2016 Georgia Corporation and Business Organization
Case Law Developments

Michael P. Carey
Bryan Cave LLP
Fourteenth Floor
1201 West Peachtree Street, N.W.
Atlanta, GA 30309
(404) 572-6600

March 30, 2017

This paper is not intended as legal advice for any specific person or circumstance, but rather a general treatment of the topics discussed. The views and opinions expressed in this paper are those of the author only and not Bryan Cave LLP.

All rights reserved © 2017

TABLE OF CONTENTS

Page

I. Introduction 1
II. Overview 1
  A. DUTIES AND LIABILITIES OF CORPORATE DIRECTORS, OFFICERS AND EMPLOYEES 1
  B. LIMITED LIABILITY COMPANY DEVELOPMENTS 3
  C. NONPROFIT CORPORATIONS 4
  D. TRANSACTIONAL CASES 4
    1. Standing and Capacity to Sue 4
    2. Secondary Liability 5
    3. Jurisdiction, Venue and Service of Process 6
    4. Evidentiary Issues 8
    5. Insurance Decisions 8
    6. Professional Liability 8
    7. Bankruptcy-Related Questions 9
  E. FULTON COUNTY BUSINESS COURT DECISIONS 9
III. Review of Decisions 10
  A. DUTIES AND LIABILITIES OF CORPORATE DIRECTORS, OFFICERS AND EMPLOYEES 10
  B. LIMITED LIABILITY COMPANY DEVELOPMENTS 18
  C. NONPROFIT CORPORATIONS 27
  D. TRANSACTIONAL CASES 28
  E. LITIGATION ISSUES. 31
    1. Standing and Capacity to Sue 31
    2. Secondary Liability 34
    3. Jurisdiction, Venue and Service of Process 41
    4. Evidentiary Issues 50
    5. Director and Officer Liability Insurance Decisions 51
    6. Professional Liability 53
    7. Bankruptcy-Related Questions 55
  F. FULTON COUNTY BUSINESS COURT DECISIONS. 56

TABLE OF CASES

Cases

Alter Vail Ventures, LLC v. Wiles,
2016 WL 2757746 (N.D. Ga. May 12, 2016).......... 7, 46

Anderson v. American Family Ins. Co.,
2016 WL 3633349 (M.D. Ga. June 29, 2016).......... 6, 39

Ashline v. Marinas USA, L.P.,
336 Ga. App. 503, 784 S.E.2d 856 (2016).......... 6, 39

Barnes v. Smith,
339 Ga. App. 607, 794 S.E.2d 262 (2016).......... 6, 40

Befekadu v. Addis International Money Transfer, LLC,
339 Ga. App. 806, 795 S.E.2d 76 (2016).......... 8, 53

Brewton v. Liberty Mutual Holding Co., Inc.,
2006 WL 410009 (M.D. Ga. Feb. 2, 2016).......... 5, 37

Bryant v. Optima International, Inc.,
339 Ga. App. 696, 792 S.E.2d 489 (2016).......... 5, 36

Cobra 4 Enterprises v. Powell-Newman,
336 Ga. App. 609, 785 S.E.2d 556 (2016).......... 5, 34

Dasan USA, Inc. v. Weapon Enhancement Solutions, LLC,
2016 WL 3996242 (N.D. Ga. July 26, 2016).......... 7, 46

Davis v. Crescent Holdings & Investments, LLC,
336 Ga. App. 378, 785 S.E.2d 51 (2016).......... 5, 33

Edwards v. Campbell,
338 Ga. App. 876, 792 S.E.2d 142 (2016).......... 4, 30

Envision Printing, LLC v. Evans,
336 Ga. App. 635, 786 S.E.2d 250 (2016).......... 3, 26

Fang v. HEI Investments, LLC,
No. 2015-cv-261534 (Ga. Super. Nov. 28, 2016).......... 9, 62

FDIC v. Loudermilk,
No. 1:12-cv-04156-TWT (N.D. Ga. Oct. 26, 2016).......... 1, 10

Garraway v. Sa,
2016 WL 4245358 (N.D. Ga. Aug. 11, 2016).......... 7, 46

Georgia Dermatologic Surgery Centers, P.C. v. Pharis,
339 Ga. App. 764, 792 S.E.2d 747 (2016) 2, 17

Georgiacarry.org, Inc. v. Allen,
299 Ga. 716, 791 S.E.2d 800 (2016) 4, 31

Homeland Self Storage Management, LLC v. Pine Mountain Capital Partners, LLC,
No. 2014-cv-246999 (Ga. Super. June 24, 2016) 9, 57

In re Brooks,
2016 WL 235132 (Banks. S.D. Ga. Jan. 12, 2016) 4, 32

In re McKeever,
550 B.R. 623 (Bankr. N.D. Ga. 2016) 9, 55

Liberty Capital, LLC v. First Chatham Bank,
338 Ga. App. 48, 789 S.E.2d 303 (2016) 7, 45

Miller v. Lynch,
No. 2015-cv-256817 (Ga. Super. July 27, 2016) 9, 61

Niloy & Rohan, LLC v. Sechler,
335 Ga. App. 507, 782 S.E.2d 293 (2016) 3, 23

Nix v. Carter Brothers Security Services, LLC,
No. 2014-cv-253536 (Ga. Super. Aug. 29, 2016) 9, 60

Occidental Fire and Casualty of North Carolina v. Goodman,
339 Ga. App. 427, 793 S.E.2d 606 (2016) 5, 34

Pandora Franchising, LLC v. Kingdom Retail Group, LLLP,
299 Ga. 723, 791 S.E.2d 786 (2016) 6, 41

Perry Golf Course Development, LLC v. Columbia Residential, LLC,
337 Ga. App. 525, 786 S.E.2d 565 (2016) 3, 22

Piedmont/Maple, LLC v. Eichenblatt,
No. 2014-cv-253094 (Ga. Super. Oct. 31, 2016) 9, 58

Post-Confirmation Committee for Small Loans, Inc. v. Martin,
2016 WL 3251408 (M.D. Ga. June 13, 2016) 2, 14

Raiford v. National Hills Exchange LLC,
2016 WL 2908412 (S.D. Ga. May 17, 2016) 3, 18

Rollins v. Rollins,
338 Ga. App. 308, 790 S.E.2d 157 (2016) 2, 13

PGDOCS\6673434.1

Sager v. Ivy Falls Plantation Homeowners Association Inc.,
339 Ga. App. 111, 793 S.E.2d 455 (2016) 4, 27

SavaSeniorCare, LLC v. Beazley Ins. Co.,
2016 WL 4357521 (N.D. Ga. July 14, 2016) 8, 51

Sentinel Insurance Co. v. USAA Insurance Co.,
335 Ga. App. 664, 782 S.E.2d 718 (2016) 8, 52

Sims v. Natural Products of Georgia, LLC,
337 Ga. App. 20, 785 S.E.2d 659 (2016) 4, 28

Souza v. Berberian,
No. 2015-cv-257652 (Ga. Super. Apr. 20, 2016) 9, 59

State of Georgia ex rel. Hudgins v. O'dom,
No. 2015-cv-258501 (Ga. Super. June 29, 2016) 9, 56

Tanner Medical Center, Inc. v. Vest Newnan, LLC,
337 Ga. App. 884, 789 S.E.2d 258 (2016) 6, 44

Techjet Innovations Corp. v. Benjelloun,
2016 WL 4942351 (N.D. Ga. Aug. 17, 2016) 7, 47

The Guarantee Co. of North America v. Gary's Grading & Pipeline Co., Inc.,
016 WL 1181698 (M.D. Ga. Mar. 25, 2016) 3, 24

Thomas v. Bank of America, N.A.,
2016 WL 632522 (N.D. Ga. Feb. 17, 2016) 7, 49

Titan Construction Co., LLC v. CBC National Bank,
2016 WL 3771249 (S.D. Ga. July 11, 2016) 7, 46

Veterans Parkway Developers, LLC v. RMW Development Fund, II, LLC,
300 Ga. 99, 793 S.E.2d 398 (2016) 3, 21

Yugueros v. Robles,
300 Ga. 58, 793 S.E.2d 42 (2016) 8, 50

PGDOCS\6673434.1

I. Introduction

This paper addresses decisions handed down in the past 12 months by Georgia state and federal courts addressing questions of Georgia corporate and business organization law. It includes both decisions with significant precedential value and others dealing with less momentous questions of law as to which there is little settled authority. Even those cases in which the courts applied well-settled principles serve as a useful indication of the types of claims and issues that are currently being litigated in corporate and business organization disputes and how the courts are dealing with them.

The year 2016 saw a rare jury trial involving bank director and officer liability for gross negligence and ordinary negligence in *FDIC v. Loudermilk*, the same case in which the Georgia Supreme Court previously issued a major decision clarifying Georgia's business judgment rule. The year also saw a large number of decisions involving limited liability companies, continuing a trend from recent years. The Georgia Supreme Court addressed some interesting and novel questions of corporate law, including whether an out-of-state LLC (or corporation) can avail itself of the removal right that permits Georgia-based companies to shift certain tort litigation from the county in which it is brought to the county where it maintains its principal office, and whether a nonprofit corporation has standing to pursue a writ of *quo warranto* against public officials.

The decisions are organized first by entity type—i.e., business corporations, limited liability companies and partnerships. The remaining sections deal with transactional issues equally applicable to all forms of business organizations and litigation issues that are common to all business forms, such as secondary liability, jurisdiction and venue, evidence questions, and insurance disputes.

II. Overview

A. DUTIES AND LIABILITIES OF CORPORATE DIRECTORS, OFFICERS AND EMPLOYEES

One of the most closely watched Georgia corporate governance cases in recent years, ***FDIC v. Loudermilk*, No. 1:12-cv-04156-TWT**, went to trial in 2016. *Loudermilk* was one of over two dozen lawsuits brought by the FDIC as receiver for a Georgia bank that failed during the Great Recession asserting negligence and gross negligence claims against the bank's former directors and officers, based on their approval of loans and other transactions that ultimately caused losses to the bank. It was the first of these suits to go all the way to trial. While it may also be the last such trial dealing with the bank that closed during the Great Recession, given that most if not all of the FDIC's other cases have settled, the *Loudermilk* case will nonetheless have a lasting impact on bank and corporate governance in Georgia. It was in this case that the Supreme Court of Georgia clarified the contours of the business judgment rule in 2014, holding that the business judgment rule forecloses claims that sound in negligence that attack the wisdom

of a business decision, but does not absolutely foreclose a negligence claim that challenges only the carefulness of the decisionmaking process. The upshot of the Supreme Court's opinion, as far as the present case was concerned, was that the FDIC could go forward with its claims that the defendants negligently approved loans, provided that the claims had to be based on the carefulness of the process.

At trial in the Northern District of Georgia, the FDIC sought over $21 million in connection with ten loans it claimed were approved because of negligence or gross negligence. The jury found for the defendants as to six of the loans and the FDIC as to the other four, and awarded damages of $4.98 million. The verdict form did not specify the level of negligence found by the jury as to those loans where liability was found, and did not apportion liability among the several defendants. The defendants have filed an appeal, challenging the failure to apportion damages, as well as two interesting pretrial rulings: a decision by the trial court to preclude the defendants from introducing evidence that the Great Recession caused the bank's losses, and one permitting the jury to find a defendant liable for a loan regardless of whether that director attended the meeting in which the loan was approved.

The dispute over the handling of the Wayne Rollins estate made its *fifth* visit to the appellate courts in 2016. In ***Rollins v. Rollins,*** **338 Ga. App. 308, 790 S.E.2d 157 (2016)**, the Georgia Court of Appeals held that summary judgment was properly granted to the estate's administrators as to certain claims challenging their conduct as directors of family corporations, but held for the third time that summary judgment had to be denied as to other claims premised on trust and partnership liability, holding that the summary judgment record raised a genuine question of fact as to the defendants' good faith. The Court of Appeals' earlier uncertainty about what standard of review to apply when a defendant simultaneously has two fiduciary roles (i.e., trustee of a trust and director of a corporation held within the trust) seems to have been resolved by the Supreme Court's 2015 ruling in the same case, but the Court of Appeals nonetheless was unconvinced that good faith could be determined as a matter of law from the summary judgment record. The defendants have petitioned for certiorari, seeking a third round of review from the Georgia Supreme Court.

In ***Post-Confirmation Committee for Small Loans, Inc. v. Martin*****, 2016 WL 3251408 (M.D. Ga. June 13, 2016)**, the Middle District of Georgia held that issues of fact precluded summary judgment against a director of a family-owned corporation who allegedly sat silent while the corporation's assets were allegedly siphoned off by other related family entities (including a trust for the defendant's children). The court found that there were questions of fact as to whether the defendant intended to prefer himself given his professed lack of knowledge about the related party transactions and his claims that he relied on the company's management and accountants. The case ultimately proceeded to a trial in which the jury assessed damages of approximately $3 million, a small portion of which was assessed to this defendant. Finally, in ***Georgia Dermatologic Surgery Centers, P.C. v. Pharis*****, 339 Ga. App. 764, 792 S.E.2d 747 (2016)**, the Court of Appeals held that its prior order voiding a professional corporation's termination of the plaintiff did not preclude the plaintiff from asserting a breach of contract claim against the corporation based on the termination. The court struck a portion of the jury's award to the plaintiff, however, finding that it included damages that were sustained not by the plaintiff but by a new entity the plaintiff formed to continue his practice.

B. LIMITED LIABILITY COMPANY DEVELOPMENTS

In ***Raiford v. National Hills Exchange LLC,*** **2016 WL 2908412 (S.D. Ga. May 17, 2016)**, the Southern District of Georgia considered a novel question of LLC law: whether an interest holder in an LLC can have "vested rights" with respect to the LLC that cannot be taken away through an amendment to the operating agreement. Specifically, an equity interest holder claimed that an earlier operating agreement giving him an option to become a member and defaulting to the LLC Act's requirement of unanimous approval of a sale of assets gave it vested rights that could not be taken away by a subsequent amendment making membership subject to the managing member's discretion and permitting a sale of assets by a supermajority vote. Reviewing the vested rights doctrine in Georgia corporate law, which has all but ceased to be discussed for decades, the court determined that a right pertaining to an LLC can only be "vested" if it relates to an economic interest, and not solely to the way in which the LLC is managed. Since the admission of new members and voting requirements fell within the latter category of management questions, the plaintiff had no vested right here.

Another opinion discussing the rights of an interest holder in an LLC was ***Veterans Parkway Developers, LLC v. RMW Development Fund, II, LLC*****, 300 Ga. 99, 793 S.E.2d 398 (2016)**, in which the Georgia Supreme Court unanimously reversed a trial court's grant of a preliminary injunction in favor of an LLC's majority member, which had blocked the managing member's plans to construct a driveway on property owned by the LLC. The Supreme Court found that the majority member should not have been permitted to assert an interest in protecting the land from permanent alteration, since the land belonged to the LLC, not the member. Since the majority member could not otherwise show irreparable harm, it was not entitled to an injunction.

In ***Perry Golf Course Development, LLC v. Columbia Residential, LLC*****, 337 Ga. App. 525, 786 S.E.2d 565 (2016)**, the Georgia Court of Appeals held that an arbitration clause in an LLC operating agreement was enforceable regardless of whether the LLC's members had abandoned the operating agreement, finding that the clause was broad enough to encompass the entire business relationship between the members. In ***Niloy & Rohan, LLC v. Sechler*****, 335 Ga. App. 507, 782 S.E.2d 293 (2016),** the Court of Appeals held that an LLC member who also financed the LLC's operations could not recover debts that were owed to affiliated companies rather than the member itself, citing the rule that each plaintiff must prove its own damages.

Two cases addressed the effect of an LLC member's signature on documents executed in connection with transactions with third parties. In ***The Guarantee Co. of North America v. Gary's Grading & Pipeline Co., Inc.*****, 2016 WL 1181698 (M.D. Ga. Mar. 25, 2016)**, the Middle District of Georgia held that an LLC was bound by the signature of one of its three members on an indemnity agreement, even though that member had not been authorized to execute the agreement without the consent of the other two members. The third party was not made aware of the consent requirement, and therefore could rely on O.C.G.A. § 14-11-301. In ***Envision Printing, LLC v. Evans*****, 336 Ga. App. 635, 786 S.E.2d 250 (2016)**, the Court of Appeals held that an LLC member did not bind himself personally to a promissory note that he claimed he executed only in his official capacity on behalf of the LLC. The signature block was ambiguous as to the signer's capacity, so the Court of Appeals looked to other clues of the parties' intent

from the document, as well as parol evidence, and determined that there was no intent to bind the LLC member individually.

C. NONPROFIT CORPORATIONS

In ***Sager v. Ivy Falls Plantation Homeowners Association Inc.*, 339 Ga. App. 111, 793 S.E.2d 455 (2016)**, the Court of Appeals held that a homeowners' association purportedly formed to replace a prior association had failed to take the steps necessary to show that it had succeeded to the interest of the prior association. The new association was formed with the same name as the prior association (which had dissolved), but there had never been a vote of the prior association's members or other act vesting the new association with the authority to govern the subdivision. The Court of Appeals held that the trial court erred by engaging in a "continuity of interest" analysis in which it found that the new association was essentially a continuation of the prior one. This test, which is normally employed to determine when a successor entity is liable for the debts of its predecessor, was found to be not applicable to the question of a homeowners' association's power to govern its members.

D. TRANSACTIONAL CASES

In ***Sims v. Natural Products of Georgia, LLC*, 337 Ga. App. 20, 785 S.E.2d 659 (2016)**, the Court of Appeals affirmed a judgment rendered at a bench trial holding that two principals of an LLC did not defraud an investor about the use of the investment proceeds. The plaintiff argued on appeal that the defendants' payment of $600/week salaries to themselves was evidence of fraudulent intent, since they had represented that they would use the investment proceeds to build new facilities. The Court of Appeals held that the trial court was entitled to find that these payments were not suspicious or indicative of fraud. In ***Edwards v. Campbell*, 338 Ga. App. 876, 792 S.E.2d 142 (2016)**, the Court of Appeals addressed a claim that the seller of a business was liable to an injured third party for the negligent training of the buyer. The Court of Appeals affirmed a lower court decision finding that there was no liability, noting that the injury happened two years after the sale and that the buyer had made an independent decision, based in part on industry research, to continue the seller's practices and procedures. This, in the court's view, was an intervening cause sufficient to break the chain of causation between the seller's training and the injury.

1. Standing and Capacity to Sue

A unanimous Georgia Supreme Court held in ***Georgiacarry.org, Inc. v. Allen*, 299 Ga. 716, 791 S.E.2d 800 (2016)** that a non-profit corporation lacks standing to pursue a writ of *quo warranto* under O.C.G.A. § 9-6-60. The plaintiff, an advocacy group, sought to challenge the right of the members of the Georgia Code Revision Commission to continue to serve on that body. The Court found that the statute limited standing to persons capable of claiming the public office, which necessarily limited standing to natural persons. The situation therefore presented an exception to the usual rule that corporations are persons capable of suing and being sued.

In ***In re Brooks*, 2016 WL 235132 (Banks. S.D. Ga. Jan. 12, 2016)**, the Bankruptcy Court for the Southern District of Georgia held that a foreign LLC did not need to have obtained a certificate of authority to do business in Georgia in order to pursue its interests as a creditor in

a bankruptcy proceeding pending in Georgia. The court held that the LLC's activities with regard to the bankruptcy proceeding fell within exceptions to the definition of "transacting business in the state" under O.C.G.A. § 14-11-702. The court further held that the LLC did not bear the burden of proving that it was exempt from qualifying to do business in the state. In ***Davis v. Crescent Holdings & Investments, LLC***, the Georgia Court of Appeals reversed a trial court's modification of an order substituting the law firm that was named in the prior order, which was an LLP, with a newly-created firm having the same name and address, which was organized as an LLC. The Court of Appeals found that the trial court's modification was substantive rather than ministerial, because of the substantive nature of the law firm's reorganization itself. This meant that the modification was untimely because it was made outside of the term of court in which the original order was entered. In ***Occidental Fire and Casualty of North Carolina v. Goodman*, 339 Ga. App. 427, 793 S.E.2d 606 (2016)**, the Court of Appeals affirmed a trial court decision reforming an insurance contract to correct the name of the insured party to reflect its current owner. The court reasoned that the reference in the policy to the business's former owner rather than its current owner had to be a mutual mistake, since the policy was obtained by the current owner immediately following the sale.

2. Secondary Liability

In ***Cobra 4 Enterprises v. Powell-Newman*, 336 Ga. App. 609, 785 S.E.2d 556 (2016)**, the Court of Appeals addressed a novel question, though one that is likely to arise again in the future: whether a party can pierce the corporate veil "horizontally" to hold one corporation liable for the debts and torts of another corporation having the same owner. Here, the trial court had allowed the plaintiff, who was injured in a truck accident, to bring claims against both the company that operated the truck and a leasing company that was under common ownership with the operator. The Court of Appeals examined decisions from other jurisdictions which generally held that horizontal piercing is not permitted absent some showing of ownership or control. But the Court of Appeals stopped short of adopting a categorical rule against horizontal piercing. Instead, it reversed the trial court using a traditional veil piercing analysis, finding that there was a lack of evidence that the two companies commingled funds and were treated interchangeably. A similar situation was presented in ***Bryant v. Optima International, Inc.*, 339 Ga. App. 696, 792 S.E.2d 489 (2016)**, a case involving two separate companies owned by the same person that loaned money to the plaintiff. One of the companies foreclosed on its loan, but failed to record the foreclosure sale. When both companies later sought to recover the debts, the plaintiff argued that they were barred from doing so by their failure to record the sale. The Court of Appeals held that under alter ego principles, it was possible that both companies would be barred from recovering against the plaintiff, not just the company that conducted the earlier foreclosure. The Court did not indicate that it was piercing the veil horizontally, however. Instead, it reasoned that if the facts supported an alter ego theory, both corporations could be deemed to be the alter ego of the owner, and all of the loans would be deemed to have been made by him.

Two other federal decisions addressed whether an insurance policy holder could assert alter ego claims against the parent company of the insurer, as well as other affiliated companies. In ***Brewton v. Liberty Mutual Holding Co., Inc.*, 2006 WL 410009 (M.D. Ga. Feb. 2, 2016)**, the plaintiff showed evidence that the various companies shared common offices, had common officers and directors, maintained a common website and operated under a common trade name, among other things. The Middle District of Georgia found that this was insufficient to pierce the

corporate veil, because there was no evidence that the primary defendant was insolvent or that the defendants' corporate structure would allow the primary defendant to evade its contractual obligations to policyholders. The court also rejected the plaintiff's theories based on agency and joint venture liability. The same court reached the same result in a similar lawsuit brought against another insurance carrier and its client, ***Anderson v. American Family Ins. Co.*****, 2016 WL 3633349 (M.D. Ga. June 29, 2016).**

In ***Ashline v. Marinas USA, L.P.*****, 336 Ga. App. 503, 784 S.E.2d 856 (2016)**, the Court of Appeals held that the purchasers of a marina did not assume the marina's pre-closing liabilities, finding that the relevant sale documents contained assumption of liability language that was limited to the marina's post-closing liabilities. Finally, in ***Barnes v. Smith*****, 339 Ga. App. 607, 794 S.E.2d 262 (2016)**, the Court of Appeals held that the general rule holding corporate officers personally liable for their personal participation in torts by the corporation does not extend to claims involving negligent training of the corporation's employees. The Court held that if the essence of the claim is that the officer failed to properly train an employee, the officer can only be held personally liable to injured third parties under veil-piercing principles.

3. Jurisdiction, Venue and Service of Process

One of the most far reaching decisions of 2016 involved the application of Georgia's corporate and LLC venue statutes to businesses that are based out of state. In ***Pandora Franchising, LLC v. Kingdom Retail Group, LLLP*****, 299 Ga. 723, 791 S.E.2d 786 (2016)**, the Georgia Supreme Court unanimously held that an LLC whose principal place of business is outside of Georgia cannot avail itself of the removal remedy in O.C.G.A. § 14-2-510(b)(4), which allows Georgia-based companies to move certain tort cases from the county in which it is brought to the county in which the company maintains its principal place of business. Since the LLC venue statute at issue in *Pandora Franchising* expressly refers to the corporations code, the same rule will apply to corporations based out of state. The defendant, an LLC based in Maryland, is registered to do business in Georgia and had a registered office in Gwinnett County which it called its principal office. It successfully removed a tort action brought in Thomas County to Gwinnett, arguing that Gwinnett was the county where it had its most significant presence within the state. On appeal, the Supreme Court found that the text of the statute reflected the General Assembly's intent that only a company whose "principal place of business" is in Georgia can exercise the removal right. It also found that "principal place of business" refers to a corporation's "nerve center," similar to the analysis used by federal courts to determine a corporation's state of citizenship in diversity cases.

Two other decisions addressed corporate venue questions. In ***Tanner Medical Center, Inc. v. Vest Newnan, LLC,*** **337 Ga. App. 884, 789 S.E.2d 258 (2016)**, the Court of Appeals held that an LLC planning to build a hospital in Coweta County could file a petition for judicial review under Georgia's Administrative Procedure Act ("APA") in that county, even though it had not yet conducted any business (in part because it had been denied the necessary certificate to begin operatiosn). The APA allows an action to be brought in either Fulton County or the county where the petitioner "maintains its principal place of doing business in this state." Here, the Court of Appeals found that the petitioner's preparatory activities, such as entering into a letter of intent and applying for regulatory approvals, satisfied the definition of "doing business" in

Coweta County. In ***Liberty Capital, LLC v. First Chatham Bank*, 338 Ga. App. 48, 789 S.E.2d 303 (2016)**, the Court of Appeals affirmed a trial court's decision to retain venue in a tort and contract suit, finding that the defendant abandoned its venue argument by failing to explain how venue was improper under O.C.G.A. § 14-2-510(b).

There were several federal district court decisions dealing with the citizenship of a limited liability company for diversity jurisdiction purposes. The decisions highlight some of the difficulties that can arise when trying to establish that the court has diversity jurisdiction over a case involving an LLC, which is considered to be a citizen of every state in which one of its members is a citizen. In ***Dasan USA, Inc. v. Weapon Enhancement Solutions, LLC*, 2016 WL 3996242 (N.D. Ga. July 26, 2016)**, the Northern District of Georgia held that a plaintiff failed to demonstrate complete diversity of citizenship because it failed to allege the citizenship of all of the members of the defendant, an LLC. The plaintiff alleged only the citizenship of the members that were known to the plaintiff, which the court found to be insufficient. In ***Alter Vail Ventures, LLC v. Wiles*, 2016 WL 2757746 (N.D. Ga. May 12, 2016)**, the same court found that a plaintiff alleging that it was a Delaware LLC failed to allege *its own* citizenship, because it did not completely identify all of its members' members. This decision illustrates that when an LLC's members are themselves LLCs, they are deemed to be a citizen of every state in which one of its members' members is a citizen. In ***Garraway v. Sa*, 2016 WL 4245358 (N.D. Ga. Aug. 11, 2016)**, the same court again held that a plaintiff had failed to allege the citizenship of an LLC. The decision also addresses the requiremenst for alleging the citizenship of a corporation. A final decision on diversity of citizenship issues worth mentioning is ***Titan Construction Co., LLC v. CBC National Bank*, 2016 WL 3771249 (S.D. Ga. July 11, 2016)**, in which the Southern District of Georgia held that an LLC seeking to defeat removal failed to establish that it was a Florida citizen (which would have destroyed diversity) on the basis that one of its members was a Florida citizen. The LLC's problem was that the alleged Florida citizen was its registered agent, and O.C.G.A. § 14-11-209 provides that a Georgia LLC's registered agent must reside in Georgia. The court found that the LLC's filings with the Secretary of State identifying the member as its registered agent was the most compelling evidence of the member's citizenship.

In ***Techjet Innovations Corp. v. Benjelloun*, 2016 WL 4942351 (N.D. Ga. Aug. 17, 2016)** the Northern District of Georgia held that an out-of-state CEO of a company that contracted with a Georgia resident was subject to personal jurisdiction in a Georgia court due to his close personal involvement in forming the contractual relationship. The court reiterated that Georgia does not recognize the "fiduciary shield" doctrine, under which a nonresident individual's acts undertaken in a corporate capacity could not be used to establish that the defendant had minimum contacts with the forum state. Finally, in ***Thomas v. Bank of America, N.A.*, 2016 WL 632522 (N.D. Ga. Feb. 17, 2016)**, the Northern District held that an LLC was not properly served where the plaintiff failed to show that he delivered the complaint and summons to an officer who was authorized to accept service. The plaintiff sought reconsideration of a prior ruling to this effect, pointing out that the same officer that he tried to serve had signed verifications in documents filed in other litigation involving the defendant. The court denied the motion, explaning that it was not mutually exclusive that the defendant's representative could be authorized to verify pleadings and discovery responses but not be authorized to accept service.

4. Evidentiary Issues

In ***Yugueros v. Robles*, 300 Ga. 58, 793 S.E.2d 42 (2016)**, the Georgia Supreme Court unanimously held that the trial court correctly excluded testimony of a 30(b)(6) representative of one of the parties, a medical practice, because the opposing party had not qualified the witness as an expert. In so holding, the Supreme Court reversed the Court of Appeals, which had ruled that the testimony was admissible as an admission against interest under O.C.G.A. § 9-11-32(a)(2), which provides that 30(b)(6) deposition testimony "may be used by an adverse party for any purpose." The Supreme Court held that § 9-11-32 does not supersede the Evidence Code as it concerns the use of deposition testimony at trial.

5. Insurance Decisions

There were two notable decisions involving insurance questions. In ***SavaSeniorCare, LLC v. Beazley Ins. Co.*, 2016 WL 4357521 (N.D. Ga. July 14, 2016)**, the Northern District of Georgia held, on cross-motions for judgment on the pleadings, that a policy's allocation provision required the insurer to pay the defense costs of two of an LLC's former directors and managers. The court found that the two individuals were sued in an insured capacity, citing allegations of wrongful acts that could only have been committed by the individuals as a result of their official status. In ***Sentinel Insurance Co. v. USAA Insurance Co.*, 335 Ga. App. 664, 782 S.E.2d 718 (2016)**, the Court of Appeals addressed how the priority of uninsured motorist coverage should be resolved as between an employer policy and a family policy when the employer is an LLC. The Court reasoned that LLCs should be treated similarly to corporations in priority disputes, and should be entitled to the same assumption that the business entity is separate from its individual constituents. Thus, when determining whether the business or individual policy is the one with which the individual is more closely identified, which is often the decisive factor in determining priority, an individual or family policy will likely be determined to be the primary policy, as was the case here.

6. Professional Liability

In ***Befekadu v. Addis International Money Transfer, LLC*, 339 Ga. App. 806, 795 S.E.2d 76 (2016)**, the Court of Appeals, voting 8-1 under its new "nine-judge" procedure to decide cases where a judge dissents, affirmed a trial court's decision to disqualify an attorney who was involved in forming an LLC and then represented one of the LLC's members in a trial against the LLC. The Court of Appeals had reversed a previous disqualification order, holding that the trial court did not apply the correct analysis in disqualifying the attorney. This time, the Court of Appeals was satisfied that the trial court had properly evaluated whether the issues in the litigation were "substantially related" to the attorney's earlier work in forming the LLC. The dissent questioned why disqualification was appropriate, finding that the attorney had discontinued representing the LLC and was unlikely to have learned any special knowledge relevant to the litigation from his work in forming the entity.

7. Bankruptcy-Related Questions

In ***In re McKeever*, 550 B.R. 623 (Bankr. N.D. Ga. 2016)**, the bankruptcy court addressed the legal effect of reincorporating a business over 15 years after it was dissolved. The court found that the formation of the new entity did not serve to reinstate the previously dissolved corporation, because § 14-2-1422(a) provides that a dissolved corporation ceases to exist if an application for reinstatement is not made within five years of the dissolution. In, this case, the bankruptcy court's ruling meant that the debtor could not treat insurance proceeds as corporate property of the dissolved corporation.

E. FULTON COUNTY BUSINESS COURT DECISIONS

There were a number of noteworthy decisions handed down by the Fulton County Business Court in 2016. In ***State of Georgia ex rel. Hudgins v. O'dom*, No. 2015-cv-258501 (Ga. Super. June 29, 2016)**, the court denied a motion to dismiss claims that a corporation's president and CEO negligently permitted the return of a loan which had been made to an affiliated company. In the same order, the court dismissed claims based on a theory of "deepening insolvency," finding that Georgia had not recognized a cause of action based on that theory. In ***Homeland Self Storage Management, LLC v. Pine Mountain Capital Partners, LLC*, No. 2014-cv-246999 (Ga. Super. June 24, 2016)**, the court held that an LLC employee's significant responsibilities, which included handling the LLC's finances and preparing its tax returns, raised a question of fact as to whether he owed fiduciary duties to the LLC notwithstanding his lack of an official title. In the same order, the court ruled in favor of the employee as to the LLC's claims that he diverted funds to his own similarly named venture, noting that a special master's review failed to turn up evidence of such conduct. In ***Piedmont/Maple, LLC v. Eichenblatt*, No. 2014-cv-253094 (Ga. Super. Oct. 31, 2016)**, the court ruled that there were issues of fact as to whether an LLC's sole member breached fiduciary duties to an equity interest holder by failing to increase rents it charged to a related company, where the operating agreement specified that rents were to increase annually. In ***Souza v. Berberian*, No. 2015-cv-257652 (Ga. Super. Apr. 20, 2016)**, the court held that an email outlining terms of a potential LLC operating agreement did not create an enforceable contract between the parties, which would have made the plaintiff a member of the LLC. In ***Nix v. Carter Brothers Security Services, LLC*, No. 2014-cv-253536 (Ga. Super. Aug. 29, 2016)**, the court granted summary judgment in favor of a selling shareholder of a business who was alleged to have violated the Georgia RICO statute and breached fiduciary duties to the purchaser in connection with the sale. A critical factor was the fact that the plaintiff conducted months of due diligence into the business prior to consummating the sale, and did not allege that the selling shareholder made any representation or played any role during due diligence. In ***Miller v. Lynch*, No. 2015-cv-256817 (Ga. Super. July 27, 2016)**, the court evaluated choice of law questions pertaining to tort claims brought against a member of a Delaware LLC that is headquartered in Georgia. Applying the internal affairs doctrine, the court held that the substance of the claims had to be evaluated under Delaware law, but that the defendant's statute of limitations defense was procedural and had to be evaluated under Georgia law. Finally, in ***Fang v. HEI Investments, LLC*, No. 2015-cv-261534 (Ga. Super. Nov. 28, 2016)**, the court ruled that a plaintiff's claims for the return of investments made pursuant to subscription agreements were excluded from coverage under the defendants' insurance policy, citing the

policy's exclusion for losses relating to contract claims. The defendants later cited that ruling in a motion for judgment on the pleadings as to the plaintiff's unjust enrichment claim and other claims that assumed there was no contract. The court denied the motion, finding that its coverage ruling did not foreclose the possibility of a successful tort claim based on a duty arising independently from the subscription agreements.

III. Review of Decisions

A. DUTIES AND LIABILITIES OF CORPORATE DIRECTORS, OFFICERS AND EMPLOYEES

FDIC v. Loudermilk

No. 1:12-cv-04156-TWT (N.D. Ga. Oct. 26, 2016)—Jury awards over $4.9 million to FDIC in negligence and gross negligence action against former bank directors and officers.

The FDIC's lawsuit against former directors and officers of the failed Buckhead Community Bank, one of the most closely watched Georgia corporate governance cases in years, went to trial in October, 2016. The jury returned a verdict of nearly $5 million against the defendants for their role in the approval of four large commercial development loans that later defaulted. It was less than a complete victory for the FDIC, which had sought over $21 million in damages based on ten bad loans, but the verdict nonetheless represents a significant recovery against directors and officers of a Georgia bank. The case is all the more significant because it was the first known jury trial to evaluate negligence and gross negligence claims under the business judgment rule as defined by the Georgia Supreme Court earlier on in the proceedings.

Buckhead Community Bank was closed by the Georgia Department of Banking and Finance in December, 2009, during the heart of the financial crisis. The FDIC was named as receiver for the Bank. In 2012, the FDIC filed suit against the Bank's former directors and officers, alleging that they pursued an aggressive growth strategy aimed at building a "billion dollar bank," and in pursuit of that objective caused the Bank's loan portfolio to become heavily concentrated in commercial real estate acquisition and development loans. The FDIC made similar allegations in dozens of other cases involving similarly situated banks that failed during the Great Recession. In all, the FDIC filed over 100 civil actions between 2010 and 2015 in its capacity as its receiver for failed banks throughout the country, 25 of which were filed in Georgia against directors and officers of Georgia banks. The vast majority of these cases have settled. In fact, *Loudermilk* was only the second of these cases to proceed all the way to trial, and the first in Georgia.

As the case progressed to trial, the FDIC's claims eventually focused on ten specific loans that were approved directly by the defendants in their capacity as members of the Bank's loan committee. As to each of these loans, the FDIC alleged that approving the loans violated the Bank's own loan policy, banking regulations, prudent underwriting standards and sound banking practices. For instance, it was alleged that some loans exceeded the Bank's loan-to-value guidelines but were approved anyway. Other loans were approved without certain documentation that the FDIC alleged was necessary, such as current financial statements of

borrowers and guarantors. Other loans were allegedly approved before the loan application paperwork was final. There was no claim that any of the loans directly or indirectly provided a personal benefit to any of the defendants.

The FDIC asserted gross negligence claims based on Georgia law and the federal Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"), which establishes gross negligence as the national minimum standard for bank director and officer liability. FIRREA does not preclude the FDIC from recovering under a state law standard that is stricter than gross negligence. Accordingly, the FDIC also asserted an ordinary negligence claim under Georgia law. It did the same in all of its other complaints against Georgia bank directors and officers. The defendants in many of the cases, including *Loudermilk*, moved to dismiss the ordinary negligence claims, arguing that such claims were barred by Georgia's business judgment rule as then interpreted by the Georgia Court of Appeals. In most of these cases, the district court agreed and dismissed the ordinary negligence claims. But in *Loudermilk*, Judge Thrash expressed doubt that the business judgment rule could be applied to eliminate liability for ordinary negligence in cases involving banks, citing the perceived role that imprudent lending played in bringing about the financial crisis. Rather than rule on the motion to dismiss, Judge Thrash certified questions to the Georgia Supreme Court as to how the business judgment rule was to be applied to an ordinary negligence claim against the directors and officers of a bank. At about the same time, the Eleventh Circuit, hearing an appeal from a similar motion to dismiss that had been granted in *FDIC v. Skow*, expressed doubt that the Court of Appeals' business judgment rule decisions were reconcilable with the Banking Code's statutory standard of care, O.C.G.A. § 7-1-490, because of the statute's description of an ordinary prudence standard. The Eleventh Circuit certified *Skow* to the Supreme Court as well.

The Supreme Court responded to the questions posed by the federal courts in a landmark opinion that clarified Georgia's business judgment rule. *FDIC v. Loudermilk*, 295 Ga. 579, 761 S.E.2d 332 (2014). The Supreme Court recognized that the business judgment rule was a settled part of Georgia common law and was not abrogated by the adoption of § 7-1-490 or the substantially similar standard of care provisions for corporate directors and officers at O.C.G.A. § 14-2-830 and § 14-2-842, respectively. The Court nonetheless overruled the Court of Appeals decisions that the *Loudermilk* and *Skow* defendants had relied on, holding that insofar as those decisions established a gross negligence floor for liability in all cases, they could not be squared with the standard of care statutes. Instead, the Court drew a distinction between negligence allegations directed at the process employed by the directors and officers on one hand, and negligence allegations challenging only the wisdom of the resulting decisions on the other. The Court held that negligence claims going only to the wisdom of decisions were clearly barred by the business judgment rule, but claims alleging that the process failed to comport with the statutory standard of care were not barred. In short, the Supreme Court recognized the theoretical existence of an ordinary negligence claim based on a violation of the statutory standard of care—i.e., that a director or officer failed to exercise the care of an ordinarily prudent director or officer of a similarly situated bank (or corporation), which was not barred by the business judgment rule at the motion to dismiss stage. The Court gave no direction as to how its analysis should be applied in any specific case, but the obvious import in the case at bar was that the FDIC could proceed against the defendants on a negligence theory based on lack of process due care.

As the case neared trial, the district court made a number of significant pretrial rulings. The court granted a motion in limine that prohibited the defendants from introducing evidence that the Bank's losses were caused by intervening economic factors, including the widespread collapse of financial and real estate markets starting in 2008. The court found that the Great Recession and other events subsequent to the making of the loans were irrelevant to causation. The court denied a separate motion in limine which would have prevented the defendants from using examination reports that were generally favorable to the Bank prior to the Great Recession. Though the defendants were permitted to use the reports, they could not do so to prove the applicable standard of care, only to show their state of mind at the time. Finally, the court rejected a verdict form proposed by the defendants that would have required the jury to apportion fault among the defendants, rather than impose joint and several liability. The final approved verdict form permitted the jury to determine that particular defendants were not liable for particular loans, but the court declined to adopt the defendants' position that individual directors who were not present for the meetings in which particular loans were approved cannot have any liability for those loans.

At trial, the FDIC presented the defendants as pursuing an aggressive growth strategy and identified various ways in which the ten loans deviated from the Bank's policies. The defense emphasized that the FDIC's allegations were not grounded in fraud or any claim of self-dealing. Both sides presented expert testimony on the standard of care and whether the defendants had met it. The defendants also presented testimony from a representative of the Department of Banking and Finance, who testified as a friendly witness to the defense. (The DBF had also submitted an *amicus* brief in the earlier Supreme Court proceedings expressing concern that an ordinary negligence floor of liability would create disincentives to serving on Georgia bank boards.)

At the end of the two-week trial, the jury returned a verdict for the defense as to six of the ten loans and for the FDIC as to the other four. All of the defendants were charged with at least some liability. Some defendants were assigned no liability for certain loans; however, there were also instances in which a defendant was held liable for a loan that was approved in his absence. (There does not appear to have been any finding that any defendant was chronically absent from meetings.) Consistent with the court's earlier rulings, the jury did not apportion fault among defendants. The final compensatory damages award was $4,986,993, more than half of which related to a single $3.4 million loan for the acquisition and development of a 30-acre parcel in Douglasville. The verdict form did not ask the jury to make findings that were specific as to each liability theory; i.e., whether the defendants were grossly negligent or merely negligent. Thus it is difficult to determine what effect the insertion of an ordinary negligence claim had on the result of the trial, or how it may have proceeded differently had only gross negligence claims gone forward.

The defendants have appealed the verdict to the Eleventh Circuit. The FDIC did not file any cross-appeal. The defendants' appeal focuses on three issues: (1) whether the trial court erred in not applying Georgia's apportionment statute, which had the effect of making the defendants jointly and severally liable; (2) whether the court erred in permitting the jury to find individual defendants liable in connection with loans approved at meetings in which the defendant did not attend, and (3) whether the court erred in excluding evidence about the Great Recession.

Rollins v. Rollins

338 Ga. App. 308, 790 S.E.2d 157 (2016)—On remand, Court of Appeals finds issues of fact requiring a jury trial as to questions of trust and partnership liability.

This longstanding dispute between trust beneficiaries and their trustees, who also served as directors of companies in which the trusts held minority interests, returned to the Court of Appeals after the Georgia Supreme Court found in *Rollins v. Rollins*, 298 Ga. 161 (2015) that the summary judgment record was sufficient to permit a determination as to the specific capacities in which the defendants acted when they undertook actions challenged in the lawsuit. This time, the Court of Appeals held once again that a jury trial was needed, finding that there were disputed factual issues pertinent to the defendants' performance of their duties as trustees and as partners. The Court of Appeals also held that the defendants did not have liability as corporate directors for actions that were specifically authorized under the relevant corporate bylaws.

The Court of Appeals viewed the legal questions of which standard of care to apply as effectively having been settled by the Georgia Supreme Court's November, 2015 opinion. The decision by Gary and Randall Rollins to amend the RIF partnership agreement in 1993, which the Court of Appeals termed as the "catalyst around which all the disputes in this case revolve," was evaluated under a trust standard as to Gary Rollins, who voted the interests of his childrens' trusts in favor of the amendment, and under a partnership standard as to both defendants, based on the duties that partners owe to each other and to the partnership. The Court's opinion described and compared these standards in considerable detail. The trust standard applied to Gary Rollins is the most stringent of all the relevant standards. The Court wrote that a trustee "has a duty to exercise discretionary powers in good faith" and cannot be exculpated for breaches of trust committed in bad faith or with reckless indifference to the interests of the beneficiaries. The Court found sufficient evidence of bad faith in connection with the RIF amendment to create a triable issue. It cited evidence that the amendment caused partnership assets to be diverted to other partners, that it created a conflict of interest in which the defendants could (and allegedly did) favor their own interests, and that it purported to limit the defendants' liability to a greater extent than had existed before the amendment. Notably, the Court specifically found that a jury could consider the post-amendment conduct of the defendants—which it called the "fruits of [the] amendment"—as evidence of their intent at the time of the amendment. The Court nonetheless stopped short of finding that the defendants had acted in bad faith as a matter of law, finding that there was also evidence that the defendants had legitimate reasons for amending the partnership agreement (such as tax advantages) and consulted with counsel and expert advice, from which a jury could conclude that they exercised good faith.

Turning to issues of partnership liability arising from the defendants' decision to amend the RIF partnership agreement, the Court cited O.C.G.A. § 14-8-18, which provides that the rights and duties of partners is "subject to any agreement between them." The Court noted that the original RIF partnership agreement gave the defendants broad powers and that the defendants had not exceeded those powers. But the Court found that regardless of the breadth of their powers under the agreement, the defendants still owed their partners the "utmost good faith" and "finest loyalty." Thus the same factual question of good faith versus bad faith that required a jury trial as to Gary Rollins' performance of his trust duties was applicable here.

Based on its reading of the Supreme Court's opinion, the Court of Appeals found that partnership law governed the defendants' decision to implement a behavioral "code of conduct" as a criterion for receiving distributions.[1] The Court assumed, without deciding, that the defendants had the power under the amended RIF partnership agreement to implement the code of conduct, but held that this did not relieve them of the duty to implement such a code in good faith. It concluded that a jury could find bad faith under the partnership standard based on evidence that the defendants applied the code of conduct only to other beneficiaries and not themselves, and because there was no evidence that the code advanced any partnership interest. The Court also found that a jury could conclude that the code of conduct was implemented in good faith because "at least facially," it applied equally to all of the grandchildren-beneficiaries.

Finally, the Court evaluated certain actions undertaken by the defendants as directors of two corporations held within the family trusts. The Court followed the prior rulings of the Supreme Court in finding that their actions as corporate directors had to be evaluated under the corporate standard of care. It then found that to the extent that the defendants took actions that were specifically authorized by the bylaws of the two corporations, there was no breach of fiduciary duty as a matter of law. But when the defendants executed corporate shareholder agreements that restricted the shareholders' ability to dispose of assets, they were acting on behalf of the trusts who where shareholders, and thus owed trust duties.

The case has not yet returned to the trial court, for the defendants have filed a petition for writ of certiorari, seeking a third round of review from the Georgia Supreme Court.

Post-Confirmation Committee for Small Loans, Inc. v. Martin

No. 1:13-cv-195 (WLS), 2016 WL 3251408 (M.D. Ga. June 13, 2016)—Factual issues precluded summary judgment in favor of plaintiff in suit against director of allegedly insolvent company.

This federal district court opinion addresses claims that a director of a close corporation breached fiduciary duties to preserve an insolvent corporation's assets, and also was negligent in allowing the corporation to be "looted" by affiliate companies (including one in which the defendant's family claimed an interest). The district court's holding blazes no new legal ground in that it simply denied summary judgment to the plaintiffs due to numerous outstanding factual questions, but the decision is nonetheless noteworthy for its lengthy discussion of the fiduciary duties applicable to directors of insolvent corporations. The decision also briefly mentions the business judgment rule, one of the first cases from any Georgia court to do so after *FDIC v. Loudermilk*, 295 Ga. 579 (2014). The case later went to a jury trial which resulted in a verdict of over $2 million in favor of the plaintiffs, of which a portion was assessed to this defendant.

---

[1] This presented yet another complication, since some of the plaintiffs were not themselves partners of RIF. All of the plaintiffs were beneficiaries of S-Trusts until reaching age 45, at which point they became partners. The Court noted that the defendants owed no duties to the under-45 plaintiffs as partners, but that those plaintiffs whose trusts were managed by Gary Rollins as trustee might have recourse under trust law.

The plaintiff was a committee formed in connection with the bankruptcy of several consumer finance businesses referred to herein as the "Debtors". The committee brought suit against various defendants in the Middle District of Georgia asserting claims on behalf of the Debtors. This is one of several opinions issued by the district court dealing with dispositive motions filed by the defendants. The subject of this opinion was the plaintiff's motion for summary judgment against one of the defendants, who was a director of the Debtors between February 2008 and April 2012. The defendant's father founded the Debtors as well as several other affiliated businesses, and operated them until 2006. One of these affiliated businesses, Martin Family Group, owned properties that were leased to the Debtors for use in their business, and other affiliated businesses provided various services for customers of the Debtors. The defendant held a 33% interest in Martin Family Group as trustee for his childrens' trusts. He claimed, however, that he had no involvement in the management of Martin Family Trust.

The opinion (and other opinions) describe a lengthy history of financial transactions among the Debtors, Martin Family Trust, other affiliated entities, and the Martin family members who were the ultimate beneficiaries of the various family trusts. As it pertained to the defendant, the plaintiff asserted that Martin Family Group received over $2.3 million from the Debtors between January, 2008 and the bankruptcy petition date, and that approximately $980,000 of this amount was transferred to the defendant's children's trusts. The plaintiff alleged similar transfers of money from the Debtors to the defendant and his family trusts via other affiliated companies during the same period. The defendant claimed that he had no involvement in the operation, management or control of Martin Family Group and was not involved in its leasing and other arrangements with the Debtors. He similarly asserted a lack of direct involvement in the management of a second affiliated company from which his trusts received about $200,000.

The plaintiff alleged that the Debtors were insolvent throughout the entire period in which the defendant served as a director of the Debtors. The defendant executed public filings with the Securities and Exchange Commission that the plaintiff cited as evidence of the Debtors' insolvency (and the defendant's knowledge of the same). Despite this, the defendant denied having knowledge of the Debtors' insolvency and denied having any involvement in the preparation of the Debtors' financial statements. He claimed that as to all significant business matters, he relied on information provided to him by the Debtors' officers, legal counsel and auditors.

In this opinion, the district court addressed two questions of Georgia corporate law: (1) whether the defendant had breached his fiduciary duties to the Debtors as a matter of law based on his alleged failure to preserve the Debtors' assets during insolvency and (2) whether the business judgment rule and the defendant's alleged reliance on experts precluded summary judgment for the plaintiff on its claim that the defendant failed to monitor the Debtors' activities. The court also addressed a dispute over what test to apply to determine the date on which the Debtors became insolvent.

Addressing the first question, the district court applied settled Georgia law recognizing that the nature of a corporate director's duties changes when a corporation becomes insolvent. "When a corporation becomes insolvent, its directors are 'bound to manage the remaining assets for the benefits of its creditors, and cannot in any manner use their powers for the purpose of

obtaining a preference or advantage to themselves." *Hickman v. Hyzer*, 261 Ga. 38 (1991). The court held that for the plaintiff to be entitled to summary judgment on a breach of fiduciary duty claim under this theory, it had to show (1) that the corporation was insolvent, (2) that the defendant owed a duty to protect the corporation's remaining assets, and (3) that the defendant breached the duty by preferring his interests over those of the corporation's creditors. Here, the court found that there were issues of fact as to the first and third issues. In ruling that there was a disputed issue of fact as to the date of insolvency, the court rejected an argument by the plaintiff that Georgia law recognized a different definition of insolvency from the "fair valuation" standards employed in bankruptcy law and under the Uniform Fraudulent Transfer Act. Specifically, the plaintiff argued that under Georgia law, a debtor corporation is insolvent when its property is insufficient to pay its existing debts. The court found that this formulation of the test for insolvency was without support in the Georgia caselaw, except for brief passing citations that were referring to the definition of insolvency under the 1933 version of Georgia's fraudulent conveyance statute. The court then went on to find that the actual date on which the debtors became insolvent was a disputed question of fact.

The district court also found that there was a dispute of fact as to whether the defendant breached his duty. The court noted that it was unnecessary for the plaintiff to show that the various leasing arrangements and other intracompany transactions involving the Debtors were illegal, only that the defendant intended to prefer himself and his interest over those of other creditors. It found that a dispute remained as to whether the defendant intended to prefer himself, as the defendant's level of knowledge about the transfers was disputed.

The court then addressed a claim by the plaintiff that the defendant, while serving as director of the Debtors, "negligently" sat silent while the Debtors were "looted" through the fraudulent schemes they alleged in their complaint. The court observed that "[a]ccording to the record, the extent of [the defendant's] business decisions seemed to be based on his unwavering reliance on the knowledge, expertise and experience of 'the management of the company to make the best decisions.'" The plaintiff asserted that the defendant had breached his fiduciary duty by failing to independently monitor the companies' operations. The defendant argued in response that his actions were protected by the business judgment rule and by his reliance on management and experts. Since the case was before the district court on the plaintiff's motion for summary judgment, the court was required to view the evidence in the light most favorable to the defendant. The court cited the Georgia Supreme Court's statement in *Loudermilk* that the business judgment rule "generally precludes claims against officers and directors for their business decisions that sound in ordinary negligence, except to the extent that those decisions are shown to have been made without deliberation, without the requisite diligence to ascertain and assess the facts and circumstances upon which the decisions are based, or in bad faith." Thus to enter summary judgment in the plaintiff's favor, the court had to find that the defendant *indisputably* acted without deliberation or the requisite diligence to ascertain and assess the reasoning behind his decisions, or that he acted in bad faith. The court felt that it could not do so on the record before it, though it recognized that defendant's "seemingly incessant reliance on management" could be interpreted to resemble the characterization of a "do-nothing director" found in early Georgia decisions discussing director liability. Because there were also facts in the record that arguably justified the defendant's reliance, the court declined to make such a finding as a matter of law. Finally, the court discussed the possibility that the plaintiff's

allegations of a conflict of interest might be sufficient to rebut the business judgment rule's presumption. It found that no Georgia appellate court has explicitly held that a conflict of interest is sufficient to rebut the presumption, but noted that other courts, including the Delaware Supreme Court, have recognized this possibility. The court did not resolve the question here, since it found that the existence and extent of a conflict of interest was in dispute.

Georgia Dermatologic Surgery Centers, P.C. v. Pharis

339 Ga. App. 764, 792 S.E.2d 747 (2016)—Jury verdict against professional corporation that terminated employee in violation of bylaws affirmed in part and reversed in part.

This dispute involving the breakup of a two-person medical practice returned to the Georgia Court of Appeals for a second time. Previously, the Court affirmed a pre-trial order holding that the professional corporation's president exceeded his authority under the bylaws when he terminated the plaintiff without first obtaining director and shareholder approval. Since the plaintiff was a 50-percent owner and a director, any attempt to obtain this approval obviously would have resulted in deadlock. Nonetheless, this did not excuse the corporation from following its bylaws, and its failure to do so rendered the termination void. *See Georgia Dermatologic Surgery Centers, P.C. v. Pharis*, 323 Ga. App. 181, 746 S.E.2d 678 (2013).

After the case returned to the trial court, a jury trial was held, resulting in a $1.3 million verdict against the corporation for breach of the plaintiff's employment agreement. In this appeal, the corporation argued that it could not have liability for breach of contract given that its termination had been ruled void and of no effect. The Court of Appeals disagreed and affirmed the trial court on this point, holding that there was no inconsistency between its prior ruling and the availability of a breach of contract claim, and no legal principle that precluded the plaintiff from asserting that the corporation breached the contract by preventing him from returning to work and failing to pay him amounts owed, even if this action was later voided by a court.

The corporation also argued that the trial court wrongly excluded the shareholders' agreement between the two doctors, which was executed on the same day as the employment agreement in question. The corporation believed that the shareholder agreement's buy/sell provisions provided an exclusive remedy for breach of the employment agreement. The Court of Appeals rejected this argument as well, holding that the shareholders' agreement did not preclude recovery of other damages because the buy/sell provision was specifically limited to circumstances constituting a valid termination.

The Court held that the $1.3 million award had to be reduced, however, because it included over $250,000 in startup costs incurred by a new entity the plaintiff formed in order to continue his medical practice (as opposed to by the plaintiff himself). The Court found that these costs were not the plaintiff's own damages but rather were incurred by the new corporation, which was not a party to the litigation. It cited the cardinal precept that corporations are separate legal entities from their members, even when owned by one person. Notably, the Court held that even funds that were contributed by the plaintiff to the new corporation for purposes of paying for these startup costs were not recoverable as breach of contract damages from the defendant, for these funds represented a capital contribution to the new corporation, not payment for the costs themselves.

B. LIMITED LIABILITY COMPANY DEVELOPMENTS.

Raiford v. National Hills Exchange LLC

No. 1:11-cv-152, 2016 WL 2908412 (S.D. Ga. May 17, 2016)—Holder of LLC equity interest did not have a "vested right" to become a member under former version of operating agreement.

This federal district court opinion addresses the question of when, if at all, an interest holder in a Georgia limited liability company can rely on the "vested rights" doctrine to avoid the effect of an amendment to the LLC's operating agreement adversely impacting that right. As it pertains to business organizations, the "vested rights" doctrine is rarely cited anymore, as evidenced by the fact that the court had to look back to 19th century and early 20th century cases to describe how the doctrine is applied in this context. While the district court stopped short of declaring the use of a vested rights analysis dead in the corporate governance disputes, its holding suggests that the doctrine may have very limited application. As the court observed, the likely reason for this is the adoption of corporate and LLC codes, which (particularly in the corporate context) expressly set forth rules regarding amendments to governing documents.

The case is a longstanding dispute involving a shopping center in Augusta. The plaintiffs, who were the prior owners of the complex, sold it to an LLC and obtained a 15% equity interest in the LLC. This interest entitled the plaintiffs to a share of the profits from a subsequent sale of the shopping center, but the property was eventually sold in 2011 at a price below the profit threshold. The plaintiffs sued the LLC and its members, claiming, *inter alia*, that the defendants fraudulently concealed material information from them prior to the sale regarding the shopping center's leasing prospects and prospective tenants. In earlier proceedings, the court found that the defendants owed the plaintiffs a duty of candor to disclose material facts in connection with the sale of the complex, and that the information withheld was material, but that the plaintiffs failed to establish loss causation and damages because there was nothing they could have done to prevent the defendants from consummating the sale. *See Raiford v. National Hills Exchange, LLC*, 2013 WL 1286204 (S.D. Ga. Mar. 27, 2013). The plaintiffs argued that O.C.G.A. § 14-11-308(b)(3), which requires a unanimous vote of an LLC's members to approve the sale of substantially all of the LLC's assets, should have applied here because the shopping center was the LLC's sole asset. The district court rejected that argument in its 2013 opinion because the plaintiffs were not members of the LLC—their 15% equity interest did not purport to grant membership status.

A key component of the court's earlier holding was the belief of both the parties and the court that during the relevant period, the LLC was governed by an operating agreement which the LLC's members had adopted in August, 2009. As it turned out, there was another relevant operating agreement, which the plaintiffs were unaware of until it was produced in related litigation after the district court issued its 2013 ruling. This opened the door for a reconsideration of the district court's opinion. The newly discovered operating agreement (referred to in the opinion as "Operating Agreement II") was adopted in August, 2007 and was the governing document until it was replaced by the August, 2009 operating agreement (referred

to as "Operating Agreement III"). The plaintiffs believed that Operating Agreement II provided a path for them to argue that they could have been members at the time of the sale and therefore could have blocked the sale under O.C.G.A. § 14-11-308(b)(3). Specifically, Operating Agreement II provided that a transfer of an interest in the LLC "entitle[d] the transferee to become a Member and to exercise any rights of a Member." Since the plaintiffs obtained their 15% interest by transfer, they argued that Operating Agreement II gave them a right to become members, which they further contend they would have exercised in time to block the sale.

While this argument was based in part on some disputed facts, the district court in its reconsideration order assumed that Operating Agreement II was in effect when the plaintiffs received their interest and that the plaintiffs indeed would have had the unfettered opportunity to become a member under Operating Agreement II. The critical question remained, however, whether Operating Agreement II was superseded by Operating Agreement III when it was adopted in 2009. It was undisputed that Operating Agreement III was in effect by the time of the sale. Operating Agreement III eliminated the provisions of Operating Agreement II that would have permitted an interest holder to become a member. Moreover, Operating Agreement III enacted a provision authorizing the sale of substantially all of the LLC's assets upon a supermajority vote. Operating Agreement II had been silent on this point, meaning that the default unanimity rule in O.C.G.A. § 14-11-308(b)(3) applied. In short, so long as the amendments to the operating agreement in 2009 were permissible, they were fatal to the plaintiffs' argument that they could have had an opportunity to block the sale in 2011.

The plaintiffs first argued that their entitlement to become a member under Operating Agreement II and the unanimity rule under O.C.G.A. § 14-11-308(b)(3) were "enforceable" rights, as that term is used in O.C.G.A. § 14-11-101(18) ("[a]n operating agreement may provide enforceable rights to any person, including a person who is not a party to the operating agreement, to the extent set forth therein.") The district court found this to be inconsequential, since the enforceability of a right has nothing to do with the ability of the governing body granting that right to amend its laws or rules. The plaintiffs similarly argued that they had enforceable rights as a third party beneficiary of Operating Agreement II, but the court found this argument to be unavailing for the same reason. In the court's view, the question raised by the plaintiffs had to be evaluated under the plaintiffs' alternative argument, which rested on the "vested rights" doctrine. The right had to be not merely enforceable, but one that could not be taken away from the plaintiffs (as Operating Agreement III purported to do).

As the court observed, the concept of "vested rights" is not specific to the corporations context. For instance, in 2013 the Georgia Supreme Court cited the principle in holding that the state constitution prohibits the enactment of retroactive laws that impair vested rights. The district court further observed that Georgia courts have not discussed the vested rights concept in corporate cases for decades, but that older decisions recognizing the doctrine remained on the books and had not been questioned in later cases. To illustrate just how old the doctrine is, the court identified the leading case as a 1901 Georgia Supreme Court decision, *Interstate Bldg. & Loan Ass'n v. Wooten*, 38 S.E. 738 (Ga. 1901). In *Wooten*, a member of a building and loan association stopped paying her loan after the association amended its bylaws to change the repayment terms applicable to its loans. The Supreme Court recognized a corporation's authority to amend its bylaws but held that "inasmuch as they enter into and form a part of the contracts it

makes with its members, they cannot, under the guise of amending its by-laws, impair the obligations of such contracts." Thus if the contract gave the member a vested right, the association could not deny that right without the member's consent. The *Wooten* court went on to distinguish this situation from "amendments which do not increase [a member's] obligations but provide a different method." The district court noted that this distinction was carried forward in subsequent cases, describing it as a distinction "between amendments that affect vested rights and those that relate to the plan upon which its businesses shall be transacted."

The court also hinted that a likely reason why the discussion of "vested rights" does not come up in modern corporate cases was the enactment of corporate codes. In fact, the court found no Georgia decision that postdates the original enactment of the Georgia Business Corporations Code in 1968, and no decision applicable to the LLC context at all. As the court recognized, the GBCC "expressly disclaims the view that a corporation's articles of incorporation vest rights relating to 'management, control, capital markets, dividend entitlement, or purpose or duration of the corporation.'" O.C.G.A. § 14-2-1001. Without much discussion, the court assumed that the "vested rights" doctrine would apply to LLCs to the same extent that it would to corporations.

The court concluded its lengthy discussion of the history of the doctrine by declaring the state of the law as follows: "Vested rights are those related to a member or shareholders' economic interest in a business entity, including the members' ability to withdraw their economic interest. Conversely, bylaws regulating who may become members, how many members are needed to take action, and the distribution of responsibilities between managers and members, just regulate how the business conducts its affairs."

Applying that test to the dispute at hand, the court found that the plaintiffs had no vested right implicated by the adoption of Operating Agreement III. First, the plaintiffs had no vested right in becoming a member. Instead, the court reasoned that the relevant provisions of Operating Agreement II granting the plaintiffs a right to become a member were merely designed to "distribute the power to control membership." In support of this conclusion, the court pointed to the fact that under Operating Agreement II, in most situations the admission of new members was subject to the manager's discretion. Second, the court held that the unanimous voting requirement set forth in O.C.G.A. § 14-11-308(b)(3) conferred no vested right. The court observed that the statute itself is nothing more than a default rule which can be modified by a written operating agreement, and that the supermajority provision of Operating Agreement III clearly fell within the category of amendments that simply regulate the manner in which business is conducted.

Having found that the plaintiffs could not identify a vested right stemming from Operating Agreement II, the district court denied the motion for reconsideration as to plaintiffs' fraud claim, on the grounds that they still could not show a causal connection between the alleged fraud and any injury they suffered.

Veterans Pkwy Developers, LLC v. RMW Development Fund, II, LLC

300 Ga. 99, 793 S.E.2d 398 (2016)—LLC majority member not entitled to injunctive relief based on claimed potential injury to land owned by LLC.

The Supreme Court unanimously reversed a decision enjoining an LLC's managing member from using LLC funds to complete a construction project on land owned and managed by the LLC. The Court held that the injunction was improper because, among other things, the majority member who obtained the injunction had no direct interest in the land at issue such that it could claim that an injunction was necessary to protect the land from permanent alteration.

The case arose from a protracted dispute between the two members of an LLC formed to own and manage commercial properties. Both members were themselves LLCs. Defendant-Appellant VPD was the managing member and held a 25% interest. Plaintiff-Appellee RMW held a 75% interest. The LLC purchased an apartment complex in Columbus, whose acquisition and construction was financed by a $24 million HUD-insured loan. RMW made some additional, smaller loans to VPD and the LLC in connection with the project. In May, 2015, RMW filed a lawsuit seeking to remove VPD as the managing member, claiming among other things that VPD was diverting funds that should have been used to pay down the loans to RMW. The LLC was not a party to the lawsuit. Shortly before the lawsuit was filed, VPD purchased a small strip of land for the LLC, for purposes of constructing a second entrance to the property. According to VPD, the construction of a median on the parkway serving the property had inconvenienced residents and created safety issues at the main entrance, necessitating the second entrance.

RMW moved for an injunction halting the planned construction, claiming that it would be irreparably harmed in the absence of equitable relief because (1) the construction would permanently alter the physical layout of the property, (2) the project would incur significant costs, and (3) the LLC's expenses should be limited to necessary day-to-day expenses while the petition to remove VPD as managing member was pending. The trial court entered a TRO, which it converted into an interlocutory injunction prohibiting the use of LLC funds to construct the second entrance, limiting the use of LLC funds to "normal day-to-day expenses", and requiring a monthly accounting of expenses to be made to the trial court.

On appeal, VPD argued that the injunction violated the business judgment rule, and alternatively, that there was no risk of irreparable harm to RMW because money damages were available to redress any injury. The Supreme Court unanimously reversed on the grounds that there was no showing of irreparable harm. Of particular note was the Court's conclusion that RMW was not in a position to assert arguments based on the potential for injury to land owned by the LLC. The Court acknowledged that equitable relief can sometimes be appropriate to protect a party's interest in land. But it found that when the land is owned by an LLC, as was the case here, an individual member's interest in the land is indirect. The Court cited O.C.G.A. § 14-11-501(a), which provides that "[a] limited liability company interest is personal property. A member has no interest in specific limited liability company property." It concluded that RMW therefore had no direct interest in the land such that it could request equitable relief on a claim of threatened injury to the land.

Turning to RMW's claims that the construction would be costly (i.e., that it would divert funds away from loan repayment), the Court held that there was no showing that money damages would not be recoverable. Having found that there was no proper showing of irreparable harm, the Court held that the injunction was an abuse of the trial court's discretion. The Court did not reach any of VPD's other arguments, including whether its conduct was protected by the business judgment rule.

Perry Golf Course Development, LLC v. Columbia Residential, LLC

337 Ga. App. 525, 786 S.E.2d 565 (2016)—Alleged abandonment of LLC operating agreement did not render arbitration clause to be unenforceable in dispute between members.

In this case, the Court of Appeals held that an arbitration clause in an LLC's operating agreement was enforceable in a dispute among the LLC's members, rejecting arguments by the opponent of arbitration that the operating agreement had been held unenforceable in a prior proceeding and was then abandoned by the members. The court reasoned that the arbitration provisions of the operating agreement had never been found unenforceable or void, and even if the parties had indeed abandoned the operating agreement, the arbitration clause was broad enough to encompass the present dispute.

The case involves an LLC formed for the purpose of redeveloping the Perry Homes public housing project in Atlanta. The LLC had three members: Perry Golf, whose contemplated role was to build a golf course, Columbia Residential, whose role was to develop multi-family housing, and Brock Built, LLC, whose role was to develop single family housing. The LLC had a contract with the Atlanta Housing Authority ("AHA") to develop the complete project. The three members entered into an operating agreement in 2002. The operating agreement contained an arbitration provision that stated, in relevant part, that "[i]f any Dispute (as defined below) arises between the parties in relation to this Agreement ... any party ... may demand binding arbitration…" "Dispute" was defined to include "any difference, disagreement[,] or failure to agree between the parties arising out of or in connection with this Agreement or any of the Project Documents including any question regarding the application, existence, validity, performance, withdrawal from or non-performance, or termination of this Agreement or any clause contained within this Agreement or any Project Document or *any matter in any way connected with this Agreement or the rights, duties, or obligations of any party to this Agreement or any Project Document*." (emphasis in opinion).

In 2005, a dispute arose between Perry Golf and Brock Built, which resulted in an arbitration in which the project-related obligations in the operating agreement were held to be unenforceable as between Perry Golf and Brock Built. Thereafter, the members agreed that their mutual authority with respect to the LLC would be governed by the LLC Act. In 2006, the LLC amended its agreement with the AHA to eliminate the golf course portion of the project. Perry Golf voted against amending the agreement, while the other two members voted in favor. Perry Golf then filed a lawsuit, alleging that it was unfairly shut out of the project and asserting contract and tort claims against the other two members as well as the AHA. Columbia, who had not been a party to the earlier arbitration, moved to compel arbitration. The trial court ordered binding arbitration, and the arbitrator entered an award in favor of Columbia.

Appealing from the trial court's order confirming the arbitration award, Perry Golf argued that the case should not have been sent to arbitration in the first place because (1) the operating agreement had previously been held unenforceable and (2) the parties had abandoned the operating agreement. The Court of Appeals rejected both arguments. First, the Court observed that Columbia was not a party to the earlier arbitration, and that decision was not binding on Columbia under traditional collateral estoppel principles. Moreover, the earlier ruling did not find the arbitration provision to be unenforceable (indeed, the fact that the case was resolved by arbitration meant that the provision was actually enforced). Thus the Court concluded that it was not bound by any prior ruling as to the enforceability of the operating agreement. Second, turning to the effect of the parties' alleged abandonment of the operating agreement, the Court questioned whether the parties had truly abandoned the agreement, since they continued to perform the same roles as had been contemplated in the operating agreement. Even if the operating agreement was deemed terminated by the parties' abandonment, the Court added, it would not necessarily render the arbitration clause unenforceable because that clause could be read to encompass the entire business relationship between the parties. For instance, the arbitration clause referred specifically to "Project Documents," a defined term that included the LLC's contract with the AHA. The Court cited previous cases in which courts have recognized that disputes arising from conduct after the termination of a contract can still be subject to its arbitration provisions, if the wording of the arbitration clause is broad enough to encompass such claims. Finding that the clause in question was sufficiently broad, the Court affirmed the trial court's decision to compel arbitration.

Niloy & Rohan, LLC v. Sechler

335 Ga. App. 507, 782 S.E.2d 293 (2016)—Member of LLC could not recover debts owed to affiliates of the member who were not themselves members or parties to the litigation.

This case illustrates some of the difficulties that can arise when the founders of an LLC depart from the written terms of their agreement for long periods of time. The dispute was between the two members of an LLC formed to purchase land and develop office condominiums. When the LLC was formed in 2004, it was contemplated that the plaintiff would be responsible for funding the LLC's projects, while the defendant would be responsible for managing the LLC's operations, which included marketing and selling the condominiums. The LLC's operating agreement formalized this understanding: in it, the plaintiff agreed that it would loan the LLC up to $2 million and both members agreed to execute a personal guaranty for 50 percent of the loan amount.

The loan documents were never prepared, however, and the parties' course of business deviated from the original arrangement over time. While the plaintiff did loan a substantial amount of money to the LLC, so too did various other companies that were affiliated with the plaintiff. In all, over $8 million was loaned to the LLC over time, only $1.3 million of which came from the plaintiff. The manner in which the LLC's revenues were distributed also changed over time. According to the defendant, in 2006, he and the plaintiff's manager (who also owned or controlled the other creditors) reached an agreement to apply 65 percent of the LLC's net proceeds to pay off expenses and debt and the other 35 would be paid to the members. (The operating agreement had provided for all proceeds to be paid first to expenses and debt before

PGDOCS\6673434.1

any proceeds could be distributed to members.) The defendant further claimed that the plaintiff's portion of that 35 percent distribution was for loan repayment while his portion of the distribution was profit.

When the business soured in 2008, the plaintiff requested an accounting, which resulted in the parties agreeing that the LLC had an outstanding principal debt between $1.8 and $2.6 million. (The rest of the debt, about $6.6 million, had been paid back over time.) The plaintiff found that during the life of the LLC, the defendant had paid himself nearly $900,000 in sale proceeds and also had paid nearly $400,000 to a real estate brokerage he owned. The plaintiff sued for breach of the operating agreement and breach of fiduciary duty, claiming that the defendant wrongfully diverted funds that should have been paid to creditors. None of the other creditors were made parties to the lawsuit. After a bench trial, the trial court held that the defendant was liable both under the contract and for breach of fiduciary duty, but declined to award any damages to the plaintiff. The trial court's rationale was twofold. First, it held that the plaintiff had failed to establish that any of the money owed was actually paid to the LLC by the plaintiff as opposed to the other creditors. Second, it held that the parties had mutually departed from the operating agreement, thus precluding the plaintiff from recovering damages.

On appeal by the plaintiff, the Court of Appeals upheld some of the trial court's findings, but found others to be contrary to Georgia law. The Court agreed with the trial court insofar as it had reasoned that the plaintiff had to prove its own damages and could not recover damages suffered by absent creditors. The plaintiff argued that this amounted to a finding that the other creditors were indispensable parties, but the Court disagreed, holding that it was simply an application of the rule that every plaintiff must prove its own damages. But the Court accepted the plaintiff's argument that it had actually made a satisfactory showing of its own damages when it produced an accounting showing the exact amount of money that had been repaid to all creditors and the exact portion of that money (only about $190,000) that was diverted specifically to the plaintiff. This accounting was undisputed, which led the Court to conclude that the trial court should have found it satisfactory to prove the plaintiff's damages. Having so held, the Court vacated the trial court's decision and remanded for further proceedings.

The Court also held that in those further proceedings, the parties' mutual departure from the operating agreement should not be considered an absolute bar to the plaintiff's ability to recover damages, in light of the trial court's holding (which was not disturbed on appeal) that the defendant breached a fiduciary duty to the plaintiff. The court noted that an LLC member owes both contractual duties and fiduciary duties, and therefore may have liability for breach of fiduciary duty that is independent of whether the contract was breached. Therefore, while the parties' reformation of their contract might preclude damages under the contract, it might not preclude an award of damages for breach of fiduciary duty. (The court did not opine on the ultimate question of whether any damages should be awarded here.)

The Guarantee Co. of N. America v. Gary's Grading & Pipeline Co., Inc.

No. 3:15-cv-83 (CDL), 2016 WL 1181698 (M.D. Ga. Mar. 25, 2016)—LLC liable to third party notwithstanding member's lack of authority to sign agreement creating the LLC's obligation.

This case demonstrates that provisions of an LLC operating agreement that purport to limit a manager's authority will not necessarily insulate the LLC from liability to a third party when that manager actually exercises authority he did not have.

This was an action brought by a surety seeking to recover under an indemnity agreement for payments it had been required to make under payment and performance bonds it had issued to a construction company in 2012. The plaintiff sued the construction company and a number of related individuals and corporate entities, including a Georgia LLC called Pine Plantation. Pine Plantation was owned and co-managed by three brothers. Its operating agreement contained a provision stating that "[a]t any time when there is more than one Manager, no one Manager may take any action permitted to be taken by the Managers without agreement of the other Manager or Managers, or unless other approval requirements of the Managers are expressly set forth elsewhere in this Operating Agreement or the Georgia [LLC] Act."

Pine Plantation was one of the signatories to the indemnity agreement forming the basis for the plaintiff's claim. Pine Plantation executed the document through the signature of one of the three brothers, who also signed the document in his individual capacity and on behalf of two other companies. A second brother's signature also appeared on the document on behalf of himself and the construction company, but that brother later claimed that his signature was forged. More significantly for purposes of the LLC's alleged liability, he also claimed that he did not give his brother permission to sign the indemnity agreement on behalf of Pine Mountain, meaning that his brother lacked authority to bind Pine Mountain under the operating agreement.

The plaintiff moved for summary judgment against Pine Mountain, arguing that the manager who signed the indemnity agreement had either actual or apparent authority to sign the document on behalf of Pine Mountain. In support of its motion, the plaintiff presented testimony from its employee who issued the bonds in 2012, who testified that he had no reason to doubt that any signature was genuine and no concerns about the signing brother's authority to sign on behalf of Pine Plantation. There was no evidence that the surety was ever made aware of the provision of the operating agreement that limited the signing brother's authority, nor was there any dispute that the signing brother was "carrying on in the usual way" Pine Plantation's business when he executed the agreement. Thus, in the plaintiff's view, this was at the very least a case of apparent authority.

In response, Pine Plantation argued that the signature could not bind the company because the required consent of all managers was not given. The court rejected this argument, resting its analysis on its interpretation of the operating agreement and Section 301 of the LLC Act, O.C.G.A. § 14-11-301.

Reviewing the operating agreement, the court focused on the clause "unless other approval requirements of the Managers are set forth elsewhere in this Operating Agreement or the Georgia Act," which was specifically defined to refer to the LLC Act. In the court's view, the Operating Agreement thus incorporated O.C.G.A. § 14-11-301(b)(2), which provides that "[e]very manager is an agent of the limited liability company for the purpose of its business and affairs." That section further provides that certain acts of a manager are deemed to be binding on the LLC unless the manager so acting "has in fact no authority to act" <u>and</u> the third party with

whom he or she is dealing has knowledge of the manager's lack of authority. The provision cites one specific example of an act that can bind the corporation under these circumstances: executing an instrument "for apparently carrying on in the usual way the business and affairs of the [LLC]." Applied here, that meant that the execution of the indemnity agreement, which indisputably was business being carried on "in the usual way," bound Pine Plantation unless it could be shown that the plaintiff knew about the signing brother's lack of authority.

The court found further support from O.C.G.A. § 14-11-301(d), which provides that "[n]o act of a manager or member in contravention of a restriction on authority shall bind the limited liability company *to persons having knowledge of the restriction*." (emphasis added). Since the plaintiff's lack of knowledge of a restriction was not in dispute, Pine Plantation's attempt to invoke its operating agreement failed as a matter of law, and the plaintiff was entitled to summary judgment.

The court reaffirmed its holding in a subsequent opinion, *Guarantee Co. of N. America v. Gary's Grading & Pipeline Co., Inc.*, 2016 WL 4386082 (M.D. Ga. Aug. 16, 2016). The matter is now on appeal to the Eleventh Circuit.

Envision Printing, LLC v. Evans

336 Ga. App. 635, 786 S.E.2d 250 (2016)—LLC officer did not bind himself personally to promissory note where signature block was ambiguous as to signer's capacity and other evidence did not demonstrate intent to bind officer individually.

In this case, a creditor sought to enforce a promissory note against the chief executive officer of an LLC, who signed the note. The defendant claimed that he signed the note solely in his official capacity on behalf of the LLC. The signature block of the note was ambiguous as to this fact. It indicated the name of the LLC and contained three signature lines underneath. The first stated the name of the manager (a different individual than the defendant) preceded by the word "By:" and indicating his title. The second line stated the name of the same individual with no indication of any position and without the word "By:". The third and final line had the defendant's name, again without the word "By:" or any indication of title. The only signature line that was actually filled in was the defendant's line. The other two lines were crossed out. In the body of the note, the LLC is clearly identified as the maker of the note.

The defendant moved for summary judgment in the trial court based on his assertion that he only signed the note in his official capacity and therefore was not personally bound under it. He submitted an affidavit in which he attested to this fact and pointed to a few supporting facts. First, the text of the document contained no language indicating that he would incur personal liability. Second, the term "Maker" was always used in the singular form. Third, the note included the LLC's address but not the defendant's home address. Finally, there was parol evidence that supported the defendant's position, including emails suggesting that the plaintiff knew that the defendant was signing on behalf of the LLC only and did not object. The plaintiff submitted a competing affidavit asserting that the defendant "accepted the note as a personal obligation." The plaintiff's primary argument was that the note did not indicate that the plaintiff was signing in a representative capacity. It cited O.C.G.A. § 11-3-402(b)(2) as supporting its argument. That section provides that "if the form of the signature does not show unambiguously

that the signature is made in a representative capacity or the represented person is not identified in the instrument, the representative is liable on the instrument to a holder in due course that took the instrument without notice that the representative was not intended to be liable on the instrument. With respect to any other person, the representative is liable on the instrument unless the representative proves that the original parties did not intend the representative to be liable on the instrument."

The trial court entered summary judgment in favor of the defendant, and the Court of Appeals affirmed. The Court agreed with the plaintiff that the form of the defendant's signature did not unambiguously show that he signed the note in a representative capacity. Accordingly, liability depended on whether the plaintiff had notice that the defendant was not intended to be liable on the instrument. Here, the Court found that the plaintiff had such notice. It reasoned that the note, when viewed as a whole, did not indicate that the defendant was personally guaranteeing the LLC's debt. The Court further cited the canon of contract interpretation that "if a contract is capable of being construed two ways, it will be construed against the preparer and in favor of the non-preparer," which here favored the defendant. The Court further held that it was appropriate for the trial court to consider parol evidence in its ruling, finding that the document was ambiguous as to the capacity in which the defendant signed.

C. NONPROFIT CORPORATIONS

Sager v. Ivy Falls Plantation

339 Ga. App. 111, 793 S.E.2d 455 (2016)—Court of Appeals holds that homeowners' association did not succeed to the interest of prior association in absence of vote or other action evidencing that transfer of governing authority occurred.

This was a dispute between a homeowners' association purporting to have authority to govern a residential subdivision and a homeowner who challenged that authority. The Court of Appeals held that the association had failed to take the steps necessary to show that it had succeeded to the interest of an earlier association which had dissolved, such as a vote of the original association's members to transfer governing authority. Since the trial court held to the contrary in granting summary judgment in favor of the association, the Court of Appeals reversed.

In 1996, the developer of the Ivy Falls Plantation subdivision incorporated the Ivy Falls Plantation Homeowners Association, Inc., and recorded covenants that granted a membership interest in the association to each lot owner. In 2005, this association was administratively dissolved. It was never reinstated. In 2006, two residents of the subdivision formed a new entity which was also called Ivy Falls Plantation Homeowners Association, Inc. The two residents filed articles of incorporation for the new entity, and it began to function just as the prior association had. According to the summary judgment record, however, there was no transfer of assets from the earlier association to the new one, no vote of members to incorporate the new association, and no other act of the member that vested the new association with authority. In fact, the original board was not aware that a new association had been formed until it learned of this fact through the litigation.

The plaintiff purchased a home in the subdivision in 2010. She understood that she was a member of the new association, that a majority of members had voted to dissolve the new association, and that it conducted no business for several years. In 2014, the new association notified the plaintiff of a delinquency on her dues. The plaintiff disputed the new association's authority to collect dues from her, and eventually sued the new association and its officers. The new association counterclaimed for declaratory judgment and to collect the unpaid dues. The parties made cross-motions for summary judgment. The trial court ruled in favor of the new association, holding that it was a successor to the original, dissolved association because of a "continuity of interest" between the two associations.

The Court of Appeals began its analysis by questioning exactly what the trial court meant in citing a "continuity of interest test." The lower court believed such an analysis to be appropriate based on two prior appellate decisions that the Court of Appeals found to be inapposite. The first, *Floyd v. Springfield Plantation Property Owners' Ass'n*, 245 Ga. App. 535 (2000), involved a modification to an 8-year old judgment rendered on a jury verdict to reflect that the judgment plaintiff was the full successor in interest to an earlier homeowners' association. The Court of Appeals found that in *Floyd*, it did not undertake its own analysis into whether the judgment plaintiff actually was a successor in interest because the jury had decided that issue in the underlying case 8 years earlier. The second, *Rice v. Lost Mountain Homeowners Ass'n*, 269 Ga. App. 351 (2004), involved a question of whether a homeowners' association formed to govern only the first phase of a development could exercise authority over homes built in later phases. The Court found that its decision in *Rice* did not rest on any question about successor authority but rather turned on a specific majority vote of lot owners to have the original association's authority expanded to cover the entire subdivision. In the Court's view, neither *Floyd* nor *Rice* thus directly addressed the question of successor liability presented here.

The Court found its 2015 decision in *Dan J. Sheehan Co. v. The Fairlawn on Jones Condo. Ass'n, Inc.*, 334 Ga. App. 595 (2015) to be more enlightening. In *Sheehan*, the members of a condo owners' association voted to amend the condo declarations and bylaws to form a new association. When the new association was incorporated, the board voted to cease operation of the old association, and the owners voted to adopt restated declarations transferring responsibility for governing the new condominium to the new association. The Court compared the situation in *Sheehan* to the present case and found that none of the same formalities had been followed with respect to Ivy Falls Plantation. The Court observed that "[t]he only legal act reflected in the record is the mere filing of articles of incorporation of an entity with the same name." It found that even if the doctrine of corporate continuity—which normally is applied to determine when a successor company has assumed the liabilities of a former company—had relevance to the situation, the new association had not not observed the formalities that would be needed to create a legally enforceable successor interest.

The Court thus reversed the trial court's rulings insofar as they found that the new association had authority to govern the subdivision under a corporate continuity analysis.

D. TRANSACTIONAL CASES.

Sims v. Natural Products of Georgia, LLC

337 Ga. App. 20, 785 S.E.2d 659 (2016)—LLC officers' payment of salaries to themselves was insufficient to support inference that they defrauded investor about the use of investment proceeds.

In this case, the Court of Appeals held that the fact that two principals of an LLC paid themselves weekly salaries of $600 was not sufficient evidence that they intended to defraud an investor who believed the investment proceeds were being used to fund the construction of a greenhouse. The plaintiff invested $150,000 in Natural Products of Georgia, LLC, a venture founded by two individuals to sell tomatoes grown in greenhouses in Barrow County. The two individuals represented to the plaintiff that they intended to raise a total of $1.5 million and needed the $150,000 to fund the company for a few months until other investments could be secured. In exchange for the $150,000 investment, the LLC promised the plaintiff that it would pay him $525,000 in semi-monthly installments beginning in twelve months. The two individuals executed a promissory note on behalf of the LLC to document this agreement. The promissory note stated that the funds would be used only for the purpose of constructing greenhouses in Barrow County.

No such greenhouses were built, and the LLC defaulted after making a single payment. The plaintiff sued the LLC under the note and also sued the two individuals for fraud in the inducement and securities fraud under the Georgia Securities Act, O.C.G.A. § 10-5-50 ("GSA"). Following a bench trial, the plaintiff prevailed on its claims under the note, but the two individuals prevailed on the fraud claims. One of the two individuals filed for bankruptcy protection and received a discharge, so the plaintiff brought his appeal only against the remaining individual.

The dispositive question was whether the individuals had the requisite intent to defraud at the time that the promissory note was executed. The Court recited the general rule that "actionable fraud cannot be predicated on a promise contained in a contract because the promise is to perform some act in the future, and normally, fraud cannot be predicated on statements which are in the nature of promises as to future events." It also recognized that an exception to the rule exists when "a promise as to future events is made with a present intent not to perform or where the promisor knows that the future event will not take place. Additionally, if the particular statement at issue in the contract was not a future promise but a present misrepresentation of fact, it is sufficient to support a claim for fraud." The Court noted that the necessary fraudulent intent can sometimes be proven by the subsequent conduct of the defendant if that conduct is "unusual, suspicious, or inconsistent with what would be expected from a contracting party who had been acting in good faith."

Here, the plaintiff's chief evidence of fraud was the fact that the two individuals paid themselves a $600/week salary and did not build new greenhouses as had been contemplated. The Court held that "these payments are not, as a matter of law, a business practice that is unusual, suspicious, or inconsistent with what would be expected from a contracting party who had been acting in good faith" and that the trial court, sitting as finder of fact, was therefore authorized to find that the defendants lacked fraudulent intent. It bears noting that because the plaintiff was appealing from a judgment rendered after a full trial, the appellate standard of review was highly deferential to the trial court's findings of fact, and the Court's ruling should be

understood in that context. There was other evidence that weighed against a finding of fraud, such as the fact that the company continued to operate using its existing facilities even as no new greenhouses were built.

The Court affirmed the trial court's rulings as to both common law fraud and fraud under the GSA. Addressing the GSA claim, the Court also considered whether the promissory note itself was fraudulent because it omitted the fact that the LLC needed $1.5 million before it would construct a greenhouse. The Court ruled that based on the oral representations made by the individual defendants about the need for the $1.5 million in order to start the business, the trial court was authorized to find that the plaintiff was not misled by any omission in the note.

Edwards v. Campbell

338 Ga. App. 876, 792 S.E.2d 142 (2016)—Former owner not liable for negligent training of new owner in action brought by injured customer.

This negligence action addressed the potential duties and liabilities owed by the seller of a business to third parties who claimed to have been injured by the company's products and services after it is sold. Affirming the grant of summary judgment to the former owner, the Court of Appeals found that a negligent training claim against the former owner could not be maintained as a matter of law, because proximate causation could not be proven.

The longtime owner of a tire company sold it in 2009 to an admitted novice in the business. In connection with the asset purchase agreement through which the company was sold, the previous owner agreed to provide 60 days of training to the new owner, during which time he instructed the new owner as to the company's standard installation procedure when a customer purchases only two new tires instead of four. Two years later, the company followed this procedure in installing two new tires for the plaintiff's grandmother. The plaintiff had a serious accident, which he blamed on the manner in which the tires were installed. The plaintiff sued various parties for negligence, including the former owner, whom he claimed provided negligent training to the new owner and other employees.

During discovery, it was learned that the former owner instructed the new owner to install two new tires on the front axles, which had been the company's standard policy for over 20 years. The new owner testified at his deposition that he also conducted his own industry research which informed him that there was a debate within the industry regarding correct tire placement, and acknowledged that he would have changed the procedure if he believed that it was improper. The former owner moved for summary judgment, claiming that he owed no duty to the plaintiff and also that his training two years earlier could not have been the proximate cause of the plaintiff's injury. The trial court granted the motion, focusing on the element of causation. On appeal, the plaintiff argued that the trial court had essentially held that the passage of time alone broke the chain of causation. The Court of Appeals observed that even if the trial court had focused only on the passage of time, this would not necessarily constitute error, as it is possible that a substantial lapse of time by itself would render an injury to be unforeseeable as a matter of law. The Court deemed it unnecessary to determine whether this was such a case, since the trial court had also taken into consideration the new owner's independent research and his continuing decision to install two new tires on the front axles, which constituted an intervening cause. The

Court further noted that the new owner "had certain legal obligations to ensure, on an ongoing basis, that his company was selling and installing tires in a manner that would not render his customers' vehicles unsafe." The Court thus concluded that it was not foreseeable to the former owner that the new owner would continue to blindly follow the instructions he received during the training period for two years without questioning them.

E. LITIGATION ISSUES.

1. Standing and Capacity to Sue

Georgiacarry.org, Inc. v. Allen

299 Ga. 716, 791 S.E.2d 800 (2016)—Quo warranto statute held to apply to natural persons only, depriving nonprofit corporation of standing to challenge eligibility of members of public commission.

A unanimous Georgia Supreme Court held that a non-profit corporation lacked standing to pursue a writ of *quo warranto* under O.C.G.A. § 9-6-60. In so holding, the Court found that a non-profit corporation (and presumably any organization that is not a natural person) is not a "person" under the statute. The Court also found that the plaintiff lacked standing as an association to pursue the writ on behalf of its individual citizen and taxpayer members.

The plaintiff, the non-profit advocacy group Georgiacarry.org, filed in the Fulton County Superior Court an "Application for Leave to File an Information in the Nature of *Quo Warranto*" against the individual members of Georgia's Code Revision Commission, a body created by statute to oversee various activities related to the publication of updates to the Official Code of Georgia Annotated. The plaintiff's ostensible purpose in seeking the writ was to challenge the right of each Commission member to continue to serve on the Commission. The superior court found that the plaintiff lacked either individual standing or associational standing on behalf of its members to pursue the writ. The plaintiff appealed the decision to the Supreme Court.

The Court's initial task was to determine whether the plaintiff, a non-profit corporation, was a "person either claiming the office [of the Commission members] or interested therein" and therefore had direct standing to pursue the writ. The Court recognized that the Georgia Code generally considers corporations to be "persons," but explained that individual statutes can define "person" in such a way as to exclude corporations and other non-natural persons. The Court read O.C.G.A. § 9-6-60 as limiting the definition of "person" to natural persons. As the Court explained, the text of the statute limited the remedy of a writ of *quo warranto* to a person that is capable of "claiming" the public office (such as the losing candidate in an election) or who is otherwise interested in the office. Since an organization cannot hold one of the positions on the Commission, the Court reasoned, it cannot possibly claim any relevant interest in the office, and therefore cannot be a "person" for purposes of the statute.

The Court then turned to the question of the plaintiff's organizational standing. As a general rule, an association (including a non-profit corporation) has standing to bring suit on behalf of its members when its members would otherwise have standing to sue in their own right, the interests the association seeks to protect are germane to its purpose, and neither the claim

asserted nor the relief sought requires the participation of individual members. Here, the Court found that the plaintiff failed to show that that its pursuit of the writ was germane to its stated purpose of "focus[ing]…on public interest matters of self-defense and gun laws of the State of Georgia…" The Court noted that the Commission's work is non-substantive: it involves contracting with publishers to ensure that revisions to the Code are reflected in updated published copies. While the plaintiff did cite that one of its concerns dealt with the proper codification of certain bills, the Court was not persuaded that there was any connection between the Commission's work and the plaintiff's advocacy objectives.

In re Brooks

No. 13-10860, 2016 WL 235132 (Bankr. S.D. Ga. Jan. 12, 2016)—Foreign LLC entitled to pursue claim against bankruptcy debtor despite lack of certificate of authority to do business in Georgia.

This bankruptcy court decision addressed a debtor's claim that a foreign limited liability company lacked standing to file a proof of claim because it was not authorized to do business in Georgia. Ruling on the debtor's motion for summary judgment, the court held that the debtor had not shown as a matter of law that the LLC's failure to obtain a certificate of authority from the Secretary of State disqualified it from filing a proof of claim in a Georgia bankruptcy court. The decision was similar to that reached by the same court last year in a related matter involving the same creditor, *In re Mohr*, 538 B.R. 882 (Bankr. S.D. Ga. 2015).

The debtor guaranteed several promissory notes that had been executed by an LLC in which he held a substantial interest. The original creditor, BB&T, assigned its interest in the notes to RREF, who then filed proofs of claim in the debtor's bankruptcy. It was undisputed that RREF was a foreign corporation that was not registered to do business in Georgia. In response to the debtor's objection, RREF argued that it was exempt from registration requirements, and also submitted an affidavit from an asset manager who testified that RREF had no employees, offices, or business records in Georgia, and that its business in Georgia was conducted by the affiant's employer, Rialto Capital Advisors, LLC.

The court addressed two separate questions. The first was whether the Georgia Code allowed RREF to participate in the bankruptcy proceeding (i.e., to file proofs of claim and defend its interests in court) without registering to do business. As the court previously recognized in *Mohr*, O.C.G.A. § 14-11-702 sets forth a non-exhaustive list of activities that are excluded from the definition of "transacting business in the state" such that an LLC is not required to obtain a certificate of authority simply to engage in those activities. The court identified three items on the list that were relevant here: "[m]aintaining or defending any action or administrative or arbitration proceeding or effecting the settlement thereof or the settlement of claims or disputes;" "[m]aking loans or creating or acquiring evidences of debt, mortgages, or liens on real or personal property or recording the same;" and "[s]ecuring or collecting debts or enforcing any rights in property securing the same[.]" O.C.G.A. § 14-11-702(b)(1), (7)-(8). The court concluded that based on those provisions, RREF could "undertake all of the actions it is pursuing in this bankruptcy court" without having to obtain a certificate of authority. It also noted that under O.C.G.A. § 14-11-711(b), the failure of a foreign LLC to obtain a certificate of authority does not impair the validity of any contract or act of the LLC.

That did not fully resolve the dispute here, because the debtor separately argued that RREF had failed to meet its burden of proof to establish that it is exempt from qualifying to do business in Georgia. The court rejected the premise that RREF bore the burden of proof, finding it to be contrary to both bankruptcy law and Georgia substantive law. First, the court observed that in bankruptcy proceedings, a proof of claim is deemed to have prima facie validity, and the objecting party has the burden of negating that validity. The court then found that "Georgia law allocates the burden of proof to the party challenging a party's authority to conduct business within the state," citing several Georgia appellate opinions. Since the debtor did not dispute anything that was said in RREF's affidavit, and pointed to no evidence that RREF had engaged in non-exempt conduct requiring it to obtain a certificate of authority, the debtor was not entitled to summary judgment on his objection.

Davis v. Crescent Holdings & Investments, LLC

336 Ga. App. 378, 785 S.E.2d 51 (2016)—Amendment to court order substituting reorganized law firm for original firm was substantive modification and not correction of a clerical error.

In this case, an award of attorneys' fees was assessed as a sanction against a law firm which was structured as an LLP, based on its handling of an action to set aside a sheriff's sale in which the LLP represented the plaintiff. While the motion for sanctions was pending, the attorney serving as counsel for the plaintiff reorganized the law firm from an LLP into an LLC. The firm otherwise had the same name and maintained the same business address. Despite the reorganization, the order assessing the sanction was entered against the original LLP. Nearly a year later, after the term of court in which the order was entered had expired, the trial court entered an amended order substituting the LLC for the LLP. The order also added, for the first time, the attorney serving as counsel in the underlying case as an additional sanctioned party. The court's order indicated that its purpose was "to correct an error found in the original order."

The attorney and the LLC moved to set aside the order on the grounds that the trial court lacked authority to enter it outside of the term of court in which the original order was entered. The trial court denied this motion. On appeal, the Court of Appeals reversed. It found that the trial court's action was not a proper exercise of a trial court's inherent power to revise, correct or modify a judgment because no motion had been made. There is an exception to the rule requiring a motion which allows a trial court to modify orders outside of the term of court in which they are entered if the purpose of the modification is to correct a clerical error or irregularity, but this exception may not be invoked to make substantive changes to the earlier order. The Court of Appeals found that the change here was substantive. It noted that the award as entered against the LLP was valid insofar as a partnership is capable of being sued by a third party for the wrongful acts of its partners under O.C.G.A. § 14-8-13 and § 14-8-15. Thus the initial order was not erroneous in that sense. Nor could the modification of the award be considered the correction of a misnomer, the Court of Appeals held. The LLC was a new and separate party (and, of course, so was the individual attorney). Finding the substitution of parties to be a substantive change, the Court ruled that the motion to set aside the amended order should have been granted. The Court did not opine on whether the LLC might have liability for the LLP's debts under any other theory, as that question was not before it.

Occidental Fire and Casualty of North Carolina v. Goodman

339 Ga. App. 427, 793 S.E.2d 606 (2016)--Reformation of insurance contract held proper to correct mutual mistake as to insured status of purchaser of business.

In this insurance dispute, the Court of Appeals held that the trial court acted properly in reforming a policy that misidentified the owner of the insured party, on the grounds of mutual mistake. In 2008, an LLC purchased the Irish Bred Bar & Grill, a bar in McDonough, from a corporation named Irish Bred Bar & Grill V, Inc. The selling corporation conveyed its entire interest in the bar and its assets in the sale. The purchaser, through its sole member, applied for commercial insurance coverage with the defendant. On the application, the new owner identified the insureds as "Irish Bred Pub & Grille V, Inc." and "Irish Bred Pub & Grill". The application was accepted and the defendant issued a policy listing the insured as Irish Bred Pub & Grill, Inc. Later on, the purchaser was named in a wrongful death suit involving an incident at the bar. The defendant denied coverage to the purchaser, citing the fact that it did not fall within the definition of an insured. The purchaser thereafter assigned its claims against the defendant to the wrongful death plaintiffs in connection with a settlement of the underlying suit.

The trial court held, and the Court of Appeals agreed, that the doctrine of mutual mistake applied. It was clear to the court that the purchaser of the bar mistakenly identified the prior owner of the bar in the application for insurance coverage. (The individual who submitted the application explained that he believed he should list the prior owner to be sure that the bar was completely covered under the policy). The Court held that it was proper to consider the mistake to be mutual, because the defendant failed to come forward with any material fact that would indicate why either party would have intended to purchase insurance for only the bar's prior owner and not its new owner. The Court found that the "clear intent of the contracting parties" was to provide insurance for the new, post-sale business. The Court also rejected the defendant's argument that it would be prejudiced by reformation, holding that the defendant bargained to insure the operations of the bar and the loss of a potential windfall caused by mistake cannot be characterized as prejudicial.

2. Secondary Liability

Cobra 4 Enterprises v. Powell-Newman

336 Ga. App. 609, 785 S.E.2d 556 (2016)—Court of Appeals rejects "horizontal piercing" theory against corporate sibling of primary defendant.

This Court of Appeals decision addressed an unusual application of the alter ego doctrine. The plaintiff sought to hold a corporation responsible for the tort liability of a separate LLC that was owned by the same person. This type of claim, which the Court of Appeals called "horizontal" veil piercing, has not previously been recognized in Georgia. Here, the Court of Appeals found that the facts before it failed to give rise to a viable claim for horizontal veil piercing, without deciding whether such a claim could ever be brought.

The plaintiff was injured in an accident involving a truck that was being leased by defendant Yellow Ribbon Tree Experts ("Yellow Ribbon"). Yellow Ribbon was an LLC formed in 2006 by its sole owner, Robertson. In 2009, Robertson formed Cobra 4 Enterprises ("Cobra 4") to serve as a leasing company for Yellow Ribbon's trucks. Cobra 4 bought the trucks for $1 and then leased them back to Yellow Ribbon for $2,500 a month. Robertson was Cobra 4's sole shareholder. The evidence in the record showed that Cobra 4 had failed to hold shareholder meetings and elect officers, as its articles of incorporation had required. Cobra 4 and Yellow Ribbon shared a common owner (Robertson), a common principal office and common registered agent. Other facts in the record, however, indicated some effort on Robertson's part to keep the two companies separate. They did not commingle funds or share bank accounts. They did not use the funds of one company to pay the expenses of another. And Cobra 4 had some business that was not related to Yellow Ribbon. Much of the business operations of the two companies, however, was "overlapping", as they regularly performed common tasks and did frequent business with each other.

Specifically with regard to the leasing of trucks such as the one that injured the plaintiff, the evidence showed that Cobra 4 was the owner and Yellow Ribbon a lessee pursuant to a written agreement. Under the lease agreement, Cobra 4 did not have control over trucks while they were leased. Yellow Ribbon was required to maintain liability insurance for personal injuries up to $500,000, but the evidence showed that it only obtained insurance up to $150,000.

The plaintiff sued the driver, Robertson, and the two companies, asserting with respect to Cobra 4 that it was liable as an alter ego of Yellow Ribbon, as a joint venturer with Yellow Ribbon, and for negligent entrustment. Cobra 4 moved for summary judgment. The trial court denied the motion as to the plaintiff's alter ego and negligent entrustment claims, finding that there were disputed issues of fact for the jury. After that ruling, all of the other defendants entered into a settlement and release with the plaintiff, leaving Cobra 4 as the sole defendant. Cobra 4 moved for summary judgment again, claiming that it was an "agent" under the terms of the release and therefore entitled to enforce it. The trial court denied the motion, and this appeal followed. Cobra 4 appealed the trial court's earlier decisions on the issues of alter ego and negligent entrustment, while the plaintiff appealed the trial court's decision to grant summary judgment to Cobra 4 on the issue of joint venture.

Notably, the fact that Robertson settled with the plaintiff and was released in connection with that settlement meant that the court did not have to decide whether he was responsible for Yellow Ribbon's liability based on traditional veil piercing principles. In fact, the Court of Appeals observed that it would probably have been an open and shut case against him. It was undisputed that Robertson set up his companies for the purpose of limiting his personal liability, that he failed to observe corporate formalities, and that he caused Yellow Ribbon to be underinsured.

But because Robertson was released, the only remaining question was whether the plaintiff could pierce the veil between Cobra 4 and its sibling Yellow Ribbon. The Court observed that "Georgia courts have never applied the alter ego doctrine to impose liability in this manner." It also found two decisions from other jurisdictions, Ohio and Alabama, in which similar claims had been rejected. The Ohio case cited by the Court, *Minno v. Pro-Fab, Inc.*, 905

N.E.2d 613 (Ohio 2009), hinted that such claims were categorically barred, while the Alabama case, *Madison Co. Comms. Dist. v. CenturyLink, Inc.*, 2012 WL 6685672 (N.D. Ala. 2012) appeared to turn on a lack of evidence. The Court of Appeals' approach was closer to that of the Alabama court. The Court evaluated whether there was evidence that the two companies were "interchangeable entities" and found the evidence to be insufficient. The most significant evidence, in the Court's view, was the fact that the companies maintained their finances separately. The Court wrote: "[T]here was no evidence that the two corporations commingled their assets or otherwise confused their separate records or control. Therefore, after a thorough review, we are constrained to conclude that there is no evidence in this case to raise a question of fact for the jury regarding whether Cobra 4 was an alter ego of Yellow Ribbon."

The Court also held, addressing the plaintiff's appeal, that there was no evidence that Cobra 4 and Yellow Ribbon were joint venturers such that liability could extend to Cobra 4 under the facts presented. The Court found no evidence that Cobra 4 had any right to direct or control the conduct of Yellow Ribbon, meaning that the mutual control needed for a finding of joint venture liability was not present. This lack of control was also the dispositive factor on the issue of negligent entrustment. Under that theory, a party may be liable for entrusting another party with an instrumentality, where that party knows that the person to whom he has entrusted the instrumentality is incompetent by reason of, among other things, a habit of recklessness. In the court's view, a negligent entrustment claim could not be sustained here because there was no evidence that Cobra 4 had any right to control the conduct of Yellow Ribbon, such as any decision with respect to who drove its trucks.

The Court thus found that summary judgment should have been granted to Cobra 4 on all of the plaintiff's claims. One of the justices on the panel concurred in the judgment only as to the Court's decision on alter ego liability, meaning that that part of the decision stands as physical precedent only.

Bryant v. Optima International, Inc.

339 Ga. App. 696, 792 S.E.2d 489 (2016)—Court of Appeals addresses debtor's reliance on alter ego doctrine against two creditors owned by same individual, finds question of fact precluding summary judgment in favor of creditors.

This case presents a situation in which the alter ego doctrine can be used in favor of a debtor against a creditor's attempts to recover the debt. The Court of Appeals held that the creditors should not have been granted summary judgment on a claim to collect on a note because of a question of fact as to whether the lender was an alter ego of a previous lender who failed to confirm an earlier foreclosure sale on the collateral property. The Court found the alter ego argument to be relevant to whether the two loans were owed to the same creditor and therefore "inextricably intertwined" such that the second debt could not be recovered until the foreclosure on the first debt was confirmed.

The debtor, Bryant, operated a nightclub on property he owned. His accountant, Madan, was the sole owner, registered agent, CEO, CFO and corporate secretary of two separate corporations, Optima and Innovative. In 2001, Optima loaned Bryant $200,000, and Bryant gave Optima a security deed on the real property on which the club was situated. In 2004, Innovative

loaned Bryant $345,000. This loan, like the 2001 Optima loan, was for the purpose of financing the club's business. The 2004 note stated that it was to be secured by both the property on which the club was situated and the property next to it, where Bryant lived. Optima made a second loan to Bryant in 2007, again for the purpose of financing the business. The 2007 note stated that the loan was to be secured by only the club property. The security deeds referenced in the 2004 and 2007 notes were never recorded. Later in 2007, Optima foreclosed on the property. Optima, acting as attorney-in-fact for Bryant, executed a Deed Under Power which stated, among other things, that Bryant had delivered the 2004 security deed *to Optima*. In April, 2008, Optima transferred the property to Madan.

Bryant filed suit against Madan, Optima and Innovative, asserting a number of tort and statutory claims and seeking to set aside the foreclosure of the club property under the security deeds he gave. Optima and Innovative counterclaimed to recover on their notes. The trial court entered summary judgment in favor of the creditors. On appeal, Bryant asserted that the counterclaims were barred by Optima's failure to confirm the foreclosure sale pursuant to O.C.G.A. § 44-14-161(a), which provides that no action may be taken to obtain a deficiency judgment unless the person instituting foreclosure proceedings reports the sale to the superior court of the county where the land is located for confirmation and approval, and such confirmation is given. Previous Court of Appeals decisions established a rule that where there are "inextricably intertwined" debts that are owed to the same creditor and secured by the same property, the creditor cannot recover the later debt after foreclosing on the first one unless the foreclosure is confirmed. The Court of Appeals found, with respect to the two Optima loans, that there was a question of fact as to whether they were both made for the same purpose, precluding summary judgment in favor of Optima.

Turning to the 2004 loan by Innovative, the Court of Appeals found that this loan could also be treated as "inextricably intertwined" with the 2001 under alter ego principles. The Court concluded that a jury could find that Optima and Innovative were both alter egos of Madan, in which case all of the loans could be deemed to have been made by the same lender (Madan). In support of this conclusion, the Court cited the fact that Madan was the sole owner and officer of both corporations and that they shared a business address. Interestingly, the Court also cited the fact that Madan and the two corporations were jointly represented by counsel and filed pleadings that suggested that the two entities and Madan treated themselves as one and the same. Finally, the Court viewed the creditors' conduct during and after the foreclosure, leading to the eventual transfer of the club property to Madan, as potentially raising an inference that the two corporations were alter egos of Madan. The Court noted that if the jury found that the corporate creditors were alter egos of Madan, the trial court could then find that the efforts to collect the 2004 Innovative note were barred by the failure to record the earlier foreclosure sale.

Brewton v. Liberty Mut. Holding Co., Inc.

No. 5:14-cv-436, 2016 WL 410009 (M.D. Ga. Feb. 2, 2016)—Parent and affiliate of insurer not liable under alter ego theory absent allegations that insurer was insolvent; agency and joint venture theories of secondary liability also rejected.

This is a putative class action brought by the holder of a homeowners insurance policy issued by First Liberty Insurance Corporation ("First Liberty"), alleging that First Liberty violated Georgia law and breached its insurance contract by failing to properly assess and pay

losses for diminution in value caused by water damage. The plaintiff sued First Liberty along with three affiliated companies (including First Liberty's ultimate parent corporation) that she sought to hold liable on the secondary liability theories of alter ego, agency and joint venture. The three affiliates were not parties to the insurance contract. The plaintiff cited a litany of close interconnections between First Liberty and the affiliates, including that they shared a common principal place of business, had multiple common officers and directors, "coordinate[d] and commingle[d] financial and other resources," operated under a common trade name and used common logos, and maintained a common website. There were also allegations that the plaintiff's premium payments were required to be made to "Liberty Mutual," which all of the companies used as a trade name.

The affiliated companies moved to dismiss. Two of the affiliates moved for failure to state a claim, while the parent corporation (Liberty Mutual Holding Company) moved to dismiss for lack of personal jurisdiction. The issues before the court were essentially the same for all three movants: whether the allegations were sufficient to support any of the plaintiff's secondary liability theories. The court found that they were not, and dismissed all three defendants without prejudice.

With regard to the plaintiff's attempt to pierce the corporate veil under the alter ego doctrine, the court held that the plaintiff's allegations of close interrelationships between the companies was sufficient at the pleadings stage to show that First Liberty was a "mere instrumentality" of the other defendants. But this only satisfied the first prong of a veil piercing claim. The court found that the plaintiff failed to allege facts showing that First Liberty was insolvent or that the defendants' corporate structure would allow First Liberty to fraudulently evade its contractual obligations. The court cited two Georgia Supreme Court decisions for the proposition that a plaintiff cannot state a claim for piercing the corporate veil without alleging insolvency or insufficient assets to satisfy a claim, for the remedy of piercing the veil is permitted only in the absence of an adequate remedy at law. *See Baillie Lumber Co.*, 279 Ga. 288 (2005); *Johnson v. Lipton*, 254 Ga. 326, 327 (1985).

The plaintiff did not allege that First Liberty was insolvent or had insufficient assets to satisfy the claim. Instead, she argued that it would be inequitable for the corporate affiliates to benefit from the use of the "Liberty Mutual" name in connection with her contract and subsequently disclaim any interest in litigation stemming from that contract. The plaintiff cited a 1986 decision from the Southern District of Georgia, *Najran Co. For Gen. Contracting & Trading v. Fleetwood Enters., Inc.*, 659 F. Supp. 1081 (S.D. Ga. 1986) in which the court pierced the corporate veil against a parent corporation that earned "substantial favorable publicity" from its subsidiary's contract, making it "offensive" for the company to "subsequently disclaim interest in the transaction." (Internal punctuation omitted). The court expressed some skepticism that *Najran* could be reconciled with *Baillie Lumber* and *Johnson* insofar as it read those cases to require an allegation of insolvency or insufficient assets. The court did not rule on this basis, however, finding instead that the facts in this case were distinguishable. Here, the plaintiff tried to draw an analogy to *Najran* by pointing to her allegation that she was required to send payments to "Liberty Mutual," the common trade name used by the several defendants. The court was unpersuaded that this presented a comparable situation to *Najran*, and held that the alter ego claim was insufficiently pled.

The plaintiff's agency and joint venture theories were both rejected on the grounds that the plaintiff did not make the requisite allegations of control to sustain either theory. To hold a secondary actor liable under an actual agency theory, Georgia law requires the plaintiff to show that the principal "assumed the right to control the method, manner, and time of the purported agent's work." Here, the mere existence of a parent-subsidiary relationship was not enough to demonstrate control, and the plaintiff's allegations that the two companies market and underwrite each other's policies also did not support an inference that any of the other defendants controlled First Liberty.[2] To sustain a joint venture theory, meanwhile, a plaintiff must allege and show that the parties entered into a joint undertaking with mutual control. Here, the court found that there were no such allegations of mutual control.

Finding no basis to hold the moving defendants liable under the complaint, the court dismissed them without prejudice. Its opinion noted that as the case proceeded against First Liberty, it was possible that facts learned through discovery would reveal a basis for alter ego liability.

Anderson v. American Family Ins. Co.

5:15-cv-475, 2016 WL 3633349 (M.D. Ga. June 29, 2016)—Parent of insurer not liable under secondary liability theories.

In another decision by the same court that decided *Brewton*, involving a similar lawsuit brought against American Family Insurance Company ("AIFC") and its parent company American Family Mutual Insurance Company ("AmFam Mutual"), the court once again found that the plaintiff's allegations of alter ego, agency and joint venture liability were insufficient to state a claim against the parent company. The court's reasoning was largely the same as it had been in *Brewton.* The court reaffirmed that a plaintiff cannot sustain an alter ego claim in the absence of any allegation of insolvency or insufficient assets. Since the plaintiff in *Anderson* did not specifically allege having sent payments to a common trade name, the court did not further discuss the *Najran* decision.

Ashline v. Marinas USA, L.P.

336 Ga. App. 503, 784 S.E.2d 856 (2016)—Purchasers of marina did not assume pre-closing liabilities either expressly or through release provisions.

In this case, the Court of Appeals held that the purchaser of a marina did not assume the marina's pre-closing liabilities, including a default judgment obtained by a boat owner against the marina relating to a conversion that allegedly occurred shortly before the closing of the sale.

---

[2] The plaintiff also asserted an apparent agency theory, which the court rejected on the grounds that there were no allegations that AmFam Mutual held First Liberty out as its agent, or that the plaintiff justifiably relied on the care or skill of First Liberty based upon any such representation. The court noted that the use of common logos and a common website do not demonstrate apparent agency under Georgia law.

Though the relevant sale documents contained assumption of liability language, the purchasers' obligations were limited to post-closing liabilities.

The boat owner initially brought a conversion suit against the limited partnership that operated the marina, alleging that the conversion occurred in July, 2005. The plaintiff obtained a default judgment against the limited partnership, and then sought to add or substitute two new entities who he alleged were the successors in interest based on their purchase of the marina. The sale agreement was executed in May, 2005. The closing date for the sale was not specified in the opinion, but apparently occurred after the alleged conversion.

The trial court denied the motion to add or substitute the purchasers, and the Court of Appeals affirmed. In Georgia, the general rule is that a purchasing corporation does not assume the seller's liabilities. One exception to the rule is when there is an express agreement to assume liabilities. Here, the plaintiff argued that the sale documents constituted such an agreement, pointing to three transaction documents that referenced assumption of liabilities. One of the documents, an assignment of lease whose language was representative of the others, provided that the purchasers "assume[d] the payment and performance of, and agree[d] to pay, perform and discharge, all the debts, duties and obligations to be paid, performed, or discharged from and after (but not before) the effective date hereof by the lessee." The Court of Appeals found that the purchaser's assumption of liabilities was expressly limited to liabilities occurring at or after closing, while the alleged conversion had taken place before.

The court also rejected the plaintiff's argument that certain release language found in the principal sale document could be read as an assumption of liability. One of the releases related to the seller's representations and warranties and appeared to be referring to an indemnification basket, while the other was specific to certain real property. The court found the release language to be too narrow to be read as assumptions of liability by the purchasers, and also recited prior case law explaining that a release is not necessarily synonymous with an assumption of liabilities, as the two types of provisions perform different functions. In the context of a sale, the former serves to liberate a seller from a potential claim belonging to the purchaser that otherwise could have been brought by the purchaser, while the latter is a provision whereby the seller's obligations are assumed by the purchaser.

Barnes v. Smith

339 Ga. App. 607, 794 S.E.2d 262 (2016)—Owner and officer of corporation held not personally liable for corporation's negligent training of employee.

In this case, the Court of Appeals held that the general rule holding corporate officers personally liable for torts by the corporation in which the officer personally participates does not apply to claims involving negligent training of the corporation's employees. This means that if the essence of the claim is that the officer failed to properly train an employee, resulting in tort liability to the corporation, the officer can only be held personally liable under veil-piercing principles. The Court also held, unanimously, that the plaintiff's evidence failed to support a negligent supervision claim as a matter of law.

The case involved a claim under Georgia's Dram Shop law, O.C.G.A. § 51-1-40, against a corporation that owned a Rockdale County tavern and the corporation's principal and sole shareholder, Smith. The plaintiff, who was seriously injured in a car accident caused by an intoxicated patron, asserted that Smith negligently trained and supervised the tavern's employees. Smith moved for summary judgment on the grounds that the plaintiff had failed to pierce the corporate veil, and the trial court ruled in favor of Smith.

The Court recognized that as a general rule, a corporate officer who takes no part in the commission of a tort committed by the corporation is not personally liable unless he specifically directed the particular act to be done or participated therein. This rule is subject only to veil-piercing principles. By contrast, an officer who directly participates in a tort may be personally liable without regard to veil-piercing rules. Here, the claim was premised on Smith's inaction; i.e., his failure to properly train the tavern's staff. The Court cited its prior decision in *Beasley v. A Better Gas Co.*, 269 Ga. App. 426 (2004), which held that the failure to properly train an employee "does not constitute sufficiently direct participation in a tort leading to a plaintiff's injuries." The Court found the case indistinguishable from the situation described in *Beasley* and affirmed. It also affirmed the trial court's determination that the plaintiff had not shown evidence sufficient to establish the elements of a negligent supervision claim.

One judge on the panel wrote a separate opinion concurring specially in the Court's ruling but disagreeing that a corporate officer can never be personally liable for negligent training under the "direct participation" rule. The concurring opinion questioned the majority's reliance on *Beasley*, arguing that *Beasley* did not establish a bright line rule applicable to negligent supervision claims, and that any statement to that effect was dicta. Because the ruling on this issue was not unanimous, the Court's opinion stands as physical precedent only.

3. Jurisdiction, Venue and Service of Process

Pandora Franchising, LLC v. Kingdom Retail Group, LLLP

299 Ga. 723, 791 S.E.2d 786 (2016)—Georgia Supreme Court holds that companies headquartered outside of Georgia cannot invoke the Georgia Code's removal provisions to move tort suits to another county.

In this tort action arising out of a failed attempt to purchase jewelry stores, a unanimous Georgia Supreme Court addressed a novel question that may have significant implications on out-of-state businesses that are registered to do business in Georgia: does a business that has its headquarters outside of the state have the same right as businesses headquartered in the state to remove a tort case from the county in which it is brought to the county in which the business maintains its principal office? The Court answered this question in the negative. Here, it meant that a Maryland-based LLC sued in a tort action in Thomas County could not move the case to Gwinnett County, where it maintains its registered office. The decision could impact any tort action brought in a Georgia state court in which the only basis for venue is that the cause of action originated there, and in which the defendant is a corporation or LLC whose main "corporate nerve center" is outside the state.

For background, O.C.G.A. § 14-2-510(b) provides that domestic and foreign corporations are deemed to reside, for purposes of venue:

> (1) In civil proceedings generally, in the county of this state where the corporation maintains its registered office;
> (2) In actions based on contracts, in that county in this state where the contract to be enforced was made or is to be performed, if the corporation has an office and transacts business in that county;
> (3) In actions for damages because of torts, wrong, or injury done, in the county where the cause of action originated, if the corporation has an office and transacts business in that county;
> (4) In actions for damages because of torts, wrong, or injury done, in the county where the cause of action originated. If venue is based solely on this paragraph, the defendant shall have the right to remove the action to the county in Georgia where the defendant maintains its principal place of business.

The statute was adopted in Georgia as part of the Civil Litigation Improvement Act of 2000. Georgia's LLC Code effectively adopts the same rules to establish the residency of an LLC for venue purposes. The subsection at issue here is Subsection 4, which permits a plaintiff to sue a corporation (or LLC) in a tort action in the county where the cause of action originated. This permits a plaintiff to file the action in a county in which the corporate defendant maintains no office and conducts no regular business, provided that the plaintiff can demonstrate that the cause of action originated in that county. (For many types of claims, the cause of action will be said to originate where the plaintiff resided when the injury was sustained.) However, if the plaintiff's selection of venue is premised *solely* on Subsection 4—i.e., if venue would not be proper under any other subsection—the defendant has a right "to remove the action to the county in Georgia where the defendant maintains its principal place of business." To illustrate, a business headquartered in Fulton County that maintains no office in Chatham County and does not transact business there can remove a tort action from Chatham County to Fulton County.

The application of this rule is relatively simple as it applies to companies headquartered in Georgia. The defendant here, however, was based in Columbia, Maryland. According to the defendant, it was registered to do business in Georgia as a foreign LLC and it maintained its registered office in Gwinnett County. The defendant was in the business of franchising independent jewelry stores. The plaintiff, a resident of Thomas County, alleged that the defendant unlawfully interfered with its attempt to purchase a number of franchises from a third party (the location of whom was not known to the court). The plaintiff filed suit in Thomas County asserting a number of tort claims, including tortious interference with contract and fraud. In response, the defendant sought to remove the case to Gwinnett County. It filed a supporting affidavit asserting that it "maintains its registered office [in Gwinnett County] as its principal place of business in the State of Georgia." The Thomas County court held a hearing and ordered that the case be removed to Gwinnett County pursuant to O.C.G.A. § 14-2-510(b)(4). The Court of Appeals granted interlocutory review and reversed, holding that "Georgia case law shows that in determining questions of residency and jurisdiction, the term 'principal place of business' is used almost exclusively to refer to a single place in the world meeting a certain standard, not to a

place within a state meeting that standard." *Kingdom Retail Group, LLP v. Pandora Franchising, LLC*, 334 Ga. App. 812 (2015).

The Georgia Supreme Court granted certiorari "to determine whether the Court of Appeals correctly construed OCGA § 14-2-510 (b) (4) to mean that, in a claim in which the basis for venue is the allegation that the cause of action originated in the county where the claim was filed, only a corporation with its worldwide principal place of business, or 'nerve center' in Georgia has the right to remove the claim to the county in Georgia where that principal place of business is located."

The defendant argued that a natural reading of the statute supported its position rather than that of the plaintiff and the Court of Appeals. The Court disagreed, finding that in other contexts, the words "principal place of business" have been understood to refer to "the place where the corporation's high level officers direct, control, and coordinate the corporation's activities." In short, the term referred to the corporation's "nerve center." The Court agreed with the Court of Appeals that this could only refer to one place in the world with respect to any one company. The Court then compared O.C.G.A. § 14-2-510(b)(4) with various other Georgia statutes establishing venue for specific types of actions. It found § 14-2-510(b)(4) to differ from these statutes in one important way—the placement of the words "in Georgia." For instance, the Georgia Administrative Procedure Act's venue provision (which, coincidentally, is addressed in *Tanner Med. Ctr., Inc. v. Vest Newnan, LLC* below) states that a corporation may bring suit "where the petitioner maintains its principal place of doing business *in this state*." Section 14-2-510(b)(4), on the other hand, grants a right to remove actions "to the county *in Georgia* where the defendant maintains its principal place of business." Citing legislative history which showed that many examples of statutes using the "principal place of business in this state" formulation were in existence when the present version of § 14-2-510(b)(4) was enacted in 2000, and noting the omission of the words "in this state" from the end of the statute, the Court concluded that the General Assembly must have intended to limit the right of removal to companies whose principal place of business is somewhere in Georgia. Finally with regard to the defendant's statutory interpretation argument, the Court compared the four different subsections of the statute, agreeing with the Court of Appeals that Subsection (b)(4) "easily could have been written to provide that a defendant could remove the case to another deemed residence as provided in the statute" but did not do so.

The defendant also argued that the term "principal place of business" was undefined in the statute and therefore presented a factual question fit for case-by-case determination. This, in the defendant's view, would permit a court to find (as the Thomas County court did) that a defendant was entitled to remove an action to the place within Georgia where it maintains its most significant office within the state. The Court interpreted this approach as giving a defendant license to venue shop, noting that before the corporate venue statute was amended in 2000, corporations had the ability to manage the location of tort suits brought against them through where it chose to place its registered office. In the Court's view, the 2000 amendment broadened the plaintiff's power to control the venue for tort suits by permitting suits to be brought in the county where the cause of action arose regardless of whether the defendant maintained an office there. While the Court acknowledged that the right of removal in

Subsection (b)(4) allowed corporations to retain some control over venue, it concluded that it could not read the statute in a way that it viewed as frustrating the intent of the amendment.

Finally, the defendant noted the apparent unfairness of a rule that would grant a right of removal to a business headquartered in Georgia but not to a business headquartered outside the state. The Court disagreed that the rule was unfair, pointing out that the statute does not discriminate between Georgia corporations and those incorporated in other states. Indeed, as interpreted by the Court, § 14-2-510 applies equally regardless of the state of incorporation. The Court was not persuaded that the statute presented an issue of fundamental fairness, finding that it was unaware of any authority that would treat out-of-state corporations as a protected class. It further held that the statute presented no concern under the Georgia Constitution, which provides that a defendant can only be sued where it is deemed to reside. The Court noted that the right of removal under § 14-2-510(b)(4) has no effect on where a defendant resides, which is defined elsewhere in the statute.

Tanner Medical Center, Inc. v. Vest Newnan, LLC

337 Ga. App. 884, 789 S.E.2d 258 (2016)—Preparations to purchase and develop property held sufficient to constitute "doing business" in a county for purposes of Administrative Procedure Act's corporate venue rules.

This case raised another interesting venue question applied to a business entity. Here, the Court of Appeals was asked to evaluate whether a company can be said to be "doing business" when that business has yet to commence. While the issue was governed by a specific corporate venue provision in the Georgia Administrative Procedure Act rather than O.C.G.A. § 14-2-510, the Court's holding may be relevant to future disputes over venue that are governed by the latter statute.

The case involved a petition for judicial review of a decision by the Georgia Department of Community Health ("DCH") to deny a certificate of need ("CON") to establish a psychiatric hospital in Coweta County. The petitioner, Vest, sought to purchase an existing hospital in Coweta County and submitted a letter of intent to purchase the property. It had no other relevant business dealings in Georgia. Vest filed an application with the DCH to establish a new freestanding psychiatric facility at the Coweta County site, listing the address of the facility on its application. DCH denied the petition. After multiple rounds of administrative review, Vest filed a petition for judicial review in the Coweta County Superior Court.

The Administrative Procedure Act contains a specific venue provision at O.C.G.A. § 50-13-19(b) stating that a petition for judicial review "may be filed in the Superior Court of Fulton County or in the superior court of the county of residence of the petitioner; or, if the petitioner is a corporation, the action may be brought in the Superior Court of Fulton County or in the superior court of the county where the petitioner maintains its principal place of doing business in this state." Here, Vest asserted that venue was proper in Coweta County because that was its principal place of doing business (indeed, its only place of doing business) in the state. It submitted an affidavit from its vice president testifying about its efforts to purchase the hospital and to apply for a CON.

Three hospitals who opposed Vest's CON application intervened in the matter. In addition to opposing the petition for merits-based reasons not addressed here, the opposing hospitals moved to transfer venue to Fulton County, arguing that Vest had no principal place of business in Georgia because it was not conducting any business. The trial court denied that motion and ultimately ruled in favor of Vest. On appeal, the opposing hospitals claimed, *inter alia*, that the case should have been transferred to Fulton County. Addressing this contention, the Court of Appeals addressed what it means to be "doing business" for purposes of O.C.G.A. § 50-13-19(b). The Court turned to the Black's Law Dictionary definition of "doing business," which includes "[t]he act of engaging in business activities." It held that by beginning "the process of purchasing property" in Coweta County and applying for necessary regulatory approval to develop a facility at that site, Vest was "doing business" in Coweta County for purposes of the statute. The Court concluded that venue was there proper in the trial court.

As a side note, the Court briefly addressed O.C.G.A. § 14-2-510(b)(4) and noted the distinction between the language of that statute and the one it was evaluating, O.C.G.A. § 50-13-19(b). Section 14-2-510(b)(4) uses the words "principal place of business", while Section 50-13-19(b) uses the words "principal place of doing business in this state." It would seem that the biggest difference between the two statutes is the use of the words "in this state," whose omission from § 14-2-510(b)(4) proved to be essential in *Kingdom Retail*, above. But the general corporate statute also omits the word "doing", which might mean that the Black's definition of "doing business" is of limited help in interpreting that statute. While the Court's discussion of § 14-2-510(b)(4) was clearly dicta, it appeared to be reading that statute as referring to a corporate nerve center (which is similar to how it was read in *Kingdom Retail*).

Liberty Capital, LLC v. First Chatham Bank

338 Ga. App. 48, 789 S.E.2d 303 (2016)—Venue held proper as to corporate defendant based on allegations that cause of action originated in forum county.

The Court of Appeals once again addressed O.C.G.A. § 14-2-510(b)(4) in this dispute involving an agreement to purchase loans from a bank. The plaintiff, First Chatham, sued the counterparty to the agreement, Liberty Capital, and four co-defendants in Chatham County. The plaintiff asserted a mixture of contract and tort claims. As it regarded Liberty Capital, the plaintiff contended that venue was proper for the tort claims under § 14-2-510(b)(4) because the cause of action originated in Chatham County, where the plaintiff resides, and venue was proper for the other claims under the principle of "pendent venue." This principle vests a trial court with discretion to exercise jurisdiction over related claims arising from the same transaction as a claim for which jurisdiction and venue are established as proper.

Liberty Capital moved for summary judgment on the merits, and also sought to transfer the case to the Superior Court of Cobb County, where it maintains its registered office. (It is not clear from the opinion whether Liberty Capital's principal place of business is also in Cobb County). Liberty Capital argued that because its summary judgment motion was meritorious as to the tort claims, venue would no longer be proper as to the remaining claims. According to the Court of Appeals, Liberty Capital did not couch its argument under the framework of § 14-2-510(b)(4) or argue why venue was improper under the statute. The Court therefore deemed Liberty Capital's venue argument to be abandoned.

Titan Construction Co. LLC v. CBC National Bank

No. CV411-224, 2016 WL 3771249 (S.D. Ga. July 11, 2016)—Court determines citizenship of LLC for purposes of diversity jurisdiction.

In this federal court removal action, a dispute arose as to the citizenship of the plaintiff, a Georgia LLC. For purposes of diversity jurisdiction, an LLC is a citizen of each state in which one of its members resides. The plaintiff brought suit against a Florida bank in the State Court of Chatham County. The defendant removed the case to federal court, alleging that the plaintiff was a Georgia resident and that the case satisfied the other prerequisites for diversity jurisdiction. The plaintiff moved to remand the case to state court, submitting an affidavit from one of its members stating that he was a Florida resident at the time of the filing of the suit. If accepted, this fact would destroy diversity. But there was an odd twist here—the member who submitted the affidavit was also the LLC's registered agent, as reflected in records filed with the Secretary of State. O.C.G.A. § 14-11-209 provides that a registered agent of an LLC "must be an individual resident of Georgia, a corporation, or a foreign corporation having a certificate of authority to transact business in this state." In addition, pleadings filed by the plaintiff in other cases alleged that the member resided in Georgia. Faced with a "sparse" and conflicting record of the member's residence, the district court found the Secretary of State filings to be the most compelling evidence. After all, if the member had not resided in Georgia at the times of those filings, the LLC would not be in compliance with the law. Furthermore, as the court reminded, O.C.G.A. § 14-2-129 provides that "[a] person who signs a document he knows is false in any material respect with intent that the document be delivered to the Secretary of State for filing shall be guilty of a misdemeanor[.]" The district court thus concluded that the member resided in Georgia, that the plaintiff had therefore not shown that it was a citizen of Florida, and that it could exercise diversity jurisdiction over the case.

Alter Vail Ventures, LLC v. Wiles

No. 1:16-cv-1246-WSD, 2016 WL 2757746 (N.D. Ga. May 12, 2016)

Garraway v. Sa

No. 1:16-cv-2830-WSD, 2016 WL 4245358 (N.D. Ga. Aug. 11, 2016)

Dasan USA Inc. v. Weapon Enhancement Solutions LLC

No. 1:16-cv-2566, 2016 WL 3996242 (N.D. Ga. July 26, 2016)—Failure to allege citizenship of all LLC members deprived federal court of diversity jurisdiction.

This year saw a number of other decisions, all originating from the same district court judge, finding that diversity of citizenship had not been adequately pled in cases involving an LLC either as plaintiff or defendant. These cases illustrate the potential difficulties that either a plaintiff or a removing defendant can face in establishing the existence of diversity jurisdiction when one of the parties is an LLC. As noted in the discussion of *Titan Construction* above, for purposes of diversity jurisdiction an LLC is a citizen of every state in which one of its members

is a citizen. In some cases, the LLC will have many members, including members who themselves are LLCs or other unincorporated business entities. In other cases, the identity of the LLC's members (and the members of its members) might not be easily ascertainable by a third party. In addition, this rule can mean that an LLC can be a citizen of many states at once (as opposed to a corporation, which is only deemed to be a citizen of its state of incorporation and the state in which it maintains its principal office. Since diversity jurisdiction requires complete diversity of citizenship among the plaintiffs and defendants, it may be harder to establish where a party is an LLC.

In *Dasan USA Inc. v. Weapon Enhancement Solutions LLC*, the plaintiff brought suit against an LLC in federal court asserting only state law claims. The court denied the plaintiff's initial complaint for failure to adequately allege diversity jurisdiction. The plaintiff filed an amended complaint, and this opinion followed. For the second time, the court held that the allegations were insufficient to demonstrate the complete diversity of citizenship needed for diversity jurisdiction. The plaintiff's amended complaint alleged that the defendant's single *known* member was a resident of Jacksonville, Florida. It attached an exhibit purporting to show the member's current mailing address. The district court found this to be insufficient in two respects. First, citing *Travaglio v. American Express Co.*, 735 F.3d 1266 (11th Cir. 2013), the court found that alleging the member's current *residence* was not equivalent to alleging his state of citizenship. The citizenship of an American citizen for diversity purposes means both residency and "an intention to remain there indefinitely." Second, the court found that it was not enough for the plaintiff to allege the citizenship of only the "known" members of the LLC; instead, the citizenship of each member must be alleged.

Alter Vail Ventures and *Garraway* follow a similar pattern. *Alter Vail Ventures* is notable because the plaintiff failed to allege its own citizenship. The plaintiff initially alleged only that it was a Delaware LLC maintaining its principal place of business in Skokie, Illinois. The district court ordered the plaintiff to replead facts showing diversity of citizenship, citing the rule applicable to LLCs. The plaintiff filed an amended complaint alleging that it had two members, both of whom were LLCs, and proceeded to allege facts about the members of its members (which also were unincorporated entities). The plaintiff described many of the ultimate members as "Illinois trusts," without providing any other information about those trusts. It also alleged the state of residence as to those ultimate members who were natural persons. The district court held that the amended complaint was still insufficient. It cited an Eleventh Circuit case, *Laborers Local 938 Joint Health & Welfare Tr. Fund v. B.R. Starnes Co. of Fla.*, 827 F.2d 1454 (11th Cir. 1987), which held that "the citizenship of trust fund members is determinative of the existence of diversity of citizenship." Here, the ultimate beneficiaries of the trusts were not identified; therefore, the plaintiff had not done enough to allege its citizenship. The complaint also failed to allege the citizenship of the individual members for the same reason identified in *Dasan USA*—the complaint must allege facts showing citizenship, which does not necessarily equate to residence.

Techjet Innovations Corp. v. Benjelloun

No. 1:15-cv-4074-AT, 2016 WL 4942351 (N.D. Ga. Aug. 17, 2016)—Out-of-state CEO's personal involvement in forming contractual relationship with Georgia resident subjected him to personal jurisdiction in Georgia.

In this contract and tort dispute arising from a multi-phase project to develop and build unmanned aircraft, the district court held that the out-of-state CEO of one of the contracting parties was subject to personal jurisdiction in Georgia, based on his alleged primary role in the conduct giving rise to the claims. The court's opinion includes a lengthy and helpful discussion of prior Georgia state and federal caselaw applying Georgia's long-arm statute to corporate officers and directors.

The plaintiff was a Georgia-based company that received a proposal in 2013 by Earth and Water Consulting, Inc. ("EWC") to work on a project to build drones. The plaintiff alleged that EWC's President, CEO and majority shareholder, Benjelloun, personally participated in soliciting the plaintiff to work on the project, and further alleged that one of the reasons why the plaintiff was selected was his relationship with Georgia Tech. As a result of the solicitations, the plaintiff entered into a contract with Bio-Cellular Design Aeronautics, Inc. ("BDA"), another company controlled by Benjelloun. The plaintiff entered into a second contract with BDA in early 2014, and a third contract with EWC and BDA in late 2014. In all cases, Benjelloun signed the contracts on behalf of his companies. There were no meetings held in Georgia to negotiate or discuss the contracts, but the work performed under at least the first two contracts was performed in Georgia. A dispute arose in early 2015. According to the plaintiff, the defendants (who included other individuals not relevant here) defaulted on their payment obligations. The parties exchanged correspondence and emails relating to the dispute, and in July 2015, a representative of the plaintiff met with Benjelloun in Arizona. There were no facts alleged that would have indicated the presence of regular or systematic contacts between Benjelloun and the state of Georgia.

Benjelloun argued that the plaintiff failed to allege that he was an alter ego of his corporations, and that he did not engage in any business in Georgia in his personal capacity. The district court found these arguments to be irrelevant in light of Benjelloun's personal participation in the alleged misconduct. The plaintiff had alleged that he was directly involved in soliciting the business relationships giving rise to its claims, and that he orchestrated the acts and omissions that caused the companies to default on their contractual obligations.

The district court understood that in substance, Benjelloun was seeking to avail himself of the "fiduciary shield" doctrine, which is not recognized in Georgia. Under the fiduciary shield doctrine, a nonresident individual cannot be subject to personal jurisdiction in a forum based solely upon acts taken in a corporate capacity in that forum. The court cited and discussed at length the Georgia Supreme Court's decision rejecting the fiduciary shield doctrine in *Amerireach.com, LLC v. Walker*, 290 Ga. 261 (2011). The *Amerireach* court held that "employees of a corporation that is subject to the personal jurisdiction of the courts of the forum may themselves be subject to jurisdiction if those employees were primary participants in the activities forming the basis of jurisdiction over the corporation." The district court cited several Georgia federal court decisions after *Amerireach* that have found corporate directors and officers to be subject to personal jurisdiction in Georgia based on conduct directed towards Georgia. As the court noted, the conduct found to be relevant in those cases included soliciting and negotiating contracts with a Georgia-based company, acting as the "primary decision maker" in stealing trade secrets from a Georgia resident, and initiating an illegal debt adjustment program that targeted Georgia residents. The court found that there was no one decision that was similar

enough to the case before it to be considered controlling, but that the present case had facts in common with all of them. Specifically, it was alleged that the defendant "communicated with Georgia residents; solicited business from a Georgia company because of its ties to Georgia Tech; his foreign corporation's only partner was a Georgia corporation; all of the work done in connection with the contracts was done in Georgia; and he allegedly personally participated in a significant number of events surrounding, leading up to, and following the alleged breach by BDA and EWC."

Notably, the court found that Benjelloun was subject to personal jurisdiction in Georgia despite his denials that he had ever set foot in Georgia in connection with the contracts that were the subject of the suit. In its discussion of the case law, the court found precedent for exercising jurisdiction even in the absence of a single visit to Georgia. The court concluded that a physical presence in Georgia was unnecessary where the defendant "allegedly directed his and his business' conduct at and communicated with Georgia residents in connection with a significant contractual relationship over an extended period of time."

Thomas v. Bank of America, N.A.

1:11-cv-0391-WSD, 2016 WL 632522 (N.D. Ga. Feb. 17, 2016)—LLC not properly served where plaintiff failed to demonstrate that its officer was authorized to accept service.

This opinion addresses several related issues dealing with service of process on an LLC that dissolved shortly before the plaintiff filed his complaint. The plaintiff filed suit against the LLC and other defendants asserting various claims arising from the foreclosure sale of his property. The plaintiff served a copy of the complaint and summons on a Mr. Messer, whom he identified as the LLC's president. The LLC, who did not answer or respond to the complaint, moved to set aside the clerk's entry of default, arguing that Messer was not authorized to accept service on behalf of the LLC. The LLC further showed that it had dissolved two weeks before the plaintiff filed suit and had filed its Certificate of Termination with the Georgia Secretary of State. The LLC's last annual registration with the Secretary of State had identified a Mr. Sander as its registered agent. The LLC argued before the district court that the plaintiff had to serve Sander. The trial court agreed and set aside the clerk's default. The plaintiff filed an amended complaint and served it on the LLC by personally serving Sander. The LLC moved to dismiss that complaint for failure to state a claim, and prevailed. The plaintiff appealed the trial court's ruling with respect to setting aside the default, and the Eleventh Circuit affirmed. *See Thomas v. Bank of America, N.A.*, 557 Fed. Appx. 873 (11th Cir. 2014).

The plaintiff moved to reconsider, giving rise to the present order. The plaintiff asserted that new evidence had surfaced showing that Messer was indeed authorized to accept service on the LLC's behalf. This evidence consisted of statements that Messer had made on the record in other litigation involving the parties in state court, including a verification signed by Messer in connection with the LLC's responses to interrogatories. The court held that these filings did not present a valid reason to depart from its prior ruling, noting that it was not mutually exclusive that Messer could be authorized to verify discovery responses in litigation but not be authorized to accept service of process. The plaintiff also argued that because he was unaware of the dissolution, and the LLC did not file a Statement of Commencement of Winding Up, he was permitted to serve the LLC through Messer under O.C.G.A. § 14-11-604 and § 14-11-606.

Under O.C.G.A. § 14-11-604(b), "prior to the filing of a statement of commencement of winding up, the limited liability company shall be bound to any person who lacks knowledge of the dissolution with respect to any transaction which would bind the limited liability company if dissolution had not taken place." The Court rejected the plaintiff's premise that the failure to file a statement of commencement of winding up gave him any entitlement to treat the LLC as if it had not dissolved, and also found the argument to be irrelevant insofar as the plaintiff had not shown that Messer was authorized to accept service prior to dissolution. As to the latter point, the Court applied Federal Rule 4(h), which incorporates Georgia state law principles regarding service of a limited liability company. In Georgia, an LLC can be served in the same way as a corporation: by delivering a copy of the summons and complaint "to the president or other officer of the [LLC], secretary, cashier, managing agent, or other agent thereof." The Court found that there was no evidence in the record showing that Messer was authorized to accept service of process at the time the plaintiff attempted to serve the LLC. While some public filings by the LLC indicated that Messer had been a Vice President of the LLC in 2006, the Court found that to be irrelevant to whether he had authority to accept service in 2011, when the summons and complaint were served.

4. Evidentiary Issues

Yugueros v. Robles

300 Ga. 58, 793 S.E.2d 42 (2016)—Rule permitting use of testimony of corporate representative against corporation "for any purpose" is limited by applicable evidentiary rules, including expert testimony requirements.

The Supreme Court reversed a Court of Appeals decision which had permitted the 30(b)(6) testimony of a representative of a medical practice to be offered at trial as a statement against interest, above an objection that the 30(b)(6) witness was offering expert testimony and had not been qualified as an expert. The Court unanimously held that such testimony should only be admitted if it satisfies the evidentiary rule governing expert testimony, see O.C.G.A § 24-7-702. The case serves as a reminder that while testimony of a corporate representative during a properly noticed 30(b)(6) deposition may generally be used against the corporation, that rule remains subject to other relevant rules of evidence.

This was a medical malpractice action brought against a plastic surgeon and the practice that employed her. One of the critical issues in the case was that the surgeon, while treating the patient for post-surgery pain, failed to order a CT scan. During discovery, the plaintiff took the deposition of the founder and co-owner of the practice pursuant to O.C.G.A. § 9-11-30(b)(6). When asked whether it would have been part of the standard of care to order a CT scan under the circumstances, the deponent stated that it would have been. The trial court excluded this testimony at trial, sustaining a motion in limine brought by the practice group, which argued that the deponent was not qualified to give expert testimony in the matter because, among other things, she had not been provided all data necessary to form an opinion. The trial resulted in a verdict for the defense. The Court of Appeals reversed the trial court's evidentiary ruling, holding that the testimony should have been admitted as an admission against interest under O.C.G.A. § 9-11-32(a)(2). That section provides that the deposition testimony of a 30(b)(6) witness (as well as a corporate officer, director or managing agent) "may be used by an adverse

party for any purpose." The Court of Appeals read this to mean that the testimony at issue here did not need to be offered as expert testimony in order to be admissible.

The Supreme Court held that this "does not accurately reflect the law" as it regards the use of 30(b)(6) testimony. The Court reasoned that the statement in § 9-11-32(a)(2) permitting the testimony of a corporate representative to be used "for any purpose" was qualified by the prefatory language in § 9-11-32(a) stating that a deposition may be used against a party "so far as admissible under the rules of evidence applied as though the witness were then present and testifying." Since the testimony in question concerned a medical standard of care and therefore invoked the rules governing expert testimony, those rules needed to be applied, and the testimony could not be used unless it satisfied the requirements of § 24-7-702. Accordingly, the Supreme Court reversed and remanded the case to the Court of Appeals.

5. Director and Officer Liability Insurance Decisions

SavaSeniorCare, LLC v. Beazley Ins. Co.

No. 1:14-cv-2738-RWS, 2016 WL 4357521 (N.D. Ga. July 14, 2016)—Allocation provision of D&O policy covered defense costs of LLC directors; court finds that directors were sued in an insured capacity.

In this dispute between an LLC and its excess D&O insurer, the district court determined that the policy's allocation provision required the insurer to pay the defense costs of two of the LLC's former directors and managers. The action turned on whether the two individuals were sued in an insured capacity, an issue the district court resolved in the LLC's favor.

The plaintiff, Sava, was sued in New York by a real estate investor in a complex, 15-count suit seeking specific performance of an option to purchase Sava's former parent company. Also named in the suit were two of Sava's former directors. Sava and the New York plaintiffs had a number of business relationships that the New York plaintiffs argued created a fiduciary relationship between the two directors and themselves. The two directors sought indemnification from Sava pursuant to an operating agreement between Sava and its parent. Under that agreement, the directors were entitled to indemnification so long as the claims related to actions they took on behalf of Sava. Sava agreed to indemnify the directors and ultimately paid them millions of dollars in connection with their defense of the New York suit.

Sava sought reimbursement for these defense costs as well as its own defense costs connected to the New York lawsuit. Zurich, the primary carrier, reimbursed Sava for a portion of its own defense costs, but denied coverage for the costs it paid to the directors, claiming that the New York plaintiffs "did not allege wrongful acts against [the directors] in their capacities as 'insured persons.'" By the time of this opinion, Zurich was no longer a party to this dispute. The defendant, Beazley, adopted Zurich's position with respect to the two directors.

Both parties moved for judgment on the pleadings as to the question of coverage for the directors' defense costs. There was no dispute as to the relevant policy language. The policy contained an allocation provision which provided that "If the Insureds incur both Loss covered by this policy and loss not covered by this policy either because a Claim against the Insureds

includes both covered and uncovered matters or because a claim is made against both Insureds and others (including the Company in a Claim other than an Employment Practices Claim), then 100% of such Defense Costs will be considered covered Loss and all other such loss shall be allocated by the Insured Persons, the Company and the Underwriter between covered Loss and uncovered loss based upon the relative legal exposure of the parties to covered and uncovered matters." Sava argued that at least one of the "wrongful acts" alleged against the directors involved their conduct in an insured capacity, and as a result, the allocation provision required Beazley to pay 100% of their defense costs. In response, Beazley argued that the two directors were not sued in an insured capacity at all, meaning that there was no coverage for their defense costs.

The dispositive question, therefore, was whether the two directors were sued in an insured capacity. The court cited Georgia law holding that the insurer has a duty to defend an action if the facts alleged "even arguably bring the occurrence within the policy's coverage." The court identified three claims in the New York complaint that related to conduct "that plausibly could not have been performed by [the directors] absent their relationship to Sava." This was sufficient to trigger coverage for all defense costs under the allocation provision. Accordingly, the court granted Sava's motion and denied Beazley's motion.

Sentinel Insurance Co. v. USAA Insurance Co.

335 Ga. App. 664, 782 S.E.2d 718 (2016)—Court of Appeals applies priority of coverage rules to limited liability companies.

In this case, the Court of Appeals addressed for the first time how the priority of uninsured motorist ("UM") coverage should be resolved as between an employer policy and a family policy when the employer is an LLC. The Georgia courts have resolved similar disputes in which the business policy is for a corporation or for a sole proprietorship, but not where the business is an LLC.

The case involved an automobile accident in which the plaintiff was driving a car owned by her business, a Georgia LLC. The plaintiff brought a personal injury suit against the driver who caused the accident as well as two insurance carriers who provided UM coverage. The first carrier, Sentinel, provided coverage under a business policy in which the LLC was the named insured and for which the LLC paid premiums. It was undisputed that the plaintiff used the car for business purposes. The second carrier, USAA, provided coverage under a personal auto insurance policy issued to the plaintiff's husband, under which the plaintiff was an additional insured. The plaintiff sought to recover from both carriers. In such cases, the court must determine the priority of UM coverage. For background, under Georgia law, the priority of UM coverage can be determined using a "receipt of premium" test or a "more closely identified with" test. Because the plaintiff did not pay the premiums for either policy, the Court of Appeals employed the latter test. This required the Court to determine "the policy with which [the plaintiff] is more closely identified."

The court found two of its earlier decisions to be instructive. In the first, *Travelers Indem. Co. v. Maryland Cas. Co.*, 190 Ga. App. 455 (1989), the plaintiff was driving a vehicle owned by her employer, which was a corporation. She was insured under both the corporation's

policy and her mother's family policy. The Court of Appeals held in *Travelers* that the plaintiff was more closely identified with her mother's policy, as an additional insured family member. It noted that in applying the "more closely identified" test, the key consideration was not the relationship between the accident and the policies, but the relationship between the plaintiff and the policies. The plaintiff's relationship to the corporation's policy was deemed to be not particularly close because of the corporation's separate identity from its individual constituents. In the second case, *Southern Guaranty Ins. Co. v. Premier Ins. Co.*, 219 Ga. App. 413 (1995), the injured plaintiff was a sole proprietor, and was insured under both a business policy and a family policy. This time, the Court of Appeals held that the plaintiff was more closely identified with the business policy, because her business was not a corporation and its obligations and benefits inured to her directly.

Since the Court had not previously been faced with a scenario in which the business was an LLC, it had to decide whether the situation was more analogous to *Travelers* or *Southern Guaranty*. It held that the analogy to a corporation was more appropriate. The court noted that an LLC, like a corporation, is designed to protect its members from personal liability, debts and obligations of the business. As a result, the same "corporate veil" that exists for a corporation also exists for an LLC. This meant that the plaintiff had a closer relationship to her husband's policy as an insured family member than to her company's policy. Because the trial court held otherwise, the Court of Appeals reversed and found that USAA was the primary carrier.

6. Professional Liability

Befekadu v. Addis International Money Transfer, LLC

339 Ga. App. 806, 795 S.E.2d 76 (2016)--Court of Appeals affirms disqualification of attorney who assisted in formation of LLC that was opposing party in litigation.

The Court of Appeals, in an 8-1 ruling under the Court's new "nine-judge" procedure,[3] affirmed a trial court's decision disqualifying an LLC member's attorney from representing the member in litigation brought against him by the LLC and its other members. This was the second time the disqualification issue had come before the Court of Appeals. The first time, the Court vacated and remanded an earlier disqualification order on the grounds that the court had failed to apply the correct legal standard for disqualification. After the trial court conducted a full evidentiary hearing on the matter, the majority was satisfied that the court had this time applied the correct legal standard and affirmed.

The case involves a money transfer company that was formed as an LLC in 2006 by the defendant and three business partners. The attorney who was the subject of the disqualification order was hired by the defendant on behalf of the LLC to perform the legal work necessary to form the company. The attorney drafted articles of incorporation, obtained an employer tax identification number, and served as the LLC's registered agent through 2011. The LLC's

---

[3] The Court of Appeals recently adopted new operating procedures which include a requirement that in the event of a dissent within the panel assigned to the case, two additional panels will participate in the decision, meaning that such cases will be decided on by nine justices.

PGDOCS\6673434.1

members believed that the attorney had also prepared an operating agreement for the LLC, but that was not the case. The underlying dispute involved allegations that the defendant wrote over $55,000 in unauthorized checks on the LLC's account. A small portion of that money went to pay for the attorney's legal services. In addition, the plaintiffs (the LLC and its other members) alleged that the defendant breached his fiduciary duty by not having an operating agreement prepared as had been contemplated.

The attorney ultimately represented the defendant throughout the course of the litigation, which went all the way to trial. At trial, the attorney's questioning of one of the plaintiffs regarding payments made to his law firm prompted the trial judge to interject that the attorney was giving testimony disguised as questioning. After the questioning continued to delve into areas relating to the formation of the company, the trial judge excused the jury and ordered that the attorney be disqualified. That decision was vacated by the Court of Appeals on the basis that the trial court failed to engage in the correct legal analysis. *See Befekadu v. Addis Int'l Money Transfer*, 332 Ga. App. 103, 772 S.E.2d 785 (2015). In that decision, the Court of Appeals held that disqualification based on a prior representation is only warranted when the current matter is substantially related to the prior representation.

Upon remand, the trial court held a full evidentiary hearing at the individual LLC members and the disqualified attorney testified. The trial court entered a written order finding that the attorney's prior representation of the LLC was "substantially related" to the LLC's claims that the defendant converted company funds and breached his fiduciary duty by failing to have an operating agreement drafted that would have prevented him from diverting the funds. The trial court further found that the question concerning the attorney's failure to prepare an operating agreement for the LLC, and his firm's receipt of funds, were core issues in the case. Because no transcript of the hearing was included in the appellate record, the Court of Appeals applied a presumption that the trial court properly considered the evidence and that its findings of fact were supported by evidence. The majority opinion found that the trial court correctly applied the standard announced in its prior decision insofar as it determined that the issues presented at trial were substantially related to the attorney's prior representation.

One of the justices dissented, finding that the trial court had not applied the correct legal standard but instead ruled solely on the basis of an "appearance of impropriety." The dissent noted that the trial court had found that the attorney did not continue to represent the LLC after performing the tasks needed to form it, and also that there was no evidence that the attorney may have learned any special knowledge from the prior representation which could have been used to the LLC's disadvantage in the litigation. In the dissent's view, the relationship between the attorney's work in forming the LLC and the issues that arose thereafter was too attenuated to support disqualification, particularly in light of the countervailing interest in preserving the defendant's right to the counsel of his choice.

7. Bankruptcy-Related Questions

In re McKeever

550 B.R. 623 (Bankr. N.D. Ga. 2016)--Alleged reincorporation of business 15 years after dissolution of other entity of same name did not have effect of reinstating the dissolved entity.

This bankruptcy proceeding presented a question regarding whether the debtor validly reinstated his previously dissolved corporation, such that insurance proceeds could be treated as corporate property rather than the debtor's property. The bankruptcy court found that no valid reinstatement occurred here, due to the passage of time.

The debtor and his family operated a body shop business named MP&B for many years on property that was owned by the debtor personally. The debtor formed a corporation named MP&B, which, among other things, guaranteed a personal loan taken out by the debtor to finance the purchase of the body shop property. In 1998, the debtor suffered a serious injury which left him incapacitated for some time. MP&B's corporate registration lapsed and it was administratively dissolved at that time. Other family members continued to operate businesses on the property, using other corporate entities to conduct these activities. Years later, the debtor returned to doing business under the trade name MP&B, but he did not re-establish the corporation. In 2013, three years after the debtor initially filed for bankruptcy under Chapter 13, an accident occurred on the property which led to the filing of an insurance claim. The insurance carrier issued a $40,000 check to MP&B and a creditor. The debtor received the check and, after it was endorsed by all payees, sought to open a bank account for MP&B so that the proceeds could be deposited. To do this, he incorporated MP&B again, showed proof of incorporation to the bank, and opened an account. The debtor then proceeded to withdraw nearly all of the proceeds.

The Trustee sought to have the debtor's request for a discharge denied and filed an adversary proceeding against the debtor and other family members and entities. The debtor argued that the insurance proceeds were corporate property of MP&B rather than part of the debtor's estate. The bankruptcy court disagreed, citing that MP&B had been administratively dissolved for over 12 years before the bankruptcy petition was filed and remained dissolved at the time the insurance claim was made and the check was issued. While an administratively dissolved corporation may apply for reinstatement, § 14-2-1422(a) provides that the application for reinstatement must be made within five years of the dissolution, or the corporation ceases to exist. Therefore, the court reasoned, MP&B was no longer in existence at the time of the insurance claim, and its "reincorporation" fifteen years after dissolution of the original entity did not serve to reinstate the previous entity. The court noted that the result may have been different if the reinstatement period were still running at the time, but it had long expired. The court found it irrelevant that the debtor continued to use MP&B as a trade name after the corporation had dissolved, citing precedent holding that trade names are not legal entities but instead serve as the alter ego of the individual. Having so held, the bankruptcy court found that the insurance proceeds were property of the debtor's estate.

F. FULTON COUNTY BUSINESS COURT DECISIONS.

State of Georgia ex rel. Hudgins v. O'dom

No. 2015-cv-258501 (June 29, 2016) (Order on Motions to Dismiss)

The business court granted in part and denied in part a complaint brought by the Georgia Insurance Commissioner in his capacity as liquidator of a failed automobile insurance company against the company's former officers and directors as well as a group of banks who provided financing for the company. The Commissioner alleged that the company lacked effective internal controls to safeguard assets and experienced significant losses in 2008 and 2009 that were revealed in an independent audit. The Commissioner placed the company under administrative watch in 2010, and then declared it insolvent in 2013 after problems persisted. The complaint alleged that the officer and director defendants' mismanagement of the company and failure to put competent employees in key positions caused these losses. Meanwhile, as troubles mounted, the company continued to receive financing from the financial entity defendants. The loans were not made directly to the company, but rather to affiliated companies and individuals. The Commissioner alleged that these loans were deliberately structured so as to enable the company to maintain statutorily-required capital and surplus levels without having to book the loans as liabilities. One particular loan, for $7 million, was made in November, 2012 by one of the financing entities to one of the individual defendants, but the money was returned to the financing entity two weeks after it was received.

Several noteworthy issues were addressed in the motions to dismiss. One key question was whether the Commissioner could bring a negligence action against the company's president and CEO for his failure to prevent the return of the $7 million loan (which separately was alleged to be a fraudulent transfer under the Insurance Code). The CEO argued that the claim was an attempt to expand liability under the fraudulent transfer laws to a non-transferee, as there was no allegation that either he or the company ever handled the money. The court disagreed, finding that there were sufficient allegations to raise a question of fact as to whether the actual recipient of the loan was the company's alter ego. On the other hand, the court dismissed the Commission's claim against the same defendant for aiding and abetting a breach of fiduciary duty, holding that the defendant (as President and CEO of the company and a controlling shareholder of the company's managing agent) was not a stranger to the fiduciary relationship.

The court also addressed whether Georgia law recognizes a right of action for "deepening insolvency." The deepening insolvency theory posits that a company's directors, officers or other managers may be liable for actions that cause a financially troubled company to incur more liabilities and thus deepen its insolvency. Some courts in other jurisdictions have found that deepening insolvency can give rise to an independent cause of action, while others, including Delaware, have held that it does not. The Georgia appellate courts have not addressed the question, so the business court evaluated the caselaw from other jurisdictions. It found the most persuasive case to be a 2009 Tennessee bankruptcy decision finding that the deepening insolvency theory was duplicative of other existing remedies available to bankruptcy trustees, receivers and other potential plaintiffs. The court concluded that the Georgia appellate courts would be unlikely to recognize a novel cause of action where other complete remedies exist.

Another defendant, who served as the company's chief operating officer, moved to dismiss the Commissioner's negligence claim, which appeared to have been framed to fit the requirements of *Loudermilk*. The Commissioner alleged that the defendant breached his fiduciary duties "by making management decisions without deliberation, without the requisite diligence to ascertain and assess the facts and circumstances upon which the decisions were based, and/or in bad faith." Under Georgia's notice pleading rules, the court found these allegations to be sufficient at the motion to dismiss stage.

Homeland Self Storage Management, LLC v. Pine Mountain Capital Partners, LLC

No. 2014-cv-246999 (Ga. Super. June 24, 2016) (Order on Defendants' Motion for Summary Judgment)

This was a fraud and breach of fiduciary duty suit brought by an LLC against a former employee who was responsible for performing various tax and accounting related functions for the LLC. The trial court granted the employee's motion for summary judgment in part and denied it in part, holding that the employee's significant responsibilities to the LLC were sufficient to raise a genuine fact that he owed fiduciary duties, and that there was evidence of a breach, but that there was insufficient evidence of causation to support some of the LLC's claims, and also insufficient evidence to support a fraud theory.

The plaintiff, Homeland Self Storage Management, was an LLC in the business of managing the affairs of various self-storage facilities organized as partnerships. It was co-owned by two individuals who were also partners in the partnerships. The individual defendant, a CPA, was hired by the LLC in 2005. He was given the title of chief financial officer, though he never entered into a formal employment agreement. The defendant's duties included handling the LLC's finances and accounting needs, preparing the LLC's and its employees' tax returns, managing various projects, negotiating contracts, and paying vendors. He did not have final authority to approve payments of invoices, enter into contracts, sign checks or transfer money; instead, this authority was retained by the co-owners. Once sign-off was given, the co-owners claimed that they trusted the defendant to take final steps to submit the payment to vendors. In June, 2011, SunTrust notified the LLC (through an email to the defendant) that certain taxes had not been paid by the partnerships. The defendant informed one of the co-owners of this, saying that it was a mistake, but he then resigned within a month. The LLC later discovered that the defendant had created his own company, whose name also began with "Homeland", which paid certain vendors.

The LLC sued the individual defendant, the newly discovered "Homeland" entity, and another company created by the defendant that he also used to pay invoices. The LLC claimed that the individual defendant breached fiduciary duties to the LLC and committed fraud and that the corporate defendants engaged in a civil conspiracy. A special master was appointed to review the LLC's records for evidence that funds had been diverted. This review failed to turn up such evidence. One reason it did not may have been the fact that one of the co-owners voluntarily had at least 50 bankers' boxes destroyed following the individual defendant's resignation, which allegedly contained all of the documentation that the individual defendant had maintained.

The defendants moved for summary judgment. As to the claim that the individual defendant breached his fiduciary duty by failing to report outstanding taxes, the court found that a genuine issue of material fact existed. Specifically, the court found that even though the defendant had no formal employment agreement and did not have the power to bind the LLC without prior approval, the scope of his responsibilities were significant enough that a jury could determine that he and the LLC were in a confidential relationship. A jury could also find that the individual defendant failed to properly notify the co-owners about tax liabilities and that this proximately caused the LLC to suffer damages. As for the rest of the LLC's claims, which were based on theories that the defendant diverted funds and/or failed to competently perform his accounting duties, the court found that there was no evidence of causation, citing the Special Master's review. While there was much speculation that the defendant had created the other "Homeland" entity as part of a scheme to divert funds, there was no evidence of any particular improper transfer, no evidence that the defendant had forged a signature, and no evidence that checks were made for debts not owed. Accordingly, there was no evidence that the defendant's actions or inaction caused loss, and also insufficient evidence to support any of the claims based on the alleged diversion of funds.

Piedmont/Maple, LLC v. Eichenblatt

No. 2014-cv-253094 (Ga. Super. Oct. 31, 2016) (Order on Plaintiffs' Motion for Summary Judgment on Defendant's Counterclaims)

In this case, an equity interest holder in a dissolved LLC that previously owned and managed commercial property alleged that the LLC's sole member breached the LLC's operating agreement and breached fiduciary duties owed to him. The LLC's member filed an action for declaratory judgment after the LLC was dissolved, seeking a court ruling confirming that the equity holder had received the correct distribution. The equity holder then counterclaimed, alleging that the member had mismanaged the resolution of a loan it was owed that went into default, made decisions that decreased the sale value of the LLC's assets, and undercharged its own general partner for rent.

The plaintiff moved for summary judgment as to the equity holder's counterclaims. The business court granted the motion in part and denied it in part. The court noted that with respect to the breach of contract claims, the plaintiff owed the equity holder an implied duty of good faith and fair dealing as to matters in which performance was left to its discretion, but that the contract could also be written in such a way as to eliminate the implied duty of good faith. Here, in the court's view, the operating agreement allowed the member to resolve the matter involving the defaulting loan in exactly the way it was done (by providing a member loan to the LLC), so long as the terms were no less favorable to the LLC than the terms that would have been available from a third party. Since the equity holder presented no evidence that more favorable terms were available, the business court found that there was no breach of contract as a matter of law. The court reached a different conclusion as to the claim concerning the charging of rents to the plaintiff's managing partner. Here, the contract specified that rents were to rise by a specified percentage every year, but the plaintiff failed to make these increases. The court found that this created a genuine issue of material fact as to whether the plaintiff breached the operating agreement.

The court made similar rulings regarding the breach of fiduciary duty claims, which were based on the same alleged misconduct. As an initial matter, it ruled that a jury could determine from the facts that the parties were in a fiduciary relationship notwithstanding that the defendant was only an equity interest holder in the LLC and not a member. The court then noted the rule that actions specifically permitted by the operating agreement cannot constitute a breach of fiduciary duty. This meant that the plaintiff could not have breached its fiduciary duties in connection with the defaulting loan, since the actions it took were expressly permitted under the agreement. But since there was a question as to whether the plaintiff violated the terms of the agreement by not raising rent to its general partner, summary judgment was precluded as to that claim.

Souza v. Berberian

No. 2015-cv-257652 (Ga. Super. Apr. 20, 2016)

Ruling on cross-motions for summary judgment, the business court held that an email outlining terms of a potential operating agreement did not create an enforceable contract making the plaintiff a member of the LLC. Since the plaintiff had no other proof that he had entered into an enforceable agreement to become a member of the LLC, none of his claims that were premised on the fact of his membership were maintainable as a matter of law.

The plaintiff and defendant made plans to form a new business that would provide allergy testing services for a medical practice. The parties discussed forming an LLC in which the plaintiff would have a minority ownership interest. The defendant formed the LLC, with himself as its only member, and the parties thereafter had discussions about the terms of the plaintiff's interest. No formal agreement was ever executed. The plaintiff argued that the parties nonetheless formed an agreement to give him a 21% interest, citing an email sent to him by the defendant. This email provided that the plaintiff would have a 21% interest which was subject to change based on the result of other related negotiations. The email also stated other terms, but the defendant noted that he was working from memory of the terms of another LLC of his, and that he would "maybe add or change some points" once he could review the operating agreement he planned to use as a template. The defendant also stated in the email that he was not certain he had covered all of the points, that the agreement was not "set in stone", and that it was a "high level view" of the parties' discussions to that point.

In the court's view, this email did not evidence the meeting of the minds necessary for contract formation, given the language indicating that there would be further review and discussion of the material terms. The court also noted that the parties had further negotiations after the email was sent, that substantial points of disagreement emerged, and that no agreement was ever signed. Because several of the plaintiff's claims (including breach of contract, specific performance and breach of fiduciary duty) were premised on the plaintiff having a membership interest in the LLC, the court granted summary judgment on those claims in favor of the defendant.

Nix v. Carter Brothers Security Svcs., LLC

No. 2014-cv-253536 (Ga. Super. Aug. 29, 2016) (Order on Plaintiff's Motion for Partial Summary Judgment)

The business court granted a motion for summary judgment against the purchaser of a controlling interest of a business, holding that the purchaser had failed to demonstrate that the selling shareholder had the requisite scienter for a RICO violation premised on fraud or that he breached any fiduciary duty in connection with the sale.

The case involved the sale of a controlling interest in an electrical contracting company in January, 2014. The company had experienced significant financial hardship in the period leading up to the sale, and its controlling shareholder (the plaintiff) had ceased to be closely involved in its day-to-day affairs. In September, 2013, the defendant, an LLC, provided a $500,000 loan to the company in exchange for a 7.5% interest in its common stock. The defendant then negotiated for the purchase of the plaintiff's controlling interest. The parties executed a letter of intent in November, 2013, and the defendant then conducted two months of due diligence, and hired accountants and legal counsel to assist it with due diligence. There was no evidence in the summary judgment that the plaintiff was personally involved in the due diligence. From the company's perspective, due diligence requests were handled by company employees and accountants. The parties agreed to a purchase price containing a fixed component and a contingent component. When the defendant failed to pay the contingent part of the price, the plaintiff filed this suit. The defendant then counterclaimed, alleging that the plaintiff misrepresented the company's value by overstating assets and concealing the extent of self-dealing with related companies. The counterclaims at issue were based on the Georgia RICO statute and breach of fiduciary duty.

The court held that summary judgment was warranted in favor of the plaintiff on the defendant's Georgia RICO counterclaim because the defendant had come forward with no evidence of fraudulent intent, an essential element of the alleged predicate acts (securities fraud, mail fraud and theft by deception). The defendant's main argument in this regard was that it had not yet taken the plaintiff's deposition and therefore had not had the opportunity to examine his intent. The trial court found this unavailing, noting that the defendant had had ample time to conduct discovery, had not yet noticed the deposition, and did not ask for a continuance to take additional discovery under O.C.G.A. § 9-11-56(f).

Turning to the breach of fiduciary duty counterclaim, the court noted that the parties negotiated at arms' length, but since the defendant was already a shareholder, the plaintiff (as a director of the selling company) was under a common law obligation to make a full disclosure of material facts, to the extent the sources of information were not equally accessible to both parties. The court concluded that there was no genuine factual dispute as to whether a fiduciary duty had been breached, given that the defendant had undertaken substantial due diligence, so much so that it had even greater access to information about the company than the plaintiff had during the same time. There was also no evidence that the plaintiff had made any affirmative representation or undertaken to conceal any fact during due diligence.

Miller v. Lynch

No. 2015-cv-256817 (Ga. Super. July 27, 2016) (Order on Defendants' Motion for Summary Judgment)

In this summary judgment order, the business court evaluated choice of law questions pertaining to tort claims involving the duties and liabilities of a member of a Delaware LLC headquartered in Georgia. The court found that the plaintiff's claims, which included breach of fiduciary duty, aiding and abetting a breach of fiduciary duty, breach of the covenant of good faith and fair dealing, and a separate count for "oppression", all had to be evaluated under Delaware law. The defendants' statute of limitations defense, however, was evaluated under Georgia law.

The plaintiff was a former minority member and officer of FiberLight, LLC, which was formed under Delaware law in 2005 and had its principal place of business in Georgia. He sued the LLC and its majority members, claiming that they restructured the LLC's operating agreements over a period of several years in a manner that reduced his interest and was oppressive to him. The LLC eventually terminated him and attempted to redeem his interest, prompting the filing of this suit. The plaintiff alleged that his injuries occurred entirely in Georgia. The court found that this did not affect its choice of law analysis. It applied the settled rule, which is codified for LLCs at O.C.G.A. § 14-11-701, that the laws of the jurisdiction in which the entity is organized govern the entity's organization and internal affairs and the liabilities of its managers, members and other owners. Since this was a dispute regarding the internal affairs of FiberLight and the liabilities of its members, the court was required to apply Delaware law. In addition, FiberLight's operating agreements, which played a significant role in the dispute, specifically designated Delaware law as controlling.

Evaluating the substance of the plaintiff's tort claims under Delaware law, the court found that there was no evidence of a breach of fiduciary duty. In the court's view, the majority members did owe fiduciary duties to the defendant given their substantial power to control the LLC's affairs—they possessed the power to control a majority of the votes of the LLC's board and held a 98% interest, among other things—but the acts complained of were consented to by the plaintiff, and there was no evidence that the plaintiff was coerced into agreeing to them under Delaware's economic duress doctrine. Delaware law requires three elements for a finding of economic duress: (1) a wrongful act which (2) overcomes the free will of the person (3) who has no adequate legal remedy to protect his interests. The court found that these elements were not present here, citing the fact that the plaintiff was a sophisticated business man who consulted with legal counsel in connection with the amendments to the operating agreements that he now complained of as wrongful, and reviewed and understood these amendments. The court also reviewed Delaware law regarding oppression and expressed skepticism that Delaware would recognize a cause of action for oppression under the circumstances, but held that this did not matter because the alleged oppressive acts were all expressly permitted under the amended operating agreements in effect at the time.

Finally, the court also held that Georgia law, not Delaware law, would govern any limitations defense. The court explained that statutes of limitations are procedural in nature since they look only to the remedy, and noted that there was no Georgia statutory directive to apply the

statutory bar of a foreign state when that state's law governs the substance of the dispute. Here, the Georgia statute of limitations provided an additional reason to dispose of certain of the plaintiff's claims which were based on amendments to the operating agreements that became effective in 2006. In Georgia, any claim that a contract is voidable due to duress in executing it is subject to a seven-year statute of limitations, and breach of fiduciary duty claims arising from a written contract are subject to a six-year statute. The court rejected the plaintiff's argument that the statutes did not begin to accrue until a later time, finding that the weight of Georgia law holds that a cause of action for breach of fiduciary duty arising from a written contract begins to accrue upon execution of the document.

Fang v. HEI Investments, LLC

No. 2015-cv-261534 (Nov. 28, 2016) (Order Denying Plaintiffs' Motion for Partial Summary Judgment)

In this case, the business court addressed some interrelated questions arising from the plaintiff's assertion of both contract-based claims and tort claims that were premised on the absence of any contract. The main dispute was between a group of investors in a failed hotel construction project and the project's developers. The developers solicited nearly $2 million in investments from the plaintiffs. In connection with the investment, the plaintiffs alleged that they executed subscription agreements; however, some of these agreements were never signed by the entity created to build the hotel. The subscription agreements indicated that the plaintiffs' investments were made in accordance with the terms of a private placement memorandum. The PPM was not signed by any party. The plaintiffs alleged that under the terms of the subscription agreements and PPM, they were entitled to a full refund of their investment if less than all of the available investment units were sold by a certain date. They further alleged that the project never came to fruition and the money was never refunded—instead, it was transferred to another prospective investor. The plaintiffs' complaint asserted 20 separate counts. One of the counts was for breach of the subscription agreements and PPM. Other claims, including fraud and breach of fiduciary duty, sounded in tort. Some of the plaintiffs' counts, including unjust enrichment, could only have arisen in the absence of a contract.

The developer defendants were insured parties under a management liability insurance policy issued by Hanover Insurance Company. These defendants sought coverage for the plaintiffs' claims under the policy. Hanover denied coverage, citing (among other things) an exclusion for "'Loss' on account of any 'Claim' made against any 'Insured' directly or indirectly based upon, arising out of, or attributable to any actual or alleged liability under a written or oral contract or agreement.'" The developers filed a third party complaint against Hanover, alleging that the exclusion for contract-based claims did not apply because of an exception to the exclusion stating that it did not apply "to your liability that would have attached in the absence of such contract or agreement." The developers pointed out the presence of claims that can only be brought in the absence of a contract, and argued that these claims had to fall within the exception to the exclusion. Ruling on cross-motions for summary judgment, the court rejected the third party plaintiffs' position and agreed with Hanover's. The court reasoned that the legal theories asserted by the plaintiffs in the underlying action were not controlling. Instead, the court had to evaluate the underlying facts in determining whether the exclusion applied. Since all of the plaintiffs' causes of action related to the same allegations that plaintiffs entered into agreements

that were memorialized by the subscription agreements and PPM, it could not be said that "no liability would attach" in the absence of the agreements. The developers also argued, to no avail, that the plaintiffs' breach of fiduciary duty claim could have arisen by operation of O.C.G.A. § 23-2-58 regardless of whether a contract existed. The court noted that the developers could not identify any alternative source of a confidential relationship between the parties to the main action, and it appeared that there was no allegation that did not relate directly or indirectly to the subscription agreements.

The developers, attempting to seize on the court's finding that there was no alternative source of a confidential relationship, then moved for judgment on the pleadings in the main action, arguing that the court's ruling on coverage issues effectively meant that the investors had no viable tort claim. It is settled law in Georgia that a plaintiff in a breach of contract case can only assert a tort claim if, in addition to breaching the contract, the defendant also breached an independent legal duty. The court nonetheless found the developers' attempt to connect this principle to its earlier ruling on coverage issues to be unavailing. The court reasoned that Hanover's contract exclusion operated to bar coverage of all claims, regardless of whether they would otherwise be barred, directly *or indirectly* arising from the alleged contractual relationship, and that a tort claim could be indirectly related to the subscription agreements and yet be based on a duty arising independently from the contract at issue.

Three months later, the court denied a motion for summary judgment by the investors, finding that there were unresolved issues of fact regarding the existence of a contract. The court suggested in a footnote that the investors' assertion of causes of action that can only be asserted in the absence of a contract, and the position taken by the parties in the earlier proceedings, contributed to the uncertainty regarding whether an enforceable contract existed.