

# Don't Throw the Baby Out with the Bath Water: Remedies to Keep an LLC Alive

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Connecticut's current Limited Liability Act allows a judge to dissolve an LLC upon application by a member "whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement."<sup>1</sup> It does not expressly allow the court to grant any other remedy if the LLC members are in conflict. In other words, it's all or nothing—the court either dissolves the LLC and "throws the baby out," or the LLC continues its dysfunctional operation. This article advises two solutions to keep the LLC alive and resolve the underlying problem in a dissolution action.

Dissolution is, of course, a very drastic remedy.<sup>2</sup> It's a death knell to a company that is likely providing jobs, tax revenue to local and state government, and possibly even critical products and services.

Typically, the dispute that brings LLC members to court is a squabble over distributions or control—frequently, claims that ignore the overall good of the company. The LLC is often a small, family-owned business, and these disputes can turn out to be more personal than about operating the business. When members cannot set this baggage aside, and work out their differences, one of them runs to the courthouse and files an action to dissolve the LLC, usually just to gain leverage for a negotiated buyout. But what if the other members do not agree to a buyout, or make unreasonable demands? What if the operating agreement lacks a divorce clause?

The first possible solution is a court-ordered buyout. If an LLC member is faced with defending an expensive dis-

solution action, he should be allowed to buy the other member's interest at a fair price. Connecticut courts should, and likely would, order a remedy that makes more sense—an election to purchase the other member's (usually the dissenting member's) interest. Other jurisdictions, including New York, have recognized an equitable power to order a buyout of the complaining party's ownership interests even in the absence of statutory authorization.<sup>3</sup> Some jurisdictions expressly provide for this buyout option in their LLC Act.<sup>4</sup> Connecticut's Corporations Act allows a buyout at "fair value" of all shares owned by the shareholder petitioning for judicial dissolution.<sup>5</sup> Members of an LLC should have the same opportunity.

Our newly enacted Uniform LLC Act ("CULLCA"), which goes into effect on July

1, 2017, will likely make this remedy easier to obtain. It doesn't expressly authorize a buyout, but it does permit the court to "order a remedy other than dissolution" upon application for judicial dissolution of the LLC. The statutory grounds in CULLCA, for dissolution or some other remedy, require that the managers or members controlling the company have acted or are acting in a manner that is: (A) illegal or fraudulent; or (B) oppressive and was, is, or will be directly harmful to the applicant.<sup>6</sup> This new section, combined with Connecticut courts' equitable powers, and authoritative, though not binding, caselaw from sister states, should allow the court to order more prompt, less-expensive resolutions to LLC member disputes short of dissolution.

CULLCA also creates a second possible solution. It expressly permits a member to go to court and have a member expelled, a provision that does not exist under the current act. There are three bases for expulsion:

1. The member engages in wrongful conduct that has or will adversely and materially affect the LLC;
2. The member materially breaches the operating agreement or his or her duty in a willful or persistent manner; or
3. The member engages in conduct in the LLC's affairs that makes it not reasonably practicable to carry on the LLC's affairs with the person as a member.<sup>7</sup>

Accordingly, if a court finds that an LLC member meets one of the three conditions, it must grant the remedy of expulsion. The first two appear straightforward, and the final condition includes the same "reasonably practicable" language as the current LLC Act; thus, Connecticut caselaw, though sparse, will provide some guidance on its meaning, as should caselaw under the Uniform Partnership Act, which uses the same "reasonably practicable" language.<sup>8</sup>

New Jersey has enacted a Revised Uniform Limited Liability Company Act (RULLCA), containing the same provi-

sion. The New Jersey Supreme Court, in a recent case where an LLC filed an action to expel a member, set forth a seven-factor test to assess whether an LLC can "reasonably" carry on, notwithstanding a member's conduct:

1. the nature of the LLC member's conduct relating to the LLC's business;
2. whether, with the LLC member remaining a member, the entity may be managed so as to promote the purposes for which it was formed;
3. whether the dispute among the LLC members precludes them from working with one another to pursue the LLC's goals;
4. whether there is a deadlock among the members;
5. whether, despite that deadlock, members can make decisions on the management of the company, pursuant to the operating agreement or in accordance with applicable statutory provisions;
6. whether, due to the LLC's financial position, there is still a business to operate; and
7. whether continuing the LLC, with the LLC member remaining a member, is financially feasible.<sup>9</sup>

Because Connecticut does not have a strong body of caselaw providing guidance for the meaning of "reasonably practicable," this New Jersey case may be helpful in analyzing expulsion under the new Act. Cases interpreting and applying the meaning of "reasonably practicable" under the Uniform Partnership Act should also help lawyers involved in these types of cases.

If you bring an LLC dissolution action before the new Act goes into effect, and seek to avoid "throwing the baby out with the bathwater," quickly file a motion or election to buy interests, after including an equitable claim for buyout in the complaint. When defending such an action, try to avoid pre-answer motion tactics, which only delay the proceedings (unless of course such motions are necessary), answer the complaint with a counterclaim for equitable buyout, and then file a simi-

lar motion. Or, after the new Act goes into effect, attempt to settle the dispute, then seek to expel the opposing member so the company can remain intact. **CL**

## Notes

1. Conn. Gen. Stat. § 34-207.
2. The trial court has discretion to order dissolution or not. *Brennan v. Brenna Associations et al.*, 293 Conn. 60, 79 (2009). Therefore, if the trial court orders dissolution, that determination is subject to the difficult to overcome "abuse of discretion" standard. *Id.*
3. *See, e.g., Mizrahi v. Cohen*, 961 N.Y.S.2d 538, 542 (N.Y. App. Div. 2d Dept. 2013) (While "[t]he Limited Liability Company Law does not expressly authorize a buyout in a dissolution proceeding . . . [n]onetheless, in certain circumstances, a buyout may be an appropriate equitable remedy upon the dissolution of an LLC."), *leave to appeal dismissed*, 992 N.E.2d 421 (N.Y. 2013); *In re Super. Vending, LLC*, 898 N.Y.S.2d 191, 192 (N.Y. App. Div. 2d Dept. 2010); *Lyons v. Salamone*, 32 A.D.3d 757, 821 N.Y.S.2d 188 (1st Dep't 2006). *But see, Kassab v. Kasab*, 137 A.D.3d 1138, 1140, 27 N.Y.S.3d 680, 682-83 (N.Y. App. Div. 2016) ("Here, since . . . the petitioner failed to state a cause of action for the judicial dissolution of the LLC pursuant to Limited Liability Company Law § 702, there is no basis to invoke the equitable remedy of a buyout.").
4. States that offer express statutory buyout guidelines in their LLC statutes include California (Cal. Corp. Code § 17707.03(c) (1) (West)), Florida (Fla. Stat. Ann. § 605.0706 (West)), Illinois (805 Ill. Comp. Stat. Ann. 180/35-1(b)), Minnesota (Minn. Stat. Ann. § 322B.833(2) (West)), North Dakota (N.D. Cent. Code Ann. § 10-32.1-50(2) (West)), and Utah (Utah Code Ann. § 48-3a-702 (West)).
5. Under Conn. Gen. Stat. § 33-900, when a shareholder petitions for judicial dissolution, other non-petitioning shareholders or the corporation itself may buy out that interest and have the matter dismissed. Within ten days after commencement of the dissolution proceeding, the corporation must notify all shareholders of the right to purchase petitioner's shares, and if the parties cannot agree on a fair price, the court, upon application, will stay the proceeding under § 33-896 and determine a fair value.
6. Uniform Limited Liability Company Act, 2016 Conn. Legis. Serv. P.A. 16-97 (H.B. 5259) (WEST), Section 56(b).
7. Uniform Limited Liability Company Act, 2016 Conn. Legis. Serv. P.A. 16-97 (H.B. 5259) (WEST), Section 54(5).
8. Conn. Gen. Stat. § 34-555(5).
9. *IE Test, LLC v. Carroll*, 226 N.J. 166, 183