BUSINESS ASSOCIATIONS

EVAN J. LEIBHAN[†] AND CLARA L. SEYMOUR[††]

---

† Partner, Honigman Miller Schwartz and Cohn LLP. B.A., 2004, High Honors, Michigan State University; J.D., 2007, *cum laude*, Wayne State University Law School.
†† Associate, Honigman Miller Schwartz and Cohn LLP, B.A., 2007, with High Distinction, University of Michigan; J.D., 2010, University of California Berkeley School of Law.

I. INTRODUCTION

This Article discusses significant developments in the law of business associations during the *Survey* period.[1] This Article focuses primarily on the published decisions of the Michigan Court of Appeals decided during the *Survey* period and recent amendments to the Michigan Limited Liability Company Act[2] enacted during the *Survey* period. During the *Survey* period, the Michigan Court of Appeals reported only three cases concerning the law of business associations and the Michigan Supreme Court did not report any cases concerning the law of business associations. In addition, there were no amendments to the Michigan Business Corporation Act,[3] the Michigan Revised Uniform Limited Partnership Act,[4] or the Michigan Uniform Partnership Act[5] during the *Survey* period.

II. BACKGROUND

A. Dutton Partners LLC v. CMS Energy Corporation

1. Plaintiff Unable to Pierce the Corporate Veil Without a Showing of Fraud, Wrongdoing, or Some Misuse of the Corporate Form by the Defendant

In *Dutton Partners LLC v. CMS Energy Corporation*,[6] the trial court denied the defendant's motion for summary disposition where the defendant claimed that the plaintiff sued the wrong party.[7] On appeal, the court of appeals reversed and remanded the trial court's denial of the defendant's motion for summary disposition.[8] In doing so, the court of appeals held that "a showing of fraud, wrongdoing, or misuse is required under Michigan law in order to prevail on an alter-ego theory of liability

1. The *Survey* period covers statutes enacted or repealed and cases decided between June 1, 2010, and May 31, 2011.
2. *See* MICH. COMP. LAWS ANN. §§ 450.4101-5200 (West 2002).
3. *See* MICH. COMP. LAWS ANN. §§ 450.1101-2099 (West 2002).
4. *See* MICH. COMP. LAWS ANN. §§ 449.1101-2108 (West 2002).
5. *See* MICH. COMP. LAWS ANN §§ 449.1-48 (West 2002).
6. 290 Mich. App. 635, 645 n.5, 802 N.W.2d 717 (2011).
7. *Id.* at 640.
8. *Id.* at 645-46.

. . . ."[9] The court of appeals held that the plaintiff failed to demonstrate any such fraud or wrongdoing on the part of the defendant.[10]

In this case, the plaintiff, Dutton Partners LLC, sued the defendant, CMS Energy Corporation ("CMS"), a holding company with no employees or operations, for damages that resulted from a gas pipeline rupturing on plaintiff's property.[11] The pipeline was owned and operated by CMS's subsidiary, Consumers Energy Company ("Consumers").[12] The plaintiff filed its lawsuit one day before the statute of limitations expired and failed to name Consumers as a co-defendant.[13] The plaintiff later moved to amend its complaint to add Consumers as a co-defendant, but the trial court denied the motion.[14] Accordingly, in order to recover for damages, the plaintiff had to demonstrate either (1) that CMS was responsible for the pipeline's maintenance, repair, or inspection or (2) that CMS was responsible for the negligence of its subsidiary, Consumers, under an alter-ego or veil piercing theory of liability.[15] The evidence revealed that CMS had no responsibility for the pipeline's maintenance, repair, or inspection, leaving the plaintiff with only an alter-ego theory of liability to pursue its claim for damages.[16]

To pierce the corporate veil and obtain relief from the parent entity or owners of a company, the court of appeals noted that a plaintiff must demonstrate that "(1) the corporate entity is a mere instrumentality of another entity or individual, (2) the corporate entity was used to commit fraud or a wrong, and (3) that as a result, the plaintiff [must have] suffered an unjust injury or loss."[17] In general, the mere instrumentality or alter-ego test of prong one goes to whether there was some abuse of the corporate form.

With respect to the mere instrumentality or alter-ego test, the trial court determined that the undisputed evidence presented material questions of fact on whether CMS and Consumers were alter egos of each other.[18] In particular, the trial court noted the following facts: (1)

---

9. *Id.* at 645.

10. *Id.* at 646.

11. *Id.* at 636-38.

12. *Dutton Partners*, 290 Mich. App. at 637. The majority of CMS's income is derived from Consumers, although CMS has other subsidiaries involved in the power and energy industry. *Id.*

13. *Id.*

14. *Id.* at 649.

15. *See id.*

16. *Id.* at 640.

17. *Id.* at 643 (citing RDM Holdings, Ltd. v. Continental Plastics Co., 281 Mich. App. 678, 715, 762 N.W.2d 529 (2008)).

18. *Dutton Partners*, 290 Mich. App. at 640-41.

defendant's 2007 Annual Report lists Consumers's gas pipelines as assets of defendant; (2) the companies share the same physical address and phone number; (3) the Universal Resource Locator or website used by Consumers was registered to CMS and not Consumers; (4) the companies share the same in-house counsel; (5) Consumers's letterhead describes itself as "A CMS Energy Company;" and (6) defendant "enjoys the accounting benefit of depreciating the gas pipelines which are supposedly owned by Consumers (collectively, the "Alter Ego Facts").[19] There were other facts suggesting that CMS and Consumers were separate and distinct entities in both form and substance, including that the entities had separate boards of directors and officers, separate board meetings, maintained separate books and records, and reported their financial results separately (albeit on joint filings with the Securities Exchange Commission).[20] Although the court of appeals reversed and remanded the trial court's judgment on other grounds, it agreed with the trial court's determination that the Alter Ego Facts presented legitimate questions regarding whether Consumers was a mere instrumentality of CMS.[21]

With respect to the second prong of the corporate veil piercing test, however, the court of appeals held that "plaintiff failed to demonstrate any evidence of fraud, wrongdoing, or misuse of the corporate form."[22] The plaintiff argued that "Michigan law does not require such a showing in order for a parent corporation to be held liable for the acts of its subsidiary."[23] The plaintiff, however, cited no binding authority for this proposition, and the court of appeals was unable to find any Michigan case confirming plaintiff's position.[24]

2. Practical Implications of Dutton Partners LLC

Other than the practical lesson that a plaintiff should name the correct defendants in its complaint, and prior to the expiration of the relevant statute of limitations, this case is significant for two other reasons. First, it reinforces the rule that Michigan law requires a showing of "fraud, wrongdoing, or misuse of the corporate form" to pierce the corporate veil. Second, it suggests that facts that are not traditionally cited to constitute a showing of alter ego (e.g., ownership of websites,

19. *Id.*
20. *Id.* at 638.
21. *Id.* at 644.
22. *Id.* at 644.
23. *Id.* at 645.
24. *Dutton Partners*, 290 Mich. App. at 644-45.

accounting treatment, same in-house counsel, etc.) could form a valid basis for satisfying the alter-ego test, even if the court of appeals ultimately did not have to decide the case on this issue.

B. Florence Cement Company v. Vettraino

1. Plaintiff Able to Pierce the Corporate Veil

Plaintiff Able to Pierce the Corporate Veil Where (i) the Defendant Company and Defendant Owners Treated Each Other's Liabilities as Their Own, (ii) Defendant Company Was Intentionally Undercapitalized at Time of Contracting With Plaintiff, and (iii) an Officer and Member of the Defendant Company Falsified Documents to the Company's Lender Relating to Amounts Owed to Plaintiff.

In *Florence Cement Company v. Vettriano*,[25] the trial court refused to pierce the corporate veil with respect to all amounts owed by the defendant company to the plaintiff because it held that the plaintiff failed to demonstrate a fraudulent act or wrongdoing.[26] On appeal, the court of appeals reversed and remanded the trial court's (i) no cause of action judgment against two defendants that were members of Shelby Property Investors, L.L.C. ("Shelby"), a development company that breached its construction contract with the plaintiff by failing to pay for services rendered to Shelby, and (ii) judgment for limited damages on a several basis against two other members of Shelby who received improper distributions.[27] In doing so, the court of appeals held that plaintiff successfully pierced the corporate veil, and that certain conversions of capital investments and other payments by Shelby to its members constituted improper distributions.[28]

In July of 2006, Shelby contracted with the plaintiff, Florence Cement Company ("Florence"), for concrete and asphalt services for Shelby's residential development project.[29] Despite completing the contract, Shelby never paid the full amount of the contract to Florence, and Florence obtained a consent judgment against Shelby in the amount of $114,000.[30] Shelby had four members: Ernest Essad, Dante Bencivenga, A.V. Investment Corporation ("AVIC"), and Antonio

25. 292 Mich. App, 461, 807 N.W.2d 917 (2011).
26. *Id.* at 467.
27. *Id.* at 464.
28. *Id.* at 471-72, 477-78.
29. *Id.* at 464.
30. *Id.* at 467.

Vettraino, the latter of whom became a former member at the time plaintiff filed its suit.[31]

The facts and circumstances surrounding Shelby and its members, including certain transactions between Shelby and some of its members, led the court of appeals to characterize the facts regarding "mere instrumentality" in this case as "a hallmark of a claim for piercing the corporate veil."[32] First, Shelby was undercapitalized when it entered into its contract with Florence and treated certain financial obligations of its members as its own obligations.[33] After obtaining its initial cost estimate for the project, Shelby determined that it would need an additional $700,000, which was obtained through a private loan with Comerica Bank ("Comerica"). The loan was guaranteed by its members, as opposed to the members making loans or contributing capital to Shelby.[34] Later, Shelby needed additional funds for the project.[35] To obtain these funds, Essad and Bencivenga personally borrowed $300,000 from Comerica and transferred these funds to Shelby.[36] These proceeds were not documented as capital contributions and no promissory note was delivered by Shelby to Essad or Bencivenga regarding any loan or the terms thereof.[37] Instead, Essad testified that Shelby reimbursed him and Bencivenga by paying Comerica on account of the loans taken by Essad and Bencivenga with Comerica.[38] In other words, Shelby treated the debt owed by Essad and Bencivenga as its own. In January 2005, Shelby obtained another loan that was guaranteed by its members for $2,134,000, a portion of which was used to pay off the original $700,000 loan.[39] In February 2005, Shelby paid Bencivenga $20,000 for earnest money and $104,000 of the purchase price for certain parcels of land that Bencivenga had acquired for Shelby's development project.[40] The parcels that Bencivenga acquired, however, were never formally transferred to Shelby.[41] Shelby also paid Essad $97,350 for expenses that Essad paid as pre-construction carrying costs.[42] In addition, plaintiff's expert witness testified that Shelby was insolvent from 2004 through

31. *Florence*, 292 Mich. App. at 464.
32. *Id.* at 470
33. *Id.* at 470-71.
34. *Id.* at 464-65.
35. *Id.* at 465.
36. *Id.*
37. *Florence*, 292 Mich. App. at 465.
38. *Id.*
39. *Id.* at 465-66.
40. *Id.* at 466.
41. *Id.* at 469.
42. *Id.* at 466.

2006.[43] This evidence was later corroborated after examining Shelby's tax returns.[44]

In addition to the facts above, in November 2006, Essad signed a sworn statement to Comerica stating that Shelby owed Florence $142,000.[45] The actual amount owed to Florence, however, was $256,577.27.[46] Essad testified that he wanted to draw the full amount on Shelby's mortgage with Comerica to pay Shelby's contractors, even though this amount, coupled with Shelby's cash on hand, was insufficient to pay Florence along with all of Shelby's other contractors.[47] In an attempt to explain the false statement, Essad testified that he talked to someone at Comerica and notified Comerica about what he was trying to accomplish.[48] This conversation, however, did not change the amounts that Essad swore Shelby owed to Florence.[49]

Based on the foregoing facts, the trial court decided not to pierce the corporate veil with respect to Shelby's members, stating "'as you go through the inventory of records that have been provided[,] this project was not underfunded,' and there was no fraudulent act."[50] The court of appeals, however, applied the three-pronged test explained above in the *Dutton* case summary, and it held that all elements were satisfied.[51] First, regarding the "mere instrumentality" element, the court of appeals held that Bencivenga and Essad "clearly did not treat Shelby as an entity separate from themselves."[52] First, Bencivenga acquired parcels of property and "turned [them] over to Shelby without a formal transfer."[53] In addition, both Essad and Bencivenga paid expenses concerning Shelby's development projects, and Shelby reimbursed them directly.[54] Shelby also "made payments at the behest of the defendants" that were not beneficial to Shelby, with Essad writing those distribution checks as Shelby's financial manager.[55] Finally, to remedy Shelby's undercapitalization, on multiple occasions the defendants personally borrowed money from Comerica and treated the debt as an obligation of

43. *Florence*, 292 Mich. App. at 467.
44. *Id.* at 469.
45. *Id.* at 466-67.
46. *Id.* at 466.
47. *Id.* at 467.
48. *Id.*
49. *See Florence*, 292 Mich. App. at 467.
50. *Id.* at 467-68 (alteration in original).
51. *Id.* at 469, 471-72.
52. *Id.* at 469.
53. *Id.*
54. *Id.*
55. *Florence*, 292 Mich. App. at 469-70.

Shelby by having Shelby make payments to Comerica directly for those personal loans.[56] Thus, the defendants "treated their personal liabilities to Comerica as Shelby's liabilities."[57]

With respect to the "fraud or wrongdoing" requirement for piercing the corporate veil, the court of appeals decided contrary to the trial court's conclusion that the plaintiff failed to satisfy the requirement. The court of appeals heavily weighted Essad's false sworn statement to Comerica.[58] The sworn statement contained a representation that Shelby "OWES NO MONEY FOR THE IMPROVEMENT OTHER THAN AS SET FORTH ABOVE," and Essad knowingly swore that Shelby owed about half of the amount it actually owed to Florence.[59] In addition, the court of appeals noted that "Essad, a licensed attorney, is held to a higher standard. His extensive experience and expertise in business formations and transactions clearly should have provided him with the knowledge that falsifying a sworn statement is fraudulent."[60] Also, the court of appeals noted that Shelby made distributions to its members while it was insolvent, and this knowledge (or constructive knowledge) also pointed to fraudulent intent.[61] Finally, with respect to the "unjust injury or loss" element, the court of appeals held that "Florence suffered a significant loss as a result of defendants treating Shelby as a mere instrumentality of themselves and deliberately undercapitalizing Shelby" when Florence "lost over $100,000 of its contractual payment for the work that it undisputedly performed."[62] Having satisfied all three elements, the court of appeals held that the plaintiff could successfully pierce the corporate veil.[63]

2. Improper Distributions

Improper Distributions Made By a Company To or For the Benefit of Its Members While Such Company is Insolvent Are Subject to Recapture, and Any Member Who Votes For or Assents To Such Distributions is Jointly and Severally Liable

Under the Michigan Limited Liability Company Act (the "MLLCA"), a distribution is "a direct or indirect transfer of money or

56. *Id.* at 470.
57. *Id.*
58. *See id.* at 470-71.
59. *Id.* at 471.
60. *Id.*
61. *Florence*, 292 Mich. App. at 471-72.
62. *Id.* at 471.
63. *Id.* at 471-72.

other property or the incurrence of indebtedness by a limited liability company to or for the benefit of its members or assignees of its members in respect of the members' membership interests."[64] The trial court held that Shelby incorrectly recharacterized two separate $20,000 capital contributions from Essad and Bencivenga into loans of $19,000 and that such recharacterization was an improper distribution subject to recapture under the MLLCA.[65] Accordingly, the trial court held that Essad and Bencivenga were liable on a several basis for $19,000 each for such improper distributions.[66] The court of appeals, however, held that the improper distributions far exceeded these recharacterized capital contributions.[67] The court of appeals held that the following payments were also improper distributions because they were transfers of money to or for the benefit of Shelby's members while the company was insolvent: (1) Shelby's 2005 payments of $104,039.50 to Bencivenga, (2) Shelby's 2005 payments of $97,500 to Essad, (3) interest payments to Comerica on the $300,000 loan taken in October 2003, and (4) interest payments on another $226,000 loan taken in November 2005 by Shelby's members where the proceeds were transferred to Shelby.[68]

Finally, with respect to the joint and several liability issue, contrary to the trial court's determination, the court of appeals held that, under the MLLCA "a member . . . that votes for or assents to a distribution" while the entity is insolvent "is personally liable, *jointly and severally*, to the limited liability company for the amount of the distribution that exceeds what could have been distributed" without rendering the entity incapable of paying its debts as they became due.[69] The court of appeals held that Essad's and Bencivenga's assent to the distributions was clear because Essad "personally controlled Shelby's finances and wrote the checks," and Bencivenga, along with Vettraino and Essad, controlled Shelby's operations generally.[70] Therefore, the court of appeals held Essad and Bencivenga "personally liable, jointly and severally," to Shelby for all improper distributions.[71]

---

64. MICH. COMP. LAWS ANN. § 450.4102(2)(g) (West 2002).

65. *Florence*, 292 Mich. App. at 473.

66. *Id.* at 473.

67. *See id.* at 472-73.

68. *Id.*

69. *Id.* at 474 (quoting MICH. COMP. LAWS ANN. §§ 450.4307(1), 450.4308(1) (West 2002)).

70. *Id.* at 474.

71. *Florence*, 292 Mich. App. at 474-75.

3. Practical Implications of Florence Cement Company

There are several practical implications of the *Florence Cement Company* ruling. First, this case reinforces the concept that transactions between a company and its members should be properly evidenced through appropriate documentation and instruments of transfer. It appears that there are several things that Shelby's members could have done to prevent being held personally liable for Shelby's obligations. The members could have documented their transfers of the Comerica loan proceeds to Shelby as separate loans from the members to Shelby and had Shelby make payments directly to the members. Although this approach would arguably strengthen the case that Shelby was undercapitalized, it would demonstrate a respect for the separate corporate form (making it more difficult to satisfy the "mere instrumentality" test) and payments to the members on the account of such loans might not be considered improper distributions. In addition, Essad and Bencivenga should have incurred the pre-construction and other related expenses on behalf of Shelby and purchased the two real estate parcels in Shelby's name (or had some sort of reimbursement contract in place prior to incurring such expenses). Moreover, at minimum, Shelby and Bencivenga should have executed formal purchase and sale documents conveying the real estate parcels to Shelby.

Second, this case illustrates that the "fraud" or "wrong" element of the corporate veil piercing test does not require a showing that defendant committed a "wrong" or "fraud" directly against the plaintiff.[72] Here, Essad committed a "fraud" directly against Comerica, which was not involved in the lawsuit, and the court deemed this fraud (coupled with knowledge of Shelby's insolvency) sufficient to satisfy the test.[73] The "fraud" or "wrong" committed arguably was for the benefit of the plaintiff, as Shelby would have had even less funds with which to pay Florence if Essad had not submitted the false sworn statement. Accordingly, this case seems to stand for the proposition that the "fraud" or "wrong" in the corporate veil test is broadly interpreted and could apply to circumstances where the "fraud" or "wrong" is unrelated to the plaintiff or even inures to the plaintiff's benefit.

Finally, it should be noted that any member that votes for or assents to an improper distribution will be jointly and severally liable for the recapture of these amounts.[74] This represents significant actionable liability against members of limited liability companies and should be

72. *Id.* at 470-71.
73. *See id.* at 470-72.
74. *Id.* at 473-75.

fully considered in connection with all actions taken by a company's members. This case illustrates that assenting to a distribution could be as simple as writing checks to pay for improper expenses or being in a position to control operations generally.[75] This places a high burden on members that participate in company expense decisions to scrutinize any payments the company makes while insolvent, to ensure that such payments are not improper distributions and to object (preferably in writing) to all distributions that are improper.[76]

C. Lakeview Commons Ltd. Partnership v. Empower Yourself, LLC

1. The "Mere Continuation" Prong of Michigan's Successor Liability Test

Under the "Mere Continuation" Prong of Michigan's Successor Liability Test in a Non-Acquisition Context, a Genuine Issue of Material Fact May Exist Where (i) Operations of the Old Company Cease the Same Month as Operations of the New Company Commence, (ii) Both Companies Are in the Same Business, Serve the Same Geographic Area, Operate in the Same Manner, and Maintain Similar Practices With Respect to Corporate Formalities, (iii) Both Companies Have the Same Ownership Structure, Officers, and Bank Signatories, (iv) Both Companies Have the Same Telephone Number, and (v) the New Company's Website Indicates That It Was Formerly Known As the Old Company

In *Lakeview Commons Ltd. Partnership v. Empower Yourself, LLC*,[77] the court of appeals reversed and remanded the trial court's entry of defendant's motion for summary disposition with respect to the issue of whether co-defendant, Hamsa, L.L.C. ("Hamsa") was a "mere continuation" of prior company and co-defendant Empower Yourself,

---

75. See *id.*

76. The recent amendments to the MLLCA adds further clarification. The amendment to MICH. COMP. LAWS ANN. § 450.4308(2) provides as follows:

> For purposes of liability under subsection (1), a member or manager entitled to participate in a decision to make a distribution is presumed to have assented to a distribution unless the member or manager does 1 of the following:
>
> (a) Votes against the distribution.
>
> (b) Files a written dissent with the limited liability company within a reasonable time after the member or manager has knowledge of the decision.

MICH. COMP. LAWS ANN. § 450.4308(2) (West 2002). This presumption increases a member's risk of liability and imposes a significant objection burden.

77. Lakeview Commons Ltd. P'ship v. Empower Yourself, LLC, 290 Mich. App. 503, 802 N.W.2d 712 (2010).

L.L.C. ("Empower") under Michigan successor liability doctrine.[78] The court of appeals also affirmed the trial court's ruling that neither Empower's nor Hamsa's corporate veil should be pierced because the corporate forms of these entities were respected.[79]

In August 2007, Empower ceased operations and Hamsa was created by the former owners of Empower, Troy Swalwell and Phyllis Swalwell.[80] Consequently, the plaintiff sued Empower for breach of a lease agreement with the plaintiff and sued Hamsa under a successor liability theory.[81] Troy admitted that Empower ceased operations in part to avoid its lease agreement with plaintiff.[82] Although no evidence of any purchase of assets between Empower and Hamsa was presented, in its opinion, the court of appeals held that in an acquisition

> where the purchase is accomplished by an exchange of cash for assets, the successor is not liable for its predecessor's liabilities, unless one of the five narrow exceptions applies[:] (1) where there is an express or implied assumption of liability; (2) where the transaction amounts to a consolidation or merger; (3) where the transaction was fraudulent; (4) where some of the elements of a purchase in good faith were lacking, or where the transfer was without consideration and the creditors of the transferor were not provided for; or (5) where the transferee corporation was a mere continuation or reincarnation of the old corporation.[83]

The court of appeals did not focus on the first four exceptions listed above, but instead focused primarily on the fifth exception. The court of appeals cited *Turner v. Bituminous Casualty Company*[84] to explain that a prima facie case for "mere continuation" exists where the plaintiff establishes:

> (1) there is a continuation of the seller corporation, so that there is a continuity of management, personnel, physical location, assets, and general business operations of the predecessor corporation; (2) the predecessor corporation ceases its ordinary

78. *Id.* at 505.
79. *Id.* at 510.
80. *Id.* at 508.
81. *Id.* at 507-08.
82. *Id.* at 510.
83. *Lakeview Commons*, 290 Mich. App. at 507.
84. Turner v. Bituminous Cas. Co., 397 Mich. 406, 417 n.3, 244 N.W.2d 873 (1976).

> business operations, liquidates, and dissolves as soon as legally and practically possible; and (3) the purchasing corporation assumes those liabilities and obligations of the seller ordinarily necessary for the uninterrupted continuation of normal business operations of the selling corporation.[85]

In addition, the court of appeals noted that an additional relevant principal in determining successor liability was "whether the purchasing corporation holds itself out to the world as the effective continuation of the seller corporation."[86] The court of appeals noted the following as evidence demonstrating "mere continuation": (1) Empower ceased operations the same month that Hamsa was created; (2) both entities engaged in the health, fitness, personal training, and yoga industries and provided a venue for independent yoga instructors to teach classes; (3) the entities served the same geographic location; (4) they had identical capital and management structures, with Troy and Phyllis fulfilling the same official roles and owning the same percentage interest in each entity; (5) they had the same registered agent; (6) neither entity had an operating agreement, kept minutes of meetings or distributed earnings to its members; (7) Troy signed tax returns and prepared annual reports for both entities; (8) Troy and Phyllis were authorized signatories for both entities' bank accounts; (9) "Empower's business telephone number became Hamsa's"; and (10) "Hamsa's website stated that it was formerly known as Empower."[87] After reviewing the above facts in the light most favorable to the plaintiff, the court of appeals determined that there was a genuine issue of fact regarding whether Hamsa could be held liable for Empower's breach of the lease agreement based on successor liability.[88]

2. Practical Implications of Lakeview Commons

There are several practical implications of the *Lakeview Commons* ruling. First, this case demonstrates that, despite the prima facie case for "mere continuation" set forth in *Turner*, a plaintiff's successor liability claim can survive summary disposition even if (1) the defendants do not use the same location for their business, (2) there is no evidence that any ordinary accrued expenses or trade payables were expressly assumed or paid by the new company, and (3) other than perhaps the use of the same telephone number in the instant case, there is no evidence presented that

85. *Id.*
86. *Id.*
87. *Lakeview Commons*, 290 Mich. App. at 509.
88. *Id.* at 510.

any assets of the prior company were purchased, transferred, or acquired by the new company.[89] This potential application of successor liability in a non-acquisition context presents risks to entrepreneurs seeking a second chance on a prior failed business effort. Other than using the same telephone number and a website representing the company as being formerly known as Empower, all of the factors relied upon by the court of appeals are consistent with a legitimate attempt to start up the same type of business after a prior venture failed. Under the rationale of the court of appeals, this makes it difficult for members of a limited liability company to start a new business similar to a prior venture without risking potential exposure under Michigan's successor liability doctrine, unless they change the ownership or management structure, change their business operations, change their target market, or wait for an extended (and uncertain) period of time before commencing operations with the new company. These changes may be very doable with a multi-member limited liability company, but could present challenges for a single-member limited liability company where the sole member lacks the ability or desire to provide other services. For example, it would be difficult for the member of a single-member limited liability company law firm to start a new law firm following a bankruptcy or other insolvency event without running the risk of violating the successor liability doctrine enunciated in *Lakeview Commons*. Unless the individual formed a partnership, the ownership structure, management, resident agent, business operations, and target consumer base could very likely be the same. This could significantly impact small entrepreneurs' chances at a fresh start.

III. AMENDMENTS TO THE MICHIGAN LIMITED LIABILITY COMPANY ACT

On December 16, 2010, the MLLCA underwent several amendments.[90] These amendments created several changes to the MLLCA. Many amendments addressed clarification issues, minor technical changes, and other clean-up issues. The most notable amendments, however, are summarized below.

89. *Id.* at 510-11.

90. *See* MICH. COMP. LAWS ANN. §§ 450.4101-5200 (West 2002) and 2010 Mich. Pub. Acts 290.

A. Conversion of Limited Liability Companies into Business Organizations and Conversion of Corporations into Business Organizations

The prior version of the MLLCA only provided that a domestic partnership or domestic limited partnership could convert into a limited liability company.[91] The recent amendments to the MLLCA now provide that a domestic limited liability company may convert into any business organization (i.e., permitting a domestic limited liability company to convert into a corporation).[92] The requirements for converting a domestic limited liability company into a business organization are set forth in MCLA section 450.4708(1).[93] The main requirements include creating a plan of conversion that meets the statutory requirements, approving the plan of conversion by a vote of the limited liability company's members, and filing a certificate of conversion with the administrator under the MLLCA.[94] The amendment requires a "unanimous vote of the members . . . to approve the plan of conversion[,] unless the company's articles or an operating agreement provide otherwise."[95] In addition, if the company's articles or operating agreement provide that conversion may be approved by less than a unanimous vote, then any member that does not vote in favor of the conversion may withdraw from the company and receive the fair value of his interest in the limited liability company.[96]

Conversely, the amendments to the MLLCA also provide that any business organization may convert into a domestic limited liability company.[97] The requirements for converting a business organization into a domestic limited liability company are similar to the requirements for converting a domestic limited liability company into a business organization, except that the specific member voting requirements and appraisal rights are replaced with the requirements under the law governing the internal affairs of the converting business organization.[98]

---

91. *See* MICH. COMP. LAWS ANN. § 450.4707 (West 2002); *see also* James R. Cambridge, James L. Carey, & Daniel Minkus, *Recent Amendments to the Michigan Limited Liability Company Act*, 31 MICH. BUS. L.J. 10 (2011).

92. *See* MICH. COMP. LAWS ANN. § 450.4708 (West 2002). The prior method of converting a domestic limited liability company into a corporation involved merging the limited liability company into the corporation with the corporation being the surviving entity. *See* Cambridge, *supra* note 91, at 10.

93. MICH. COMP. LAWS ANN. § 450.4708(1) (West 2010).

94. *See* MICH. COMP. LAWS ANN. § 450.4708(1)(b)-(d).

95. MICH. COMP. LAWS ANN. § 450.4708(1)(c).

96. *See id.*

97. *See* MICH. COMP. LAWS ANN. § 450.4709 (West 1993), *amended by* 2010 Mich. Pub. Acts 290.

98. *See id.* § 450.4709(1)(c).

B. Permitting a Limited Liability Company to Provide Indemnification to or Insure Members, Managers, or Other Persons

The prior version of the MLLCA only provided that a limited liability company had the right to indemnify its managers.[99] The recent amendments, however, extend indemnification to cover not only managers, but also members and other persons.[100] The amendment also provides that the company may defend such persons where the prior act did not include such powers.[101] In addition, the amendment provides that the limited liability company may "purchase and maintain insurance on behalf of [its] members, managers, or [any] other person [for] any liability or expense asserted against or incurred by that person."[102] This was a power that was not previously contained in the MLLCA.[103]

C. Procedures to Address and Approve Interested Party Transactions

The new MCLA section 450.4409 provides that

> transaction[s] in which a manager or agent of a limited liability company is determined to have an interest . . . [will not be void,] set aside, or give rise to damages if the interested manager or agent establishes any of the following:
>
> (a) The transaction was fair to the company at the time entered into.
>
> (b) The material facts of the transaction and the manager's or agent's interest were disclosed or known to the managers and the managers authorized, approved, or ratified the transaction.
>
> (c) The material facts of the transaction and the manager's or agent's interest were disclosed or known to the members entitled

99. *See* MICH. COMP. LAWS ANN. § 450.4707; *see also* Cambridge, *supra* note 91, at 10-11.

100. *See* MICH. COMP. LAWS ANN. § 450.4216(a) (West 1993), *amended by* 2010 Mich. Pub. Acts 290.

101. *See* MICH. COMP. LAWS ANN. § 450.4707; *see also* Cambridge, *supra* note 91, at 10-11.

102. MICH. COMP. LAWS ANN. § 450.4216(b) (West 1993), *amended by* 2010 Mich. Pub. Acts 290.

103. *See* MICH. COMP. LAWS ANN. § 450.4707 (West 2002).

> to vote and they authorized, approved, or ratified the transaction.[104]

A transaction can be authorized, approved, or ratified for the purposes of subsection (b) above, if a majority of the disinterested managers vote for such action.[105] In addition, a transaction can be authorized, approved, or ratified for the purposes of subsection (c) above, if a majority of the disinterested members entitled to vote approve such action.[106] This amendment helps salvage transactions that might otherwise be void and helps bring the MLLCA more in line with the Michigan Business Corporation Act with respect to addressing interested party transactions.

D. Methods to be Admitted as a Member to a Limited Liability Company in Connection with the Formation of the Company

The amendments to MCLA section 450.4501 expand the methods to which a person may be admitted as a member of a limited liability company.[107] The prior act provided that a person could only become a member of a limited liability company in connection with the formation of the company if the person signed the initial operating agreement.[108] The revised act provides that a person will be admitted as a member of the limited liability company in connection with the formation of the company as follows:

> (a) If an operating agreement includes requirements for admission, by complying with those requirements. (b) If an operating agreement does not include requirements for admission, if either of the following are met: (i) the person signs the initial operating agreement or (ii) the person's status as a member is reflected in the records, tax filings, or other written statements of the limited liability company, or (c) in any manner established in a written agreement of the members.[109]

---

104. MICH. COMP. LAWS ANN. § 450.4409(1)(a)-(c) (West 1993), *amended by* 2010 Mich. Pub. Acts 290.

105. MICH. COMP. LAWS ANN. § 450.4409(2).

106. *Id.* § 450.4409(3).

107. *See* MICH. COMP. LAWS ANN. §450.4501.

108. *See* MICH. COMP. LAWS ANN. § 450.4707; *see also* Cambridge, supra note 91, at 11.

109. MICH. COMP. LAWS ANN. §450.4501(1)(a)-(c).

E. Rights of Judgment Creditors

The amendments to MCLA section 450.4507 clarify that a charging order obtained by a judgment creditor of a member does not give the judgment creditor the right to become a member of the limited liability company.[110] The judgment creditor only has the right to receive distributions that the debtor. member has the right to receive; all membership interests and voting rights of the debtor member are retained unless otherwise provided for in the operating agreement or unless the judgment creditor is admitted as a member under MCLA section 450.4501.[111] In addition, although the judgment creditor has a lien on the debtor member's interests in the limited liability company, the judgment creditor may not foreclose on that lien.[112] The remedies under this provision are the exclusive remedies that a judgment creditor may pursue with respect to a judgment against a member's membership interests.[113] Furthermore, any "court order to which a member may have been entitled that requires the limited liability company to take an action, provide an accounting, or answer an inquiry are not available to such a judgment creditor."[114]

F. Dissolution of a Limited Liability Company Before Commencing Business

Finally, the amendments to the MLLCA also provide that a limited liability company may be dissolved by a vote of the majority of its organizers at any time prior to commencing business.[115] This represents another way to dissolve a limited liability company.

110. *See* MICH. COMP. LAWS ANN. § 450.4507(4) (West 1993), *amended by* 2010 Mich. Pub. Acts 290.

111. *See* MICH. COMP. LAWS ANN. § 450.4507(2).

112. *Id.* § 450.4507(5).

113. *Id.* § 450.4507(6).

114. *Id.* § 450.4507(c).

115. MICH. COMP. LAWS ANN. § 450.4801(e) (West 1993), *amended by* 2010 Mich. Pub. Acts 290.