v. CSC Associates III, L.L.C., 547 S.E.2d 216 (Va. 2001).

In addition to addressing breach of fiduciary duty and other issues in this case, the Virginia Supreme Court examined the meaning of two provisions in an LLC operating agreement relating to dissolution, continuation and purchase of a member's interest. Article 13 of the operating agreement provided for dissolution on the death, resignation, bankruptcy, or dissolution of a member unless the procedures of Article 9 were followed resulting in an election to continue the LLC. Article 9 provided that, on the death of a member, the remaining members could elect to purchase the interest of the deceased member or elect to continue the LLC. If the remaining members did not make "either of these elections" the LLC was dissolved. The court rejected the defendants' argument that the "election" referred to in Article 13 referred only to the election to continue and did not include the election to buy the departed member's interest. The court agreed with the trial court that either of the two elections referred to in Article 9 would result in continuation of the LLC. The court relied upon general rules of contract construction and considered the purposes of the parties and the circumstances surrounding execution of the operating agreement, including the terms of a restated partnership agreement drafted for the partnership that was the predecessor to the LLC. (The court went on to uphold sanctions imposed upon the parties who alleged fraud and mutual mistake with respect to the inclusion of these terms in the operating agreement. The sanctions were based upon the fact that the parties who claimed they were misled had the assistance of "experienced"

and “sophisticated” attorneys who specialize in this type of work. According to the trial court, it was “ridiculous” to say that the plaintiff could mislead such attorneys.)

Whitmore v. Hawkins, No. 99-1443, 2000 WL 828285 (4th Cir. June 27, 2000).

Whitmore was hired as chief operating officer of an LLC that operated fast food restaurants. He also received a 5% membership interest in the LLC and a 5% interest in a second LLC that was being formed to acquire additional fast food franchises. When Whitmore’s employment was terminated, he claimed that he was entitled to receive the value of his membership interests under provisions of the Maryland LLC act in effect at the time. The court pointed out that the statutory provisions relied upon by Whitmore were default provisions and that the operating agreements of the two LLCs had provisions addressing withdrawal and buy-out. The court concluded that the termination of Whitmore’s employment did not amount to a withdrawal or entitle Whitmore to receive the value of his interest under either of the operating agreements; therefore, Whitmore was not entitled to be bought out.

Oil and Grease on Wheels, Inc. v. Medicare Supply Co. of New England, No. C.A. 96-1789, 2000 WL 622584 (R.I. Super. April 26, 2000).

A receiver was appointed for Medicare Supply Co. of New England (“Medicare”), a member of a Rhode Island LLC. Medicare argued that appointment of the receiver constituted an event of dissociation under the LLC agreement which in turn entitled Medicare to be bought out under the agreement. Events of dissociation included a change in control of a member of the LLC. Control was defined under the agreement as an ownership interest sufficient to carry any motion, the right to elect or appoint directors or managers, or the right to manage. The court concluded that a change in control had occurred because the shareholders, directors, and officers of Medicare no longer controlled Medicare. The court stated that control did not have to shift to the receiver for a change in control to occur; it was sufficient that those formerly in control no longer had control. The court rejected the argument that the receiver was an assignee but did accept that the receiver was analogous to a judgment or lien creditor of Medicare. As a type of lien creditor, the court said the receiver succeeded to the rights of the dissociated member to be bought out.

Fausel v. JRJ Enterprises, Inc., 603 N.W.2d 612 (Iowa 1999).

JRJ Enterprises, Inc. (“JRJ”), a member of a Wyoming LLC involved in a Colorado casino operation, sued for anticipatory breach of a contract for the sale of JRJ’s membership interest in the LLC. The contract for the sale of the membership interest was captioned “Agreement for Sale of Stock” (“Stock Agreement”) and it contained a provision wherein JRJ warranted its membership units were not subject to any restrictions on transfer other than those set forth in the operating agreement or articles of organization of the LLC. This, the court concluded, incorporated by reference the provisions of the operating agreement restricting transfer of JRJ’s membership interest. Thus, interpretation of the Stock Agreement required the court to interpret restrictions on transfer in the LLC operating agreement as well. At issue were timing requirements of right of first refusal provisions in the operating agreement and requirements in the Stock Agreement regarding approval of the Colorado Gaming Division and closing of the sale. The court concluded that the deadline for closing the sale under the right of first refusal provisions did not constitute a deadline for purposes of the Stock Agreement because failure to close by that date would simply require that the membership interest would have to be offered to the LLC and remaining members again under the right of first refusal provision. Since the trial court had viewed the deadline under the right of first refusal provisions as the final deadline for performance of the sale under the Stock Agreement, the court remanded for further determinations relating to the anticipatory breach claim.

Donnelly v. Brown, Winick, Graves, Gross, Baskerville, Schoenbaum and Walker, P.L.C., 599 N.W.2d 677 (Iowa 1999).

A lawyer left his firm (a professional LLC) and went to another firm, and there was a dispute over the provision of the operating agreement dealing with benefits to be paid to a retiring member. The specific issue on appeal was whether the “continuation payments” under the operating agreement qualified as “retirement benefits” under Iowa DR 2-108(A). The payments were conditioned on the lawyer’s termination of the private practice of law in Iowa. The lawyer argued that this was an impermissible covenant not to compete. The court concluded that the provisions in this case (requiring ten years of service and sixty years of age or twenty-five years of service) clearly constituted a retirement plan, and the restriction on future practice was therefore valid, even though the plan applied to situations involving less than full retirement.

Lusk v. Elliott, No. Civ. A. 16326, 1999 WL 644739 (Del. Ch. Aug. 13, 1999).

An LLC member (“Elliott”) assigned his 99% interest in the LLC to a family trust, and the 1% member (“Lusk”) claimed that he was the sole remaining member and manager on the basis that the assignment was not effective to transfer

membership rights. The court determined that the assignment transferred Elliott's membership along with his 99% financial interest. The operating agreement prohibited assignment of a member's interest other than to another member; however, both members signed a consent to the transfer of Elliott's 99% membership interest and agreed that the assignment would not constitute a prohibited assignment under the operating agreement. The parties agreed that the consent amended the prohibition on transfer in the operating agreement but disagreed as to whether the consent authorized the conveyance of Elliott's membership along with the financial interest. Lusk relied upon the Delaware LLC act provisions that characterize an assignment as carrying only the financial interest of the member. Since the operating agreement did not define "assignment," Lusk argued the court should look to the Delaware act for the effect of an assignment. The court disagreed. The court said that the consent and assignment indicated what was meant by the term "assignment" since the instruments referred to assignment of Elliott's "entire undivided membership interest." The court concluded that this language encompassed Elliott's membership as well as his 99% ownership interest.

Sherrets v. The Lund Company, No. A-97-1350, 1999 WL 502138 (Neb. App. July 6, 1999).

An LLC member who was bought out pursuant to a push-pull provision in the LLC operating agreement claimed that he was entitled to a portion of net rental income held by a third party under a property management agreement at the time of the closing of the sale of the member's interest. The court examined the provisions of the operating agreement and the property management agreement and agreed that the member was entitled to recover a portion of the net rental. The court viewed the member as a third party beneficiary of the property management contract executed by the LLC and disagreed with the defendant's argument that the member assigned his interest in the disputed funds when he sold his interest in the LLC.

Clark v. Kelly, No. C.A. 16780, 1999 WL 458625 (Del. Ch. June 24, 1999).

This case was a dispute over who were the managers of a Delaware LLC, and the determinative issue was whether the transfer of all of the shares of a corporate member of the LLC to a trust was a "transfer" of an LLC interest within the meaning of the operating agreement. Plaintiff Clark, the sole shareholder of one of the members of the LLC claimed to be the sole manager of the LLC. The other member of the LLC was La Empresa De La Mar D'Oro, Inc. ("La Empresa"), a California corporation. The stock of La Empresa was titled in Danis at the time La Empresa became a member of the LLC. After formation of the LLC, Danis transferred the stock of La Empresa to a living trust of which Danis and his wife were the trustors and co-trustees. The issue was whether the transfer of the shares to the trust triggered a provision of the operating agreement requiring consent. If the transfer requiring consent occurred without such consent, the transferee's status was that of a mere assignee. The definition of "transfer" under the operating agreement included a transaction whereby the equity owners of a member as of the date of the member's admission to the LLC own less than 90% of the equity securities of the member after the transaction. The court determined that the transfer of the shares of La Empresa to the trust did not fall within the definition of a transfer under the operating agreement because the shares were community property under California law and Danis's wife therefore had a 50% equitable interest in the shares before the transfer to the trust. The court rejected the plaintiff's argument that the Delaware choice of law clause in the operating agreement, together with the internal affairs doctrine, required Delaware law to apply to the determination of ownership of the shares of La Empresa. According to the court, "Even if the choice of law provision in the Operating Agreement were found to govern, the internal affairs doctrine – which is a well-established principle of Delaware substantive law – requires this Court to look to the law of the state of incorporation to determine the relationships between the corporate entity and its directors, officers, and stockholders. . . . Because La Empresa is a California corporation, . . . this Court would be required to look to California law in all events to determine who are the equity owners of La Empresa."

March Trading, Inc. v. Sloan, 25 Conn.L.Rptr. 339, 1999 WL 732955 (Conn. Super. Aug. 30, 1999).

The plaintiff brought a bill of discovery action against a member of an LLC seeking sworn copies of the member's membership certificate giving notice of a pledge of the membership interest. Under an agreement between the member and the plaintiff, the member was to pledge a 20% LLC interest as partial security for a promissory note. The agreement also required the member to place a legend on the certificate indicating that the interest had been pledged. When the member refused to provide the plaintiff proof that the language had been placed on the certificate, the plaintiff brought this action. The court found that the plaintiff was entitled to maintain the bill of discovery seeking proof of compliance with the agreement.

Five Star Concrete, L.L.C. v. Klink, 693 N.E.2d 583 (Ind. App. 1998).

The court determined that a dissociating member of an LLC had no right under the LLC's operating agreement or the Indiana LLC act to receive a distribution of income allocated to the member for tax purposes, but the court refused

to render summary judgment on the issue of whether the buy-out of the dissociating member divested the member of its entire economic interest in the LLC, in part because the meaning of the term “units” was not clear under the operating agreement. Klink, Inc. (“Klink”) and four other corporations formed an LLC. Klink withdrew from the LLC, and the remaining members decided to purchase Klink's ownership units and continue the business. The members agreed that Klink would receive \$61,047.22 for the value of Klink's “units.” After the end of Klink's fiscal year, Klink was allocated its share of the LLC's income for the portion of the year that Klink was a member. Klink asserted that it was entitled to a distribution in this amount. The court concluded that neither Indiana law nor the operating agreement gave a member a right to a distribution of income allocated to the member for income tax purposes. The remaining issue involved the meaning of the term “units” inasmuch as Klink's units were bought out on its withdrawal. The LLC contended that Klink divested itself of its entire interest when it sold its units to the LLC. Klink argued that it sold less than all of its economic rights. Klink pointed to the operating agreement reference to a unit as “an interest in the Company representing a contribution to capital.” The LLC pointed out, however, that the operating agreement generally entitled each unit to a vote and a proportionate share of the LLC's net income, gains, losses, deductions, and credits. The court concluded that fact issues precluded resolution of this issue by summary judgment. The court addressed as a separate issue the valuation method and whether it represented the fair market value of Klink's entire interest. The court concluded that summary judgment was not appropriate on this issue either.

Y. Improper Distributions

In re IDS Holding Co., LLC (IDS Holding Co., LLC v. Madsen), 292 B.R.233 (Bankr. D. Conn. 2003).

A bankrupt LLC, in its capacity as debtor-in-possession, sought to recover a distribution made to its dominant member (Madsen) in connection with the sale of substantially all of the LLC's assets. The LLC was insolvent at the time of the sale, and all of the proceeds of the sale (consisting of shares of stock in the purchaser) were distributed to the members in accordance with their interests. The LLC's members had an agreement about the distribution of the proceeds of the sale whereby the members pledged some of the shares they received for the benefit of certain LLC creditors and Madsen agreed to dismiss a pending lawsuit against one of the LLC's suppliers and another member. The LLC claimed that the distribution violated the Connecticut LLC act, was a fraudulent transfer under the Bankruptcy Code and the Connecticut Uniform Fraudulent Transfer Act, was a voidable preference under the Bankruptcy Code, and was a breach of Madsen's fiduciary duty as a member of the LLC to its creditors. Madsen argued the transfer was supported by consideration and that he was entitled to summary judgment. The LLC argued that Madsen's receipt of the shares violated the provisions of the Connecticut LLC act regarding the distribution of assets on a winding up. However, the court found this provision inapplicable because the LLC had not dissolved and was not in the process of winding up. The LLC conceded that the Connecticut LLC act does not prohibit an insolvent LLC from distributing its assets to its members, but the LLC argued that the court was permitted to apply corporate law restrictions under the provision of the LLC act that provides the principles of law and equity supplement the act. The court concluded that it need not address this argument because the LLC conceded that it had never actually dissolved. Thus, the court granted Madsen summary judgment on the claim that the distribution violated the Connecticut LLC statutes. The court found that there were fact issues regarding whether the distributions were made with intent to hinder or delay LLC creditors and whether Madsen gave reasonably equivalent value. Madsen argued that the distribution could not be a voidable preference because he was only an equity owner and not a creditor or claim holder. The court concluded that Madsen was a creditor by virtue of the distribution agreement and the Connecticut LLC act, which states that a member has the status of a creditor at the time a member becomes entitled to a distribution. Finally, the court applied case law from the corporate context to conclude that Madsen owed a fiduciary duty to LLC creditors when the LLC became insolvent.

In re Brentwood Lexford Partners, L.L.C., 292 B.R. 255 (Bankr. N.D. Tex. 2003).

The Chapter 7 trustee brought an adversary proceeding to set aside alleged fraudulent transfers. The court held that certain excess cash flow distributions to the members of an LLC engaged in the property management business were fraudulent transfers because they were made with the intent to hinder and delay collection of a note owed by the LLC. The court rejected the argument that the distributions were in the nature of compensation for services of the members. The court noted that there were no employment contracts providing that excess cash flow distributions would be part of their salary or bonus, no funds withheld from the distributions for income tax purposes, and no board resolutions treating the excess cash flow as salary or bonus. The LLC's major creditor, which held a note permitting the excess cash flow distributions, did not consider the distributions as compensation, but rather considered the distributions to be dividends or payments on account of the equity interests of the members. The court thus concluded that the LLC did not receive reasonably equivalent value for the distributions. (This case is further summarized above under the heading “Fiduciary Duties” and below under the heading “Fraudulent Transfer.”)

Dover Place, LLC v. Coffey, No. A098399, 2003 WL 178832 (Cal.App. Jan. 28, 2003) (concluding that member was not required to return distribution because it did not violate statutory restrictions and operating agreement could not reasonably be interpreted to impose greater restrictions than statute).

Imperial Trading Co., Inc. v. Uter, 837 So.2d 663 (La.App. 2002)(affirming trial court's finding that manager was personally liable, along with member, for assenting, without reasonable care or inquiry, to distribution to member while LLC was unable to pay its debts as they came due and that other manager was not liable where evidence supported his lack of knowledge of the distribution, but reversing trial court's finding on other payments on basis record did not support imposing liability for checks payable to manager without evidence that they were distributions or that such a distribution violated the statutory restrictions).

In re Chicago Trading Group, Inc. (Fogel v. Spike Trading, L.L.C.), Nos. 97 B 19843, 99 A 00410, 2001 WL 40071 (Bankr. N.D. Ill. Jan. 17, 2001).

A bankruptcy trustee sued an LLC and its members seeking to recover from the members improper distributions made during the winding up of the LLC. The parties agreed that under Illinois law an LLC member may be liable for a dissolved LLC's debts to the extent of any improper distributions received. The trustee argued that he had a direct cause of action against the LLC members resulting from improper distributions, but the court agreed with one of the LLC members that the trustee could only recover in supplementary proceedings after obtaining a judgment against the LLC. Since the trustee had not obtained a judgment against the LLC, the claim against the member failed. Additionally, the court stated that the trustee would have to identify property of the debtor held by the member and the value of the property.

Z. Equity Compensation Agreements

Aggarwal v. Nexabit Networks, Inc., No. CIV.A. 99-6174, 2001 WL 34032503 (Mass.Super. May 30, 2001).

An LLC employer sought summary judgment against an at-will employee on the employee's breach of covenant of good faith and fair dealing claim. On three occasions, the employee was granted shares in the LLC subject to certain conditions and a vesting schedule under an Equity Incentive Plan. Shortly before the date on which some of the shares would have vested, the employee was terminated. The court found that these shares, as well as shares that were apparently awarded for past work on a patent, were compensation already earned that could support a claim for breach of the implied covenant of good faith and fair dealing. The court concluded that other shares could not be considered compensation for past services and would not support a claim for breach of the covenant of good faith and fair dealing.

AA. Dissolution and Dissociation

1. Accounting

Yakima Medical Group, LLC v. Khan, M.D., No. 20718-1-III, 2003 WL 1962786 (Wash.App. April 29, 2003).

Three doctors formed an LLC. When disputes arose, two of them voted to remove the third, Khan, as president and Chief Clinical Officer. Khan tried to persuade the employee doctors that they were employed by him personally rather than the LLC and had the locks changed at the clinic where the records and assets of the LLC were located. He instructed the employees not to allow the other two members or the employee doctors on the premises. The other two members brought suit seeking an injunction and damages and removal of Khan as a member. The court upheld an injunction against Khan enjoining him from harassing the doctors, taking payments for services rendered by the LLC, and obstructing access to patient charts, other records, and medical equipment. The court also found that the trial court did not err in the date it used for an accounting. Khan argued that the trial court should have used the date on which he was removed from the LLC as president, but the court pointed out that he was not dissociated as a member on that date, and the Washington LLC act does not specify how a final accounting date for an LLC is determined. The court said the act indicates that a member is dissociated either 90 or 120 days after legal action is taken. Although the date the trial court used was earlier than this, the court found it was nevertheless appropriate under the circumstances. The court stated that Khan had suggested a final accounting date that preceded legal action for dissociation, and the documents available to the court valued the assets as of the date used by the court. The court indicated that Khan's activities after that date negatively impacted the LLC and its profitability and stated that he had not shown the court's determination was error.

2. Bankruptcy

In re Farmland Industries, Inc. (Farmland Industries, Inc. v. SF Phosphates Co.), ___ B.R. ___, 2003 WL 1950004 (Bankr. W.D. Mo. April 23, 2003).

The debtor and another entity (Simplot) formed a Utah LLC owned 50% by each. Simplot filed a complaint for declaratory judgment determining that the debtor ceased to be a member of the LLC due to its bankruptcy filing and was reduced to the status of an assignee with no right to participate in the management and affairs of the LLC and no right to assume or assign the operating agreement. The debtor counterclaimed for declaratory relief seeking judicial dissolution. The court characterized both claims as essentially seeking judicial dissolution and stated that all of the issues raised were “to be determined by Utah state law” and that there were “no real bankruptcy issues involved.” The court determined that the dispute was not a core proceeding nor was it “related to” bankruptcy. The court also considered the appropriateness of discretionary abstention and concluded that abstention was the proper course. The court noted that there appeared to be unsettled issues of state law and little reported case law on judicial dissolution of a Utah LLC. The court felt bound by principles of comity to permit a court in Utah to resolve these unsettled issues. The court also found it significant that the operating agreement contained a forum selection clause designating state and federal courts in Utah as the forum for any actions arising out of the agreement.

In re Garrison-Ashburn, L.C., 253 B.R. 700 (Bankr. E.D. Va. 2000).

In this case, a member of a Virginia LLC filed bankruptcy, and the court concluded that the LLC operating agreement was not an executory contract and thus not within the provisions of Bankruptcy Code § 365(c) and (e) preventing enforcement of certain ipso facto clauses. The court explained the history of and reasons for amendments to the Virginia LLC act that eliminated reference to events that would automatically dissolve an LLC. Pursuant to the amendments, events that formerly triggered dissolution became events of dissociation. Under the amended statute, the bankruptcy of a member results in dissociation, and the dissociated member stands in the same relationship to the LLC as an assignee of a membership interest. The court distinguished the *DeLuca* and *Broyhill* cases as having been decided prior to the check the box regulations and changes to the Virginia statute. The court pointed out that this case did not involve an entity whose organic documents or enabling statute dissolved the LLC on the member’s bankruptcy, and the operating agreement merely provided for the management structure of the LLC. It imposed no additional duties or responsibilities on members and permitted a member to resign from all offices and committees at any time without breaching the agreement. The court stated that such a person would stand in an analogous position to the LLC as a shareholder to a corporation. Under these circumstances, the court said, there is no executory contract.

In re DeLuca (Broyhill v. DeLuca), 194 B.R. 65 (Bankr. E.D. Va. 1996).

The DeLucas were real estate developers who were members of D & B Countryside, L.L.C., a Virginia LLC. The LLC operating agreement provided, consistent with the Virginia LLC statute, that bankruptcy of a member dissolved the LLC unless the remaining members elected to continue the business of the LLC. If the bankrupt member were also the only manager, the remaining members could elect a new manager. After the DeLucas filed bankruptcy, the remaining members voted to continue and replaced them as managers. The DeLucas claimed that the provisions of the operating agreement permitting this action were unenforceable under the United States Bankruptcy Code. The court, like the court in *Daugherty*, concluded that the operating agreement was an executory contract. However, the court found that the provisions triggering dissolution upon a member's bankruptcy and granting remaining members the right to continue the business and elect a new manager were enforceable because the operating agreement was a personal service contract that could not be assumed over the objections of the other members under Section 365 of the Bankruptcy Code. (In *In Re Garrison - Ashburn, LC*, 253 B.R. 700 (Bankr. E.D. Va. 2001), the court distinguished this case as having been decided prior to changes to the Virginia LLC act.)

In re DeLuca (JTB Enterprises, L.C. v. D & B Venture, L.C.), 194 B.R. 79 (Bankr. E.D. Va. 1996).

The second DeLuca decision addressed the ramifications of the DeLuca bankruptcy with respect to D & B Venture, L.C. ("D & B"), a Virginia LLC whose members were two other LLCs, R & M Kiln Creek, L.C. ("R & M") and JTB Enterprises, L.C. ("JTB"). R & M was the manager of D & B, and the sole members of R & M were Robert and Marilyn DeLuca. JTB argued that the bankruptcy of the DeLucas dissolved R & M, which in turn dissolved D & B, and conferred upon JTB, as the sole remaining member, the right to wind up D & B's affairs. The D & B operating agreement provided that D & B would be dissolved upon certain events, including dissolution or bankruptcy of either of its members, and that the manager would liquidate the affairs of D & B upon dissolution. The court agreed with JTB that the bankruptcy of the DeLucas dissolved R & M. The dissolution of R & M in turn dissolved D & B. However, the court determined that the terms of the operating agreement vesting the right to liquidate D & B in the manager should

control and that R & M thus had the right to wind up D & B's affairs as well as its own affairs. (Though R & M, rather than the DeLucas, held the membership interest in D & B, the court engaged in its analysis, at least in part, as if the DeLucas owned their interest in D & B directly, stating that it was appropriate to "disregard the form of the DeLucas' interest in D & B Venture and to look to the substance." The court noted that the DeLucas did not even list their interest in R & M on their schedules, and the court characterized R & M as little more than a "conduit or shell" of the DeLucas whose function was holding "technical title to what [was] in substance the DeLucas' interest in D & B Venture." The R & M operating agreement provided that R & M would be dissolved upon the bankruptcy of a member, and there were no other members to object to the assumption of its management by the DeLucas regardless of whether the operating agreement was considered a personal service contract. Though the DeLucas had not taken any steps to assume the R & M operating agreement, the only purpose of doing so would be to continue, through it, the management of D & B. The court found no policy that protected R & M from its own dissolution since it was not itself in bankruptcy.) (In *In Re Garrison - Ashburn, LC*, 253 B.R. 700 (Bankr. E.D. Va. 2001), the court distinguished this case as having been decided prior to changes to the Virginia LLC act.)

Matter of Daugherty Construction, Inc., 188 B.R. 607 (Bankr. D. Neb. 1995).

The bankruptcy court held that a Chapter 11 bankruptcy filing by a member of two Nebraska LLCs did not terminate the membership of the debtor member and dissolve the LLCs even though the Nebraska LLC statute and the articles of organization and operating agreements of each LLC provided that the LLC would be dissolved upon the bankruptcy of a member. The court first concluded that the LLC membership interests constituted property of the bankruptcy estate and that any provisions of state law or the LLC articles of organization or operating agreements purporting to dissolve the LLC and terminate the debtor's membership interest were unenforceable under Section 541(l) of the Bankruptcy Code. The court also found Section 365(l) of the Bankruptcy Code applicable. That provision voids any provision in a contract or applicable state law that forfeits, modifies, or terminates the debtor's interest in property based upon the insolvency or financial condition of the debtor or the commencement of a bankruptcy case. Finally, the court found that the articles of organization and operating agreements were executory contracts that could be assumed by the debtor in possession under Section 365 of the Bankruptcy Code and that Section 365(e) prevented the termination or modification of the articles of organization and operating agreements any time after the commencement of the bankruptcy solely because of a provision conditioned upon insolvency or bankruptcy.

3. Expulsion or Termination of Member

River Links at Deer Creek, LLC v. Melz, No. M2002-00043-COA-R3-CV, 2002 WL 31890897 (Tenn.Ct.App. Dec. 31, 2002).

Under the terms of its operating agreement, River Links at Deer Creek, LLC ("River Links") dissolved upon the administrative dissolution of Deer Creek Golf Interests, LLC ("Deer Creek"), a member of River Links, for failure to file required annual reports. After the administrative dissolution, the remaining members of River Links voted to continue its business, amend the operating agreement, redeem the interest of Deer Creek, and remove Melz (Deer Creek's "principal") from the Board of Managers of River Links. After these actions, Deer Creek was reinstated. Melz argued that the retroactive nature of the reinstatement rendered the actions taken by the other members of River Links after the administrative dissolution invalid. Melz also sought to arbitrate the claims because the operating agreement of River Links contained an arbitration clause. The court held that the trial court should retain jurisdiction of the issue because of the lack of LLC case law. "An arbitrator dealing with the complex facts of this case would have no guidance on the proper interpretation of the Limited Liability Company Act, and would have to expend a great deal of time and energy to reach a well-considered conclusion, but his ultimate decision would have no precedential value." It thus appeared reasonable to the court for the trial court to retain jurisdiction over the declaratory judgment claim.

Baker v. Jones & Henry Engineers, LTD, No. L-00-1198, 2001 WL 304088 (Ohio App. March 30, 2001).

A member of an engineering firm LLC sued for wrongful termination after the other members voted to terminate his employment and demanded he resell his membership interest. The plaintiff argued that termination of his employment was wrongful because the operating agreement and membership interest subscription agreement contractually obligated the LLC to retain him. The member based this argument on the inclusion of the phrase "long-term investment" in each of these agreements, which the member asserted was evidence that a member was entitled to employment until he voluntarily left the firm or retired. The court concluded that there was no evidence of an express or implied contract in this regard. The court also rejected other arguments based upon promissory estoppel, public policy, and fraud.

Walker v. Resource Development Company Limited, L.L.C., 791 A.2d 799 (Del. Ch. 2000).

Walker, a first cousin of former President Bush, was brought in as a member of a Delaware LLC in order to utilize his connections and reputation to help the LLC secure needed financing. After Walker failed to secure financing and the other members became concerned about Walker's drinking problem, financial irresponsibility, and other matters, he was relieved of his official duties for a period of time. He was later given his job back, and the members entered into a formal operating agreement designating Walker as an 18% member. Ultimately, however, the relationship soured completely, and the other members purported to remove him as a member and terminate his ownership interest. The members referred to Walker's poor performance and misconduct in the written notice of his removal, but there was also a dispute over whether Walker had a side deal that constituted a conflict of interest. The court concluded that the other members had no authority to remove Walker as a member either under the Delaware LLC act or the operating agreement. The court rejected the argument that the members had the inherent power to remove Walker and deprive him of his ownership interest based upon his alleged breach of fiduciary duty. Although the court recognized that there was a relationship of sufficient trust and confidence to impose on Walker a duty to disclose a material fact such as a conflict of interest, the court concluded that the members did not rely on any understanding that Walker was independent in entering into the operating agreement. Thus, the court rejected the members' misrepresentation claim against Walker. The court also rejected the members' claim that they were protected from liability for their effort to appropriate Walker's interest based upon a good faith reliance on the operating agreement. After purporting to remove Walker, a series of financing transactions led to the exchange of the members' membership interests in the LLC into shares of a Canadian corporation. Walker failed to prove the value of his 18% interest in the LLC, thus there was no basis for an award of damages; however, the court imposed a constructive trust in Walker's favor upon 18% of the shares the other members had received in the Canadian corporation.

Whitmore v. Hawkins, No. 99-1443, 2000 WL 828285 (4th Cir. June 27, 2000).

Whitmore was hired as chief operating officer of an LLC that operated fast food restaurants. He also received a 5% membership interest in the LLC and a 5% interest in a second LLC that was being formed to acquire additional fast food franchises. When Whitmore's employment was terminated, he claimed that he was entitled to receive the value of his membership interests under provisions of the Maryland LLC act in effect at the time. The court pointed out that the statutory provisions relied upon by Whitmore were default provisions and that the operating agreements of the two LLCs had provisions addressing withdrawal and buy-out. The court concluded that the termination of Whitmore's employment did not amount to a withdrawal or entitle Whitmore to receive the value of his interest under either of the operating agreements, thus Whitmore was not entitled to be bought out.

Gee v. Bullock, 1996 R.I. Super. 941, 1996 WL 937009 (R.I. Super. Nov. 16, 1996).

Two members of an LLC sued the third member, Bullock, seeking injunctive relief barring Bullock from operating the LLC and permitting them to carry on the business. Bullock sought dissolution and an accounting. The court found that Bullock made fraudulent representations when she claimed to have sole ownership of an existing business into which she induced the plaintiffs to invest and when she promised to sign an operating agreement giving the plaintiffs a fifty-one percent controlling interest in their newly formed LLC. In fact, another individual had a substantial interest in the business Bullock claimed to own, and Bullock later refused to sign the operating agreement for the new LLC. Ultimately, Bullock locked the other two members out of the business premises and transferred the assets of the LLC to a new corporation formed by Bullock and yet another investor. The court concluded that the LLC dissolved when Bullock wrongfully excluded/expelled the other two members from the business and that the LLC could only continue for winding up purposes. Thus, the court denied the plaintiffs' requested injunctive relief. The court went on to discuss the fraudulent nature of the transfer of the LLC's assets to Bullock's new corporation under Rhode Island's Uniform Fraudulent Transfer Act. Finally, the court appointed an attorney to conduct the winding up of the LLC because Bullock, having wrongfully caused the dissolution of the LLC, was not entitled to participate in the winding up of the LLC's affairs.

4. Sharing of Post-Dissolution Profits

Hurwitz v. Padden, 581 N.W.2d 359 (Minn. App.1998).

The court in this case applied partnership law to determine how fees from contingent fee files should be divided between the members of a dissolved LLC law firm. Hurwitz and Padden formed a two-person law firm in 1991. In 1993, articles of organization were filed, and the firm became a limited liability company. In 1996, the parties dissolved the firm and successfully resolved all issues except the division of fees from several contingent fee cases. The parties had no written agreement on the allocation of fees, but prior to dissolution the parties shared all firm proceeds on a 50-50

basis. Since the Minnesota LLC act borrowed the concept of dissolution from the UPA, the court concluded that it was appropriate to apply partnership law to resolve the issue at hand. Specifically, the court concluded that “partnership principles, including the ‘no-compensation’ rule’ [under which partner other than surviving partner has no right to compensation for services rendered in furtherance of partnership business in winding up stage], govern the division of fees obtained from pre-dissolution contingency files.” Thus, the court held that the fees should be split equally, consistent with the pre-dissolution method of allocation of fees. The court noted by way of footnote the change to Minnesota partnership law made by RUPA effective 1/1/99 whereby a partner is entitled to reasonable compensation for services rendered in winding up the business of the partnership.

5. Judicial Dissolution/Appointment of Liquidator

In re Farmland Industries, Inc. (Farmland Industries, Inc. v. SF Phosphates Co.), __ B.R. __, 2003 WL 1950004 (Bankr. W.D. Mo. April 23, 2003).

The debtor and another entity (Simplot) formed a Utah LLC owned 50% by each. Simplot filed a complaint for declaratory judgment determining that the debtor ceased to be a member of the LLC due to its bankruptcy filing and was reduced to the status of an assignee with no right to participate in the management and affairs of the LLC and no right to assume or assign the operating agreement. The debtor counterclaimed for declaratory relief seeking judicial dissolution. The court characterized both claims as essentially seeking judicial dissolution and stated that all of the issues raised were “to be determined by Utah state law” and that there were “no real bankruptcy issues involved.” The court determined that the dispute was not a core proceeding nor was it “related to” bankruptcy. The court also considered the appropriateness of discretionary abstention and concluded that abstention was the proper course. The court noted that there appeared to be unsettled issues of state law and little reported case law on judicial dissolution of a Utah LLC. The court felt bound by principles of comity to permit a court in Utah to resolve these unsettled issues. The court also found it significant that the operating agreement contained a forum selection clause designating state and federal courts in Utah as the forum for any actions arising out of the agreement.

Rubin v. Wright, No. 398112, 2002 WL 31954879 (Conn.Super. Dec. 30, 2002) (denying LLC member’s application for injunction to prevent dissolution of LLC investment banking firm where plaintiff conceded dissolution was inevitable, and there was no reason to believe the plaintiff’s interest in the LLC would not be protected in judicial dissolution).

In re Extreme Wireless, LLC, 750 N.Y.S.2d 520 (N.Y.A.D. 2 Dept. 2002).

The court stated that the appropriateness of an order of dissolution of an LLC is a matter vested in the sound discretion of the trial court and that the lower court had properly exercised its discretion in granting the petition for dissolution on the basis that it was no longer reasonably practicable to carry on the business of the LLC in conformity with the articles of organization or operating agreement. The court also upheld the trial court’s denial of an injunction prohibiting the petitioner from opening a competing business in violation of the LLC operating agreement’s covenant not to compete. The court stated that the dissolution rendered the injunctive relief academic because “there is no longer a company in existence with which to compete.”

In re Pontchartrain Plaza, No. 02-CA-54, 2002 WL 1066924 (5th Cir. May 29, 2002) (looking to corporate dissolution provisions for guidance on effect of initial ex parte order ordering LLC’s dissolution (which court concluded merely commenced the dissolution process) and rejecting member’s challenge to ex parte order where member was then served with petition and order, had opportunity to present defenses to dissolution at hearing, and did not contest factual allegations that LLC had failed to achieve its objective, LLC was out of money and members could not agree on how to carry out business, thus rendering it not practicable to carry on the business).

Reig v. Amore II, L.L.C., 31 Conn. L. Rptr. 620, 2002 WL 819080 (Conn. Super. 2002) (granting member’s request for dissolution and appointment of person to wind up LLC’s affairs over other member’s objections, concluding that inability of equal members to work together constituted “other cause” for judicial winding up under the statute).

Cogniplex, Inc. v. Ross, Nos. 00 C 7463, 00 C 7933, 2002 WL 483411 (N.D. Ill. March 29, 2002) (interpreting Illinois LLC act provisions providing for LLC’s opportunity to buy out dissociating member’s interest and requiring dissolution of LLC if LLC fails to comply with buy out procedures and concluding that claim for dissolution was stated where purchase offer was not made within time-frame required by statute).

Weinmann v. Duhon, 818 So.2d 206 (La. App. 2002) (interpreting operating agreement provisions that created impasse (because one faction could fire general manager while other faction could re-hire him) and stating such a situation was precisely one where judicial dissolution is authorized on basis that it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement).

Lindsay, Marcel, Harris & Pugh, L.L.C. v. Harris, 752 So.2d 335 (La. App. 2000).

Harris and Pugh gave notice of their withdrawal from their four member law firm LLC and formed their own law firm. When the LLC filed suit against the withdrawn members, the withdrawn members answered and sought dissolution. The court of appeals determined that the withdrawn members had no right to seek judicial dissolution because the statute conferred no such right on former members. In addition, the court found no basis in the operating agreement for the withdrawn members to obtain dissolution. Included among the causes of dissolution listed in the operating agreement was “reduction in the number of Members to 1,” but the court pointed out that two members remained after the withdrawal of the other members.

McConnell v. Hunt Sport Enterprises, 725 N.E.2d 1193 (Ohio App. 1999).

The court determined that judicial dissolution of the LLC in this case on the basis that it was no longer reasonably practicable to carry on the business in conformity with the LLC’s articles of organization and operating agreement was not “wrongfully caused” by the member who acted wrongfully in breaching the operating agreement and usurping control of the LLC. The reason it was no longer practicable to carry on the business was the LLC’s failure to obtain the hockey franchise it sought rather than the wrongful conduct of a member. Thus, no member was precluded from participating in the winding up by the terms of the operating agreement that allowed only members who have not wrongfully caused dissolution to participate in winding up. The issue was moot, however, because there was a liquidating trustee appointed by the court.

Investcorp, LP v. Simpson Investment Company, L.C., 983 P.2d 265 (Kan. 1999).

The court’s analysis of the meaning of the term “member” in the operating agreement is discussed above. After concluding that “members” entitled to participate in winding up included withdrawing members, the court addressed the request of the withdrawing members for appointment of a receiver. The withdrawing members claimed that the current members were incompetent to conduct the liquidation of the LLC. The court denied the withdrawing members’ request for a receiver, characterizing the allegations of incompetence as “minor” and insufficient, even if proved, to warrant appointment of a receiver. The court noted that there were no allegations of fraud, breach of fiduciary duty or waste, nor a showing of “good cause.”

Suntech Processing Systems, L.L.C. v. Sun Communications, Inc., No. 05-98-00799-CV, 1998 WL 767672 (Tex. App. Nov. 5, 1998).

In this case, a member of two LLCs claimed that a proposed transfer of funds by one LLC to the other would constitute a fraudulent transfer. The trial court in the case entered an injunction against the payment and ordered the LLCs dissolved under the statutory provision that an LLC may be judicially dissolved if it is not reasonably practicable to carry on the business of the LLC in conformity with its articles of organization or regulations. The trial court appointed a liquidator under another statutory provision authorizing the court to wind up an LLC’s affairs or appoint a person to carry out the liquidation. The liquidator was given control of the two LLCs and had essentially all of the powers of a receiver. The court of appeals concluded that the order appointing a “liquidator” was an order appointing a “receiver;” therefore, the court had jurisdiction over the interlocutory appeal. The court held that the order of judicial dissolution and appointment of a liquidator was improper in this case as it did not properly preserve the subject matter of the suit until the trial court could finally determine whether the payment would be a fraudulent transfer. In other words, the court found the trial court’s order was improper because it gave the LLC member its ultimate relief.

6. Winding Up

Josey v. George, No. CV010810269, 2003 WL 231665 (Conn.Super. Jan. 9, 2003) (making findings of fact and conclusions of law in aftermath of dissolution of LLC, which the parties and the court referred to intermittently as a partnership).

Rubin v. Wright, No. 398112, 2002 WL 31954879 (Conn.Super. Dec. 30, 2002) (denying LLC member’s application for injunction to prevent dissolution of LLC investment banking firm where plaintiff conceded dissolution

was inevitable, and there was no reason to believe the plaintiff's interest in the LLC would not be protected in judicial dissolution).

Bio-Septic Systems, LLC v. Weiss, 60 P.3d 943 (Mont. 2002).

Weiss, Cullinan, and others formed an LLC to market a device invented by Weiss. Acrimonious relations developed between Cullinan and the other members. The LLC eventually collapsed, and Weiss ultimately assumed management. Weiss informed Cullinan that he intended to dissolve the LLC and disburse the assets as required by law. Cullinan accused Weiss of wrongdoing in connection with certain payments and Weiss's commencing work for a company with which the LLC had previously contracted for marketing of the device. Cullinan brought suit for dissolution of the LLC and accused Weiss of breach of fiduciary duty. Weiss counterclaimed and joined in the request for dissolution. Cullinan filed an amended complaint alleging sole ownership to the LLC and waiving any further winding up. The court found that Weiss had acted properly in the winding up pursuant to agreements made by the members. Cullinan challenged the lower court's finding that an experimental prototype unit produced by the LLC belonged to Cullinan and was the responsibility of Cullinan. The court upheld the lower court's action, as it was consistent with positions taken by both Cullinan and Weiss in the proceedings.

Newman v. McLean, No. B152794, 2002 WL 31117064 (Cal. App. Sept. 25, 2002) (dismissing member's cross-claim for indemnity against co-defendant and former co-member of dissolved LLC in suit by other members on basis that member from whom indemnity was sought entered good faith settlement with plaintiffs, and dismissing breach of contract and fraud claims on basis of release executed at time of dissolution of LLC).

Benchmark Investments, LLC v. Elms at Mystic, LLC, No. 555579, 2002 WL 194492 (Conn. Super. Jan. 11, 2002) (striking claim against LLC and member based on statute permitting claims against dissolved LLC or member of dissolved LLC to extent of assets distributed in liquidation where plaintiff failed to allege LLC was dissolved but rather alleged that LLC was "at all relevant times a Connecticut limited liability company").

Regenstein v. Simon, No. CV980169421, 2001 WL 1378761 (Conn. Super. Oct. 17, 2001).

The two members of a dissolved LLC asserted various claims against each other. As the court summed up the relevant events, "[T]he defendant advised the plaintiff of her decision to immediately dissolve or terminate the company, and thereafter both parties embarked on courses of conduct aimed at maximizing their own personal interests instead of engaging in an orderly and cooperative winding down of the company." The court declined to apportion blame between the two parties and merely divided the remaining funds of the LLC between the two members in accordance with their percentage ownership interests. (At least, this appears to be what the court intended. There was an apparent typographical error in the percentages recited in dividing the remaining funds.)

In re Chicago Trading Group, Inc. (Fogel v. Spike Trading, L.L.C.), Nos. 97 B 19843, 99 A 00410, 2001 WL 40071 (Bankr. N.D. Ill. Jan. 17, 2001).

A bankruptcy trustee sued an LLC and its members seeking to recover from the members improper distributions made during the winding up of the LLC. The parties agreed that under Illinois law an LLC member may be liable for a dissolved LLC's debts to the extent of any improper distributions received. The trustee argued that he had a direct cause of action against the LLC members resulting from improper distributions, but the court agreed with one of the LLC members that the trustee could only recover in supplementary proceedings after obtaining a judgment against the LLC. Since the trustee had not obtained a judgment against the LLC, the claim against the member failed. Additionally, the court stated that the trustee would have to identify property of the debtor held by the member and the value of the property.

Skyline Partners, LLC v. Easley, No. 03-99-00602-CV, 2000 WL 1028483 (Tex.App. July 27, 2000).

This case involved a dispute as to whether an LLC's claim against a deceased member was timely presented to the administratrix of the deceased member's estate. In the course of the court's opinion, the court notes that, while the member's death dissolved the LLC, the LLC had authority to wind up its affairs, including the ability to make payments to creditors required by the deceased member's actions.

Investcorp, LP v. Simpson Investment Company, L.C., 983 P.2d 265 (Kan. 1999).

The members of a family-held Kansas LLC deadlocked on important management issues, and several members withdrew to effect a dissolution of the LLC. The withdrawing members claimed that they were entitled to participate in the LLC's winding up under the operating agreement. The LLC's remaining members argued that the withdrawing

members were no longer members and thus had no right to participate in the LLC's winding up. Both factions relied on the operating agreement, which provided for the "members" to wind up and liquidate the LLC and defined "members" as "those persons who are members of the Company from time to time, including any Substitute Members." The district court found that the withdrawing members were not entitled to participate in the dissolution process. The Kansas Supreme Court, however, examined the use of the term "member" and "remaining member" in other provisions of the operating agreement and concluded that "[t]he many references to 'member' in the Act when coupled with the operating agreement suggest that the better view is that, in dissolution, 'member' includes a withdrawing member having a financial interest in the Company's assets." The court went on to state that control of the dissolution process resided in the managers of the LLC under the operating agreement and the Kansas act.

BB. Rights of Dissociated Members

Branca v. Conley, 2001 WL 1807403 (Oct. 30, 2001) (finding member's claims for fraud, breach of fiduciary duty, and conspiracy in connection with buy-out of member's interest were released in settlement agreement executed in connection with buy-out).

Lieberman v. Wyoming.com LLC, 11 P.3d 353 (Wyo. 2000).

The court interpreted the Wyoming LLC act and the operating agreement of a Wyoming LLC to determine the rights of Lieberman, a dissociated member. Lieberman's contribution upon formation of the LLC was documented at \$20,000, consisting of services rendered and to be rendered. When Lieberman was terminated as vice-president of the LLC, he served a notice of withdrawal and demand for the return of his share of the current value of the company, which he estimated at \$400,000. The remaining members avoided dissolution of the LLC by electing to continue the LLC and approved the return of Lieberman's \$20,000 capital contribution. The court discussed a provision of the Wyoming LLC act that entitles a member to demand the return of the member's capital contribution if the operating agreement does not prohibit or restrict the right. Since the LLC operating agreement did not restrict this right, Lieberman was entitled to the return of his \$20,000 contribution. The question remained whether he was entitled to receive any further distribution. A provision permitting a member to compel dissolution upon an unsuccessful demand for the return of the member's contribution was not applicable since the LLC agreed to return Lieberman's contribution. Noting the absence of a provision in the Wyoming LLC act governing dissociation, the court turned to various provisions of the operating agreement dealing with membership certificates, transfer of interest, quorum, and voting and concluded that it remained unclear what became of Lieberman's ownership interest beyond his capital contribution. Thus, the court remanded for a further determination in this regard.

Lindsay, Marcel, Harris & Pugh, L.L.C. v. Harris, 752 So.2d 335 (La. App. 2000).

Harris and Pugh gave notice of their withdrawal from their four-member law firm LLC and formed their own law firm. When the LLC filed suit against the withdrawn members, the withdrawn members answered and sought dissolution. The court of appeals determined that the withdrawn members had no right to seek judicial dissolution because the statute conferred no such right on former members. In addition, the court found no basis in the operating agreement for the withdrawn members to obtain dissolution. Included among the causes of dissolution listed in the operating agreement was "reduction in the number of Members to 1," but the court pointed out that two members remained after the withdrawal of the other members.

Donnelly v. Brown, Winick, Graves, Gross, Baskerville, Schoenbaum and Walker, P.L.C., 599 N.W.2d 677 (Iowa 1999).

A lawyer left his firm (a professional LLC) and went to another firm, and there was a dispute over the provision of the operating agreement dealing with benefits to be paid to a retiring member. The specific issue on appeal was whether the "continuation payments" under the operating agreement qualified as "retirement benefits" under Iowa DR 2-108(A). The payments were conditioned on the lawyer's termination of the private practice of law in Iowa. The lawyer argued that this was an impermissible covenant not to compete. The court concluded that the provisions in this case (requiring ten years of service and sixty years of age or twenty-five years of service) clearly constituted a retirement plan, and the restriction on future practice was therefore valid, even though the plan applied to situations involving less than full retirement.

Investcorp, LP v. Simpson Investment Company, L.C., 983 P.2d 265 (Kan. 1999).

The members of a family-held Kansas LLC deadlocked on important management issues, and several members withdrew to effect a dissolution of the LLC. The withdrawing members claimed that they were entitled to participate

in the LLC's winding up under the operating agreement. The LLC's remaining members argued that the withdrawing members were no longer members and thus had no right to participate in the LLC's winding up. Both factions relied on the operating agreement, which provided for the "members" to wind up and liquidate the LLC and defined "members" as "those persons who are members of the Company from time to time, including any Substitute Members." The district court found that the withdrawing members were not entitled to participate in the dissolution process. The Kansas Supreme Court, however, examined the use of the term "member" and "remaining member" in other provisions of the operating agreement and concluded that "[t]he many references to 'member' in the Act when coupled with the operating agreement suggest that the better view is that, in dissolution, 'member' includes a withdrawing member having a financial interest in the Company's assets." The court went on to state that control of the dissolution process resided in the managers of the LLC under the operating agreement and the Kansas act.

Five Star Concrete, L.L.C. v. Klink, 693 N.E.2d 583 (Ind. App. 1998).

The court in this case determined that a dissociating member of an LLC had no right to receive a distribution of income allocated to the member for tax purposes and that there were fact issues precluding summary judgment on the issue of whether the buy-out of the dissociating member divested the member of its entire economic interest in the LLC. Klink, Inc. ("Klink") and four other corporations formed an LLC. Klink withdrew from the LLC, and the remaining members decided to purchase Klink's ownership units and continue the business. The members agreed that Klink would receive \$61,047.22 for the value of Klink's "units." After the end of Klink's fiscal year, Klink was allocated its share of the LLC's income for the portion of the year that Klink was a member. Klink asserted that it was entitled to a distribution in this amount. The court concluded that neither Indiana law nor the operating agreement gave a member a right to a distribution of income allocated to the member for income tax purposes. The remaining issue involved the meaning of the term "units" inasmuch as Klink's units were bought out on its withdrawal. The LLC contended that Klink divested itself of its entire interest when it sold its units to the LLC. Klink argued that it sold less than all of its economic rights. Klink pointed to the operating agreement reference to a unit as "an interest in the Company representing a contribution to capital." The LLC pointed out, however, that the operating agreement generally entitled each unit to a vote and a proportionate share of the LLC's net income, gains, losses, deductions, and credits. The court concluded that fact issues precluded resolution of this issue by summary judgment. The court addressed as a separate issue the valuation method and whether it represented the fair market value of Klink's entire interest. The court concluded that summary judgment was not appropriate on this issue either.

Goldstein and Price, L.C. v. Tonkin & Mondl, L.C., 974 S.W.2d 543 (Mo. App. 1998).

The LLC in this case converted from a partnership in January 1994 and adopted the partnership agreement as the operating agreement until a new operating agreement could be prepared. In November 1994, before a new operating agreement was adopted, one of the members, Tonkin, advised other members of the firm that he intended to withdraw. He provided a written notice of withdrawal stating an effective date of December 31, 1994. The managing members concluded that the partnership agreement that served as the LLC's operating agreement required Tonkin's withdrawal on November 30, 1994. The agreement stated that "withdrawal shall become effective on the last day of the calendar month after service of the withdrawal notice. . ." The court found this language by itself to be ambiguous but interpreted it with reference to other parts of the agreement and concluded that withdrawal was effective November 30, 1994. The parties also had a disagreement as to the withdrawn member's share of certain fees received by the firm after Tonkin's withdrawal. The court looked to the operating agreement as controlling but found no provision addressing work in progress in the withdrawal context. Thus, under the terms of the written agreement, Tonkin was not entitled to any portion of the disputed fee. However, the court concluded that the parties orally modified the operating agreement regarding the fee in question by agreeing to treat the fee as an account receivable. The agreement provided for allocation of accounts receivable, and Tonkin was awarded his share under the agreement.

Lloyd v. Horn, Inc., No. Civ.A. 95-2549-KHV, 1997 WL 150052 (D. Kan. Jan. 29, 1997), aff'd, 1998 WL 939493 (10th Cir. Aug. 21, 1998).

The court rescinded an operating agreement of an LLC on the grounds that Lloyd, one of the members, committed fraud in the formation of the LLC, and the court concluded that Lloyd's rights were governed by the partnership agreement under which the parties had operated before organizing as an LLC. However, the court concluded that it could not determine Lloyd's rights under the partnership agreement by summary judgment and scheduled the matter for trial. The court referred to confusion between the terms "capital account" and "capital contribution" and as to whether Lloyd should be treated as a withdrawing or expelled partner under the provisions of the partnership agreement.

Advanced Orthopedics, L.L.C. v. Moon, 656 So.2d 1103 (La. App. 1995).

The members of an LLC had a falling out, and one member, Moon, formed a competitive business and resigned from the LLC. Moon's attacks on the formation of the LLC were rejected by the court. Moon also argued that he was entitled to reimbursement for a capital contribution. He contended that he had made his agreed upon capital contribution of \$10,000 in the form of past experience, good will, services rendered, and equipment. While the court acknowledged that capital contributions do not have to be in the form of cash, it concluded that there was no evidence that Moon made a non-cash capital contribution.

CC. Dissenters' Rights

Pine Creek, LLC v. Pine Mount, LLC, 558 S.E.2d 44 (Ga. App. 2001).

A Georgia LLC sought to restrict a member to the remedy of dissent and appraisal under the provisions of the Georgia LLC act upon the sale of the LLC's sole asset. The court held that there were fact issues as to whether the procedural requirements of the operating agreement were met. The issues revolved around certain transfers of interests that the dissenting member claimed were in violation of transfer restrictions in the operating agreement.

Froelich v. Erickson, 96 F. Supp.2d 507 (D. Md. 2000), aff'd, 5 Fed.Appx. 287 (4th Cir. 2001).

The factual background of this case is rather complicated, but the claims involved assertions of fraud, breach of fiduciary duty, and breach of contract by Froelich, an ousted CEO and board member of a Maryland LLC. Froelich was also a member of the LLC who, along with other minority members, was cashed out in a squeeze-out merger following a reclassification of interests of the LLC approved by all members except Froelich. The court found that the reclassification and squeeze out were related parts of a transaction in which Froelich had properly preserved his statutory right to an appraisal. The court explained that the Maryland LLC statute grants a member the same appraisal rights as an objecting stockholder under corporate law. Maryland corporate law provides appraisal rights in connection with a parent-subsiary merger, and Froelich properly objected to the squeeze-out merger. The court viewed the reclassification and subsequent squeeze-out merger as a single transaction rather than separate events such that Froelich was entitled to appraisal of his interests immediately prior to the reclassification rather than appraisal of his reclassified interests immediately prior to the merger that occurred five months later.

DD. Imputed Fiduciary Duties

Barbieri v. Swing-N-Slide Corp., 65 USLW 2584, 22 Del. J. Corp. L. 1148, 1997 WL 55956 (Del. Ch. Jan. 29, 1997).

Greengrass Management LLC ("Management") and Greengrass Capital ("Capital") formed a general partnership, Greengrass Holdings ("Holdings"). Management was organized by several senior officers of Swing-N-Slide Corp., including Mueller, a director and the president and CEO of Swing-N-Slide. Holdings executed a two-step tender offer to acquire a majority stake in Swing-N-Slide. Barbieri, a Swing-N-Slide shareholder, brought an action challenging the transaction. He argued that because Mueller had an ownership interest in Management, and Management was one of the two general partners of Holdings, Management and Holdings owed fiduciary duties to the Swing-N-Slide shareholders. The court found that the persons who formed Management, as senior officers of Swing-N-Slide, owed fiduciary duties to Swing-N-Slide. Thus, the issue of apparent first impression was whether a legal entity must take on the pre-existing fiduciary duties of those who form and control it. The court determined that the fiduciary duties of the Swing-N-Slide director and officers must be imputed to the LLC they formed because "[n]either Mueller nor the others would escape their fiduciary obligations to [Swing-N-Slide] had they not formed Management. To allow them to use this State's laws allowing the formation of the limited liability company as a vehicle to avoid those very duties would be unconscionable." As to Holdings' liability, the court found that Holdings was made up of two partners, Management and Capital. Capital had no pre-existing fiduciary duties to Swing-N-Slide or its shareholders, and the court refused to assume that Management "so controls or otherwise so dominates the affairs of the partnership that the partnership itself must take on the fiduciary obligations of a single partner." Thus, the court determined that Holdings need not take on the imputed fiduciary duties of Management.

EE. Foreign LLCs

1. Personal Jurisdiction

Hartford Fire Ins. Co. v. United Restoration LLC, No. CV020813517, 2003 WL 1962864 (Conn.Super. April 4, 2003) (holding that Connecticut long-arm statute for corporations applies to LLCs).

New England National LLC v. Kabro of East Lyme LLC, No. 550014, 2000 WL 254590 (Conn. Super. Feb. 23, 2000) (applying Connecticut long-arm statute applicable to foreign partnerships and finding that foreign LLC had transacted business in Connecticut so as to justify the court's exercise of specific personal jurisdiction over the LLC).

MCNC Oil & Gas Company v. IBEX Resources Company, L.L.C., 23 F. Supp.2d 729 (E.D. Mich. 1998) (applying Michigan long-arm statute regarding specific jurisdiction over unincorporated associations to conclude that Oklahoma LLC was subject to personal jurisdiction).

2. Failure to Qualify to Do Business

Danka Funding, L.L.C. v. Page, Scrantom, Sprouse, Tucker & Ford, P.C., 21 F. Supp.2d 465 (D. N.J. 1998).

The defendant sought to have the plaintiff LLC's claims dismissed for failure to comply with the New Jersey registration requirements applicable to foreign LLCs doing business in New Jersey. The plaintiff was a New York LLC which was not registered in New Jersey at the time it filed suit. It had previously been registered, but the registration had lapsed. It subsequently re-registered after the suit was filed. The court followed corporate cases to the effect that a company's failure to register does not require dismissal so long as the company corrects the deficiency during the proceedings. The defendant argued that these cases should not apply in this case because the defendant filed suit in another jurisdiction before the LLC re-registered. The court disagreed and held that the registration related back for purposes of the first to file rule.

3. Foreign Non-Professional LLC (in Jurisdiction Limiting LLCs to Professionals)

IHS Acquisition XV, Inc. v. Kings Harbor Care Center, No. 98 CIV 7621(LBS), 1999 WL 223152 (S.D. N.Y. April 16, 1999).

The plaintiff, as successor-in-interest to an LLC, sued for payment for respiratory therapy services rendered under a contract with the defendant. The defendant moved to dismiss on the basis that the contract was void as against public policy. Specifically, the defendant argued that the LLC was a foreign non-professional LLC which was not permitted to provide or contract to provide professional services in New York. The court construed this contention as an illegality defense that could not support dismissal at this stage in the proceedings. The court noted that there was no absolute or per se rule of illegality of such contracts in New York and stated that a number of factors would have to be addressed to resolve whether the contract in issue was enforceable.

4. Law Governing Foreign LLC

Matjasich v. State of Kansas Dept. of Human Resources, 21 P.3d 985 (Kan. 2001).

The Kansas Supreme Court held that the law governing a foreign LLC operating a nursing home in Kansas included not only the LLC act of the LLC's state of organization but also provisions of the wage payment law of the state of organization under which a member of an LLC could be held personally liable for unpaid wages. The court analyzed the Kansas Wage Payment Law and concluded that it did not provide for personal liability of LLC members because the definition of employer has not been amended to include LLCs along with corporations, partnerships, etc.; however, the court concluded that the Utah wage payment law rather than the Kansas law governed the liability of the members of the Utah LLC for unpaid wages arising out of its business in Kansas. The court relied upon provisions of the Kansas LLC act that provide the laws of the jurisdiction of organization govern the internal affairs and the liability of members. The court construed these provisions to include not only the LLC act but other laws bearing on member liability.

FF. Charging Order

In re Ashley Albright, 291 B.R. 538 (Bankr. D. Colo. 2003).

The sole member of a Colorado LLC filed bankruptcy, and the court held that the Chapter 7 trustee became a “substituted member” and could cause the LLC to sell the LLC’s real property and distribute the proceeds to the estate. The court reasoned that the trustee acquired the governance rights of the bankrupt member of the LLC because the trustee succeeded to the debtor’s membership interest and there were no other members whose approval was required for admission of the trustee as a member. The court quoted provisions of the Colorado LLC act that refer to consent or approval by the “other members” for admission of an assignee as a member. The debtor argued that the trustee represented creditors’ interests and was only entitled to a charging order, but the court concluded that the charging order is for the protection of other members and thus serves no purpose in a single-member LLC. The court noted in a footnote that a non-debtor member, even one with an infinitesimal interest, would be able to prevent a bankrupt member’s trustee from acquiring the bankrupt member’s rights to govern and vote; however, the court also noted that creditors or a bankruptcy trustee would have recourse under bankruptcy avoidance provisions or fraudulent transfer laws where a “peppercorn” member is employed for purposes of hindering, delaying, or defrauding creditors.

Delta Development and Investment Co. v. Yeh, No. 47192-9-I, 2002 WL 31748937 (Wash.App. Dec. 9, 2002).

Yeh, an officer and director of a corporation formed to develop real estate, misappropriated money from the corporation and invested in other properties. The court imposed a constructive trust in favor of the corporation on Yeh’s two-thirds interest in a real estate development LLC, describing it as an interest in real property. After imposition of the constructive trust, Yeh, who had been managing the property, transferred management to MacLean, the other member of the LLC. The corporation asked for a receiver to manage the property owned by the LLC. MacLean intervened and argued that the nature of an LLC prevented the corporation from becoming a member without MacLean’s consent and from reaching the LLC’s real property. The court noted that an LLC is a separate entity from its members and that the decree of constructive trust failed to recognize the distinction but characterized the error as no more than “mere form.” The court said MacLean was arguing that, even if the court had correctly characterized Yeh’s interest in the LLC as personal property, the corporation would not have been entitled to a management role as a mere assignee. The court distinguished a judgment creditor and the charging order remedy from a beneficiary of a constructive trust because the judgment is not monetary. The court stated that the statute does not rule out the possibility that a member’s interest can be reached by constructive trust where the judgment is not for a particular amount. Having concluded that the corporation was not a “judgment creditor” limited to non-managerial rights of an assignee under the charging order statute, the court accepted the substantive effect of the judgment substituting the corporation for Yeh as the owner of the two-thirds LLC interest with all the rights, privileges, and benefits associated with ownership of the interest including the right to participate in management. The court remanded for the sole purpose of correcting the technical error of referring to the interest the corporation received as an interest in real property. The court noted in a footnote that it was not addressing MacLean’s newly raised argument that the corporation was an assignee as the transferee of the interest held by Yeh as constructive trustee because it was not presented in the opening brief.

Koh v. Inno-Pacific Holdings, Ltd., 54 P.3d 1270 (Wash. App. 2002).

The plaintiff obtained a judgment in California against the defendant, a Singapore corporation, and learned in post-judgment discovery that the defendant owned an interest in a Washington LLC. The Washington LLC owned real estate in Washington but its principal place of business was in Malaysia. The plaintiff obtained a charging order from a Washington trial court, but the trial court subsequently quashed the order on the basis that it lacked jurisdiction over the membership interest because it was personal property located outside the state of Washington. Relying on two cases dealing with charging orders in the partnership context, the court of appeals determined that an LLC membership interest is located where the LLC is formed. The court agreed with the plaintiff that the Washington LLC act allowed the plaintiff to reach the defendant’s membership interest through a charging order and rejected the defendant’s argument that the exercise of jurisdiction would offend the Constitution. The court determined that registration of a valid foreign judgment in conjunction with the presence of the property in Washington satisfied due process. In fact, the court stated, allowing the action was required in order to give full faith and credit to the California judgment.

World Fuel Services Corporation v. Moorehead, 229 F.Supp.2d 584 (N.D. Tex. 2002).

The plaintiff registered a foreign judgment in Texas and sought a turnover order and receivership with respect to the defendant’s non-exempt assets. Included in these assets were stocks, bonds, debentures, options, accounts receivable, and other property interests pledged to various third parties. The plaintiff also sought a charging order against the defendant’s interest in two limited partnerships and an LLC. The court upheld the magistrate’s issuance of a turnover

order and appointment of a receiver to take possession and control of all the defendant's non-exempt assets and property interests and to sell the assets and property interests in satisfaction of the judgment. With respect to the request for the charging order, the court upheld the magistrate's finding that the charging order was "unnecessary" because the receivership included the limited partnership and LLC interests. (The court's receivership order specifically gave the receiver authority to exercise all powers and rights exercisable by the defendant with respect to his stock, bonds, warrants, debentures, and options in corporations in which the defendant had any legal or beneficial interest, including voting rights, but the order did not mention specifically the rights of the receiver with respect to the limited partnership and LLC interests. The order generally gave the receiver authority to take possession and control of, and to sell, all the defendant's non-exempt assets and to perform any and all acts necessary and appropriate in order to take possession and control of, and to sell, the defendant's assets.)

Cadle Co. v. Ginsburg, No. CV950076811S, 2002 WL 1295027 (Conn.Super. May 16, 2002).

This opinion is merely the court's order charging the interest of the defendant with payment of the judgment entered in the action. The court's opinion analyzing why a charging order was appropriate is at 2002 WL 725500 and is summarized below.

Cadle Co. v. Ginsburg, No. CV950076811S, 2002 WL 725500 (Conn. Super. March 28, 2002).

The plaintiff obtained a judgment against the defendant and applied for a charging order against the defendant's interest in Jai Alai Associates, LLC. The defendant objected to issuance of the charging order claiming that the LLC and IRS must be made parties and that issuing a charging order would violate state law by allowing an unlicensed individual to hold an interest in a jai alai business. The court rejected the argument that the LLC must be made a party, citing the LLC provisions detailing the process and effect of obtaining a charging order (explaining that a charging order merely gives the judgment creditor the rights of an assignee to distributions and does not dissolve the LLC or entitle the judgment creditor to participate in the affairs of the LLC or become a member) and concluding that a charging order does not impact the rights of an LLC to the degree necessary to require it to be a party. The court also rejected the argument that the IRS, which allegedly had or might claim a lien on the interest, should be made a party, stating that any charging order would be subject to any superior rights of the IRS in the defendant's interest. Finally, the court rejected the argument that the charging order would violate state licensing laws. The court found the state statute requiring an individual or business engaging in jai alai to obtain a license did not preclude issuance of the charging order, which would only give the judgment creditor the rights of an assignee and would not entitle the creditor to participate in management or become or exercise the rights of a member.

Herring v. Keasler, 563 S.E.2d 614 (N.C. App. 2002).

A judgment creditor of an LLC member sought a charging order and an order directing that the member's interest be sold and proceeds applied towards the judgment. The court granted the charging order, but the court concluded that the North Carolina LLC act did not authorize the forced sale of the interest. The court quoted from the statute to the effect that a charging order entitles the judgment creditor to receive distributions and allocations to which the judgment debtor would be entitled but does not dissolve the LLC or entitle the judgment creditor to become or exercise any rights of a member. The court's reasoning for finding forced sale was not permitted was that the forced sale of a membership interest to satisfy a debt would "necessarily entail the transfer of a member's ownership interest to another, thus permitting the purchaser to become a member" in violation of statutory provisions that require consent of all members to admit a person as a member.

Baker v. David A. Dorfman, P.L.L.C., No. 99 Civ. 9385 (DLC), 2000 WL 1010285 (S.D. N.Y. July 21, 2000), *aff'd*, 232 F.3d 121 (2nd Cir. 2000).

Baker obtained a judgment against David Dorfman for legal malpractice and fraud. Subsequently, Dorfman formed a professional LLC and began to operate his law practice through the PLLC. In this action, Baker sought to hold the PLLC liable on the judgment against Dorfman as a successor in interest. The court concluded that the PLLC was liable as a successor in interest. Baker also sought assignment of a 75% interest in the PLLC and appointment of himself as receiver for the LLC. (The court explained that the request for assignment of a 75% interest was to permit Baker to receive 75% of the profits of the PLLC while leaving Dorfman an incentive to generate future profits.) The court relied upon the charging order provisions of the New York LLC act to grant Baker's request for assignment of an interest in the LLC. The court relied upon general receivership provisions to conclude that the circumstances warranted appointment of a receiver, and the court appointed Baker, through his attorney, receiver of the PLLC. In a *per curiam* opinion, the court of appeals generally affirmed the district court's judgment, including the assignment of 75% of the profits of the PLLC, but raised *sua sponte* a concern regarding the breadth of the receivership order granting sweeping

authority with regard to the PLLC's affairs. The court remanded for further consideration of the impact of the order on confidentiality and other obligations involved in the attorney-client relationship between Dorfman and his clients.

Banc One Capital Partners v. Russell, No. 74086, 1999 WL 435787 (Ohio. App. 8 Dist. June 24, 1999).

Two judgment creditors of a 50% member in an LLC obtained a charging order against the member's membership interest. One of the creditors was the other 50% member. The LLC leased a building on which it held an option to purchase. The creditors valued the option at \$500,000. The creditors attempted to exercise the option, and the debtor member complained that the trial court had improperly transferred his governance rights in the LLC and the option itself to the judgment creditors. The court found no evidence that the trial court's order reached the option itself or the member's governance rights. The court pointed out that the order stated that the member's "membership interest" in the LLC "shall be charged and transferred to" the creditors, and the order did not reference the option itself. However, the court did characterize the member as having a 50% financial interest in the option itself by virtue of his membership interest in the LLC. The court stated that the trial court's order did not reach the member's governance rights but that the other member could exercise the option under his statutory agency power. The court acknowledged that it was improper for the trial court's order to state that the interest was charged "and transferred," but found the error inconsequential.

PB Real Estate, Inc. v. DEM II Properties, 719 A.2d 73 (Conn. App. 1998).

A judgment creditor of two lawyers obtained a charging order against the LLC law firm of the judgment debtors. The order directed the LLC to pay to the plaintiff "present and future shares of any and all distributions, credits, drawings, or payments due to the defendant[s] . . . until the judgment is satisfied in full . . ." The plaintiff applied for a turnover order claiming the LLC had failed to fully comply with the order. The challenges to the turnover order basically turned on whether certain payments were "distributions" subject to the charging order. The defendants claimed that the payments in issue were merely compensation for services as lawyers and were similar to the wages paid other employees of the firm. The defendants argued they never authorized any distributions. The court rejected the defendants' arguments and held the payments were distributions subject to the charging order.

GG. Tortious Interference With Contract

Tam v. Lo, 968 F. Supp. 1326 (N.D. Ill. 1997).

The plaintiff, Tam, invested \$73,000 in an Illinois LLC, and was offered a management position. Plaintiff's brother-in-law, Tang, invested \$20,000 in the LLC. The plaintiff was subsequently asked to resign, which he agreed to do if he and his brother-in-law were paid the amount of their investments. They never received their money back, and the plaintiff's brother-in-law assigned his interest to the plaintiff. The plaintiff sued the LLC and three individuals whom the court referred to as "also part of [the LLC's] management." The plaintiff alleged breach of contract, fraud/misrepresentation, tortious interference with contract, and violation of the Illinois Limited Liability Company Act. This opinion addressed the defendants' Rule 12(b)(6) motion to dismiss. Among the conclusions reached by the court was the conclusion that the LLC could not logically be liable for tortiously interfering with an employment contract between the plaintiff and the LLC because a party cannot be held liable for inducing itself to breach a contract. Further, the court seemed to invite the individual defendants to argue that they could not be liable either. The court stated, "Whether corporate managers/officers can be held liable for inducing the corporation to breach a contract is another issue. . . . Because Defendants failed to address this issue, the Court will not address it--perhaps Defendants will address it when attacking Plaintiff's amended complaint." With respect to the plaintiff's allegation that the defendants violated the Illinois Limited Liability Company Act, the court concluded that the count could only be brought against the LLC (which the court referred to as a "corporation"), not the individuals. The court's opinion does not specify what acts constituted the alleged violation nor the provision(s) of the statute that were allegedly violated.

HH. Treatment of LLC Under Other Statutes or Contracts

1. Alcoholic Beverage Laws

Meyer v. Oklahoma Alcoholic Beverage Laws Enforcement Commission, 890 P.2d 1361 (Okla. App. 1995).

The issue in this case was whether an Oklahoma LLC is permitted to hold a liquor license under Oklahoma law. The Oklahoma Constitution prohibits licensing of "corporations, business trusts, and secret partnerships." The court rejected the argument that an LLC is in essence a partnership and concluded that an LLC falls within the constitutional prohibition because of the limited liability of members. The court did not view the provision in the Oklahoma LLC act

permitting LLCs to be organized for any lawful purpose as indicative of a legislative intent to override other specific statutory prohibitions and noted that the provision would be ineffective to override a constitutional prohibition in any event.

R & R Marketing, L.L.C. v. Brown-Forman Corporation, 729 A.2d 1 (N.J. 1999).

The New Jersey Supreme Court reversed and remanded to the Director of the Division of Alcoholic Beverage Control (“ABC”) the New Jersey appeals court’s decision that the formation of an LLC by two liquor wholesalers was in substance a merger in which the statutory anti-discrimination protection of the two wholesalers’ franchise rights was preserved. The appeals court had reversed the Director’s decision that the statutory anti-discrimination protection was lost by the transfer of the business to the LLC. Each of the wholesaler members of the LLC was authorized to distribute distilled spirits for Brown-Forman prior to the formation of the LLC. The two members hoped to transfer their supplier authorizations to the LLC with supplier consent. Alternatively, they agreed that they would purchase the alcoholic beverages and transfer them to the LLC at cost. Brown-Forman refused to fill orders by the wholesalers. ABC found that the plan to transfer products to the LLC at cost was a “sham” and that the formation of the LLC was not equivalent to a merger. The appeals court reversed ABC. It noted that the protection of the statute would have continued had the two distributors effectuated a corporate merger and concluded that the protection of the anti-discrimination statute would not defeat the purpose of that statute and would advance New Jersey’s goal in promoting formation of LLCs. The supreme court essentially agreed with the appeals court that the economic reality rather than the form of a reorganization transaction should govern a wholesaler’s rights under the anti-discrimination law but remanded the matter to ABC to reconsider the status of the parties in view of the economic reality of the restructured organization. The court felt that various economic issues were unclear in the record. Additionally, pending the appeal, one of the LLC members had acquired the other. The court assumed that the acquirer would be entitled to retain any protection previously afforded the acquired wholesaler. The court also instructed ABC to articulate the relationship between its findings in the case to the policy of the anti-discrimination law. The court admonished ABC to provide guidance through regulation, directive, or policy statement that would enable parties to shape future transactions to the law’s policies.

2. Receivership Laws

Baker v. David Alan Dorfman, P.L.L.C., 232 F.3d 121 (2nd Cir. 2000).

Baker obtained a judgment against David Dorfman for legal malpractice and fraud. Subsequently, Dorfman formed a professional LLC and began to operate his law practice through the PLLC. In this action, Baker sought to hold the PLLC liable on the judgment against Dorfman as a successor in interest. The district court held that the PLLC law firm had successor liability on the judgment against the member, assigned the judgment creditor a 75% interest in the LLC, and appointed the judgment creditor’s attorney receiver of the PLLC. The order appointing the receiver granted sweeping authority over the PLLC’s operations, and the court of appeals raised *sua sponte* a concern regarding protection of the attorney-client relationship between the judgment debtor and his clients. The court of appeals remanded for further consideration of the receivership order in light of the law and rules of legal ethics governing the attorney-client relationship and the practice of law.

Oil and Grease on Wheels, Inc. v. Medicare Supply Co. of New England, No. C.A. 96-1789, 2000 WL 622584 (R.I. Super. April 26, 2000).

A receiver was appointed for Medicare Supply Co. of New England (“Medicare”), a member of a Rhode Island LLC. Medicare argued that appointment of the receiver constituted an event of dissociation under the LLC agreement which in turn entitled Medicare to be bought out under the agreement. Events of dissociation included a change in control of a member of the LLC. Control was defined under the agreement as an ownership interest sufficient to carry any motion, the right to elect or appoint directors or managers, or the right to manage. The court concluded that a change in control had occurred because the shareholders, directors, and officers of Medicare no longer controlled Medicare. The court stated that control did not have to shift to the receiver for a change in control to occur; it was sufficient that those formerly in control no longer had control. The court rejected the argument that the receiver was an assignee but did accept that the receiver was analogous to a judgment or lien creditor of Medicare. As a type of lien creditor, the court said the receiver succeeded to the rights of the dissociated member to be bought out.

Suntech Processing Systems, L.L.C. v. Sun Communications, Inc., No. 05-98-00799-CV, 1998 WL 767672 (Tex. App. Nov. 5, 1998).

A member of two LLCs claimed that a proposed transfer of funds by one LLC to the other would constitute a fraudulent transfer. The trial court in the case entered an injunction against the payment and ordered the LLCs

dissolved under the statutory provision that an LLC may be judicially dissolved if it is not reasonably practicable to carry on the business of the LLC in conformity with its articles of organization or regulations. The trial court appointed a liquidator under another statutory provision authorizing the court to wind up an LLC's affairs or appoint a person to carry out the liquidation. The liquidator was given control of the two LLCs and had essentially all of the powers of a receiver. The court of appeals concluded that the order appointing a "liquidator" was an order appointing a "receiver;" therefore, the court had jurisdiction over the interlocutory appeal. The court held that the order of judicial dissolution and appointment of a liquidator was improper in this case as it did not properly preserve the subject matter of the suit until the trial court could finally determine whether the payment would be a fraudulent transfer. In other words, the court found the trial court's order was improper because it gave the LLC member its ultimate relief.

Diaz v. Fernandez, 910 P.2d 96 (Colo. App. 1995).

Two members with a 49% interest in a Colorado LLC sought appointment of a receiver for the LLC. The Colorado Rules of Civil Procedure provide for the appointment of a receiver when the moving party establishes "a prima facie right to the property, or to an interest therein, which is the subject of the action and is in possession of an adverse party and such property, or its . . . profits are in danger of being lost. . . or materially injured or impaired." The court first held that a receivership was authorized under appropriate circumstances without a pending request for dissolution since a member of an LLC has a personal property interest in the LLC. The court then discussed the standard for appointment of a receiver and concluded that the member in this case was entitled to an evidentiary hearing on the appointment of a receiver based upon a CPA's affidavit that there were deficiencies in various aspects of the LLC's records and financial operations, that the LLC was insolvent or in danger of insolvency, that wage related taxes, withholding and garnished amounts had not been paid, and that there were unusual related party transactions outside the ordinary course of business.

3. Securities Laws

Securities and Exchange Commission v. Phoenix Telecom, L.L.C., 231 F.Supp.2d 1223 (N.D. Ga. 2001) (ordering disgorgement and "third tier" civil penalty against former vice-president and co-founder of LLC who, knowing the LLC was operating at a loss and with a negative net worth, marketed LLC's pay-telephone plan as a safe investment and without disclosing his previous criminal history or securities laws violations).

Tirapelli v. Advanced Equities, Inc., 215 F.Supp.2d 964 (N.D. Ill. 2002) (dismissing 10b-5 securities fraud claim based upon alleged oral misrepresentations in connection with sale of preferred LLC membership interests where subscription documents contained non-reliance and integration clauses and reasonable reliance on alleged oral misrepresentations thus could not be established).

Nelson v. Stahl, 173 F. Supp.2d 153 (S.D. N.Y. 2001).

The plaintiffs alleged securities fraud in connection with the sale of their stock in a corporation and their interests in several LLCs. Applying the *Howey* test, the court concluded that the interests in the LLC were not securities. The court stated that, whether or not the members in fact abdicated their authority, the legal structure they selected precluded a finding that the membership interests were securities. The plaintiffs owned, in the aggregate, 60% of the membership interests in the LLCs, and the LLC agreements vested management in the members. The members had access to information regarding the affairs of the LLC and had ultimate control over the LLC's affairs. The court declined to treat the purchase of the LLC interests as part of the purchase of stock in a related entity so as to entertain the Rule 10b-5 action with respect to all of the transactions.

Erickson v. Horing, 2001 WL 1640142 (D. Minn. Sept. 21, 2001) (holding that the plaintiffs were collaterally estopped from bringing this federal securities fraud action (which was based upon the reorganization of a North Dakota LLC into a Delaware corporation) because of an adverse judgment in a parallel state fraud action).

Great Lakes Chemical Corporation v. Pharmacia Corporation, 788 A.2d 544 (Del. Ch. 2001).

In *Great Lakes Chemical Corp. v. Monsanto Co.*, 96 F. Supp.2d 376 (D.Del. 2000), the federal district court held that the purchase of 100% of the LLC interests in a Delaware LLC was not a purchase of securities. In this case, the plaintiff alleged that the seller warranted in the purchase agreement that the ownership interests the plaintiff purchased were securities. The court held that a reference to the interests as "equity securities" in the section of the agreement warranting title to the interests did not constitute a warranty that the interests were securities under the federal securities laws.

Dafofin Holdings S.A. v. Hotelworks.com, Inc., No. 00 CIV. 7861(LAP), 2001 WL 940632 (S.D. N.Y. Aug. 17, 2001).

The plaintiffs brought securities fraud claims in connection with an investment in a hotel enterprise. The investment involved receipt by Dafofin Holdings S.A. (“Dafofin”) of an “economic interest in connection with [a] membership interest” in an LLC that held an interest in another LLC that owned the hotel. Dafofin claimed that it relied on various misrepresentations and that the defendants refused to provide a copy of the operating agreement of the LLC that owned the hotel before the parties entered the investment agreement. The plaintiffs did not receive the operating agreement until over two years later. The alleged misrepresentations were inconsistent with provisions of the investment agreement and the LLC operating agreement. The court determined that the plaintiffs’ 10b-5 claims were barred by limitations because the investment agreement put the plaintiffs on notice that at least one misrepresentation had been made. The court also dismissed the plaintiffs’ claims under Section 12(a)(2) of the Exchange Act (because the transaction was made pursuant to a private transaction rather than a public offering) and under Section 17(a) of the Securities Act (because the Second Circuit does not recognize a private right of action under Section 17(a)).

Ak’s Daks Communications, Inc. v. Maryland Securities Division, 771 A.2d 487 (Md. App. 2001).

This case apparently involved the same LLC interests that were determined to be securities in *Nutek Information Systems, Inc. v. Arizona Corporation Commission*, 977 P.2d 826 (Ariz. Ct. App. 1998). The Maryland Court of Appeals applied the *Howey* test in determining that the LLC interests were investment contract securities. The court rejected the argument that the *Williamson v. Tucker* presumption (that general partners’ interests are not securities) applies to LLC membership interests. The court viewed the presumption as inappropriate in the LLC context given that LLC members ordinarily have limited liability and may be less involved in management than general partners.

Cogniplex, Inc. v. Hubbard Ross, L.L.C., No. 00 C 7463, 00 C 7933, 2001 WL 436210 (N.D. Ill. April 27, 2001).

Three individuals formed an LLC in which each was a 1/3 owner, but they never agreed on or executed an operating agreement. When the relationship soured, two of the members sued the third member for, inter alia, securities fraud and failure to register under the securities laws. From the LLC’s inception, the defendant member had managed and exercised controlled over the LLC, and the court concluded that the membership interests of the plaintiffs were investment contract securities under the federal and Illinois securities laws. The defendant argued that the membership interests were not investment contracts because the default rules of the Illinois LLC act that applied in the absence of an operating agreement gave each member equal rights of management and control. The court stated that it would look to the particulars of the situation rather than the generalized default rules and concluded that the plaintiffs’ interests were securities since the defendant assumed control over the LLC and its profits while the plaintiffs were passive investors. The court found that it could not perform at such an early stage of the litigation the intensive factual analysis necessary to determine whether the sale of the membership interests fell within the private placement exemption under 4(2) of the Securities Act of 1933, but the court did determine as a matter of law that the sale of the membership interests met the requirements for an exemption under Illinois law.

Tschetter v. Berven, 621 N.W.2d 372 (S.D. 2001).

The South Dakota Supreme Court applied the *Howey* and *Williamson* tests to conclude that the plaintiffs’ membership interests in the LLC in question (a restaurant) were not securities under South Dakota law. The court pointed out that the operating agreement vested management in the members and gave the members substantial power and authority. The court also stated that the record established that the plaintiffs were informed and active in the affairs of the LLC and were aware of and capable of exercising their powers as members. Although the LLC’s management was contracted out to another entity, the court said the LLC retained the ability to terminate the management contract upon a failure to perform as required, and the members retained substantial power and the ability to conduct the necessary oversight of the LLC’s operations. A dissenting opinion characterized the situation as one in which the plaintiffs had very little control and concluded that a question of fact existed as to whether the membership interests were securities.

KFC Ventures, L.L.C. v. Metaire Medical Equipment Leasing Corp., No. CIV. A. 99-3765, 2000 WL 726877 (E.D. La. June 5, 2000).

The issue in this case was whether the plaintiff’s LLC membership interest was a security under federal securities laws. In response to the defendants’ motion for failure to state a claim for securities fraud, the court held that it was possible that the plaintiff’s membership interest was a security. The focus was upon whether the investment involved an expectation of profits to be derived solely from the efforts of others. The LLC in question was manager-managed, and the operating agreement gave the manager full power and discretion to manage the affairs of the LLC.

The operating agreement did not permit a member to act as the LLC's agent and largely limited the member's role to voting on extraordinary matters such as dissolution. The manager was also an 85% member of the LLC. Thus, the court concluded the membership interest might be a security. However, the plaintiff's allegations of fraud lacked particularity, and the court dismissed the claims subject to fifteen days leave for the plaintiff to amend and plead with sufficient particularity.

Great Lakes Chemical Corporation v. Monsanto Company, 96 F. Supp.2d 376 (D. Del. 2000).

The plaintiff purchased a Delaware LLC from the defendants and brought a securities fraud suit alleging that the defendants failed to disclose material information in connection with the sale. The defendants moved to dismiss for failure to state a claim, arguing that the interests sold to the plaintiff were not securities. The plaintiff argued that the LLC membership interests were either "stock," an "investment contract," or "any interest or instrument commonly known as a 'security'." After reviewing various seminal cases in the securities area as well as recent decisions specifically addressing whether LLC membership interests constituted securities, the court addressed the plaintiff's arguments that the membership interests in issue were securities. First, the court rejected the argument that the membership interests in issue were "stock" although the court acknowledged that the interests were "stock-like" in nature. To determine whether the membership interests were investment contracts, the court applied *Howey*. The court concluded that the plaintiff did not invest in a "common enterprise" because it bought 100% of the LLC membership interests from the defendants. The plaintiffs pointed out that when the LLC was formed it involved a pooling of contributions by the two defendants; however, the court focused on the challenged transaction, which was the sale of the defendants' interests to the plaintiff, rather than the formation of the LLC. The court also concluded that the plaintiff's expectation of profits did not depend solely on the efforts of others. While the LLC was manager-managed, the operating agreement gave members the power to remove managers, with or without cause, and to dissolve the LLC. The court pointed out that the plaintiff's ownership of 100% of the LLC meant that its power to remove managers was not diluted by the presence of other ownership interests. Finally, although the purchase agreement referred to the interests as "equity securities," the court rejected the argument that the membership interests were "any interest or instrument commonly known as a security" because the interests did not satisfy the *Howey* test. Relying on Supreme Court and lower court cases, the court refused to distinguish between an "investment contract" and "any interest or instrument commonly known as a security."

Keith v. Black Diamond Advisors, Inc., 48 F. Supp.2d 326, Fed. Sec. L. Rep. ¶ 90,458 (S.D. N.Y. March 8, 1999).

The plaintiff brought a Rule 10b-5 securities fraud claim in connection with his purchase of membership interests in a New York LLC. The court found that the plaintiff's membership interests were not securities because the fourth element of the *Howey* test, an expectation of profit from the managerial or entrepreneurial efforts of others, was not met. The LLC was member-managed, and the plaintiff had a broad range of rights and powers.

Nutek Information Systems, Inc. v. Arizona Corporation Commission, 977 P.2d 826 (Ariz. App. Div. 1 1998).

The court employed a *Howey* analysis to determine that membership interests in Texas LLCs involved in telecommunications were investment contract securities under Arizona law. The focus was, predictably, on the element of the *Howey* analysis that inquires into whether the investors were led to expect profits based upon the efforts of others. The court relied heavily upon *Williamson v. Tucker*, a Fifth Circuit case addressing whether interests in a general partnership may be considered securities. Although the LLCs were member-managed, the court concluded that the membership interests were securities. The members did not exercise meaningful control and were dependent upon others for the management of the LLC. Management was contractually delegated to another LLC, and it was practically impossible to replace the manager. The members were numerous and geographically dispersed. Additionally, the members lacked technical expertise in the specific business of the LLCs. The court declined to give the LLCs the "strong presumption" that an interest in a general partnership is not a security. The court noted that limitation of liability of LLC members gives members less incentive to be informed about, and active in, the business of the LLC.

Securities and Exchange Commission v. Shreveport Wireless Cable Television Partnership, Fed. Sec. L. Rep. ¶ 90,322, 1998 WL 892948 (D. D.C. Oct. 20, 1998).

The court determined that there was a genuine issue of material fact as to whether partnership interests in two general partnerships and membership interests in a Louisiana wireless cable LLC were securities under federal securities laws, and the court thus denied the defendants' motion for summary judgment on the question. The defendants claimed that the investors did not purchase the LLC interests with the expectation that the efforts of others would generate the profits because they purchased interests in two general partnerships along with the LLC. The court treated the general partnership interests and LLC interests as the same kind of interest in its analysis because the powers granted to the

investors under the partnership agreements and the LLC agreement were the same. To determine whether the interests were investment contracts under *Howey*, the court relied upon *Williamson v. Tucker*. The SEC argued that (1) the agreements left so little power in the hands of the partners that power was in fact distributed as in a limited partnership, or (2) the partners were so dependent upon the unique entrepreneurial or management ability of the manager that they could not replace the manager or otherwise exercise meaningful power. The court examined the agreements and concluded that they appeared to confer no more responsibility on the partners or members than those of limited partners or shareholders. Thus, the court could not conclude, based upon the agreements alone, that the interests were not securities as a matter of law. The SEC argued that the interests were such diluted fractional interests that they constituted stock or limited partnership interests. The SEC also pointed to the promoters' performance of substantial post-purchase services upon which the future profits of the enterprise depended. The court noted that investors with the powers of general partners may choose to delegate their powers and remain passive without their interests becoming securities. The court found, however, that there was a fact issue as to the extent and date on which the partners controlled the enterprise.

***People v. Riggle*, 95CA1476 (Colo. App. Jan. 15, 1998).**

This case was not selected for publication and is not available on Westlaw or Lexis. The following summary is based on information supplied to the author by Robert Keatinge. The defendant in this case appealed a jury verdict finding him guilty of selling unregistered securities and employing unlicensed sales representatives under Colorado law for selling interests in a Nevada LLC (a wireless cable deal). The Colorado Court of Appeals held that the facts permitted the jury to find that the interests being sold in the Nevada manager-managed LLC were securities, but the appeals court reversed the verdict because the jury was not provided with a requested clarifying instruction regarding the definition of a security. The court appeared to acknowledge that the same presumption of non-security status applicable to general partners applies to members who have the right by a majority vote to remove the manager and assume management functions themselves. However, the court stated that a factfinder might find that (1) the number of members necessary to remove the manager would make removing the manager impractical, (2) the number of members would make management impractical, and (3) the business in which the LLC was to engage was very specialized and the operating agreement provided that it was in the members' best interest to engage a manager. On this basis, the court determined that there was sufficient evidence to support the jury's finding that the interests were investment contracts and therefore securities. The court of appeals reversed, however, because the trial court refused to respond to the jury's request for clarifying instructions on the definition of a security and the *Howey* test.

***IBS Financial Corporation v. Seidman and Associates, LLC*, 136 F.3d 940 (3rd Cir. 1998).**

A group that included LLCs filed a Schedule 13D with the SEC, and the court was called upon to interpret the "control" disclosure requirements as applied to the LLCs. The IBSF Committee to Maximize Shareholder Value (the "Committee"), a group of shareholders of IBS Financial Corporation ("IBSF"), filed a Schedule 13D which IBSF contended did not conform with the requirements of the Securities Exchange Act and SEC regulations. With respect to the LLC members of the Committee, IBSF argued that the Schedule 13D did not report information regarding the persons "controlling" the LLCs. In general, the defendants argued that it was sufficient to provide information about certain managers of the LLCs whereas IBSF argued that information about certain members and others must also be included. For those LLCs in which a majority in interest of the members had the power to remove the manager, the court held that the majority member was a person "controlling" the LLCs. Thus, information regarding the majority member should have been included in the Schedule 13D. One of the LLCs had an investment manager and an administrative manager. The Committee argued that only the investment manager was a "controlling" person while IBSF argued that the administrative manager, the majority member, and the majority member's general partner were all "controlling" persons of the LLC. The administrative manager had the power to remove the investment manager and to make management decisions. The court thus concluded that the administrative manager was a "controlling" person. However, since the operating agreement of this LLC made no provision for removal of the administrative manager, the court concluded that the Committee was not required to include information regarding the majority member or its general partner.

***Securities and Exchange Commission v. Parkersburg Wireless Limited Liability Company*, 991 F. Supp. 6 (D. D.C. 1997).**

The court held that membership interests in a wireless cable limited liability company were "securities" subject to the Securities Act of 1933 and the Securities Exchange Act of 1934. The court found that the membership interests fit the definition of an "investment contract" security under the *Howey* test. The court found that the LLC members shared "horizontal commonality" because they were told that they would receive a pro rata share of revenues from the operation. The court also found the members had "vertical commonality" with the entity, meaning that the investors'

success was inextricably linked to the success or failure of the entity (which the court referred to as a “corporation”). Finally, the investors’ profits were to be derived from the efforts of others because the investors had little, if any, input into the company. The court rejected the argument that the members exercised the ultimate power over the LLC. The court noted that they may have theoretically possessed the right to manage the affairs of the LLC under the terms of the operating agreement, but the court stated that the inexperience and geographic diversity of the more than 700 investors essentially precluded exercise of such rights.

Fransen v. Terps Limited Liability Company, 153 F.R.D. 655 (D. Colo. 1994).

The court imposed Rule 11 sanctions on the plaintiff for failure to make an adequate pre-filing investigation as to whether certain defendants were “sellers” of securities. The plaintiff sought damages for violations of federal and state securities laws in connection with the sale of membership interests in a Colorado LLC. The court did not discuss why the membership interests would be securities but assumed that to be the case in discussing the Rule 11 sanctions issue. The plaintiff named certain individuals as defendants on the basis that they were identified as promoters, but the court pointed out that to be a “seller” more is required than simply being a promoter. The plaintiff argued that consent of the members of the LLC to admission of new members, as required under the LLC subscription agreement, amounted to an act of solicitation. The court rejected this argument, pointing to case law holding directors’ authorization of the sale of a corporation’s securities insufficient to make them liable as statutory sellers.

4. Bankruptcy

See also cases under heading “Dissolution and Dissociation-Bankruptcy.”

In re Ashley Albright, 291 B.R. 538 (Bankr. D. Colo. 2003).

The sole member of a Colorado LLC filed bankruptcy, and the court held that the Chapter 7 trustee became a “substituted member” and could cause the LLC to sell the LLC’s real property and distribute the proceeds to the estate. The court reasoned that the trustee acquired the governance rights of the bankrupt member of the LLC because the trustee succeeded to the debtor’s membership interest and there were no other members whose approval was required for admission of the trustee as a member. The court quoted provisions of the Colorado LLC act that refer to consent or approval by the “other members” for admission of an assignee as a member. The debtor argued that the trustee represented creditors’ interests and was only entitled to a charging order, but the court concluded that the charging order is for the protection of other members and thus serves no purpose in a single-member LLC. The court noted in a footnote that a non-debtor member, even one with an infinitesimal interest, would be able to prevent a bankrupt member’s trustee from acquiring the bankrupt member’s rights to govern and vote; however, the court also noted that creditors or a bankruptcy trustee would have recourse under bankruptcy avoidance provisions or fraudulent transfer laws where a “peppercorn” member is employed for purposes of hindering, delaying, or defrauding creditors.

In re IDS Holding Co., LLC (IDS Holding Co., LLC v. Madsen), 292 B.R.233 (Bankr. D. Conn. 2003).

A bankrupt LLC, in its capacity as debtor-in-possession, sought to recover a distribution made to its dominant member (Madsen) in connection with the sale of substantially all of the LLC’s assets. The LLC was insolvent at the time of the sale, and all of the proceeds of the sale (consisting of shares of stock in the purchaser) were distributed to the members in accordance with their interests. The LLC’s members had an agreement about the distribution of the proceeds of the sale whereby the members pledged some of the shares they received for the benefit of certain LLC creditors and Madsen agreed to dismiss a pending lawsuit against one of the LLC’s suppliers and another member. The LLC claimed that the distribution violated the Connecticut LLC act, was a fraudulent transfer under the Bankruptcy Code and the Connecticut Uniform Fraudulent Transfer Act, was a voidable preference under the Bankruptcy Code, and was a breach of Madsen’s fiduciary duty as a member of the LLC to its creditors. Madsen argued the transfer was supported by consideration and that he was entitled to summary judgment. The LLC argued that Madsen’s receipt of the shares violated the provisions of the Connecticut LLC act regarding the distribution of assets on a winding up. However, the court found this provision inapplicable because the LLC had not dissolved and was not in the process of winding up. The LLC conceded that the Connecticut LLC act does not prohibit an insolvent LLC from distributing its assets to its members, but the LLC argued that the court was permitted to apply corporate law restrictions under the provision of the LLC act that provides the principles of law and equity supplement the act. The court concluded that it need not address this argument because the LLC conceded that it had never actually dissolved. Thus, the court granted Madsen summary judgment on the claim that the distribution violated the Connecticut LLC statutes. The court found that there were fact issues regarding whether the distributions were made with intent to hinder or delay LLC creditors and whether Madsen gave reasonably equivalent value. Madsen argued that the distribution could not be a voidable preference because he

was only an equity owner and not a creditor or claim holder. The court concluded that Madsen was a creditor by virtue of the distribution agreement and the Connecticut LLC act, which states that a member has the status of a creditor at the time a member becomes entitled to a distribution. Finally, the court applied case law from the corporate context to conclude that Madsen owed a fiduciary duty to LLC creditors when the LLC became insolvent.

Venables v. Smith, No.CIV.A. 02C-09-126JOH, 2003 WL 1903779 (Del.Super. March 14, 2003).

The plaintiff sued an attorney who failed to record a deed transferring certain property to an LLC. The plaintiff and her sisters had retained the attorney to form an LLC for the purpose of holding real estate held by the sisters as general partners. The attorney formed the LLC but failed to prepare a deed transferring the properties to the newly formed LLC. The plaintiff filed bankruptcy and paid a cash settlement to her largest creditor after the creditor threatened to partition the partnership property. The attorney defended on the basis that the creditor would have reached the property in any event since the bankruptcy of the LLC member was an “involuntary withdrawal” under the operating agreement that dissolved the LLC under the terms of the operating agreement when the other sisters did not elect to continue the LLC. The court stated that the attorney’s reasoning was flawed. The court pointed out that the LLC members had no reason to continue because its purpose was to hold the property which was never transferred to it. The court concluded that the dissolution had no bearing on the viability of the plaintiff’s claim.

In re Liimatainen (Notinger v. Liimatainen), 2002 BNH 32, 2002 WL 31317182 (Bankr. D. N.H. Oct. 10, 2002) (stating that failure to list an ownership interest in an LLC may be grounds for denial of discharge but concluding claimant did not prove that debtor/manager of LLC, who signed certificate of formation and operating agreement (as manager) but was not listed as member, was actual owner of LLC).

In re Woods (Cundy v. Woods), 284 B.R. 282 (D. Colo. 2001).

The plaintiffs and the debtor were investors who entered a joint venture agreement and formed an LLC to secure financing and manage a real estate project. The debtor was also the attorney for the LLC (referred to in the case as the joint venture) and a member of the management committee. The plaintiffs alleged that the debtor owed them a fiduciary duty as a co-venturer, management committee member, and attorney for the venture, and that his liability for the venture’s debt was non-dischargeable because it arose from a defalcation of fiduciary duty when he obligated the venture to loan amounts in excess of borrowing authorizations. The court found that there must be an express or technical trust, not merely a general fiduciary relationship like that arising out of an attorney-client, joint venture, or partnership relationship for a fiduciary relationship to exist under section 532(a)(4) (the dischargeability exception for defalcation in a fiduciary capacity). Additionally, the court found that the bankruptcy court was in error in concluding a defalcation had occurred.

In re Interiors of Yesterday, LLC (Orsini v. Interiors of Yesterday, LLC), 284 B.R. 19 (Bankr. D. Conn. 2002)(holding that LLC must be represented by attorney in bankruptcy court but that *pro se* filing of Chapter 7 petition was not void *ab initio* and LLC’s failure to appear through attorney until more than three months later did not constitute “cause” for dismissal of case).

Sumlin Construction Co., L.L.C. v. Taylor, __ So.2d __, 2002 WL 31270292 (Ala. 2002).

A member of an Alabama LLC filed bankruptcy and was granted a discharge. After the bankruptcy proceeding was closed, the member filed a derivative suit against the other members of the LLC. The plaintiff’s status as a member was critical to the plaintiff’s standing to bring the derivative suit, and the Alabama LLC act provides that a member ceases to be a member upon the voluntary filing of a petition in bankruptcy or an adjudication of bankruptcy. The plaintiff claimed this provision was an unenforceable ipso facto clause. The Alabama Supreme Court determined that the operating agreement (which did not address the effect of bankruptcy of a member) was an executory contract involving the significant services of the member and, thus, the other members would not have to accept performance by the trustee. It was therefore not necessary for the court to decide whether the provision of the Alabama LLC act that provides a member ceases to be a member upon bankruptcy would otherwise constitute an unenforceable ipso facto clause. Additionally, the court determined that Section 365(e) is intended only to apply during the pendency of a bankruptcy case and is inapplicable once the automatic stay against ipso facto termination has been lifted. Therefore, the member would have been divested of his membership when the bankruptcy was closed prior to the filing of the derivative suit. Since the Alabama LLC derivative suit provisions require the plaintiff to be a member, and the plaintiff was no longer a member, the plaintiff did not have standing.

Chase Manhattan Bank v. Iridium Africa Corporation, 197 F.Supp.2d 120 (D. Del. 2002).

As part of a financing arrangement, Iridium LLC assigned its right to certain reserve capital call obligations in the Iridium LLC agreement to Chase Manhattan Bank (Chase). Under the reserve capital call provisions, members could be called upon to purchase additional interests in the Iridium LLC. Ultimately, Iridium LLC filed bankruptcy, and Chase sought to enforce its rights against the members under the reserve capital call provisions. Whether assignment of Iridium's rights to Chase was valid and whether certain amendments to the reserve capital call provisions were properly adopted were issues in dispute in the case, and the court determined that fact issues precluded summary judgment on these issues. Chase and the defendants also made certain arguments about the application of Section 365 of the Bankruptcy Code to the LLC agreement. The defendants argued that the obligation of Iridium LLC to issue interests under the reserve capital call provisions of the LLC agreement was an executory contract under Section 365(c). Further, the defendants argued that because Iridium LLC was in bankruptcy it could not as a matter of law assume the agreement and issue the interests, and material breach thus excused the members from the obligation to pay for the interests. Chase had several counter-arguments. First, Chase argued that because Chase had no obligations to the LLC members the Iridium LLC agreement was not executory as to Chase. The court rejected this argument. Chase also argued that the LLC's issuance of interests pursuant to the reserve capital call provisions was not governed by Section 365(c) because the interests were not a "security" of the debtor or a "financial accommodation" under the Bankruptcy Code. The court rejected these arguments, as well. Thus, the court concluded the LLC agreement did create executory commitments under Section 365(c)(2). Finally, Chase argued that the interests to be issued would be worthless, thus there would be no material breach, and the LLC agreement could not be executory. The court found that the value of the interests presented a question of fact (it being possible that the interests were worthless, making the failure to issue them not a material breach and the agreement non-executory); therefore, the court denied summary judgment. The court also addressed Chase's argument that the members had waived all of their defenses in broad waiver provisions in the LLC agreement (though there was a dispute as to whether the waiver provisions were properly adopted). Assuming the waiver provision was properly adopted, Chase argued the provision applied to all defenses of the members, but the court concluded that it did not waive the protections of the Bankruptcy Code. Specifically, the provisions of Section 365(c)(2) (prohibiting assumption of executory contracts covered by that provision) cannot be waived. With respect to defenses other than non-waivable defenses under the Bankruptcy Code, the court found ambiguity in the waiver provisions with respect to their application to the failure of the LLC to issue the interests.

In re McKnew (KMK Factoring, L.L.C. v. McKnew), 270 B.R. 593 (Bankr. E.D. Va. 2001).

The issue in this adversary proceeding was whether, for purposes of § 523(a)(4) of the Bankruptcy Code, the debtor was acting in a fiduciary capacity in his role as manager of a Virginia LLC. Section 523(a)(4) prohibits discharge of an individual's debt arising from fraud or defalcation while acting in a fiduciary capacity. The proceeding involved allegations that the debtor had wrongfully withdrawn monies from the LLC in breach of his fiduciary duties as manager. The court acknowledged that other courts have held that partners or corporate officers were fiduciaries for purposes of § 523(a)(4) but noted that the question of fiduciary status of an LLC member or manager for purposes of § 523(a)(4) was an issue of first impression. The court noted the provisions of the Virginia LLC act requiring a manager to discharge the manager's duties in accordance with the manager's good faith business judgment in the best interest of the company and concluded that, based upon such provisions, LLC managers have a fiduciary duty to the LLC. (The court also concluded that there are no fiduciary obligations among members in view of the lack of a similar provision for members.) However, this generalized fiduciary relationship was insufficient under the strict approach to § 523(a)(4) fiduciary status taken by the court in prior cases. Decisions in the Eastern District of Virginia restrict the term "fiduciary" for purposes of § 523(a)(4) to express or technical trusts, and the court noted that the Virginia LLC act does not impose any trust upon funds contributed to the LLC nor in any manner address the relationship between a manager and the monies of an LLC. The court rejected the argument that the alleged conduct by the manager came within the purview of § 523(a)(4) "analogizing to Virginia decisions concerning officers or directors" and on the basis that Virginia law does not suggest anything "other than a generalized fiduciary duty would be imposed upon a limited liability company manager." The court went on to determine, however, that the manager's excess withdrawals amounted to a non-dischargeable claim for embezzlement under § 523(a)(4). The court found that actions to obfuscate and conceal the nature and amount of the excess compensation showed fraudulent intent. In various financial reports to, and conversations with, the other members, the manager deceived them regarding the payments. Finally, the court determined that the Virginia statutory cap on a manager's liability to the LLC did not apply because the manager's acts amounted to "willful misconduct."

In re Miller (Coleman v. Miller), 270 B.R. 303 (D. Kan. 2001).

The debtor was a 50% member in an LLC (Alma Cheese, LLC), and another LLC (Triangle Marketing, LLC) was the other 50% member. Triangle Marketing, LLC and its two members brought this adversarial proceeding

complaining of fraud by the debtor in failing to disclose certain trade debts of Alma Cheese, LLC in connection with the plaintiffs' guarantee and purchase of industrial revenue bonds of the LLC. The plaintiffs objected to the discharge of the undisclosed trade debts under § 523(a)(2)(A), which prohibits discharge of a debt obtained by fraud or misrepresentation of the debtor's financial condition. The district court upheld the bankruptcy court's dismissal of the proceeding on the basis that the trade debts were not the debts of the plaintiffs or the debtor, and the plaintiffs were not creditors to whom the debts were owed. The plaintiffs argued that the bankruptcy court erred in not interpreting their allegations to state a viable claim or in failing to allow the plaintiffs to amend, but the court found that the allegations were deficient and the bankruptcy court did not have a duty to find some interpretation that would avoid dismissal.

In re Utilimax.com, Inc., 265 B.R. 63 (Bankr. E.D. Pa. 2001).

The debtor was one of approximately 180 members of an LLC that operated as a conduit for its members and was responsible for the bulk electric power system in a multi-state area. The LLC filed an involuntary petition of bankruptcy against the debtor based upon an unpaid obligation for goods sold and delivered. Issues included whether the claim asserted by the LLC was subject to a bona fide dispute and whether fellow members of the LLC could qualify as holders of claims against the debtor. The court discussed provisions of the LLC operating agreement regarding enforcement of obligations and concluded that the joining petitioners did not have "claims" and that conversations at a members committee meeting did not amount to a de facto amendment of the operating agreement.

In re ICLNDS Notes Acquisition, LLC, 259 B.R. 289 (Bankr. N.D. Ohio 2001).

An LLC manager of an LLC prepared and filed a Chapter 7 bankruptcy petition on behalf of the LLC. The court held that an LLC comes within the definition of a "person" under the Bankruptcy Code and is eligible to be a debtor, but an LLC must be represented by counsel like a corporation or a partnership. The court further concluded that a lay person who prepares a bankruptcy petition and schedules on behalf of an LLC is engaged in the unauthorized practice of law. The court thus dismissed the case.

In re Sandman Associates, L.L.C. (Dye v. Sandman Associates, L.L.C.), 251 B.R. 473 (W.D. Va. 2000).

The court held that an LLC's letter agreement that it would grant a membership interest to a new member in exchange for a capital contribution was not an executory contract that could be rejected by the LLC. The agreement called for James Dye to make a \$350,000 capital contribution in exchange for a 25% membership interest. Dye made the contribution and was treated as a member by the LLC, though Dye never signed the operating agreement as the letter agreement required. The court found that the failure to sign the operating agreement was not a material breach and that the agreement had been substantially performed. Thus, it was not an executory contract. The court also addressed Dye's objections to the application for fees filed by the law firm for the LLC debtor. Dye objected on the grounds that the firm was representing the interests of the other members rather than the LLC in the dispute over Dye's membership. The court upheld the bankruptcy court's finding that the services of the law firm were rendered in an effort to clarify the debtor's ability to reorganize and function as an ongoing entity.

In re Forbes Property Management, L.L.C., 252 B.R. 171 (Bankr. D. Colo. 2000).

An LLC debtor filed an application for authority to hire counsel. The application was granted, but the LLC sought clarification regarding the procedures for payment since the funds to be used were not property of the estate. The \$5,000 retainer was paid by the general managing member of the LLC from personal funds, but the court's original order required application for court approval of fees and set forth guidelines for compensation. In the course of modifying the original order, the court pointed out that the managing member and the LLC had a potential, though not actual, conflict of interest and cautioned counsel that he represented and served the interests of the debtor and not those of its managing member.

In re Barman (Solomon v. Barman), 237 B. R. 342 (Bankr. E.D. Mich. 1999).

The LLC issue in this case was whether a South Carolina LLC was an "insider" of the Chapter 7 debtors. Mr. Barman was one of three members of the LLC. The debtors admitted that they were insiders of the LLC but disputed that the LLC was an insider of theirs. The court examined the Bankruptcy Code definitions of "insider" and "affiliate" and concluded that an LLC is sufficiently analogous to a corporation for purposes of determining insiders to consider similar principles. An "insider" includes a corporation of which the debtor is a director, officer, or person in control as well as an affiliate or insider of an affiliate. An affiliate includes a corporation if 20% or more of its voting securities are owned or controlled by the debtor. The court cited various provisions of the South Carolina LLC act reflecting that LLC members have voting rights. The court concluded that Barman was an insider because he was one of three members

and thus held a position analogous to a director, officer, or person in control. The court also held Barman was an affiliate, and thus an insider, because he owned or controlled one-third of the voting rights in the LLC.

In re Heritage Leasing Corporation, No. C/A 96-75946-W, 1998 WL 2016851 (Bankr. D. S.C. Sept. 17, 1998) (declining to extend *Reading Co. v. Brown* to give rise to administrative priority claim where lease entered in name of LLC that was never formed allegedly resulted in lease to partnership and post-petition breach by Chapter 7 trustee, as successor to bankrupt partner, who rejected lease and left premises).

5. Antitrust

Fraser v. Major League Soccer, L.L.C., 97 F. Supp.2d 130 (D.Mass. 2000), aff'd, 284 F.3d 47 (1st Cir. 2002).

In this antitrust case brought by professional soccer players against Major League Soccer, L.L.C., a Delaware LLC, the court concluded that the LLC should be treated as a corporation for purposes of the court's analysis of the application of Section 1 of the Sherman Act. The court cited several FTC rulings in which the FTC has treated LLCs like corporations and cited non-antitrust cases in which courts have concluded that an LLC is more closely analogous to a corporation than a partnership. The LLC argued that it was a "single entity" and thus could not violate Section 1 of the Sherman Act. Since the court determined to treat the LLC as a corporation for this analysis, the court stated that the LLC's operations should be analyzed as the operations of a single corporation, with its operator investors treated as officers and shareholders. The court then examined the LLC and concluded that it was indeed a "single entity;" therefore, the defendants were entitled to summary judgment on the Sherman Act claim. On appeal, the First Circuit thought it doubtful that this was a case where single entity status applied, but concluded that remand was not required because the jury's findings on the relevant market doomed the case. The district court also addressed the plaintiffs' argument that the formation of the LLC in the first place violated Section 7 of the Clayton Act and concluded that the defendants were entitled to judgment on that claim as well. Again, the First Circuit concluded that the jury's rejection of the plaintiff's characterization of the market doomed this claim in any event.

6. Condominium and Cooperative Conversion Protection and Abuse Relief Act

Darnet Realty Associates, LLC v. 136 East 56th Street Owners, Inc., 153 F.3d 21 (2d Cir. 1998).

A real estate development partnership which owned shares in an owners' corporation reorganized as a New York LLC, and the court found the successor LLC to be the same continuing entity for purposes of the statutory termination window under Section 3607(b) of the Condominium and Cooperative Conversion Protection and Abuse Relief Act. In a later released opinion, *Darnet Realty Associates, LLC v. 136 East 56th Street Owners, Inc.*, Nos. 98 Civ. 5864 LBS, 98 Civ. 6011 LBS, 1999 WL 47328 (2d Cir. Feb. 1, 1999), the court addressed the LLC's subsequent sale of all of its shares and proprietary leases in 136 East Main Street Owners, Inc. to another LLC (which in turn sold the shares and leases to another LLC). The court concluded that the transferee LLC was not a successor and did not have special developer status under the Act. This determination led to the conclusion that the notice was within the two year window period provided for in Section 3607(b) of the Act.

7. Right to Financial Privacy Act

Exchange Point LLC v. Securities and Exchange Commission, 100 F. Supp.2d 172 (S.D. N.Y. 1999).

A Delaware LLC challenged a government subpoena of bank records under the Right to Financial Privacy Act (RFPA). Under RFPA, a "person" with standing to challenge such a subpoena is defined as "an individual or a partnership of five or fewer individuals." The question was thus whether the LLC was a "person" under RFPA. The court examined the nature of an LLC and concluded that it did not have standing under RFPA. In addition to the fact that an LLC is not covered by the "plain meaning" of the words "individual" or "partnership," the court focused heavily on the limitation of liability in an LLC and the fact that Congress did not include corporations with 5 or fewer shareholders.

8. Gram-Leach-Bliley Privacy Act

Arbor Place, L.P. v. Encore Opportunity Fund, L.L.C., No. Civ.A. 18928, 2002 WL 205681 (Del. Ch. Jan. 29, 2002).

A member of two Delaware LLCs sought to inspect the books and records of the LLCs, and the managing member of the LLC argued it need only produce the LLC's general ledger accounts transactions histories, continuity schedules, annual reports, bank account ledger cards, and trial balances. The court interpreted the Delaware LLC act and LLC agreements (which gave access to "all books and records" of the LLCs) and concluded that the member also had the right to inspect the tax returns and member lists of the LLC. The court rejected the argument that disclosure of the member lists would violate the privacy provisions of the Gramm-Leach-Bliley Act because there is an exception to the prohibition on disclosure where disclosure is necessary to comply with other laws and legal requirements, and the court found disclosure was required to comply with Delaware law and other legal requirements.

9. Title VII

Miller v. Bloomin' Apple, L.L.C., No. 00 C 50286, 2002 WL 206541 (N.D. Ill. Feb. 11, 2002)(finding LLC that was sole member of another LLC had adequate notice of EEOC charges, though not named in EEOC charges, to be made party to Title VII suit).

10. Agricultural Lien Statute

In re Bernstein (Bernstein Ranch, LLC v. U.S.), 230 B.R. 144 (Bankr. D. N.D. 1999).

An LLC claimed an agricultural lien on cattle proceeds by virtue of feed and care provided the cattle. Two brothers who owned the cattle executed a bill of sale to the LLC, in which they were members, and the LLC later reconveyed the cattle to the brothers. The lien was challenged with respect to the period of time during which title to the cattle was held by the LLC on the basis that, under North Dakota law, an owner of crops or livestock cannot claim a supplier's lien for inputs the owner himself provides to the crop or livestock. The court compared the transfer to the LLC to a case in which a family created a partnership for the purpose of raising potatoes. A company owned by the mother provided services and claimed a lien, but it was disallowed on the basis that the mother, as a participant in the joint venture, had an interest in the crops themselves, and the expenses for which she claimed a lien constituted a contribution to the common undertaking of the joint venture. The court stated that the circumstances surrounding the LLC were similar to those in that case. If the cattle were owned by the LLC during the time in question, said the court, the logic of that case would preclude recognition of the lien. The court analyzed the circumstances of the transfer to the LLC and determined that the sale was absolute and effective upon the signing of the bill of sale. Since the cattle were owned by the LLC, it could not claim a lien for its expenses for feed and services.

11. Texas Franchise Tax

Texas Utilities Electric Company v. Sharp, 962 S.W.2d 723 (Tex.App. 1998).

This case was a suit for a refund of franchise tax paid by Texas Utilities Electric Company (TUEC). TUEC claimed that it was entitled to deduct as "debt" future rental expense under certain operating agreements. The court noted that the franchise tax applies to both corporations and LLCs in Texas, even though most of the statutory provisions use only the word "corporation," because the Tax Code defines a "corporation" to include a limited liability company. The court stated that it used the term "corporation" in its discussion for convenience even though it appeared to the court that TUEC was a limited liability company. The court concluded that the future rentals in issue were not deductible "debt" for franchise tax purposes. (It is clear that LLCs in Texas are subject to the Texas franchise tax, and the court's analysis of the particular provision of the Tax Code in issue was not uniquely affected by TUEC's status as an LLC. The court merely interpreted franchise tax provisions of the Texas Tax Code applicable to LLCs as well as corporations.)

12. Real Estate Transfer Tax

Lester Associates v. Commonwealth, 816 A.2d 394 (Pa.Cmwlth.Ct. 2003) (concluding that there was no legal transfer of title on which transfer tax could be imposed based on deeds into and out of LLC where LLC did not exist at the time of the purported conveyance to it).

Mandell v. Gavin, 816 A.2d 619 (Conn. 2003) (holding no transfer tax was due on contribution of property by individual member to wholly owned LLC under provision imposing tax where the consideration for the property conveyed equals or exceeds one thousand dollars, concluding that there was no consideration for the transfer of real property to the LLC because there was no bargained for exchange).

Ferris v. Gavin, 816 A.2d 628 (Conn. 2003) (holding that the court's decision in *Mandell v. Gavin* controlled and that no transfer tax was due on conveyance of property by individual to individual's wholly owned LLC).

Tranfo v. Gavin, 817 A.2d 88 (Conn. 2003) (holding that the court's decision in *Mandell v. Gavin* controlled and that no transfer tax was due on conveyance of property by individual to individual's 99% owned LLC).

Wolter v. Wisconsin Dept. of Revenue, 605 N.W.2d 283 (Wis. App. 1999).

A family limited partnership which owned three parcels of land reorganized as an LLC, and the family members recorded in the deed records a "Memorandum of Organizational and Operating Agreement" giving notice of the reorganization. The Wisconsin Department of Revenue assessed a real estate transfer tax on the land, and the Tax Appeals Commission found that the transaction was a taxable transfer under Wisconsin law. The appeals court agreed. The court analyzed the Memorandum and concluded it was a "conveyance" by the partnership. Then the court concluded that the conveyance was "for value" even though no cash consideration was involved because the members received capital accounts in the LLC as well as new and more beneficial rights and privileges associated with the LLC form (quoting an article that points out advantages of an LLC over a limited partnership.)

13. Passive Activity (Material Participation) Rules

Gregg v. United States, 186 F.Supp.2d 1123 (D. Or. 2000).

The issue in this case was the application of the material participation standard under IRC Section 469 (the passive activity loss provisions) to an LLC member. Gregg was a member of a service LLC in which capital was not a material income producing factor. The IRS audited Gregg's return and disallowed Gregg's characterization of a flow through loss from the LLC as an ordinary loss and re-characterized it as a passive activity loss. Gregg argued that he should be treated as a general partner for purposes of the tests determining "material participation" (thereby meeting the standard of material participation if he met any one of the seven tests in the temporary regulations under Section 469), but the IRS argued that Gregg (and any member of an LLC) should be treated as a limited partner (and thereby allowed to meet one of only three tests) because members of LLCs have limited liability. The court discussed the nature of LLCs, the nature of limited partnerships, and the legislative history of Section 469 and concluded that the limited partnership test in Temporary Treasury Reg. 1.469-5T(e)(3)(i)(B) is obsolete when applied to LLCs and their members. In sum, it is not applicable to all LLC members because LLCs are designed to permit active involvement by LLC members in the management of the business. The court concluded that Gregg could meet the standard for material participation under any one of the seven tests and went on to analyze the application of the tests to the specifics of the case.

14. Annual Gift Tax Exclusion

Hackl v. Commissioner of Internal Revenue, 118 T.C. No. 14, 2002 WL 467117 (U.S. Tax Ct. 2002).

The Tax Court held that gifts of interests in a family LLC were not present interests that would entitle the taxpayers to the gift tax annual exclusion. The taxpayers made gifts to their children and grandchildren of membership units in an LLC organized to hold and operate tree farming properties. Under the terms of the operating agreement, members could not withdraw from the LLC without the prior consent of the manager. If a member desired to withdraw, the member could offer to sell the member's interest to the LLC, but the manager had exclusive authority to accept or reject the offer. A member was not permitted to transfer or in any way alienate the member's interest except with the prior written consent of the manager, which could be withheld in the manager's sole discretion. If a transfer was made with consent, the transferee would be admitted as a substitute member; if a transfer was made in violation of the operating agreement, the transferee was not entitled to become a member, but only had the right to receive profits and distributions to which the transferor would have been entitled. The court rejected the taxpayers' contention that when a gift takes the form of an outright transfer of an equity interest in a business or property, no further analysis is needed. The court stated that a taxpayer claiming an annual exclusion must establish that the transfer conferred on the donee an unrestricted and noncontingent right to immediate use, possession, or enjoyment of property or of income from the property, both of which demand that such immediate use, possession, or enjoyment be of a nature that substantial economic benefit is derived therefrom. The court found that the terms of the operating agreement foreclosed the ability of the donees

presently to access any substantial economic or financial benefit. The court then concluded that the gifts did not afford the donees to the right to use, possession, or enjoyment of income because the parties stipulated that the LLC was to acquire and manage timberland for long-term income and appreciation, not to produce immediate income, and that it was anticipated the LLC would operate at a loss for number of years. The court said that even if the taxpayers had shown the LLC would generate income at or near the time of the gifts, they failed to show any ascertainable portion would flow out to the donees because distributions were in the sole discretion of the manager under the operating agreement.

15. Secured Transactions

In re Lea Lumber & Plywood LLC, 266 B.R. 342 (Bankr. E.D. N.C. 2001).

The court concluded that several flaws in the signature of a debtor LLC on a UCC-1 financing statement did not render the financing statement ineffective. The financing statement had been signed by a corporate officer of the corporation that was the manager of the LLC. The officer's corporate title was missing, but the court indicated that would be a "hyper-technical" ground on which to void the financing statement. The court characterized the failure to indicate the name of the corporation that was the manager of the LLC as a "more serious error" but concluded that a number of factors mitigated the error, including the fact that the debtor's signature would not even be required under Revised Article 9.

Greenville Riverboat, LLC v. Less, Getz & Lipman, P.L.L.C., 131 F. Supp.2d 842 (S.D. Miss. 2000).

An LLC brought an interpleader action, depositing with the court sums owed by the LLC to a member of the LLC under the LLC agreement. Greenville Marine Corporation asserted a prior right to part of the funds based upon its perfected security interest in the member's right to receive payments from the LLC. Another claimant challenged the enforceability of the security interest on the basis that the description of the collateral was insufficient. The court upheld the sufficiency of the assignment of "payments due under that certain agreement existing between Rainbow Entertainment, Inc. and Greenville Riverboat, LLC, a Mississippi Limited Liability Company, as evidenced by that certain Escrow and Assignment Agreement between Rainbow Entertainment, Inc. and Greenville Marine Corporation, the terms and provisions of which are incorporated herein by reference." The court said this was sufficient to identify the collateral as the member's right to receive payments from the LLC. The court went on to explain that the escrow agreement referenced in the description specifically stated that the promissory note was "secured by the unconditional assignment by Rainbow to Greenville Marine of the first sums due by Greenville Riverboat, LLC, to Rainbow."

16. Bid Submission Process

General Electric Company v. County of Cook, No. 00 C 6587, 2001 WL 417321 (N.D. Ill. March 5, 2001).

The court found that a Delaware LLC falsely represented itself as a joint venture in a bid proposal submitted in connection with construction of a county hospital. The ordinances and the instructions to bidders apparently addressed partnerships and/or joint ventures and corporations but not LLCs. The LLC identified itself as a joint venture and submitted the execution form for a joint venture. The court found that the LLC was not a joint venture for purposes of meeting certain requirements regarding participation in minority and women's business enterprises and failed to meet certain other requirements. The court stated that the LLC, as a corporate entity, failed to comply with the requirements for corporate bidders. The court found that the LLC encouraged the county to believe that one of the LLC members would be personally responsible as a member of a joint venture when in fact the member would have no liability for the LLC's obligations.

Frontier Traylor Shea, LLC v. Metropolitan Airports Commission, 132 F. Supp.2d 1193 (D. Minn. 2000).

Three members of an LLC submitted a statement during the pre-qualification process associated with bidding on an airport construction project. In the statement, the members identified their entity as "Frontier/Traylor/Shea joint venture" and identified it as a "joint-and-several joint partnership." Subsequently, the LLC submitted the lowest bid, but the airport commission rejected the bid on the basis that the entity was not pre-qualified since it was an LLC rather than a joint venture partnership, the status indicated by the Frontier entity that was pre-qualified. The LLC sought injunctive relief and argued that it was a joint venture, citing a treatise and some cases referring to an LLC as a joint venture. The airport argued that a joint venture is a form of partnership and cannot take the form of an LLC. The court concluded that the airport commission's decision was not illegal, arbitrary, capricious, or unreasonable "[g]iven the lack of clarity in the status of when a limited liability corporation [sic] is legally a joint venture and the conflicting documents presented" to the airport commission.

17. Workers' Compensation

Ingalls v. Standard Gypsum, L.L.C., 70 S.W.3d 252 (Tex. App. 2001).

Two corporations formed an LLC and entered a management agreement in which one of the corporations agreed to manage and operate the LLC and cause the LLC to maintain workers' compensation insurance. A worker was injured, and the worker sued the two members of the LLC alleging they were negligent in failing to provide certain safeguards. The members argued that they were "employers" protected from suit under the exclusive remedy provision of the Texas Workers' Compensation Act. The court considered cases dealing with this issue in the partnership and corporate parent-sub subsidiary context. The court concluded that the current statutory treatment of partnerships as entities had overruled case law treating partners as employers, and analogized to the parent/sub subsidiary context because of the liability shield provided to members of an LLC. Since the case law in the corporate parent/sub subsidiary context has recognized the separate existence of the parent and subsidiary for purposes of the workers' compensation law, the members were not permitted to argue they were the same entity as the LLC for such purposes.

18. Divorce of Member(s)

Houchens v. Boschert, 758 N.E.2d 585 (Ind. App. 2001).

The wife in a divorce action appealed the trial court's valuation of the wife's interest in an LLC. The wife complained of the trial court's failure to exclude personal goodwill, but the court of appeals faulted the wife for failing to differentiate between enterprise and personal goodwill. The wife also complained that the trial court had not properly considered the effect of transfer restrictions in the operating agreement on the value of her interest in the LLC, but the court of appeals did not find the trial court's determination to be clearly erroneous. Finally, the court upheld the equal division of the value of the wife's interest in the LLC. (While the opinion generally refers to an award of one-half of the wife's interest to the husband, it appears that the trial court actually awarded one-half of the value of the interest, rather than one-half of the interest itself, to the husband.)

Gervais v. Gervais, No. CV010511239, 2001 WL 1561829 (Conn. Super. Nov. 15, 2001).

Husband and wife were equal members of an LLC. The wife brought suit seeking a distribution of profits, accounting, past profits, and appointment of a receiver for the LLC. The court held that these matters could be properly heard in the divorce action that was already pending between the husband and wife.

19. Creditor Rights

PCL/Calumet v. EnterCitement, LLC, 760 N.E.2d 633 (Ind. App. 2001).

An LLC creditor who held a mechanic's lien sought to have the court apply the doctrine of equitable subordination with respect to a mortgage lien held by members of the LLC. The court held that the doctrine was not available outside of a bankruptcy proceeding. As further support for its refusal to subordinate the mortgage, the court noted that the LLC statutes permit members and managers to lend money and transact other business with the LLC.

20. Fraudulent Transfer

Mountview Plaza Assoc., Inc. v. World Wide Pet Supply, Inc., 820 A.2d 1105 (Conn.App. 2003) (holding that the plaintiff alleged sufficient material facts to support a default judgment against an LLC on the basis that the transfer of a corporation's assets to the LLC without consideration was a fraudulent transfer made with the intent to avoid the corporation's debt to the plaintiff).

In re IDS Holding Co., LLC (IDS Holding Co., LLC v. Madsen), 292 B.R.233 (Bankr. D. Conn. 2003).

A bankrupt LLC, in its capacity as debtor-in-possession, sought to recover a distribution made to its dominant member (Madsen) in connection with the sale of substantially all of the LLC's assets. The LLC was insolvent at the time of the sale, and all of the proceeds of the sale (consisting of shares of stock in the purchaser) were distributed to the members in accordance with their interests. The LLC's members had an agreement about the distribution of the proceeds of the sale whereby the members pledged some of the shares they received for the benefit of certain LLC creditors and Madsen agreed to dismiss a pending lawsuit against one of the LLC's suppliers and another member. The LLC claimed that the distribution violated the Connecticut LLC act, was a fraudulent transfer under the Bankruptcy Code and the Connecticut Uniform Fraudulent Transfer Act, was a voidable preference under the Bankruptcy Code, and was a breach of Madsen's fiduciary duty as a member of the LLC to its creditors. Madsen argued the transfer was supported by

consideration and that he was entitled to summary judgment. The LLC argued that Madsen's receipt of the shares violated the provisions of the Connecticut LLC act regarding the distribution of assets on a winding up. However, the court found this provision inapplicable because the LLC had not dissolved and was not in the process of winding up. The LLC conceded that the Connecticut LLC act does not prohibit an insolvent LLC from distributing its assets to its members, but the LLC argued that the court was permitted to apply corporate law restrictions under the provision of the LLC act that provides the principles of law and equity supplement the act. The court concluded that it need not address this argument because the LLC conceded that it had never actually dissolved. Thus, the court granted Madsen summary judgment on the claim that the distribution violated the Connecticut LLC statutes. The court found that there were fact issues regarding whether the distributions were made with intent to hinder or delay LLC creditors and whether Madsen gave reasonably equivalent value. Madsen argued that the distribution could not be a voidable preference because he was only an equity owner and not a creditor or claim holder. The court concluded that Madsen was a creditor by virtue of the distribution agreement and the Connecticut LLC act, which states that a member has the status of a creditor at the time a member becomes entitled to a distribution. Finally, the court applied case law from the corporate context to conclude that Madsen owed a fiduciary duty to LLC creditors when the LLC became insolvent.

In re Brentwood Lexford Partners, L.L.C., 292 B.R. 255 (Bankr. N.D. Tex. 2003).

The Chapter 7 trustee brought an adversary proceeding to set aside alleged fraudulent transfers. The court held that certain excess cash flow distributions to the members of an LLC engaged in the property management business were fraudulent transfers because they were made with the intent to hinder and delay collection of a note owed by the LLC. The court reached this conclusion based on evidence that the LLC's officers knew that a note payment was due shortly after the distributions, knew that the LLC would have insufficient cash to make the note payment, and viewed its business as worth less than the debt on the note. Furthermore, the LLC's officers and board did not tell the noteholder about the distributions, had not yet provided financial information from the prior year to the noteholder, and did not tell the noteholder that it would not make the next note payment. LLC officers testified that they intended to force the noteholder to renegotiate the note and they believed the distributions and failure to make the note payment would give the LLC leverage in the negotiations. The court found intent to hinder or delay could be inferred from this evidence. The court rejected the argument that the distributions were in the nature of compensation for services of the members. The court noted that there were no employment contracts providing that excess cash flow distributions would be part of their salary or bonus, no funds withheld from the distributions for income tax purposes, and no board resolutions treating the excess cash flow as salary or bonus. The noteholder did not consider excess cash flow distributions as compensation, but rather considered the distributions to be dividends or payments on account of the equity interests of the members. The court thus concluded that the LLC did not receive reasonably equivalent value for the distributions. The court analyzed whether the LLC was insolvent within the meaning of the Texas fraudulent transfer provisions and concluded that the LLC was insolvent. The court concluded that certain payments for legal and accounting services did not constitute fraudulent transfers, nor did the cancellation of certain contracts with the LLC and the formation of another entity that took over some of the contracts constitute fraudulent transfers. (This case is further summarized above under the headings "Fiduciary Duties" and "Distributions.")

Venables v. Smith, No.CIV.A. 02C-09-126JOH, 2003 WL 1903779 (Del.Super. March 14, 2003).

The plaintiff sued an attorney who failed to record a deed transferring certain property to an LLC. The plaintiff and her sisters had retained the attorney to form an LLC for the purpose of holding real estate held by the sisters as general partners. The attorney formed the LLC but failed to prepare a deed transferring the properties to the newly formed LLC. The plaintiff filed bankruptcy and paid a cash settlement to her largest creditor after the creditor threatened to partition the partnership property. The attorney defended on the basis that the transfer to the LLC would have been voidable as a fraudulent transfer in any event. The court denied the attorney's motion for summary judgment, finding that the attorney had failed to establish as a matter of law that the transfer of the property would have been a fraudulent transfer. The court found that there were fact issues involving the plaintiff's intent and solvency at the time the transfer was to have been made. With respect to the issue of reasonably equivalent value, the court rejected the argument that the more limited rights of LLC creditors diminished the value of the LLC membership the plaintiff was to receive in exchange for the transfer. The court stated that "[t]he fact that the transfer of the property would make it more difficult for creditors to reach does not lessen the value of the LLC interest." (The court and the parties apparently assumed that the partner's creditor could directly pursue the real estate held by the general partnership.)

Lenge v. Beizer, No. CV000802145, 2002 WL 31967553 (Conn.Super. Dec. 30, 2002) (concluding that attorney solo practitioner's transfer of his building and law practice to LLCs during pendency of litigation against

attorney was fraudulent transfer made with intent to defraud plaintiff under Uniform Fraudulent Conveyance Act and common law of fraudulent conveyance).

National Loan Investors, L.P. v. World Properties, LLC, No. X03CV980491738S, 2002 WL 1815906 (Conn. Super. June 27, 2002)(concluding transfer by partnership to LLC was fraudulent transfer to “insider” even though individual who was majority partner of the partnership owned only 1% of the LLC inasmuch as individual’s wife and children owned remaining interests in the LLC and individual exercised control over their interests and the entity).

LFG, LLC v. Navarre, No. 01C9451, 2002 WL 1379112 (N.D. Ill. June 26, 2002) (finding allegations pertaining to LLC’s fraudulent transfer claim against LLC lender satisfied particularity requirement and that pleadings also stated claims for conversion and unjust enrichment).

Mullen and Mahon, Inc. v. Mobilmed Support Services LLC, 773 A.2d 952 (Conn. App. 2001) (concluding transfer by corporation to LLC was transfer to “insider” for antecedent debt).

Litchfield Asset Management Corporation v. Howell, 799 A.2d 298 (Conn. App. 2002) (stating that judgment for damages against spouse of LLC member who allegedly conspired to fraudulently transfer assets to LLC was improper because spouse was not transferee and judgment against non-transferee was not authorized under fraudulent transfer statute).

RT Gilbane Corp. v. Neighborhood House, LLC, No. 00-1973, 2002 WL774992 (Mass. Super. Feb. 15, 2002). Three brothers formed an LLC for the purpose of acquiring and developing real estate for use by non-profit entities at below market rents. The brothers intended to and did obtain tax benefits by means of deductions for charitable contributions but did not otherwise intend to profit from the endeavor. Ultimately, the LLC ended its operations by transferring its property to a non-profit organization for substantially less than the appraised value of the property. The only significant debt at the time of the transfer consisted of unpaid and disputed invoices of the project manager for the LLC. The court rejected the arguments of the project manager that the transfer was a fraudulent transfer. The court found no indication of an actual intent to hinder, delay, or defraud the creditor. The plaintiff also claimed the transfer was actionable because the LLC did not receive reasonably equivalent value and was insolvent at the time or as a result of the transfer. The court rejected this claim, as well, concluding that a debtor is not obligated to reserve funds sufficient to defend litigation arising from a disputed claim as well as to pay the claim.

Great Neck Plaza, L.P. v. Le Peep Restaurants, LLC, 37 P.3d 485 (Colo. App. 2001).

A judgment creditor garnished the bank account of an LLC after obtaining a judgment against two corporations affiliated with the LLC. The court upheld the garnishment on the basis that the LLC was the alter ego of one of the judgment debtor corporations and that fraudulent transfers to the LLC had occurred. The LLC was formed after the creditor initiated its lawsuit against the corporations. The LLC was funded by all of the assets of one of the corporations, which became the sole member of the LLC, and the revenues from the business that had been operated by the corporation thereafter went to the LLC. Additionally, the individual who managed these various related entities and owned the ultimate parent of the LLC filed a UCC-1 financing statement to perfect an earlier security interest in the assets. The court found that the LLC and related corporations were alter egos of one another, that fraudulent conveyances had occurred, and that the judgment debtors and related parties had acted in concert to insulate assets from the judgment. The court found that both the transfer of assets to the LLC and the filing of the UCC-1 constituted fraudulent transfers made with actual intent to hinder, delay, or defraud a creditor. The court of appeals stated that the trial court had ample record support for its finding that a “pea in a shell game” had been taking place. The court rejected the argument that the transfers were not fraudulent in the absence of a finding by the trial court that the transfers were made without receipt of reasonably equivalent value. The court stated that such a finding was unnecessary since the trial court found actual intent to defraud.

21. Franchise Laws

Abraham & Sons Enterprises v. Equilon Enterprises, LLC, 292 F.3d 958 (9th Cir. 2002).

Franchisees of Shell and Texaco alleged a violation of California franchise law when Shell and Texaco transferred title, possession, and control of leased gas stations to an LLC jointly owned by Shell and Texaco. The California provision in issue stated that a franchisor who leases premises to a franchisee may not sell, transfer, or assign to another person the franchisor’s interest in the premises unless the franchisor first offers the property to the franchisee.

The court recognized the LLC as “another person,” rejecting the argument of Shell and Texaco that the LLC should not be treated as a separate and distinct entity. The court also determined that contribution of the properties to the LLC was a “transfer” under the statute.

22. Statute of Frauds

Gora v. Drizin, 752 N.Y.S.2d 297 (N.Y.A.D. 1 Dept. 2002)(holding that Statute of Frauds barred breach of contract claim based on oral promise of sole member of LLC to convey 50% interest in LLC to plaintiff after LLC acquired real property owned by the parties’ bankrupt partnership pursuant to partnership’s plan of reorganization).

Urda v. Sahl, No. CV020468800S, 2003 WL 21007160 (Conn.Super. April 17, 2003) (holding that the defendant promised to convey a 50% interest in real estate, rather than an interest in an LLC later formed to hold the real estate, in exchange for the plaintiff’s management of the real estate and thus the oral agreement was subject to the Statute of Frauds, but concluding that plaintiff’s claim survived motion to strike based on allegations of the plaintiff’s performance of the contract).

23. Land Use

Dale Properties, LLC v. County of Hennepin, No. 28918, 2002 WL 31895514 (Minn. Tax. Dec. 20, 2002) (holding that property transferred from individual to family general partnership to family LLC satisfied holding period and requirement that owner be “noncorporate entity” for purposes of favorable treatment under green acres statute.)

South Dakota Farm Bureau, Inc. v. Hazeltine, 202 F.Supp.2d 1020 (D. S.D. 2002) (striking down state constitutional provision prohibiting limited liability entities from acquiring real estate for farming and from engaging in farming in state on grounds provision violated ADA and Commerce Clause).

Town of Middlebury v. Connecticut Siting Council, No. CV010508047S, 2002 WL 442383 (Conn. Super. Feb. 27, 2002) (holding that LLC was “person” entitled to acquire and hold certificate of environmental compatibility and public need for construction and operation of electric generating facility).

24. Mechanic’s and Materialman’s Lien

Longview Production Co. v. Dubberly, 99 S.W.3d 427 (Ark. 2003) (accepting certified question as to whether the phrase “person or persons” in mechanic’s and materialman’s lien statute includes an LLC where statutory construction provision indicates reference to a party or person includes “bodies corporate”).

25. Contractual Provision Referring to “Corporation”

Foley v. Aspen Ski Lodge Limited Partnership, No. 98-1010, 2000 WL 223549 (10th Cir. Feb. 28, 2000).

As part of a financial restructuring, a limited partnership transferred all its operating assets to an LLC in exchange for a membership interest in the LLC. The plaintiff, an assignee of a limited partner’s interest, claimed that the transfer dissolved the partnership under a provision of the limited partnership agreement that provided that the partnership would be dissolved and terminated upon the sale of all or substantially all of the assets of the partnership. However, the partnership agreement provided that the sale of the partnership assets to “a corporation organized solely for the purposes of continuing the business of the Partnership in exchange for the corporation’s capital stock” would not be deemed a sale of all or substantially all of the assets for purposes of the dissolution provision. Relying on this provision, the trial court concluded that the transfer to the LLC did not constitute a sale of all or substantially all of the assets. On appeal, the plaintiff raised for the first time the argument that the transfer to the LLC fell outside the provision because the transfer was made to an LLC and not a corporation. The court refused to consider this argument because the plaintiff had not raised it in the court below.

26. Directors' and Officers' Liability Insurance

Kronemyer v. Philadelphia Indemnity Insurance Co., No. B161586, 2003 WL 21213243 (Cal.App. May 27, 2003).

Two South Dakota LLCs asserted various claims against the individual who had served as president, including conversion, breach of fiduciary duty, breach of contract, and trade libel. The president was an insured under an "Executive Safeguard" policy providing "Directors and Officers Liability & Company Reimbursement Insurance." The president demanded that the insurer defend and indemnify him against the claims. The court first determined that the policy did not require the insurer to provide a defense, and the court rejected various arguments that the policy provided coverage for the claims against the president. The president argued that the policy covered negligent mismanagement, notwithstanding an "insured versus insured" exclusion, on the basis that the claim was for contribution or indemnity on a claim not otherwise excluded under the policy. The court rejected the argument that the claims against the president were for contribution or indemnity. The president argued that the contribution or indemnity exception applied because he was entitled to "direct" indemnification by the LLC for the very damages it sought. The president relied upon South Dakota law authorizing LLCs to reimburse managers for liabilities incurred in the ordinary course of business or for the preservation of the business or its property. The president also pointed out that California law has similar provisions. The president further argued that he was entitled to contractual indemnification under the operating agreements. The court rejected the argument that these provisions brought him within the contribution or indemnity exception to the insured versus insured exclusion. The court stated that the complaint was still one for damages even if the individual himself had a claim for indemnity. The president also relied upon his right to indemnification as a basis to come within a "Presumptive Indemnification" exception to certain exclusions from coverage. The president argued that South Dakota and California law, as well as the LLC operating agreement, required the LLC to indemnify him. The court stated that South Dakota law permits South Dakota LLCs to indemnify officers and agents but does not mandate indemnification. Similarly, the court said California law permits, but does not require, LLCs to indemnify officers. The court pointed out that California law prohibits LLCs from indemnifying officers for breach of fiduciary duty. The court also determined that the terms of the operating agreement did not require indemnity because the LLC was required to do so only on advice of counsel and only after approving such an action.

II. Conversion, Merger, Reorganization

Lenge v. Beizer, No. CV000802145, 2002 WL 31967553 (Conn.Super. Dec. 30, 2002) (treating attorney's transfer of building and law practice to LLCs as conversion resulting in liability of LLCs for pre-conversion liabilities along with attorney).

Holland v. Fahnstock & Co., Inc., 210 F.R.D. 487 (S.D. N.Y. 2002) (adopting magistrate's report stating that sole proprietor was not discharged when sole proprietorship converted to LLC because a sole proprietor retains personal liability for all pre-conversion debts and obligations when it converts to an LLC).

Greenwich Global, LLC v. Clairvoyant Capital, LLC, No. CV010182930S, 2002 WL 31168715 (Conn.Super. Aug. 22, 2002) (holding conversion of limited partnership to LLC was invalid under Delaware law because conversion was undertaken without authorization of the general partner, whom limited partners had attempted, but failed, to effectively remove).

Solar Cells, Inc. v. True North Partners, LLC, No. Civ.A. 19477, 2002 WL 749163 (Del. Ch. April 25, 2002).

A member of an LLC whose interest would decrease from 50% of the voting units to 5% of the voting units in a proposed merger of the LLC sought a preliminary injunction on the basis that the other member and managers appointed by it acted in bad faith in approving the proposed merger and that the defendants would be unable to prove the entire fairness of the merger. First Solar, LLC (the "LLC"), a Delaware LLC, was formed by True North Partners, LLC ("True North") and Solar Cells, Inc. ("Solar Cells") to commercialize solar power technology. Solar Cell contributed the technology, and True North contributed and loaned money to the LLC. Solar Cells and True North each received 50% of the voting membership units, and True North received 100% of the non-voting units. True North had the right to elect three of the five managers, and Solar Cells had the right to elect the other two. The LLC's initial funding was depleted, and the members unsuccessfully negotiated various alternatives for financing and restructuring. Without notice to Solar Cells, the True North managers executed a written consent approving the proposed merger of the LLC into an LLC wholly owned by True North. Solar Cells received notice of the proposed merger four days before it was to close. Under the terms of the merger, the balance of True North's loan to the LLC would be converted into

equity, and Solar Cells would end up with 5% of the voting units in the surviving LLC. The court found that there was a reasonable likelihood that Solar Cells would prevail on the merits, that is, that True North would be required to establish the entire fairness of the merger and would be unable to do so. True North argued that the actions taken to authorize the merger were clearly authorized by the operating agreement and that the operating agreement limited fiduciary duties owed by the True North managers. The court noted that the provisions of the operating agreement limited liability stemming from a conflict of interest but that the limitation on the managers' liability did not bear on the request for injunctive relief. Further, the provisions of the operating agreement protected the managers so long as they acted in good faith. With respect to fair dealing, the court was critical of the lack of an independent bargaining mechanism and failure to give Solar Cells advance notice. ("[I]t is not an unassailable defense to say that what was done was in technical compliance with the law. . . . The fact that the Operating Agreement permits action by written consent of a majority of the Managers and permits interested transactions free from personal liability does not give a fiduciary free reign to approve any transaction he sees fit regardless of the impact on those to whom he owes a fiduciary duty.") The court also found that the valuation used to establish the price was likely not fair because it was irreconcilable with valuations only a few months before True North decided to proceed with the merger. Finally, the court found that irreparable harm was threatened because of the dilution of the equity and voting position of Solar Cells, the difficulty in valuing the LLC, and the limitation of True North's liability for conflicts arising from its fiduciary obligations.

Shoreline Care Limited Partnership v. Jansen & Rogan Consulting Engineers, P.C., No. X06CV940155982S(CLD), 2002 WL 180886 (Conn. Super. Jan. 10, 2002) (finding that standing was satisfied in suit brought in limited partnership name where limited partnership had contracted with defendant and then converted to LLC, relying on language in conversion statute and case law to the effect that LLC is deemed the "same entity" and results from a "seamless transition").

Flippo v. CSC Associates III, L.L.C., 547 S.E.2d 216 (Va. 2001).

The Virginia Supreme Court affirmed a trial court judgment holding the manager of Flippo Land & Timber Co., LLC, a family-owned LLC ("Flippo LLC") liable for breach of fiduciary duty to the LLC and barring the manager and his brother from serving as managers. Flippo LLC held timberlands and had three members: Carter Flippo, who was also manager, Carter's brother Arthur Flippo, and CSC Associates III, L.L.C. ("CSC"), an LLC owned by the three children of Carter's and Arthur's sister. In response to the refusal of CSC to allow Carter and Arthur to transfer their interests in Flippo LLC to individual LLCs for estate planning purposes, Carter consulted a law firm and chose a course of action suggested by the law firm that would allow Carter and Arthur to satisfy their estate planning goals by holding their interests in the timberland business in LLCs. Pursuant to the advice received by Carter from his lawyers, Carter, as manager of Flippo LLC, caused the LLC to transfer all of its non-cash assets to a new LLC. The transfer of Flippo LLC's assets dissolved Flippo LLC under the operating agreement, and CSC was given the option of joining the new LLC if it agreed to the terms of its operating agreement, under which Carter and Arthur could hold their interests through LLCs. (Prior to trial, the new LLC dissolved and returned the assets to Flippo LLC, rendering claims against the new LLC moot.) Carter was found liable for breach of fiduciary duty based upon his orchestration of the transfer of Flippo LLC's assets to the new LLC. He appealed, arguing that he was entitled to a defense based upon his reliance on the law firm's advice. His defense was based upon a provision of the Virginia LLC act protecting a manager who acts in good faith reliance on legal counsel or other professionals. The court found that this provision was not applicable in the instant case. The court pointed out that a manager, like a corporate director, is required by statute to discharge his duties in accordance with his good faith business judgment in the best interests of the LLC. Additionally, the LLC and corporate statutes contain nearly identical provisions protecting managers and corporate directors from liability in the exercise of that judgment under certain circumstances. The court found, however, that Carter was receiving advice in his personal capacity for his own personal interests when he consulted with the law firm, and he was therefore not protected by these provisions. Further, the court rejected the argument that reliance on advice of counsel was a defense to punitive damages, and the award of punitive damages was upheld. The court also upheld the removal of Carter as manager and the prohibition of his brother Arthur's serving as manager on the basis that this point was not properly preserved for appeal. The court finally rejected the claims of Carter and Arthur for dissolution of Flippo LLC and for rescission of the operating agreement based on fraud and mutual mistake, and the court upheld sanctions against Carter and Arthur based upon their allegations of mutual mistake and fraud.

VGS, Inc. v. Castiel, No. C.A. 17995, 2000 WL 1277372 (Del. Ch. Aug. 31, 2000), *aff'd*, 781 A.2d 696 (Del. 2001).

An LLC with three entities as members and three individuals as managers entered a merger approved by two of the three managers pursuant to the operating agreement. In the merger, two members with a combined 75% in the

LLC were relegated to a 37.5% minority interest in the surviving corporation, and Castiel, the individual who controlled the two members with the 75% interest, was excluded from management. Castiel appointed two of the three managers of the LLC (these managers consisted of Castiel and another appointee), but the third manager (the owner of the 25% member) convinced Castiel's appointee to join him in a written consent to merge the LLC without notice to Castiel. The court determined that the LLC agreement permitted a merger to be approved by a vote of a majority of the managers and that Section 18-404(d) of the Delaware LLC act literally permits written majority consents without notice to other managers, but the court concluded that the two managers breached their duty of loyalty to Castiel by failing to give him notice. The following comment by the court regarding the application of Section 18-404(d) is representative of the court's tone throughout the opinion: "The General Assembly never intended, I am quite confident, to enable two managers to deprive, clandestinely and surreptitiously, a third manager representing the majority interest in the LLC of an opportunity to protect that interest by taking an action that the third manager's member would surely have opposed if he had knowledge of it. My reading of Section 18-404(d) is grounded in a classic maxim of equity -- 'Equity looks to the intent rather than to the form.'" The court stated that the two managers who took the action to merge owed a duty of loyalty to the LLC, its investors and Castiel, their fellow manager. The court observed that the LLC agreement allowed the action to merge to be taken by a simple majority of managers (rather than following the default member approval requirement) because all parties understood that Castiel had the right to appoint and remove a majority of the managers. Had notice been given, Castiel of course would have attempted to remove his appointee and block the action. The court rejected the argument that the managers were protected by the business judgment rule. The court said the managers owed Castiel a duty to give him prior notice even if he would have interfered with a plan that they conscientiously believed to be in the best interest of the LLC. If Castiel was not suited to run the company, as claimed by the other two managers, this was an issue to be determined in board meetings with all managers present or in future litigation, if necessary.

Froelich v. Erickson, 96 F. Supp.2d 507 (D. Md. 2000), aff'd, 5 Fed.Appx. 287 (4th Cir. 2001).

The factual background of this case is rather complicated, but the claims involved assertions of fraud, breach of fiduciary duty, and breach of contract by Froelich, an ousted CEO and board member of a Maryland LLC. Froelich was also a member of the LLC who, along with other minority members, was cashed out in a squeeze-out merger following a reclassification of interests of the LLC approved by all members except Froelich. Two documents primarily governed the LLC's operations as an LLC. These documents were an Operating Agreement, which the court characterized as the LLC equivalent of a corporate charter, and a Members Agreement, which the court described as the equivalent of a stockholders' agreement. The operating agreement defined classes of preferred and common interests, the role and responsibility of the board, and the rights and duties of the members. The member agreement supplemented the operating agreement by specifically defining rights of members and restrictions on alienation of interests. The court summed up Froelich's claims as a challenge to "a handful of corporate actions taken by [the LLC's] Board and its Members." The court summed up the key issues in the case as follows: "(i) Did the corporate documents or Maryland corporate law authorize the Board to take the actions that Froelich challenges? (ii) If the Board or the Members had the power to act, by what standard (e.g., business judgment rule or fiduciary duty) should the Court review the Board's exercise of that power? and (iii) Did the Board meet the appropriate standard?" The court characterized the case as arising in the context of corporate decisions by the LLC's board of directors and applied the business judgment rule. The court noted that the LLC's operating agreement stated that the LLC's directors "are subject to the duties of a corporate fiduciary as defined by Maryland law;" thus, the court continued, the LLC board's decisions are measured against the business judgment rule "just as if [the LLC] were a traditional corporation, rather than an LLC." The court found no evidence that the board had acted in bad faith and concluded that the board's actions were protected by the business judgment rule. The court also concluded as follows: the LLC and majority member did not breach a duty of good faith and fair dealing (noting uncertainty under Maryland law as to whether there is a separate cause of action in this regard and stating that the duty in any event only prohibits a party from preventing the other party from performing under the contract); the majority member did not breach a fiduciary duty to Froelich by usurping a business opportunity (stating that a majority interest holder clearly owes the minority a fiduciary duty but finding no breach in view of the board's independent approval of the transaction); the reclassification did not breach the operating agreement or the member agreement (finding that the transaction fell outside a provision in the member agreement restricting redemptions and was governed by the operating agreement, which was amended in accordance with its terms to permit the reclassification). In Froelich's favor, the court found that the LLC owed Froelich severance pay under an employment agreement between the LLC and Froelich and that the reclassification and squeeze-out were related parts of a transaction in which Froelich had properly preserved his statutory right to an appraisal. The court explained that the Maryland LLC statute grants a member the same appraisal rights as an objecting stockholder under corporate law. Maryland corporate law provides appraisal rights in connection with a parent-subsidary merger, and Froelich properly objected to the

squeeze-out merger. The court viewed the reclassification and subsequent squeeze-out merger as a single transaction rather than separate events such that Froelich was entitled to appraisal of his interests immediately prior to the reclassification rather than appraisal of his reclassified interests immediately prior to the merger that occurred five months later.

Cole v. Kershaw, No. Civ.A. 13904, 2000 WL 1206672 (Del.Ch. Aug. 15, 2000).

The plaintiff, a former partner in a Delaware general partnership, challenged the 1993 merger of the partnership into a Delaware LLC. The merger eliminated the plaintiff's interest for cash. The plaintiff claimed the merger was invalid because it was not authorized under the Delaware partnership act or the partnership agreement and, even if otherwise valid, was invalid because it was unfair to the plaintiff. While neither the Delaware partnership act nor the partnership agreement authorized merger of the partnership, the court found that the merger was authorized under the Delaware LLC act, which authorized LLCs to merge with other entities. According to the court, "If this provision, explicitly authorizing LLCs to merge with general partnerships, is to have meaning, the General Assembly must be presumed to have intended that such a merger could go in either direction, i.e., that LLCs would be allowed to merge with general partnerships, or the reverse. Therefore, the fact that the general partnership statute was silent on the subject is of no moment." The court also found that the LLC statute was applicable even though the partnership was formed prior to the effective date of the LLC act. The court concluded that the effect of the merger was to dissolve the partnership. The court agreed with the plaintiff's claim that the merger did not meet the entire fairness test and that the plaintiff was entitled to an award of damages measured by his proportionate share of the fair value of the partnership as of the merger date.

Sinatra ex rel. Nite Life, Inc. v. Edin, 774 So.2d 191(La.App. 2000).

Edin and Sinatra formed Nite Life, Inc. to operate a night club, and each contributed \$50,000 to the corporation for a \$100,000 security deposit required to lease certain premises. Later Sinatra and Edin formed an LLC to take over all assets of the corporation including the lease and the rights to the deposit. Edin, Sinatra and their bookkeeper proceeded as if the lease had been transferred, but the court stated that the lease was not effectively transferred because the lease and deposit constituted substantially all of the assets of Nite Life, Inc. and the technical requirements under the corporate statute were not followed. Sinatra ultimately withdrew from the LLC pursuant to an agreement whereby he received \$50,000 and released the LLC from any liabilities. The corporation was dissolved by action of Edin and Sinatra. About the same time, the lease was canceled because Edin decided to purchase the property, and the \$100,000 security deposit was returned to Edin or the LLC and used as a down payment on the property. Sinatra argued that he was entitled to a distribution of \$50,000 because the lease was never effectively transferred and the deposit should have been returned to the corporation and distributed to the shareholders. The court rejected Sinatra's claim on the basis that he had failed to comply with a requirement under the corporate law that the claim be brought within 90 days of the attempted transfer of the lease. The court also rejected Sinatra's claim for breach of fiduciary duty inasmuch as Sinatra intended that, and gave instructions for, the lease to be transferred, and he proceeded as if the transfer had been accomplished.

Kanefield v. SP Distributing Company, L.L.C., 25 S.W.3d 492 (Mo. App. 2000).

A sole proprietor entered an agreement with an employee, the plaintiff in the case, whereby the proprietor agreed to give the plaintiff 10% of the proceeds from the sale of the business if the plaintiff was employed at the time of the sale. After the proprietor died, his wife operated the business as a partnership in dual capacities, as the surviving spouse and trustee of a family trust. Later the wife transferred portions of her interest to two sons, and the partners converted the partnership to an LLC. The next year, the LLC terminated the plaintiff's employment. The plaintiff sought a declaratory judgment, breach of contract damages, and imposition of an equitable lien. Later the plaintiff added a count of fraudulent conveyance. The trial court dismissed all these claims, and the plaintiff appealed. The court of appeals found that the plaintiff alleged facts that would support the existence of a contract either under successor liability theories or based upon an agreement with the wife after the proprietor's death. The plaintiff alleged that the defendants breached the contract by terminating his employment, failing to pay him his share of the net proceeds upon sale of the business, and repudiating the agreement and offering the business for further sale. The defendants argued that the conversion of the partnership to an LLC was not a sale of the business, but the court stated that there were nevertheless disputes regarding the allegations of breach of contract. The court found that the plaintiff failed to state a claim for fraudulent conveyance in that neither the addition of two partners nor the subsequent conversion to an LLC changed the plaintiff's rights or put the assets of the business beyond his reach. Finally, the court determined that the plaintiff had stated a cause of action for an equitable lien.

Nakano v. Jamie Sadock, Inc., No. 98 CIV. 0515, 1999 WL 1225259 (S.D. N.Y. Dec. 20, 1999).

After the plaintiff invested in an S corporation, the corporation was reorganized as an LLC because the plaintiff was not a U.S. citizen. The plaintiff claimed that the restructuring was a fraudulent scheme by the other members effected without her consent to deprive her of the value of her investment, which involved not only stock in the corporation but rights under a distributorship agreement. The court concluded that the plaintiff failed to allege quantifiable damages. The fact that her interest in the corporation was extinguished was insufficient alone to show damages since the plaintiff received a proportionate interest in the LLC which acquired the assets of the corporation. In a later opinion at 2000 WL 680365 (May 25, 2000), the court held that its partial summary judgment against the plaintiff in this regard did not, under the law of the case doctrine, preclude the plaintiff from amending her complaint to include claims of waste (by means of excessive compensation paid to the managing members of the LLC), misappropriation (by inexplicable withdrawal of initial capital), and breach of fiduciary duty (by the foregoing and preparation of misleading financial statements).

Wolter v. Wisconsin Dept. of Revenue, 605 N.W.2d 283 (Wis. App. 1999).

A family limited partnership which owned three parcels of land reorganized as an LLC, and the family members recorded in the deed records a “Memorandum of Organizational and Operating Agreement” giving notice of the reorganization. The Wisconsin Department of Revenue assessed a real estate transfer tax on the land, and the Tax Appeals Commission found that the transaction was a taxable transfer under Wisconsin law. The appeals court agreed. The court analyzed the Memorandum and concluded it was a “conveyance” by the partnership. Then the court concluded that the conveyance was “for value” even though no cash consideration was involved because the members received capital accounts in the LLC as well as new and more beneficial rights and privileges associated with the LLC form (quoting an article that points out advantages of an LLC over a limited partnership.)

Devereaux’s Carpentry Services, LLC v. Ericson, 25 Conn. L. Rptr. 555, 1999 WL 956768 (Conn. Super. Oct. 6, 1999).

The court held that an LLC was a continuation of its predecessor sole proprietorship and, as such, entitled to enforce a construction contract entered by the sole proprietor. The defendants entered a construction contract with Stephen Devereaux, a sole proprietor doing business as Devereaux’s Carpentry Service, for construction of an addition to the defendants’ home. Thereafter, Devereaux formed Devereaux’s Carpentry Services, LLC. The LLC filed a mechanic’s lien on the defendants’ home, and the defendants claimed that they had no agreement with the LLC. The court followed the Connecticut Supreme Court’s decision in *C & J Builders & Remodelers, LLC v. Geisenheimer*, 733 A.2d 193 (Conn. 1999), to equate the sole proprietor’s formation of the LLC to a statutory conversion such that “all the interests and obligations incurred by, or chargeable against, the sole proprietorship or its assets are transferred by operation of law.”

C & J Builders and Remodelers, LLC v. Geisenheimer, 733 A.2d 193 (Conn. 1999).

The issue in this case was whether an LLC could enforce an arbitration clause in a contract entered by the LLC’s 99% owner prior to the conversion of the owner’s sole proprietorship to an LLC. Charles Pageau, doing business as a sole proprietor, entered a contract with the defendants and later formed an LLC in which he thereafter conducted his business. The operating agreement recited that the LLC was “successor to Charles Pageau [doing business as] C & J Builders and Remodelers” and that Pageau had a 99% membership ownership interest and virtually absolute control over the business. In determining whether the LLC was a “successor in interest” to the contract, the court acknowledged that the formation of the LLC was not a statutory conversion, but the court could find no reason to distinguish between the effect of a statutory conversion of a partnership to an LLC under the Connecticut conversion statute and the conversion of a sole proprietorship to an LLC. The court stated that the conversion statute in effect treats a converted LLC as the “successor in interest” to the converting partnership. The court concluded, therefore, that “where a sole proprietorship converts to a limited liability company, all of the interests and obligations incurred by, or chargeable against, the sole proprietorship or its assets are transferred to the limited liability company by operation of law.” (In the trial court’s opinion, the trial court concluded that the LLC had the benefit of the contract, but did so using veil piercing principles.)

Town of Vernon v. Rumford Associates IV, 732 A.2d 779 (Conn. App. 1999).

The defendant, a partnership that had converted to an LLC and filed bankruptcy after foreclosure proceedings were instituted against it, complained that the trial court improperly awarded fees in connection with the foreclosure in violation of the automatic bankruptcy stay. After the partnership converted to an LLC, the LLC sought to be substituted in the pending foreclosure proceeding against the partnership or, alternatively, to intervene. The LLC also filed bankruptcy. The court denied the LLC’s motion to be substituted or intervene. Thereafter, the court awarded fees and

expenses against the partnership for delay of the foreclosure sale caused by the bankruptcy filing. The partnership claimed that this action violated the automatic stay in the bankruptcy. The court disagreed. The court discussed the effect of the statutory conversion of the partnership to an LLC and noted that the conversion statute allows an action or proceeding pending against the converting partnership to continue “as if the conversion had not occurred.” The court noted that the LLC did not appeal the denial of its motion to be substituted or to intervene. Thus, the court said, the converted LLC never became a party to the suit, and the bankruptcy protection did not apply when the court awarded the additional fees against the partnership.

Blum Shapiro & Company, P.C. v. Searles & Houser, LLC, No. CV 990586283S, 1999 WL 669824 (Conn. Super. Aug. 11, 1999).

An accounting firm organized as an LLC combined its practice with an accounting firm organized as a professional corporation pursuant to a somewhat vague letter agreement. The business continued under the auspices of the PC. The court pointed out that, while the parties used the term “merger,” Connecticut statutes do not permit an LLC to merge with a PC. The court noted that a PC is free to acquire the assets of an LLC, and apparently that was the nature of the transaction. The issue was whether the PC acquired non-compete agreements between the LLC and two of its employees who left the PC a year or so after the “merger” and solicited the firm’s clients. The court concluded that the PC did not acquire the covenants not to compete from the LLC. The court noted that restrictive covenants necessary to protect a proprietor’s business are generally deemed assigned to the purchaser of the business, but the court went on to conclude that the PC did not acquire all the assets of the LLC. Further, noted the court, the entities did not merge, and the PC assigned no value to any covenant not to compete or goodwill.

Maas Technologies, Inc. v. Henning, No. 98 01751, 1999 WL 269109 (La. App. 3 Cir. March 31, 1999).

The opinion in this case was originally available on Westlaw but was removed and is now only referenced in a table at 744 So.2d 238. Two members of an LLC sued the other two members and a third party alleging that a merger of the LLC into one of the defendant members and then into the third party constituted a conversion of the plaintiffs’ assets. The LLC operating agreement had an arbitration clause that required “a dispute arising between the Members concerning the operation, management or buyout of the interest of the LLC” to be submitted to arbitration. The court held that the plaintiffs’ claim fell within the scope of the arbitration clause. The court also found that the dispute must be arbitrated even though one of the defendants was not a party to the operating agreement. The court stated that the plaintiffs’ allegations were directed primarily against the member who controlled the entities with which the LLC merged. The court concluded that the first merger (between the LLC and one of its members) was certainly arbitrable and, if found improper, would make any complaint against the company involved in the second merger moot.

Academy Mortgage Company, LLC v. Juarez, 740 So.2d 708 (La. App. 5th Cir. 1999).

An LLC mortgage company had originally been operated as a partnership, but the partnership converted to an LLC on the advice of partners who were attorneys. Neither the manager, who was also a partner, nor his wife, who was employed in the business, were attorneys. The manager and his wife alleged that two of the attorney partners were negligent in their capacities as counsel to them as follows: failing to inform them of the effect of a conversion from a partnership to an LLC; failing to inform them of the attorney partners’ potential personal gain in power in the new LLC (specifically, failing to inform them that the conversion would enable a majority of the members of the LLC to approve certain matters without consent of the minority, such as dissolution and winding up, transfer of substantially all of the assets, and amendment of the articles of organization and operating agreement); failing to advise them of potential personal financial gain to the attorney partners due to the conversion; failing to advise them to seek separate counsel; failing to advise them as to conflicts of interest; failing to obtain their consent for having a business transaction with the client and serving as counsel to the client at the same time; and failing to give advice and obtain consent regarding the conflict of interest in writing. The manager and his wife alleged that the attorneys had provided legal services to them and the LLC or its predecessor on numerous occasions. The manager and his wife phrased the issue as whether a lawyer commits legal malpractice by entering into a business transaction with a client without the written consent required under the Louisiana Rules of Professional Conduct. The court found it unnecessary to reach the issue of whether the attorneys had an attorney-client relationship with the manager and his wife because, assuming there was an attorney-client relationship, the court found that the action was time-barred.

Child Care of Irvine, L.L.C. v. Facchina, No. Civ. A. 16227, 1998 WL 409363 (Del. Ch. July 15, 1998).

This case involved a dispute between LLC members in which it was unclear whether the parties’ rights were governed by the shareholder agreement of the predecessor corporation, the default provisions of the Delaware LLC act, the merger agreement by which the predecessor corporation was converted to an LLC, or a draft LLC agreement never

signed by the members. The plaintiff members of the LLC sought to remove the defendant member, Facchina, as manager of the LLC. The parties had originally formed the business as a Delaware corporation. The corporation was subsequently converted into an LLC by virtue of a merger of the corporation into a newly formed Delaware LLC which survived the merger. An LLC agreement for the new LLC was never signed. The plaintiffs claimed that the shareholder agreement of the predecessor corporation reflected the terms of the members' agreement for the operation of the LLC. Alternatively, the plaintiffs relied upon the default right to remove a manager under the Delaware LLC act. Facchina claimed that a draft LLC agreement never signed by the members governed their relationship. Alternatively, Facchina claimed that the merger agreement itself was the LLC agreement. The court concluded that summary judgment for either side was inappropriate because there were sharply disputed facts and insufficient undisputed facts to support a legal ruling on the issues before the court. The court noted that both the shareholder agreement and the draft LLC agreement contained arbitration provisions and encouraged the parties to pursue arbitration in California.

Darnet Realty Associates, LLC v. 136 East 56th Street Owners, Inc., 153 F.3d 21 (2d Cir. 1998).

A real estate development partnership which owned shares in an owners' corporation reorganized as a New York LLC, and the court found the successor LLC to be the same continuing entity for purposes of the statutory termination window under Section 3607(b) of the Condominium and Cooperative Conversion Protection and Abuse Relief Act.

Weinshel v. Capossela, Cohen, Engelson & Colman, P.C., No. CV 320454, 1997 WL 325835 (Conn. Super. June 6, 1997).

This case dealt principally with corporate law issues arising when an accounting firm which was operating as a professional corporation changed its name and transferred its assets to a newly formed LLC. Capossela, Cohen, Engelson & Colman, P.C. changed its name to C.C.E. & C., P.C. and transferred its assets to a newly formed LLC which began doing business under the name Capossela, Cohen, Engelson & Colman, LLC. The plaintiff, a shareholder and former employee of the PC, asserted various causes of action against the PC, the new LLC, and individual shareholders of the PC based upon the alleged failure of the defendants to make certain buy-out payments owed the plaintiff following his departure from the PC. This opinion dealt with the plaintiff's request that the court enjoin the dissolution of the PC or appoint a receiver for winding up the PC's affairs. As the basis for such relief, the plaintiff asserted that the PC's change of name, sale of assets, and proposed dissolution had not received shareholder approval as required by the corporate statutes. The court disagreed and denied the request for injunctive relief or appointment of a receiver. A subsequent related opinion appears at 1999 WL 171404 (Conn. Super. March 1, 1999).

Kansas Public Employees Retirement System v. Reimer & Kroger Associates, Inc., 60 F.3d 1304 (8th Cir. 1995).

While the focus of this case is not on LLC issues, the court does discuss in a footnote the effect of the conversion of a partnership to an LLC. A law firm that had converted from a partnership to an LLC under Missouri law sought to intervene in a lawsuit brought by the Kansas Public Employees Retirement System (KPERS) against various defendants. KPERS had previously notified the law firm that it intended to add it as a defendant in the instant case pending in federal court but later indicated that it intended to assert its claims against the law firm in a separate suit to be filed in state court. The law firm then sought to intervene in the suit in federal court. KPERS attempted to make an issue out of the fact that its correspondence and draft pleadings all referred to the law firm as a partnership rather than an LLC. The court referred to this distinction as "disingenuous" and pointed out that, under the Missouri conversion provisions, the LLC acquired all of the former partnership's "rights, privileges, powers, debts, [and] causes of action" and was burdened with all of its "duties, debts, liens, liabilities and rights of creditors." Additionally, the law firm had admitted its responsibility for paying any judgment against the former partnership.

JJ. Successor Liability

Schawk, Inc. v. City Brewing Co., LLC, No. 02-1833, 2003 WL 1563767 (Wis.App. March 27, 2003) (stating that, while Wisconsin courts typically apply successor liability rules to corporate entities, the court saw no reason why the principles of successor liability should not apply to LLCs such as the purchasing LLC in question, and concluding that the plaintiff failed to place in dispute any of the exceptions to the general rule against successor liability so as to avoid summary judgment).

Lenge v. Beizer, No. CV000802145, 2002 WL 31967553 (Conn.Super. Dec. 30, 2002) (characterizing attorney's transfer of building and law practice to LLCs as conversion resulting in liability of LLCs for pre-conversion liabilities along with attorney).

Leber v. Universal Music and Video Distribution, Inc., 225 F.Supp.2d 928(S.D. Ill. 2002).

The plaintiffs sued for breach of a collective bargaining agreement of Universal Music and Video Distribution, Inc. (“Universal”) and sought to hold an LLC in which Universal was a member and the LLC’s other corporate member (“Panasonic”) liable under various theories, including successor liability. The court applied successor liability principles as they have developed in the labor law context and concluded that neither the LLC nor Panasonic were the alter egos of Universal.

Weldon v. Great White North Distribution Services, L.L.C., 197 F.Supp.2d 893 (E.D. Mich. 2002) (applying corporate successor liability principles in context of Delaware corporation’s continuation of Virginia LLC’s business).

Crane Construction Company v. Klaus Masonry, LLC, 114 F. Supp.2d 1116 (D. Kan. 2000).

The court in this case acknowledged that corporate successor liability rules apply to other forms of business organizations and cited the *LiButti* case, in which the mere continuation doctrine was applied where the predecessor was a sole proprietorship and the successor an LLC. The court refused to apply the mere continuation doctrine to this case, in which a creditor of a deceased sole proprietor was attempting to impose liability on the LLC formed to carry on the business after the sole proprietor’s death by the sole proprietor’s son.

Kanefield v. SP Distributing Company, L.L.C., 25 S.W.3d 492 (Mo. App. 2000).

A sole proprietor entered an agreement with an employee, the plaintiff in the case, whereby the proprietor agreed to give the plaintiff 10% of the proceeds from the sale of the business if the plaintiff was employed at the time of the sale. After the proprietor died, his wife operated the business as a partnership in dual capacities, as the surviving spouse and trustee of a family trust. Later the wife transferred portions of her interest to two sons, and the partners converted the partnership to an LLC. The next year, the LLC terminated the plaintiff’s employment. The plaintiff sought a declaratory judgment, breach of contract damages, and imposition of an equitable lien. Later the plaintiff added a count of fraudulent conveyance. The trial court dismissed all these claims, and the plaintiff appealed. The court of appeals found that the plaintiff alleged facts that would support the existence of a contract either under successor liability theories or based upon an agreement with the wife after the proprietor’s death. The plaintiff alleged that the defendants breached the contract by terminating his employment, failing to pay him his share of the net proceeds upon sale of the business, and repudiating the agreement and offering the business for further sale. The defendants argued that the conversion of the partnership to an LLC was not a sale of the business, but the court stated that there were nevertheless disputes regarding the allegations of breach of contract. The court found that the plaintiff failed to state a claim for fraudulent conveyance in that neither the addition of two partners nor the subsequent conversion to an LLC changed the plaintiff’s rights or put the assets of the business beyond his reach. Finally, the court determined that the plaintiff had stated a cause of action for an equitable lien.

Baker v. David A. Dorfman, P.L.L.C., No. 99Civ.9385(DLC), 2000 WL 1010285 (S.D. N.Y. July 21, 2000), aff’d, 232 F.3d 121 (2nd Cir. 2000).

Baker obtained a judgment against David Dorfman for legal malpractice and fraud. Subsequently, Dorfman formed a professional LLC and began to operate his law practice through the PLLC. In this action, Baker sought to hold the PLLC liable on the judgment against Dorfman as a successor in interest. The court concluded that the PLLC was liable as a successor in interest. The court found no reason to doubt that the “traditional rules of successor liability are applicable to limited liability companies.” The court also commented that the facts of the case supported an inference that Dorfman formed the LLC as a fraudulent attempt to escape his obligation to Baker. The court of appeals affirmed the district court’s judgment imposing successor liability in a per curiam opinion in which it praised the lower court’s “well-reasoned and thorough” opinion. The court of appeals noted in particular its agreement with the lower court’s application of successor liability “regardless of whether the predecessor or successor organization was a corporation or some other form of business organization.” The court noted in a footnote that, because the defendants never raised the issue, it expressed no opinion regarding the extent to which New York income exemptions might limit the application of successor liability where the alleged successor is a single-member company formerly operated as a sole proprietorship.

LiButti v. United States, 178 F.3d 114 (2nd Cir. 1999).

In this tax case, the court determined that a Kentucky LLC was not subject to personal or in rem jurisdiction of the New York court under a minimum contacts analysis. The court also rejected an alternative argument by the IRS based upon Rule 25(c) and Rule 71 of the Federal Rules of Civil Procedure. The exercise of personal jurisdiction under this approach required that the LLC be a successor in interest to a sole proprietorship under New Jersey successor liability law. The court recited the four exceptions to non-liability where a company transfers assets to another company

under New Jersey law and noted that the rule and its exceptions apply regardless of whether the predecessor or successor organization is a corporation or some other form of business. The LLC did not fall into any of these exceptions.

KK. Attorney Liability, Disqualification

Falcigno v. Tesei, No. 105039/2002, 2003 WL 105349 (N.Y. Sup. Jan. 7, 2003).

Creditors of an LLC alleged that the LLC fraudulently assigned its assets for the purpose of rendering the LLC insolvent, defrauding the plaintiffs, and avoiding the LLC's obligations to the plaintiffs. The court applied corporate law to conclude that the attorney for the LLC did not owe a fiduciary duty to creditors of the LLC. The court also determined that the 10% owner of the LLC did not state a cause of action for malpractice against the LLC's attorney. Even if the 10% owner could be considered a client, said the court, he had not sufficiently alleged causation. The court had serious doubts as to whether an attorney for a "corporation" has a duty to the "corporate shareholders." The court also concluded that the plaintiffs failed to state a cause of action for participating in a fraudulent conveyance. The court concluded that the simple act of representing a client in a transaction should not be sufficient to state a claim against an attorney unless the creditor is aware of particular facts that show the attorney counseled the client to engage in a fraud.

McLeod v. Jackson, 829 So.2d 722 (Miss.App. 2002).

McLeod hired an attorney to assist him in forming an LLC with two other members. The attorney drafted the certificate of formation and an LLC agreement. The blanks regarding the contributions of the members were never completed, and McLeod sued the attorney for malpractice. The attorney had advised that the blanks regarding contributions be filled in. One of the other persons forming the LLC stated that he did not want to fill in the information regarding contributions, and the attorney advised that it was not necessary to include the information in the certificate of formation. The court cited the requirements of the Mississippi LLC act regarding formation of an LLC and maintenance of records regarding contributions. A record of contributions is required to be maintained at the LLC's principal place of business unless the information is contained in the certificate of formation. The attorney's summary judgment evidence included an affidavit from an expert on formation of LLCs who stated that the attorney met his duty by pointing out to the members that the contributions needed to be set out in writing. The expert stated that once the decision was made not to include the information in the documents filed with the Secretary of State, it was for the LLC itself to complete the document and maintain the record of contributions. McLeod failed to offer any evidence to create a fact issue, and the court upheld summary judgment in favor of the attorney.

Keyak v. Traverso, No. A095338, 2002 WL 1398060 (Cal. App. 1 Dist. June 28, 2002).

The court upheld the trial court's denial of a motion to disqualify the law firm representing the plaintiffs. The plaintiffs and the defendant entered an oral joint venture that resulted in the formation of a corporation and several LLCs to hold title to properties involved in the venture. The defendant claimed that the plaintiffs' lawyer represented him and the entities in matters related to the litigation and should be disqualified. The lawyer had written numerous transmittal letters which were copied to the defendant stating that the lawyer did not represent the defendant and advising that the defendant have his own counsel. The trial court found the defendant's testimony that he did not receive these letters was not credible. The defendant did not directly challenge this finding but argued that the letters showed that the lawyer represented the joint venture and the entities formed and, by extension, the defendant. The court of appeals found ample evidence to support the trial court's implied findings supporting its denial of the disqualification motion. Finally, the court of appeals upheld the decision of the trial court to defer decision on whether the law firm should be disqualified because the lawyer representing the plaintiff was likely to be a witness at trial. The court found that the inquiries involved with respect to this issue were appropriately deferred to a later stage of the litigation.

Credit Index, L.L.C. v. Risk Wise Intl. L.L.C., 746 N.Y.S.2d 885 (N.Y. Sup. 2002).

The plaintiff LLC sought an order disqualifying the law firm representing the defendants on the grounds that the law firm represented an individual founder, manager, and (directly and through affiliates) majority owner of the LLC plaintiff on various matters including the negotiation of the operating agreement of the predecessor to the LLC plaintiff. The law firm claimed the operating agreement of the predecessor LLC bore no similarity to the operating agreement of the plaintiff LLC, but the court concluded the law firm's representation of the individual involved matters substantially related to the issues in the case. The motion to disqualify was granted.

In re Woods (Cundy v. Woods), 284 B.R. 282 (D. Colo. 2001).

The plaintiffs and the debtor were investors who entered a joint venture agreement and formed an LLC to secure financing and manage a real estate project. The debtor was also the attorney for the LLC (referred to in the case as the

joint venture) and a member of the management committee. The plaintiffs alleged that the debtor owed them a fiduciary duty as a co-venturer, management committee member, and attorney for the venture, and that his liability for the venture's debt was non-dischargeable because it arose from a defalcation of fiduciary duty when he obligated the venture to loan amounts in excess of borrowing authorizations. The court found that there must be an express or technical trust, not merely a general fiduciary relationship like that arising out of an attorney-client, joint venture or partnership relationship. Additionally, the court found that the bankruptcy court erred in concluding a defalcation had occurred.

Roller v. Walsh, 718 N.Y.S.2d 519 (N.Y. A.D. 4 Dept. 2000).

The court reversed dismissal of a suit by three LLC members against an attorney who provided services in connection with the formation and operation of the LLC and allegedly breached his fiduciary duty and duty of care by advancing the interests of the fourth member.

Levy v. Mukdissi, No. 99-2507, 2000 WL 1473475 (Mass. Super. Aug. 2, 2000).

The court disqualified an attorney who represented a member of an LLC against the other members in a dispute arising out of their dental practice LLC. The court found that an attorney-client relationship had existed between the attorney and the defendant members and that the current representation of one of the members was adverse to the interests of the other three. The court rejected the attorney's argument that the services were solely for the benefit of the LLC, pointing to the fact that the individual members paid for his services. The court stated that the attorney represented the individual interests of all of the members when he prepared the agreement to associate and the subsequent operating agreements.

Academy Mortgage Company, LLC v. Juarez, 740 So.2d 708 (La. App. 5th Cir. 1999).

An LLC mortgage company sued its manager and his wife, who was an LLC employee, for mismanagement and breach of fiduciary duty. The manager, who was also a member of the LLC, and his wife impleaded other members of the LLC, who were attorneys, and alleged legal malpractice against those members. The LLC's business had originally been operated as a partnership, but the partnership converted to an LLC on the advice of partners who were attorneys. Neither the manager nor his wife were attorneys. The manager and his wife alleged that two of the attorney members were negligent in their capacities as counsel to them as follows: failing to inform them of the effect of a conversion from a partnership to an LLC; failing to inform them of the attorney partners' potential personal gain in power in the new LLC (specifically, failing to inform them that the conversion would enable a majority of the members of the LLC to approve certain matters without consent of the minority, such as dissolution and winding up, transfer of substantially all of the assets, and amendment of the articles of organization and operating agreement); failing to advise them of potential personal financial gain to the attorney partners due to the conversion; failing to advise them to seek separate counsel; failing to advise them as to conflicts of interest; failing to obtain their consent for having a business transaction with the client and serving as counsel to the client at the same time; and failing to give advice and obtain consent regarding the conflict of interest in writing. The manager and his wife alleged that the attorney members had provided legal services to them and the LLC or its predecessor on numerous occasions. The manager and his wife phrased the issue as whether a lawyer commits legal malpractice by entering into a business transaction with a client without the written consent required under the Louisiana Rules of Professional Conduct. The court found it unnecessary to reach the issue of whether the attorney members had an attorney-client relationship with the manager and his wife because, assuming there was an attorney-client relationship, the court found that the action was time-barred.

Arifin v. Schude, No. 98 C 1591, 1999 WL 342395 (N.D. Ill. May 14, 1999).

Two members of an LLC sued the third member for various acts of alleged wrongdoing. The plaintiffs also sued their lawyer for malpractice in connection with his representation of them in forming the LLC. The court found that the plaintiffs' pleading adequately stated a cause of action against the lawyer. Specifically, the complaint alleged an attorney-client relationship and breach of the duty of care by making false representations regarding a bank account for the LLC, failure to ensure the bank account was established as represented to the clients, and performance of legal work that furthered the interests of the third member of the LLC and damaged the interests of the clients while being paid with the clients' funds.

Burton v. Selker, 36 F. Supp.2d 984 (N.D. Ohio 1999), *aff'd*, 2002 WL 252454 (6th Cir. 2002).

The malpractice claim in this case arose out of a complex series of transactions related to the purchase by the plaintiff of an interest in a professional wrestling league. No significant insight regarding LLCs is provided in the case, but LLCs were formed and utilized in the course of the transactions involved. In general, the case highlights the issues involved in multi-party representation and participation in business ventures related to the client's business. The

defendant lawyer represented his son and a business associate of his son's in their quest to purchase a professional wrestling league. The son's business associate ultimately sued the lawyer for legal malpractice, claiming that the defendant engaged in self-dealing, favoritism toward the son to the plaintiff's detriment, failures to disclose, and multiple client representation without effective waiver of the conflicts of interest. Among the plaintiff's complaints was the alleged failure of the lawyer to disclose his role in forming and investing in an LLC that played a part in a merchandising arrangement among the plaintiff, the lawyer's son, and the wrestling league they sought to purchase. Ultimately, the court granted summary judgment in favor of the lawyer on the malpractice claim. A critical factor in the lawyer's favor was a written engagement letter signed by the plaintiff that the court deemed a sufficient waiver of the conflicts of interest.

Peaceful Family Limited Partnership v. Van Hedge Fund Advisors, Inc., No. 98 C 1539, 1999 U.S. Dist. LEXIS 1838 (D. Minn. Feb. 18, 1999).

The plaintiffs brought this lawsuit after they lost a substantial amount of their investment in an LLC. The plaintiffs sued their investment advisor for securities fraud, and the plaintiffs asserted legal malpractice, breach of fiduciary duty, and negligent misrepresentation claims against the LLC's lawyers. The plaintiffs alleged that the LLC's lawyers were negligent in drafting an Offering Memorandum, misrepresenting and omitting various material facts, and in various acts and omissions related to efforts to deal with a prohibition imposed on one of the LLC's managers that prevented his trading on the Chicago Board Options Exchange. In analyzing the plaintiff's claims, the court spoke in corporate terms and relied on case law in the corporate context. The court held that there was no attorney-client relationship between the plaintiffs and the LLC's lawyers, nor were the plaintiffs the intended beneficiaries of the attorney-client relationship between the lawyers and the LLC. Additionally, the plaintiffs failed to establish any other duty on the part of the lawyers to communicate accurate information to them. Thus, the plaintiffs failed to state a claim against the lawyers.

LL. Attorney Client Privilege

Charter One Bank, F.S.B. v. Midtown Rochester, L.L.C., 738 N.Y.S.2d 179 (N.Y. Sup. 2002) (referring to LLC as corporation throughout discussion of whether attorney/client privilege attached to written communication between two LLC employees containing recitation of oral legal advice rendered by attorneys and concluding that this "written communication between corporate employees for the purpose of facilitating the rendition of legal advice in the course of the professional relationship between the attorney and the corporate client" was privileged).

Seegerstrom v. United States, 87 A.F.T.R.2d 2001-1153, 2001-1 USTC ¶ 50,315, 2001 WL 283805 (N.D. Cal. 2001) (finding documents relating to attorney's representation of mother and son in estate planning matters, including assistance in formation of LLC, fell within legal representation, rather than "business advice" not protected by privilege, that certain non-privileged facts were protected because interwoven with privileged communications, and that communications with accountants and financial advisors were protected because they were intended to be in confidence for the purpose of assisting attorney in rendering legal services).

Medical Waste Technologies, L.L.C. v. Alexian Brothers Medical Center, Inc. No. 97 C 3805, 1998 WL 387705 (N.D. Ill. June 24, 1998) (finding defendant waived attorney/client privilege regarding attorney's representation of defendant in connection with proposed formation of LLC based upon defendant's injection of failure to form LLC as new issue constituting affirmative defense to plaintiff's claims).

MM. Unauthorized Practice of Law

Columbus Bar Assoc. v. Verne, 788 N.E.2d 1064 (Ohio 2003) (holding that accountant's advising clients regarding choice of business entity and drafting LLC articles of organization constituted unauthorized practice of law).

In re ICLNDS Notes Acquisition, LLC, 259 B.R. 289 (Bankr. N.D. Ohio 2001).

An LLC manager of an LLC prepared and filed a Chapter 7 bankruptcy petition on behalf of the LLC. The court held that an LLC comes within the definition of a "person" under the Bankruptcy Code and is eligible to be a debtor, but an LLC must be represented by counsel like a corporation or a partnership. The court further concluded that a lay person who prepares a bankruptcy petition and schedules on behalf of an LLC is engaged in the unauthorized practice of law. The court thus dismissed the case.