

MA SJC Rules on Merger-Related Fiduciary Duties

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Many operating businesses in Massachusetts are set up as limited liability companies rather than corporations. Limited liability companies can engage in many of the same activities as corporations, including participating in M&A transactions as both buyers and sellers. The rights of members in LLC's engaging in such transaction are set forth in M.G.L. c. 156C, the Massachusetts Limited Liability Company Act (the "Act"). Generally, a member in a Massachusetts limited liability company who dissents from a merger has limited rights under Section 60 (b) of the Act, to resign and receive the distributions owed in respect of the member's interest ("The exclusive remedy of a member of a domestic limited liability company, which has voted to consolidate or to merge with another entity under the provisions of [the Act], who objects to such consolidation or merger, shall be the right to resign as a member and to receive any distribution with respect to his limited liability company interest, as provided in sections thirty-one to thirty-seven, inclusive.")

However, in a recent decision, the Massachusetts Supreme Judicial Court ruled that claims of a minority member in a limited liability company that engaged in a freeze-out merger were not so limited, because the merger violated the fiduciary and contractual duties owed to the dissenting member. A freeze-out merger is a transaction that is structured so as to severely dilute or eliminate minority owners. In Allison v. Eriksson (SJC-12391 May 30, 2018), the SJC ruled that the plaintiff (Allison) was not limited to the remedies provided for in the Act, because the merger was not consummated "under the provisions of the Act." The Court held that because of the breach of duties owed to Allison, the defendants would not be entitled to the protections set forth in the Act limiting potential damages, even though the merger was conducted in technical compliance with the statute. The Court found that the structure of the merger violated many of the provisions of the company's operating agreement that provided protections to the members, thus breaching the fiduciary duties owed to Allison. The SJC relied heavily on prior rulings involving corporations and the rights of minority owners in crafting its decision.

This is the first time that the SJC has ruled on this provision of the Act, and they are sending a clear message that minority rights must be respected and complied with where a freeze-out merger is involved, even if the merger is conducted in technical compliance with the Act.

Managers and controlling members of LLCs must look to both the operating agreement for the LLC

and the statute to confirm that all required fiduciary duties have been satisfied. LLC operating agreements can greatly expand or contract those fiduciary duties, and decision-makers should be sure that they have satisfied all necessary obligations before proceeding with a merger transaction.

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