The State Bar of Georgia

BUSINESS LAW SECTION

Newsletter

Thomas R. McNeil, Chair **June 2009** **Sterling A. Spainhour, Jr., Editor**

REPORT FROM CHAIR OF BUSINESS LAW SECTION

By: Thomas R. McNeil
Bryan Cave Powell Goldenstein

Dear Business Law Section Members:

As I prepare to turn over my role as Chairman of the Section, I thought it was appropriate to report to you on our activities. I also want to enlist your support to assist our committees in the work they do assisting our members with their practices and improving the laws of our state to enhance the business climate in Georgia.

2008-2009 continued the tradition of being a very busy year for our Section and our Committees. The highlights can be summarized as follows:

Legal Education:

During the past year, our Section sponsored seven CLE programs as follows:

1. Business Law Institute, October 16-17, 2008;
2. Securities Litigation and Regulatory Practice, October 31, 2008;
3. Negotiated Corporate Acquisitions, January 8, 2009;
4. Secured Lending, Statewide Satellite Broadcast, February 6 and 12, 2009;
5. Banking Law, February 11, 2009;
6. Advanced Securities Law, March 27, 2009; and
7. LLC's and LLP's, April 10, 2009.

In particular, the Business Law Institute is the preeminent opportunity for business lawyers in the State to learn the latest business law structures and developments, as well as to spend time with each other in an effort to grow our respective practices. Programs sponsored by our Section receive very high marks from attendees and are well attended.

Committee Activities:

Our Section has historically been among the most active proponents of legislation to advance the business climate in Georgia. With respect to the 2009 legislative session, our Partnership and LLC Committee conducted the first comprehensive review of the Georgia LLC Act since it became effective in 1994. That review resulted in a package of proposed changes in legislation which the Section submitted to the State Bar in October 2008. Updating the Georgia LLC Act has taken on increased importance now that LLC formations outnumber, by a ratio of more than two to one, corporate formations in Georgia.

Our proposed legislation received approval from the State Bar and was introduced into the 2009 legislative session. Our Partnership and LLC Committee, led by Andy Immerman of the Alston & Bird firm, testified three times before legislative committees. The bill passed both the House and Senate and, as of this writing, is awaiting the Governor's signature.

The Partnership and LLC Committee has also undertaken a review of the Georgia Limited Partnership Act, which we expect will also result in proposed legislation in the future. The Partnership and LLC Committee also participated in co-sponsoring the Southeast Business Tax Forum in 2009.

The Corporate Code Revision Committee did not introduce legislation this year, instead choosing to undertake a two-year comprehensive review of the Georgia Business Corporation Act. The commencement of this process marks the 20th anniversary since there has been a comprehensive review of the Corporate Code. The Corporate Code Revision Committee, led by Bruce Wannamaker, has created subcommittees responsible for evaluating and recommending any changes to the Corporate Code.

The revision project will be assisted by Professor George Shepherd of the Emory Law School. Professor Shepherd will provide his significant expertise and support as the Committee undertakes a serious evaluation of our Corporate Code and the important balancing of the rights and responsibilities of shareholders, directors, the entity and other constituencies.

Our Section's Business Litigation Committee has created and staffed a series of monthly litigation seminars for the Fulton County Superior Business Court and other Fulton Superior Court judges who are interested in business litigation issues. This is the third year that our Section has orchestrated and operated these seminars for the judges. This year's schedule included programs on Georgia business law developments, forensic accounting, minority squeeze-outs, mergers and acquisitions, attorneys' perspective on settlement, ethics, shareholder derivative suits, injunctions and TROs and trade secret litigation. Beth Tanis of King & Spalding has provided strong leadership to the Business Litigation Committee throughout these efforts.

Our UCC Committee held its annual Secured Lending Seminar which was broadcast from Georgia Public Television and simulcast throughout the state. Topics included workouts and recent trends in our industry as a result of the current economic crisis. Angela Batterson ably led the UCC Committee this year.

Our Securities Committee sponsored its Advanced Securities Law Seminar which had both exemplary speakers and attendance of more than 110 people. A highlight was a panel of experts from the SEC. The Securities Committee, led by Bob Hussle, has also formed a subcommittee to consider proposed regulations which may be issued by the Georgia Securities Commissioner under the new Georgia Securities Act.

The Section continues to be financially stable and we look forward to assisting our membership in assisting their clients in weathering the current economic crisis.

Effective July 1, the membership of our Executive Committee will be as follows:

BUSINESS LAW SECTION
EXECUTIVE COMMITTEE 2009-2010

Officer/Committee	Individual/Chair	Firm	Email Address
Chair	Ed Snow	Burr & Forman	esnow@burr.com
Vice Chair	Elizabeth Noe	Paul Hastings	elizabethnoe@paulhastings.com
Secretary	Bruce Wanamaker	Ledbetter Johnson Wanamaker Glass LLP	bwanamaker@ljwglaw.com
Immediate Past Chair	Tom McNeill	Bryan Cave Powell Goldstein	tom.mcneill@bryancave.com
Past Chair	Walter Jospin	Paul Hastings	walterjospin@paulhastings.com
Corporate Code Committee	Bruce Wanamaker	Ledbetter Johnson Wanamaker Glass LLP	bwanamaker@ljwglaw.com
Opinion Committee	Andre Hylton	Georgia Pacific	aphylton@gapac.com

Officer/Committee	Individual/Chair	Firm	Email Address
Partnership/LLC Committee	Lee Lyman	Thompson Hine	Lee.lyman@thompsonhine.com
Publications Committee	Sterling Spainhour	Jones Day	sspainhour@jonesday.com
Securities Committee	Robert Hussle	Rogers & Hardin	rhussle@rh-law.com
UCC Committee	Angie Batterson	King & Spalding	abatterson@kslaw.com
Business Litigation Committee	Beth Tanis	King & Spalding	btanis@kslaw.com

Most importantly, our Committees always need and welcome additional help from members of our Section. Committee work is a great way to meet other lawyers who regularly practice in the same area. In addition, much of our Committee work is focused on considering recent developments in law and, as appropriate, crafting legislative solutions or responses to those developments. Working together with colleagues is a great way to develop a deeper understanding of the law in our area and to keep up with trends. I encourage you to seriously consider participating in one or more of our Committee activities.

To join a Committee, contact the appropriate Committee Chair listed above. If you have any questions about participation, please don't hesitate to contact any of the Committee Chairs or other officers. It is a great way to round out both your legal education and your network of colleagues in the Georgia business law community.

Finally, I congratulate Ed Snow of Burr & Foreman on beginning his term as Chairman of the Section. Ed has worked tirelessly in support of many of our initiatives and I know he will do a great job in moving the Section forward.

Very truly yours,

/s/ Thomas R. McNeil

2008 GEORGIA CORPORATION AND BUSINESS ORGANIZATION CASE LAW DEVELOPMENTS

By: Thomas S. Richey
Bryan Cave Powell Goldstein

I. INTRODUCTION AND OVERVIEW

INTRODUCTION

This paper surveys case law developments dealing with corporate and business organization law issues, that were handed down by the Georgia state and federal courts during 2008. Only a few of the decisions concern important matters of first impression. Some illustrate and confirm settled points of law. Others are instructive for the types of claims and defenses that are asserted in business organization transactions, internal disputes and governance and how the courts are addressing them. Due to space limitations in the newsletter, a more extensive discussion of several decisions related to litigation issues is not included herein, however, the full article can be found at http://www.bryancave.com/2008-GA-Survey or by contacting me via e-mail (tom.richey@bryancave.com).

In general, the survey is organized first by entity type – corporations, limited liability companies, partnerships and joint ventures. The survey then covers areas in which the decisions concern transactional issues that apply to all forms of business organizations, decide litigation issues characteristic of business organization litigation or involve professional liability claims in the business context.

OVERVIEW

A. Corporations.

Two decisions in 2008 dealt with shareholder agreements. Neither decision, however, addressed the Georgia Business Corporation Code provisions concerning shareholders agreements, O.C.G.A. § 14-2-732. The Georgia Court of Appeals in Levy v. Reiner, 290 Ga. App. 471, 659 S.E.2d 848 (2008) held it axiomatic that a corporation must be a party to a shareholders contract in order to be bound by it, a statement that would not be true for a shareholders agreement meeting the requirements of § 14-2-732. In other rulings, Levy held that the plaintiff could not pursue direct claims for breach of fiduciary duty based on the close corporation exception to derivative actions under Thomas v. Dickson, 250 Ga. 772, 301 S.E.2d 49 (1983) because not all shareholders were parties or adequately represented. The plaintiff could not sue derivatively, either, because his breach of fiduciary duty claims related to the value of his stock, he had dissented from a sale of the corporation's assets and was pursuing an appraisal remedy, and that remedy was exclusive. The Court of Appeals in Simpson v. Pendergast, 290 Ga. App. 293, 659 S.E.2d 716 (2008) addressed a mirror image buy-sell agreement under which one shareholder specifies the terms and the others must elect whether to buy or sell. The Court held a shareholder liable who refused to respond to such an offer because he considered that certain of the specified terms violated the agreement, but the Court reversed summary judgment for specific performance because the proposed terms would affect the corporation and might not be fair.

Planning Technologies, Inc. v. Korman, 290 Ga. App. 715, 660 S.E.2d 39 (2008) dealt with judicial review of corporate decisions entrusted to the discretion of the board of directors in the context of a determination of stock option vesting. The Court held that where the language does not clearly grant the board unbridled discretion, its decision is subject to review for whether it was made in good faith and in the exercise of honest judgment.

In Hilb, Rogal & Hamilton Co. of Atlanta, Inc. v. Holley, 295 Ga. App. 54, 670 S.E.2d 874 (2008), in a restrictive covenant context, the Court of Appeals held that a corporate employee who has authority to bind the corporation owes fiduciary duties to the corporation and can thus be held liable for diverting business from it while still employed.

The Georgia Court of Appeals decided three nonprofit corporation cases in 2008: (1) Madonna v. Satilla Health Services, Inc., 290 Ga. App. 148, 658 S.E.2d 858 (2008), in which a hospital's bylaws concerning physicians' practice privileges took precedence over a conflicting contract granting exclusive practice rights to a single physician group; (2) The Phoenix of Peachtree Condominium Association Inc. v. Phoenix on Peachtree LLC, 294 Ga. App. 447, 669 S.E.2d 229 (2008), in which the Court held a condominium association that filed suit in violation of a provision of its declaration barring suits on behalf of members, lacked standing to sue despite a later curative amendment to its bylaws and declaration; and (3) Parkridge Condominium Association, Inc. v. Callais, 290 Ga. App. 875, 660 S.E.2d 736 (2008), in which the Court ruled that the trial court's findings of a member's proper purpose and the association's absence of good faith must be upheld unless clearly erroneous, but reversed on the amount of attorney's fees awarded, holding that O.C.G.A. § 14-3-1604(c) requires a corporation to pay only the fees "incurred to obtain the order" for inspection and copying of records.

B. Limited Liability Companies.

The Georgia Court of Appeals handed down five decisions in 2008 concerning the rights and duties of limited liability companies, their managers and members to each other. In Old National Villages, LLC, v. Lenox Pines, LLC, 290 Ga. App. 517, 659 S.E.2d 891 (2008), the Georgia Court of Appeals, in a situation rife with conflicts of interest, held that an LLC general manager, authorized by the operating agreement to make all decisions on the LLC's behalf, can consent to a judgment against the LLC without notice to or approval from the sole member of the LLC. By contrast, in Internal Medicine Alliance, LLC v. Budell, 290 Ga. App. 231, 659 S.E.2d 668 (2008), the Court of Appeals found that an LLC's managing member owed duties of "utmost good faith and loyalty" to the other member and violated her duty of care and acted in bad faith when she failed to collect his receivables. That standard of conduct applies in the absence of a modification permitted under O.C.G.A. § 14-11-305(4)(A). ULQ, LLC v. Meder, 293 Ga. App. 176, 666 S.E.2d 713 (2008), applied the requirement of good faith in the exercise of discretionary authority to an LLC's decision to remove an officer and require the repurchase of his membership interest. The Court also held that the LLC could not be held liable for its manager's breach of fiduciary duty and that non-managing members do not owe a fiduciary duty to either the LLC or to other members. In Fielbon Development Co. v. Colony Bank of Houston County, 290 Ga. App. 847, 660 S.E.2d 801 (2008), the Court of Appeals interpreted the language of O.C.G.A. § 14-11-301(c), that a limited liability company is not liable for acts of a member that are "not apparently for the carrying on in the usual way the business or affairs" and held that the LLC was liable for the notes signed by one of its managers, notwithstanding his misappropriation of some of the loan proceeds. Gardnerv. Marcum, 292 Ga. App. 369, 665 S.E.2d 336 (2008) dealt with a dispute over an investment in a recording project that was paid to an LLC, where the parties disagreed on

whether an investment was a loan or an equity investment and where no rate of interest had been agreed on. The Court of Appeals held that there was no meeting of the minds, that the LLC was required to return the funds, but that, under O.C.G.A. § 14- 11-3303(a), the individual LLC members were not liable for the LLC's obligations, solely by reason of being members.

In Georgia Rehabilitation Center, Inc. v. Newnan Hospital, 283 Ga. 335, 658 S.E.2d 737 (2008), the Georgia Supreme Court refused to compel arbitration of an independent claim for judicial dissolution under O.C.G.A. § 14-11-603, where the operating agreement required arbitration of claims related to the operating agreement or its breach and provided limited rights to dissolve the company under conditions inapplicable to the circumstances at hand. The Court also affirmed the appointment of a receiver.

IH Riverdale, LLC v. McChesney Capital Partners, LLC, 292 Ga. App. 841, 666 S.E.2d 8 (2008) upheld the validity of an amendment to an operating agreement, adopted by majority vote, that abolished payment of a special fee to the plaintiff. The Court rejected the plaintiff's argument that the amendment was a major decision requiring unanimous consent.

C. Partnerships. No partnership decisions of note came to our attention during 2008.

D. Joint Ventures.

In American Association of Cab Companies, Inc. v. Parham, 291 Ga. App. 33, 661 S.E.2d 161 (2008), in a personal injury case involving an uninsured cab, the Georgia Court of Appeals, *en banc*, held there to be sufficient evidence of joint control over the cab to constitute a joint venture. A defense verdict on RICO claims was reversed for improper instructions on burden of proof. Defendants' arguments on proximate cause under RICO were rejected, the Court finding a causal nexus between the lack of insurance and the plaintiff's ability to collect on his personal injury claim.

E. Business Law Issues.

Georgia courts decided four cases involving asset sales, each illustrating a different issue likely to arise in that setting and each resolved on the basis of the provisions of the asset purchase agreement or related agreements and/or who was party to the agreements. Wilkie v. 36747, LLC, 294 Ga. App. 179, 669 S.E.2d 155 (2008) enforced provisions of an Asset Purchase Agreement specifying what obligations the purchaser had assumed; Ahmed v. CUA Autofinder, LLC, 387 B.R. 906 (Bkrtcy. M.D. Ga. 2008) dealt with entitlement to escrowed funds, where the purchaser's principal made a payment required from the company, but failed to document the contribution and where the company went into bankruptcy and the trustee claimed the funds; Kilroy v. Alpharetta Fitness, Inc., 2008 WL 5049966 (Ga. App. Dec. 1, 2008) found fraud claims viable where there was evidence of breaches of representation and warranties in the asset purchase agreement; Accurate Printers, Inc. v. Stark, 2008 WL 5049960 (Ga. App., Nov. 26, 2008) enforced an anti-assignment clause where an individual had purchased the assets and his corporation attempted to enforce the asset purchase agreement's non-competition provision.

Deljoo v. Suntrust Mortgage, Inc., 2008 WL 5174307 (Ga. App. Dec. 11, 2008) applied a rarely cited provision outside the Georgia Business Corporation Code, O.C.G.A. § 14-5-7, regarding the validity of corporate conveyances of real estate.

In Dudley v. Wachovia Bank, 290 Ga. App. 220, 659 S.E.2d 658 (2008), the Court of Appeals addressed disputed stock transfers with signature guarantees under Article 8 of the Uniform Commercial Code, deciding, in a matter of first impression in Georgia, that a signature guarantor is not liable to a stock owner under O.C.G.A. § 11-8-306, but enforcing the issuers' strict liability under § 11-8- 404.

F. Litigation Issues.

White v. Shamrock Building Systems, Inc., 294 Ga. App. 340, 669 S.E.2d 168 (2008) rejected a contractor's claims of aiding and abetting breaches of fiduciary duty, conspiracy and tortious interference with business relations as to a diverted business opportunity, based in part on allegations that the alleged third party aider and abettor "should have known" or failed to "investigate" the relationship between the contractor and his former employee before dealing with him.

In Peery v. CSB Behavioral Health Systems, 2008 WL 4425364 (S.D. Ga. Sept. 30, 2008), the Court held that the applicable statute of limitations for breach of fiduciary duty claims is determined by the nature of the conduct underlying alleged fiduciary breach.

In Fulp v. Holt, 284 Ga. 751, 670 S.E.2d 785 (2008) and Treu v. Humanism Investment, Inc., 284 Ga. 657, 670 S.E.2d 409 (2008) the Georgia Supreme Court upheld the trial court's discretion in deciding whether to appoint a receiver, affirming in Fulp the appointment of a receiver for a dissolved law firm and in Treu, the denial of a receivership where a court-appointed auditor had adequately sorted out the shareholders' interests in an investment corporation. Sampson v. Haywire Ventures, Inc., 293 Ga. App. 779, 668 S.E.2d 286 (2008) addressed the requirements for an accounting, holding that the plaintiff must be likely to obtain some recovery to warrant some recovery.

In Hampton Island Founders, LLC v. Liberty Capital, LLC, 283 Ga. 289, 658 S.E.2d 619 (2008), the Georgia Supreme Court reversed a temporary injunction prohibiting any effort to contest the voting rights of investors attempting to seize control of an LLC, oust its management and dismiss a lawsuit against a joint venture partner. The purpose of a temporary injunction should be to preserve the status quo, not to change it. The Court also held that the trial court erred in permitting the investors to intervene in the litigation, since their purpose in doing so was not to participate, but rather to dismiss the litigation.

The Georgia Court of Appeals in Stephens v. McGarrity, 290 Ga. App. 755, 660 S.E.2d 770 (2008), reversed the trial court's approval of a derivative action settlement under O.C.G.A. § 14-2-745 providing that most of the settlement funds would be paid out to the individual derivative plaintiff with the balance to be paid to senior management as bonuses. The Court found that despite the arms' length character of the negotiations, given the danger of collusion, the settlement was not entitled to a presumption of fairness and a review of its terms showed that the settlement was not in the corporation's best interest.

Three decisions addressed alter ego liability or piercing the corporate veil. In Pazur v. Belcher, 290 Ga. App. 703, 659 S.E.2d 804 (2008), the Georgia Court of Appeals held that sole ownership of a corporation, using a corporation for one's own ends, loans to or from the corporation or the forgiveness of such loans do not, without more, support piercing the corporate veil; it requires a disregard of the corporate entity, making it a mere instrumentality for transaction of personal affairs, and such a unity of interest and ownership that separateness of entity and owners ceases to exist. In an unpublished Eleventh Circuit Court of Appeals decision, BP Products North America, Inc. v. Southeast Energy Group, Inc., 282 Fed. Appx. 776 (11th Cir. 2008), the Court reversed a summary judgment piercing the corporate veil, because despite a disregard of the corporate form, there was an issue of fact whether the corporation had been used to defeat justice, perpetrate a fraud or evade liability. Bruce v. PharmaCentra, LLC, 2008 WL 1902090 (N.D. Ga. April 25, 2008) held that a plaintiff's alter-ego allegations as to an affiliate of her employer estopped her from claiming that she was not required to arbitrate her claims against both entities.

In Barnette v. Coastal Hematology & Oncology, P.C., 294 Ga. App. 733, 670 S.E.2d 217 (2008), the Court of Appeals ruled on malicious prosecution claims arising from the prosecution of personnel accused of misappropriating company funds, holding that a presumption of probable cause based on police officers' affidavits averring independent judgment in recommending prosecution does not apply where the complainant knowingly makes false statements to the arresting officer, as the plaintiffs had alleged.

In two decisions, In re Sutton, 2008 WL 4527761 (Bankr. M.D. Ga. Oct. 2, 2008), a corporate officer and in In re Wheelus, 2008 WL 372470 (Bankr. M.D. Ga. Feb. 11, 2008) two former managers of an LLC were found not to be "fiduciaries" within the meaning of 11 U.S.C. § 523(a)(4) and thus the claims against them for breach of fiduciary duty could not be determined to be non-dischargeable.

Three of 2008's decisions concerned service of process on corporations. Vibratech, Inc. v. Frost, 291 Ga. App. 133, 661 S.E.2d 185 (2008) held that, unlike the resignation of a corporate officer or director, the resignation of an agent for service of process is not effective until filed with the Secretary of State. In Brock Built City Neighborhoods, LLC v. Century Fire Protection, LLC, 2008 WL 4740396 (Ga. App. Oct. 30, 2008), the Court held that service by publication on an LLC is not authorized until after the plaintiff has attempted service directly on the company. Holmes & Company of Orlando v. Carlisle, 289 Ga. App. 619, 658 S.E.2d 185 (2008) upheld service on a bank branch manager who was supervisor of a corporation's registered agent, even though the corporation did not conduct any business at the bank and neither the bank nor the branch manager was authorized to accept service on the corporation's behalf.

QOS Network Ltd. v. Warburg Pincus & Co., 294 Ga. App. 528, 669 S.E.2d 536 (2008) involves a lengthy analysis and application of the principles of *res judicata* and collateral estoppel as to a corporation based on the results of litigation against its controlling shareholders and officers.

G. Professional Liability.

The Georgia Court of Appeals decided two merger and acquisition accountant liability cases in 2008. In Atlanto Holdings, LLC v. BDO Seidman, LLP, 290 Ga. App. 665, 660 S.E.2d 463 (2008), a 15-year old dispute, it reversed an award of damages because the trial court erred in admitting evidence of a resale of the business many years after the disputed acquisition and a reclassification of acquisition debt as equity. In a nursing home company acquisition case, PricewaterhouseCoopers, LLP v. Bassett, 293 Ga. App. 274, 666 S.E.2d 721 (2008), the Court upheld a negligent misrepresentation jury verdict, ruling on issues of reasonable reliance and due diligence by the trustee of children's trusts into which stock obtained in the acquisition was transferred.

Saye v. Deloitte & Touche, LLP, 295 Ga. App. 128, 670 S.E.2d 818 (2008) is a defamation case illustrating the risk an auditor takes in reporting to an audit client adverse information concerning one of the client's employees and refusing to give its opinion on the financial statements if the employee remained in an accounting or financial reporting role. The Court of Appeals held that, given the auditor's independence, its reporting the information to its client constituted a publication and auditor's privilege to report such information is a qualified one, hence allegations of malice sufficed to survive a motion to dismiss.

In Smith v. Morris, Manning & Martin, LLP, 293 Ga. App. 153, 666 S.E.2d 683 (2008), the Court of Appeals held that written waivers that a law firm obtained from two clients, although valid with regard to the matters identified, were ineffective to protect it from claims when its representation of one client in dealings with the other exceeded the scope of the waivers.

In re Friedman's Inc., 385 B.R. 381 (S.D. Ga. 2008), *vacated in part on reconsideration by* In re Friedman's Inc., 394 B.R. 623 (S.D. Ga. 2008) is a lengthy decision on motions to dismiss a bankruptcy trustee's action against officers, directors, investment bankers and outside counsel who represented the company and a committee of independent directors. Among other rulings, the Court held that piercing the corporate veil requires insolvency under Georgia law, that Georgia law recognizes claims for aiding and abetting fraud, and that claims for legal malpractice can be based on the alleged failure of counsel to disclose adverse information to independent directors regarding interested party transactions.

II. DISCUSSION OF CASE LAW DEVELOPMENTS

A. Corporations.

Shareholders' Agreements, Direct vs. Derivative Actions and Exclusivity of Dissenters' Rights.

In Levy v. Reiner, 290 Ga. App. 471, 659 S.E.2d 848 (2008), the Georgia Court of Appeals held that a corporation, as a separate entity, must be named a party to a contract in order to bind it to obligations that the shareholders agree to impose on it. The Court also rejected the plaintiff's efforts to pursue a direct claim for breach of fiduciary duty based on the defendants' allegedly excessive salaries, holding that the plaintiff had not satisfied the requirements under Thomas v. Dickson, 250 Ga. 772, 301 S.E.2d 49 (1983) for the close corporation exception to derivative actions. The plaintiff was unable to pursue a derivative action, as well, because his breach of fiduciary duty claims related to the value of his stock, he had dissented from a sale of the corporation's assets, he was pursuing an appraisal remedy, and that remedy was exclusive.

Michael Levy, a minority shareholder of Peek-A-Boo, Inc. ("PAB"), sued Michael Reiner and Howard Alpern individually and in their capacity as PAB directors and officers, claiming breach of contract and breach of fiduciary duty. Levy and Alpern had entered into a stock purchase agreement that provided that PAB would offer consulting opportunities to Levy equal to those provided to Alpern. Levy alleged that Alpern breached this contract when PAB did not provide Levy with PAB opportunities equivalent to what Alpern himself received. The Court of Appeals rejected that claim, stating that it was "axiomatic" that the corporation, as a separate entity from its stockholders, must be a party to the contract in order for the contract to be valid and binding as to it. Because PAB was not a party to the contract between Levy and Alpern that provision of the agreement was not enforceable. While the Court treated the principles as self-evident, the only authority it cited was Plaza Properties, Ltd. v. Prime Business Investments, 240 Ga. App. 639, 642(2)(d), 524 S.E.2d 306 (1999), which involved a contract with a third party, not a shareholders' agreement. The Court did not mention O.C.G.A. § 14-2-732, which provides:

> "(a) An agreement among the shareholders of a corporation that complies with this Code section is effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Code in that it:

> (5) Establishes the terms and conditions of any agreement for the transfer or use of property or the provision of services between the corporation and any shareholder, director, officer, or employee of the corporation or among any of them
>
> (8) Otherwise governs the exercise of the corporate powers or the management of the business and affairs of the corporation or the relationship among the shareholders, the directors, and the corporation, or among any of them, and is not contrary to public policy."

(Emphasis added) By its terms, Section 14-2-732 appears to render a shareholders' agreement binding on the corporation even if it is not a party. For a shareholders' agreement to qualify under § 14-2-732, among other things, it either must be contained in the corporation's articles or bylaws and be approved by all shareholders or must be in writing, signed by all shareholders, and must be "made known" to the corporation. O.C.G.A. § 14-2-732(b)(1). It appears that only Levy and Alpern were parties to the shareholders' agreement, in which case § 14-2-732 would not apply.

Levy also alleged that Reiner and Alpern breached their fiduciary duty as officers of PAB based on their excessive salaries. Invoking the Georgia exception to the requirement that claims based on breaches of duty to the corporation must be brought derivatively, Levy contended that he could bring a direct action against them instead of a derivative suit, because PAB was a closely-held corporation. Not all shareholders were parties. Levy argued that there was no danger of a multiplicity of proceedings, asserting that the non-party shareholders would not litigate because they benefitted from Reiner's and Alpern's actions. The Court of Appeals found that the record did not support Levy's argument.

Finally, the Court of Appeals held that Levy could not maintain a derivative action against Reiner and Alpern, either, since Levy tendered his shares to the corporation and dissented from the sale of PAB's assets. The Court found that his claims related to the value of his stock and held that the appraisal proceeding that he was separately pursuing provided his exclusive remedy.

Shareholder Buy-Sell Agreement – Specific Performance Requires Contract to Be Fair, Just and Not Against Good Conscience, Including Interests of Corporation.

Simpson v. Pendergast, 290 Ga. App. 293, 659 S.E.2d 716 (2008) illustrates the dilemma facing a shareholder who receives an offer containing unacceptable terms under a shareholders' agreement that requires the offerees to elect whether to buy or sell at the stated price and on the stated terms. The shareholder agreement in question required the offering shareholder to specify the price and set forth the terms and conditions on which he was prepared to purchase or sell shares. The offerees were then required to make their election within 60 days and, if they failed to respond, they were deemed to have elected to sell at the stated price and on the stated terms and conditions.

Joseph Pendergast, one of four shareholders in Historic Motorsports Holdings, Ltd. ("HMH") made an offer to the other three shareholders to buy or sell, naming a specific price, but adding three conditions: (a) that the corporation was required to make a pro rata distribution of 40% of its taxable income for the preceding and current year, (b) that the selling shareholder would be relieved of non- competition obligations, and (c) that the offer was based on a review of the June 30, 2004 financial statements and that there shall have been no adverse change in the company's financial condition, results of operations or assets through closing. Steve Simpson, one of the three offerees, took the position that Pendergast's offer was invalid because of the added terms and conditions and failed to respond. Pendergast brought an action against Simpson for specific performance. In analyzing the terms of the shareholder agreement, the Court of Appeals found the language of the agreement unambiguous, held that it clearly contemplated that the offeror would specify terms and conditions, and found nothing in the agreement to support Simpson's position that inclusion of Pendergast's terms relieved him of his obligation to respond. It affirmed the grant of summary judgment to Pendergast as to the enforceability of the contract provisions. The Court rejected Simpson's argument that Pendergast failed to tender performance. The Court also rejected Simpson's unclean hands defense, holding that Pendergast's alleged breach of fiduciary duty by competing with HMH did not relate to the transaction at issue.

However, the Court stated that before ordering the remedy of specific performance, the trial court must determine that the contract is "fair, just and not against good conscience." The Court noted that the offer imposed terms on HMH, a non-party to the action and that HMH had filed an amicus brief objecting to specific performance on the ground that it would affect HMH's substantive rights as to the required payment and enforcement of the non-competition agreement against Pendergast. Under these "unusual circumstances," the Court found that there were genuine issues of material fact as to the claim for specific performance. In contrast to Levy v. Reiner, the shareholder agreement itself did not impose obligations on the corporation. Instead, a shareholder exercising rights under the agreement was attempting to use the coercive buy-sell provisions of the

agreement to free himself of the obligation and deny the corporation the benefit of other portions of the agreement, namely, the non-competition provisions. By affirming summary judgment on liability, but denying that Simpson was entitled to specific performance as a matter of law, the Court implied that it was possible for him to demonstrate at trial that the agreement was fair, but offered no guidance on what evidence would suffice to establish fairness.

Stock Option Plans – Change in Control Provisions and the Standard of Review for Discretionary Decisions.

The plaintiff in Planning Technologies, Inc. v. Korman, 290 Ga. App. 715, 660 S.E.2d 39 (2008) was the former president of Planning Technologies, Inc. ("PTI"), who was a party to PTI's stock option plan. The plan provided for vesting over three years unless a change in control transaction occurred. The plan provided that determinations and decisions made by the Board or designated Committee "shall be final, conclusive and binding," and it further provided that

> "Any dispute or disagreement which may arise under, or as a result of, or in any way relate to, the interpretation, construction or application of this Agreement shall be determined by the Committee. Any determination made hereunder shall be final, binding and conclusive . . . for all purposes."

PTS entered into a transaction in which it issued stock in exchange for cash and the assets of another corporation. The Board determined that the transaction did not constitute a change in control under the stock option plan.

Korman attempted to exercise his options, was terminated for cause and sued, claiming that the transaction represented a change in control transaction under the stock option plan. The trial court agreed and granted summary judgment in Korman's favor. PTI argued on appeal that the stock option plan granted the Board absolute and uncontrolled discretion which was beyond review by the Court.

The Court of Appeals held that where there is a grant of discretionary decision-making authority, the issue to be determined is whether the decision must be made in good faith and in the exercise of honest judgment. The Court held that the language of the agreement gave the Board discretion, but not absolute and uncontrolled discretion. It then held:

> "Accordingly, the trial court was required to defer to the determination of PTI's Board of Directors that the ENS transaction was not a change in control and did not accelerate the vesting of Korman's stock options, so long as the Board's determination was made in good faith and involved the exercise of honest judgment."

Because the trial court had engaged in a *de novo* review, the Court of Appeals reversed. It elaborated on the correct standard of review, stating that a lack of good faith could be found in decisions made for arbitrary or capricious reasons, improper pecuniary motive, dishonesty or illegality, made with a total absence of any supporting factual evidence, or construing the plan agreement contrary to its obvious and exclusive meaning.

Breach of Fiduciary Duty.

Hilb, Rogal & Hamilton Co. of Atlanta, Inc. v. Holley, 295 Ga. App. 54, 670 S.E.2d 874 (2008)

The Georgia Court of Appeals affirmed a jury verdict against a former officer and employee of an insurance brokerage firm for breach of fiduciary duty in wrongfully diverting business to a new employer before leaving the plaintiff's employment. The Court found that Hugh Holley, the defendant, owed a fiduciary duty of loyalty as an officer (vice president). He also owed fiduciary duties as an employee because he had authority to "bind" the firm to certain obligations. The Court affirmed the jury's award of "nominal" damages in the amount of Holley's last two months' salary. The Court affirmed a directed verdict against the broker on its unjust enrichment claim in which it sought to recover the separate consideration paid for Holley's covenant not to compete. Since the non-compete had been held overbroad and unenforceable in a prior appeal[1], the doctrine of illegality required the Court to leave the parties as it found them and barred recovery.

[1] Hilb, Rogal & Hamilton Co. of Atlanta, Inc. v. Holley, 284 Ga. App. 591, 644 S.E.2d 862 (2007).

Nonprofit Corporations – Articles and Bylaws.

In Madonna v. Satilla Health Services, Inc., 290 Ga. App. 148, 658 S.E.2d 858 (2008), the Georgia Court of Appeals held that a hospital that has adopted bylaws to regulate clinical privileges for medical staff must abide by its own bylaws, even though they conflict with the hospital's obligations under an exclusive staffing contract.

The Satilla Regional Medical Center ("the hospital") had an exclusive Agreement with Baptist Specialty Physicians, Inc. ("BSP") to provide the hospital with Cardiologists. The Plaintiffs, Dr. Sonya Lefever and Dr. James Grigsby were affiliated with another practice group, Southern Heart Group ("SHG"). They applied for initial privileges with the hospital and were rejected because they were not members of BSP. Lefever and Grigsby sued the hospital for discrimination. Dr. John Madonna, a member of yet another practice group, South Georgia Cardiologists Associates ("SGCA"), was also denied initial privileges with the hospital and joined the suit. The distinguishing factor for Madonna was that he once held hospital privileges under BSP's exclusive agreement, but thereafter left BSP, joined SGCA and was seeking privileges as an SGCA member.

The Georgia Court of Appeals looked to the provisions of the hospital's bylaws that governed granting and denying staff privileges. The bylaws provided that "initial appointments and reappointments to the Medical Staff shall be made by the Board. .. . The Board shall act on appointments and reappointments only after there has been a recommendation from the Credentials Subcommittee and MEC. . . . Initial requests for membership. Following procedures stated in the Credentials Policy Manual, and with a recommendation of the appropriate Department Chair, the Medical Staff organization will evaluate and make recommendations to the Board." Id. at 150-51. Citing Satilla Health Services v. Bell, 280 Ga. App. 123, 633 S.E.2d 575 (2006), the Court noted that neither public nor private hospitals can arbitrarily and unreasonably deny physicians staff privileges laid out in the hospital bylaws.

Furthermore, the Court of Appeals held that Madonna should be permitted to reapply for privileges because his prior agreement through BSP did not waive his rights under the bylaws to reapply. The court determined that all three physicians had the right to apply for clinical privileges under the staff bylaws and should be allowed to do so. The hospital's conflicting "exclusive" agreement with BSP did not affect the hospital's need to comply with its bylaws, which would remain in force until duly amended.

In The Phoenix of Peachtree Condominium Association Inc. v. Phoenix on Peachtree LLC, 294 Ga. App. 447, 669 S.E.2d 229 (2008), the Georgia Court of Appeals affirmed the dismissal of an action by a condominium association for construction defects in the common areas because the association's declaration of condominium prohibited suits on unit holders' behalf. The association members passed a curative amendment to its bylaws and condominium declaration removing the prohibition, but the Court refused to give it effect, holding that standing must be determined at inception of the case.[2] However, the Court reversed the trial court's denial of the association's motion to substitute individual unit holders as real parties in interest.

Nonprofit Corporations – Books and Records Inspection Rights: Attorney's Fees.

In Parkridge Condominium Association, Inc. v. Callais, 290 Ga. App. 875, 660 S.E.2d 736 (2008), the Georgia Court of Appeals held that a Georgia nonprofit corporation that is compelled to permit a member to inspect and copy corporate records must pay only the member's reasonable attorney's fees that were directly incurred in obtaining the court order.

Gail Callais, a resident of Park Ridge Condominium ("Park Ridge") and former director of the condominium association, requested to inspect and copy Park Ridge's bank statements, board meeting minutes, and other documents in order to understand the budget for 2006 before the annual board meeting. Park Ridge refused to allow Ms. Callais to see the records, so she sued under O.C.G.A. § 14-3- 1602 and sought attorney's fees under § 14-3-1604(c). The trial court found that Ms. Callais had a proper purpose for her request and ordered Park Ridge to permit the inspection.

Section 14-3-1604(c) requires that a corporation ordered to permit inspection is liable for attorney's fees and expenses unless it proves that it refused inspection "in good faith because it had a reasonable basis for doubt about the rights of the member to inspect the records demanded." In ruling on her petition for attorney's fees, the trial court rejected the

association's contention that the inspection was made for purposes of harassment, found that the association's refusal to allow the inspection was not made in good faith and granted Ms. Callais over $26,000 in attorney's fees.[2]

The Court of Appeals held that the trial court's findings of the member's proper purpose and the association's absence of good faith must be upheld unless clearly erroneous and affirmed on those points. The Court reversed and remanded on the amount of attorney's fees awarded, however. Section14-3-1604(c) requires a corporation to pay only the fees "incurred to obtain the order" for inspection and copying of records. Callais sought payment of and was awarded fees and expenses she incurred, some of which were not directly related to her efforts to obtain the court order. The Court of Appeals directed the trial court to review and award only the expenses allowed under § 14-3-1604(c).

B. Limited Liability Companies.

Manager Powers and Conflicts of Interest.

In Old National Villages, LLC, v. Lenox Pines, LLC, 290 Ga. App. 517, 659 S.E.2d 891 (2008), the Georgia Court of Appeals held that a general manager of an LLC, who is authorized by an Operating Agreement to make all decisions on behalf of the company, can enter into a consent judgment against the company without giving notice to the sole member of the LLC and or obtaining the member's approval.

The litigation involved a $1.198 million loan that Lenox Pines, LLC ("Lenox Pines") made to Old National Villages, LLC ("Old National"). Lenox Pines was organized to make investments on behalf of a trust. David Smith, one of the trustees, was Lenox Pines' managing member. He was also general manager of the borrower, Old National. Old National's sole member was Valerie Smith, David Smith's estranged wife. Old National's operating agreement granted Mr. Smith "full, exclusive, and complete discretion, power, and authority, subject in all cases to the other provisions of this agreement and the requirements of applicable law, to manage, control, administer, and operate the business and affairs of the company. . . ."

The Smiths disagreed regarding the repayment terms of the loan, whether it had been repaid and funds that Mrs. Smith was withdrawing from Old National. Mr. Smith caused Lenox Pines to file suit against Old National on the loan. Three days later, acting as Old National's general manager, he filed a confession of judgment to Lenox Pines and shortly thereafter garnished Old National's bank account. Mrs. Smith was not given notice of either the filing of suit or the confession of judgment.

Old National, through Valerie Smith, moved to set aside the consent judgment. Her motion was denied by the trial court. Old National appealed, arguing that the consent judgment was void because Mrs. Smith, as sole member, did not receive notice of Lenox Pines' lawsuit and had not given approval for the consent judgment.

The Georgia Court of Appeals disagreed with Old National. The Court ruled that since the Smiths signed an Operating Agreement under which Mr. Smith was allowed to make all decisions concerning the business, he was authorized to enter into a consent judgment on behalf of Old National. The Court relied on well-established principle that legally separates a member of an LLC from the LLC itself. Thus, the sole member of the LLC did not need to be informed of any lawsuits against the LLC or approve of any consent judgment against the LLC, as long as the general manager is duly served and is authorized to act on behalf of the corporation.

In its opinion, the Court painstakingly lays out the actions and relationships of the parties, including David Smith's dual roles as managing member of Lenox Pines, the plaintiff/lender and as general manager of Old National, the defendant/borrower and his actions in bringing suit and confessing judgment to it. Curiously, however, the Court does not discuss or even mention the resulting conflict of interest, any arguments that Old National advanced regarding the conflict, and whether the Operating Agreement or the Georgia Limited Liability Company Code contained provisions addressing such a conflict. The clear implication is that the absolute power and discretion granted the general manager rendered any such conflict irrelevant, but there is certainly no ruling to that effect in the opinion.[3]

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[2] By contrast, the Court of Appeals held last year in Williams v. Martin Lakes Condominium Association, Inc., 284 Ga. App. 569, 644 S.E.2d 424 (2007), that under O.C.G.A. § 14-3-1422 reinstatement of an administratively dissolved nonprofit corporation can take place at any time and empower the corporation to pursue litigation filed during the period of its dissolution.

[3] Contrast the Court of Appeals' decision in Planning Technologies, Inc. v. Korman, supra, which held the grant of discretionary powers to be subject to review for good faith and the exercise of honest judgment.

Fiduciary Duties of Managing Members, Valuation of Membership Interests and Claims of Conversion.

Internal Medicine Alliance, LLC v. Budell, 290 Ga. App. 231, 659 S.E.2d 668 (2008) involved an LLC ("IMA") established by two physicians, William Budell and Izabella Verbitsky, in 2005 in order to practice internal medicine together. They never entered into a written operating agreement, but orally agreed that each would hold a 50 percent ownership interest, share equally in profits and losses and jointly manage IMA. They made $70,000 capital contributions, purchased office equipment and entered into a 7-year lease for office space. Disputes arose immediately after opening. Budell, the plaintiff, left at the end of 2005, leaving Verbitsky as the remaining managing member. Budell also left $40,000 in receivables that IMA was to collect, but were instead neglected, while Verbitsky saw to it that her own receivables were processed and collected. Verbitsky also withdrew her $70,000 capital contribution. The plaintiff sued for the value of his membership interest, asserted a claim for breach of fiduciary duty based on Verbitsky's failure to collect his accounts receivable and a claim for conversion of his capital contribution.[4] Appealing the trial court's rulings after a bench trial, IMA, Verbitsky and her husband who was involved in the dispute, raised three issues. They argued, first, that the court improperly excluded IMA's lease obligations in calculating the value of Budell's interest. The Court of Appeals rejected that argument, finding that Verbitsky had agreed to a formula of valuation that did not include the lease.

Second, they appealed the finding that Verbitsky had breached her fiduciary duty by failing to collect the receivables for Budell's patients. The Court of Appeals affirmed, stating that "Managing members of an LLC owe fiduciary duties to the LLC and its member investors," citing O.C.G.A. § 14-11- 305(1). The Court added that a managing member must act with utmost good faith and loyalty in managing the LLC, citing Quinn v. Cardiovascular Physicians, 254 Ga. 216, 326 S.E.2d 460 (1985), a case involving a closely-held corporation. The Court of Appeals noted that the members could have entered into an agreement under O.C.G.A. § 14-11-305(4)(A) modifying that standard, but did not do so. It then upheld the trial court's ruling that Verbitsky's neglect of Budell's receivables constituted a failure to exercise ordinary care and held that under the circumstances the trial court was authorized to find bad faith.

The Court of Appeals reversed on the third issue, the conversion claim, finding the plaintiff's right to the return of his capital contribution was an intangible property interest that had not been merged into a document susceptible to conversion, nor had it involved funds entrusted to Verbitsky for a particular purpose. It was nothing more than a failure to pay a debt.

No Vicarious LLC Liability for Managing Members' Breach of Fiduciary Duty; No Fiduciary Duty for Non-managing Members; Discretionary Rights of Expulsion.

In ULQ, LLC v. Meder, 293 Ga. App. 176, 666 S.E.2d 713 (2008), the plaintiff was terminated as an officer of ULQ, LLC and his membership in ULQ was also terminated, triggering an obligation to sell his interest to ULQ for the value of his capital account, which because of losses was zero. Plaintiff sued ULQ for breach of contract, breach of fiduciary duty, and conversion. ULQ counterclaimed for breach of contract, breach of fiduciary duty and tortious interference with contractual and business relations arising out of plaintiff's actions following his termination as an officer but before the sale of his ownership interest. The trial court denied ULQ's motion for summary judgment on the plaintiff's claims and granted the plaintiff's motion for summary judgment on ULQ's counterclaims. ULQ appealed.

The Court of Appeals upheld the denial of ULQ's motion for summary judgment on the breach of contract claim, finding that ULQ was bound to exercise good faith in making the determination that the plaintiff's removal was in the company's best interests. The Court held that, under Georgia law, all contracts contain an implied covenant of good faith and fair dealing, and "where the manner of performance is left more or less to the discretion of one of the parties to the contract, he is bound to the exercise of good faith." The only relevant exception to this rule is an agreement that by its express terms grants the party absolute or uncontrolled discretion in making a decision. The Court found that the exception did not apply.[5]

The Appeals Court held that the trial court erred in denying ULQ's motion for summary judgment on the breach of fiduciary duty claims and held that a limited liability company owes no fiduciary duty to its members, either directly or vicariously for actions taken by its manager. This is because, "it would make no sense to hold ULQ responsible for its

[4] The Court of Appeals noted that Budell brought the litigation as a direct claim, but that the appellants had not challenged his standing.

[5] Compare Planning Technologies, Inc. v. Korman and Old National Villages, LLC, v. Lenox Pines, LLC, supra.

manager's breach of a fiduciary duty to ULQ and its members, as it would shift the cost of that breach to the company (and indirectly to its members), thereby shifting the cost to the very parties harmed by the breach." The Court looked to other states that have held that a corporation owes no fiduciary duty to its shareholders in making its determination. The Court held that the plaintiff's conversion claim also failed because it could not be based on a breach of contract alone, and no fiduciary duty was owed. The Court also found that the claims for tortious interference with business and contractual relations failed because the plaintiff was not a stranger to the contract.

The Court also held that the trial court erred in granting the plaintiff summary judgment on ULQ's counterclaim of breach of contract. There was substantial evidence that after the plaintiff's termination as an officer, but before the purchase or redemption of his interest, he persuaded a client not to do business with ULQ for two months, which cost it $40,000 in profits. The operating agreement obligated the plaintiff to refrain from such interference activities so long as he was a ULQ member or owner.

Finally, ULQ asserted that as a member of the company, the plaintiff owed it a fiduciary duty not to interfere with customer relationships. The Court held that the plain language of O.C.G.A. § 14-11-305 states that non-managing members in manager-managed LLCs do not owe duties to the LLC or other members, and therefore held that "non-managing members owe no fiduciary duties to the LLC or the other members" unless the operating agreement or articles of organization provide otherwise.[6]

LLC Member/Manager Authority and Liability.

Fielbon Development Co. v. Colony Bank of Houston County, 290 Ga. App. 847, 660 S.E.2d 801 (2008) addresses the issue whether a limited liability company can be liable under O.C.G.A. § 14-11- 301(c) for the allegedly fraudulent borrowings by one of its managers. Colony Bank sued to recover on a promissory note signed by Fielbon Development Company, LLC and guaranteed by one of the LLC's managers, R.J. Fields. Fields and Calder Bond had formed Fielbon to develop real estate projects. Each was a fifty percent owner. Bond had the authority to manage the daily affairs while Fields was to handle the financial aspects. Bond could sign documents on behalf of Fielbon, could represent it at closings, and had authority to sign checks on the company checking account. The two also had an agreement that Bond could draw a certain amount per year from Fielbon accounts for his personal living expenses. Fielbon obtained a series of construction loans from Colony Bank, which both Fields and Bond personally guaranteed. After several months, Bond signed another promissory note on behalf of Fielbon, the note at issue, which was for a construction loan secured by a deed on a lot, Lot 4B, in one of the subdivisions being developed by Fielbon. Fields' and Bond's guarantees covered this promissory note as well.

Loan proceeds were used to purchase Lot 4B and Fielbon could make additional draws as construction on the lot progressed. The bank would inspect the property when a draw was requested to ensure that construction was progressing in proportion to the money advanced. Most draws on the loan were deposited directly into Fielbon's account. After a few months, the bank discovered that construction was not progressing. Bond told the bank that its documents were in error and that the loan was actually secured by Lot 4C. The bank changed the loan sheet and authorized subsequent draws based on its inspections of Lot 4C. In fact, the construction on Lot 4C was funded by a loan from another bank. In Colony Bank's suit on the note and guarantee, Fields and Fielbon filed lender liability counterclaims for negligence, attorney's fees and punitive damages.[7]

The Court held that the bank made out its prima facie case by producing the note and showing that it was executed by Bond, who had authority to sign such documents on Fielbon's behalf. Fielbon argued it should not be liable on the note because, under O.C.G.A. § 14-11-301(c), a limited liability company is not liable for acts of a member that are "not apparently for the carrying on in the usual way the business or affairs," the draws were not used for the development of Lot 4B and Bond allegedly embezzled some of the loan proceeds and failed to use the loan for the intended purpose. Closely examining Bond's and Fielbon's prior conduct and the circumstances of the loan, the Court found that there was nothing in Bond's actions that was so dissimilar from the acts the corporation had authorized him to perform as to make them "not apparently for the carrying on in the usual way the business or affairs" of the corporation.

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[6] But cf. Perry Golf Course Development, LLC v. Housing Authority of Atlanta, 294 Ga. App. 387, - - - S.E.2d --- (2008) holding without discussion or citation to the Georgia Limited Liability Company Code that members of an LLC formed to redevelop a housing project owed fiduciary duties to each other. Apparently the operating agreement did not provide for managing members.

[7] The claims against Bond were discharged in bankruptcy.

Gardner v. Marcum, 292 Ga. App. 369, 665 S.E.2d 336 (2008), deals with the liability of an LLC and its members for return of funds that a third party invested in an aborted transaction. In Gardner, C. Rob Marcum sued Dan Gardner, Jay Steele, and DG Productions, LLC ("DGP"), claiming that he was entitled to the return of $50,000 he had loaned to the defendants. The trial court granted summary judgment in favor of Marcum and the defendants appealed. Dan Gardner was a musician, and his personal manager, Dennis Kurtz, had approached Marcum regarding investing up to $150,000 in an album by Gardner. Marcum wrote a check to DGP (an LLC owned solely by Gardner) in the amount of $50,000 to be used for "producing, releasing, and promoting" Gardner's album. Marcum argued that these were initial funds to be used by Gardner for production, release, and promotion of the album, conditioned on the satisfactory completion of negotiations between Marcum and Gardner. If an acceptable agreement was finalized guaranteeing Marcum a proper return on his investment, he expected to invest an additional $100,000. He argued the money was therefore an "advance." Gardner argued the money was an "investment" and was the first of three investment installments with the understanding that a formal written agreement would be negotiated.

A formal agreement was never negotiated, and Marcum demanded that Gardner return the $50,000, which Gardner refused to do. Gardner claimed the project was ultimately unsuccessful because of Marcum's failure to complete his investment. The Court found that there was no assent to the essential terms of a contract because the parties never agreed on Marcum's rate of return on his investment, nor on whether the money was an unsecured loan or an equity investment, which were material terms.[8] At the most, the parties had entered into an unenforceable agreement to agree. The Court found no evidence, however, that Marcum had agreed to forfeit his money if the negotiations failed and held DGP liable for its return.

The defendants argued that the trial court erred in finding Gardner and Steele[9] individually liable. The Court of Appeals agreed and reversed.[9] The Court found that Marcum paid the money to the LLC, and the LLC was liable for the return of the money to Marcum. Citing O.C.G.A. § 14-11-3303(a), the court held that Gardner and Steele were not liable for DGP's obligations solely by reason of being members. Because piercing the corporate veil would be an issue for the jury, the court concluded that it was error for the trial court to grant summary judgment against Gardner and Steele.

In addressing the defendants' argument that an issue of fact remained as to whether the money was a loan or an investment, the Court found that the argument had no merit. It found that because there was no meeting of the minds to form a contract, the result would be the same.

LLC Operating Agreement Provisions: Arbitration, Dissolution and Amendments.

In Georgia Rehabilitation Center, Inc. v. Newnan Hospital, 283 Ga. 335, 658 S.E.2d 737 (2008), the Georgia Supreme Court held that where an LLC Operating Agreement between members requires arbitration only of claims arising out of or in connection with the Operating Agreement or its breach and provides limited rights to dissolve the company, a member cannot be required to arbitrate an independent claim for judicial dissolution. The Court also upheld the trial court's appointment of a receiver to oversee the company during the litigation.

Georgia Rehabilitation Center, Inc. ("GRC") and Newnan Hospital ("Newnan") co-owned Cowetta Rehab Services ("CRS"). CRS became financially unstable, so Newnan requested that the trial court dissolve CRS under O.C.G.A. § 14-11-603. GRC moved to compel arbitration under CRS's Operating Agreement. The trial court denied the motion and appointed a receiver. GRC appealed, arguing that the Operating Agreement required arbitration on the issue of CRS's dissolution.

CRS's Operating Agreement provided that "any dispute, controversy or claim arising out of or in connection with, or relating to, this Operating Agreement or any breach or alleged breach hereof shall, upon the request of any party involved, be submitted to, and settled by, arbitration." Id. at 335.[10] To determine whether CRS's judicial dissolution was a claim arising out of the Operating Agreement, the Georgia Supreme Court looked to the terms of the Operating Agreement concerning dissolution. The Agreement provided that "dissolution...occurs 'only upon [1] Dissolution Notice from a Member pursuant to [certain

[8] In a prior appeal, Marcum v. Gardner, 283 Ga. App. 453, 641 S.E.2d 678 (2007), the Court held that the memorandum on the check, "1/3 investment on Don Gardner," was not determinative of the issue of whether the transaction was a loan or an investment, given Gardner's testimony that the transaction was a loan.

[9] The evidence conflicted about whether or not Steele was a member of DGP.

[10] The Operating Agreement did not provide that the arbitrator should determine the issue of arbitrability, thus the scope of the arbitration clause was properly before the Court.

terms of the Operating Agreement]...[2] the unanimous written agreement of all Members...or [3] the bankruptcy or dissolution....of a Member.'" Id. The Court found it undisputed that none of those conditions applied. Since Newnan instead chose to invoke O.C.G.A. § 14-11-603 as the basis for CRS's dissolution, that the dissolution did not arise out of the Operating Agreement, and thus arbitration was required. Furthermore, since Newnan and GRC could not agree on how to move forward in any area regarding CRS, the Court held that the trial court was within its discretion to appoint a receiver to oversee CRS during the litigation.

Two justices dissented from the Court's ruling that Newnan's request for dissolution did not arise from a claim relating to the Operating Agreement. The dissent looked to the text of the statute that Newnan invoked as a grounds for dissolution, O.C.G.A. § 14-11-603(a), and also to Newnan's complaint. This statute provides that an LLC can be dissolved only "where it is not reasonably practicable to carry on the business *in conformity with* the articles of organization or *a written operating agreement*." Id. at 337. (emphasis in opinion). Newnan's complaint further clarified the choice to use that statute, specifically, "*on terms that are in accordance with . . . the provisions of the Operating Agreement between the parties.*" Id. Thus, the dissent argued, Newnan's request for dissolution was a controversy that necessarily related to the Operating Agreement, and so arbitration should not have been denied.

In a subsequent decision, the Supreme Court affirmed the trial court's expansion of the receiver's powers, Georgia Rehabilitation Center, Inc. v. Newnan Hospital, 284 Ga. 68, 663 S.E.2d 204 (2008) (citing O.C.G.A. § 14-2-1431(c) which authorizes the appointment of receivers in connection with judicial dissolution of business corporations.)[11]
IH Riverdale, LLC v. McChesney Capital Partners, LLC, 292 Ga. App. 841, 666 S.E.2d 8 (2008) dealt with the validity of an amendment to an LLC operating agreement, made by the majority member, which eliminated a special quarterly distribution to a minority member of 5% of profits. That distribution was in addition to the distributions due to the minority member for his percentage ownership in the company and was allegedly in consideration for the minority member's guarantee of the company's debt. The LLC paid the lender $60,000 to eliminate the minority member's guarantee. The operating agreement authorized amendments made in writing and signed by members holding a majority interest in the company. The Court examined the operating agreement and found nothing to prohibit the amendment. It found nothing in the provisions regarding distributions to members that stated it was not subject to amendment. The minority member argued that a provision requiring unanimous consent to "major loan documents" and the entry into contracts obligating the company to expend more than $10,000 in company funds governed the majority member's actions. The minority member offered affidavit evidence regarding the elimination of his guarantee. The Court did not decide whether elimination of the guarantee violated the provision requiring unanimity for major decisions. It stated, instead, that "the use of parol evidence to construe a contract is prohibited," but did not provide any analysis or explanation of how the parol evidence rule was implicated. Finding no express mention of the guaranty distribution in the major decisions provision of the operating agreement, it upheld the amendment as authorized under the operating agreement.

C. Partnership Law.

No significant 2008 decisions involving Georgia partnership law have come to our attention.

D. Joint Ventures.

Joint Venture, RICO Burden of Proof and Proximate Cause.

American Association of Cab Companies, Inc. v. Parham, 291 Ga. App. 33, 661 S.E.2d 161 (2008) involved a suit by an injured passenger in an under-insured taxicab against two cab companies who provided management services, including dispatching and insurance to cab drivers. The plaintiff sought to establish the cab companies' liability through alternate theories of agency, respondeat superior and joint venture. The cab companies objected to the jury charge and verdict form on the ground that there was no evidence supporting a joint venture. In a seven-judge decision with two dissenting judges, the Georgia Court of Appeals reviewed the evidence showing that there was the "mutual control" needed for a joint venture. The record reflected that the cab was co-owned by one of the cab companies and bore the insignia of the other. The driver obtained his license as

[11] Another decision regarding judicial dissolution of a Georgia LLC is Ervin v. Turner, 291 Ga. App. 719, 662 S.E.2d 721 (2008), a dispute among organizers of a bank who created an LLC through which to conduct fund-raising and organizational efforts. The trial court's order dissolving the LLC and its allocation of financial responsibility under a contribution agreement among the organizers was affirmed after rejecting a variety of arguments from the *pro se* appellants, none raising any legitimate questions for appeal.

one of the companies' listed drivers. The Court also noted that the driver himself exercised some control over his activities, although it is not clear why the mutuality of control needed to include the driver.

The Georgia Court of Appeals reversed a defense verdict on the plaintiff's Georgia RICO claim because the trial court had improperly instructed the jury that the plaintiff had to prove the defendants' RICO violations by clear and convincing evidence. The Court held that the Georgia Supreme Court's decision in Williams General Corporation v. Stone, 279 Ga. 428, 614 S.E.2d 758 (2005) establishing a preponderance of the evidence standard should be applied retroactively. The Court also rejected the defendant cab companies' argument that the plaintiff could not prove that the alleged RICO violations proximately caused his damages. The Georgia Commissioner of Insurance had issued a cease-and-desist order against one of the cab companies because it did not have the financial ability to provide coverage as a self-insurer or satisfy a judgment. Citing other decisions dealing with the applicability of RICO to fraudulently uninsured cab operations, the Court held that a jury could find that the cab companies misrepresented their financial condition and that this misrepresentation proximately compromised the plaintiff's ability to collect his judgment.

E. Business Law Issues.

Asset Purchase Agreements – Assumed Liabilities, Rights to Escrowed Funds, Breaches of Representations and Warranties, and Anti-assignment Provisions.

Assumed Liabilities. In Wilkie v. 36747, LLC, 294 GA. App. 179, 669 S.E.2d 155 (2008), a salesman seeking to recover unpaid commissions alleged to be owed by two software corporations that had sold their assets sued both the sellers and the purchaser. The Court held that the purchaser of the assets did not assume sellers' obligation to the salesman, even though purchaser was aware of the salesman's contract at the time of the purchase because the asset purchase agreement did not include the salesperson's contract among the liabilities being assumed, disclaimed responsibility for any liabilities not specifically assumed, and contained a merger clause. The transaction began with a "one-page agreement, literally on a napkin" providing for the sale of all assets of two corporations for $4,800,000 with a non-refundable "deposit" of $500,000. A dispute arose between purchaser and seller in documenting the transaction and, after litigation and mediation, formal documents were prepared and executed. Reviewing the Asset Purchase Agreement, the Court stated:

> "The contract described included and excluded assets and liabilities, and explicitly provided that the Buyer did not assume any obligation of the Seller not specifically listed in the Assumption of Liabilities section of the contract, including any liabilities to 'any present or former employee.' The Seller otherwise continued to be responsible for all liabilities 'whether known or unknown, fixed or contingent, liquidated or unliquidated and secured or unsecured, whether arising prior to, at or subsequent to the [sale] date ... and whether or not disclosed to the Buyer.'"

The asset sellers, seeking indemnification from the purchaser, contended that the salesman's contract, entitled "Franchise Agreement," was a "software contract" expressly transferred under the Asset Purchase Agreement. The Court rejected that argument, finding that the software assets were "clearly and unambiguously" identified in the Agreement. The Court also rejected the argument that the salesman's contract, providing for the payment of future commissions, was a "trade payable" that the purchaser had assumed. Finally, the Court relied on the Asset Purchase Agreement's merger clause in holding that the purchaser's awareness of the salesman's contract did not result in assumption of liability.

Escrowed Funds. In Ahmed v. CUA Autofinder, LLC, 387 B.R. 906 (Bkrtcy. M.D. Ga. 2008), the Court decided who was entitled to the return of funds paid into escrow by the sole owner-member of an LLC formed to purchase assets of an automobile dealership. The LLC was to pay $650,000 of the $1,700,000 purchase price in cash, with the balance to be paid through a promissory note that the owner-member guaranteed. In the asset purchase agreement, the LLC agreed, as part of the purchase price, to escrow an additional $50,000 to pay the sellers' tax liabilities resulting from the sale. The LLC itself did not have the money required for the cash portion of the purchase price or to fund the escrow, so the owner-member made those payments from his personal funds, but did so without any formal documentation of any right or entitlement to the funds placed in escrow. The escrow agreement provided that the LLC was entitled to the funds not paid to the sellers. The LLC filed for bankruptcy when it could not make the final $550,000 payment under the note. The Court determined that the LLC's rights to the escrowed funds were part of the bankruptcy estate and that the sellers had failed to meet the conditions of the escrow within the time allowed. The owner-member asserted that, because he had discharged the LLC's obligations under the asset purchase agreement, he was equitably subrogated to the LLC's rights to return of the escrowed funds. Relying on case law from other jurisdictions, the Court set for the required elements for equitable subrogation as follows:

> "Equitable subrogation requires that a party show that (1) it paid a debt in order to protect its own interest, (2) it was not acting as a volunteer in making the payment, (3) it was not primarily liable for the debt, (4) the entire debt was paid, and (5) subrogation would not cause an injustice to the rights of third parties."

It then addressed the issue of whether the owner-member had acted as a volunteer in funding the escrow, quoting from Franco v. Cox, 265 Ga. App. 514, 594 S.E.2d 717, 719 (2004):

> "Subrogation is never applied for the benefit of a mere volunteer who pays the debt of another without any assignment or agreement for subrogation, and who is under no legal obligation to make the payment, and is not compelled to do so for the preservation of any rights or property of his own."

The owner-member contended that his guarantee required him to perform the LLC's escrow obligations, but the Court determined that the escrow was not among the guaranteed obligations. The guarantee, moreover, contained an express waiver of rights to subrogation, which the Court held effectively waived any rights that the owner-member had against the LLC. It ruled that he had acted as a mere volunteer in funding the escrow and had no rights to return of the funds.

Breaches of Representations and Warranties. The decision in Kilroy v. Alpharetta Fitness, Inc., 2008 WL 5049966 (Ga. App. Dec. 1, 2008) concerns claims based on the alleged breach of representations and warranties by the seller in connection with the sale of assets of a Gold's Gym franchise exercise facility. The corporate purchaser, its shareholder and his wife sued the corporate seller and its shareholders for breach of contract, negligent misrepresentation and fraud, as well as fraudulent conveyance claims based on the selling corporation's distribution of proceeds to its shareholders. The trial court awarded summary judgment on the fraud and fraudulent transfer claims which the Court of Appeals reversed holding that triable issues existed as to elements of fraud and fraudulent transfer.

After the sale closed, the exercise facility produced less than expected revenues and the purchaser discovered that the seller had been factoring customer contract receivables, including the outright sale of some customer contracts. The purchaser sued, alleging that this practice breached representations and warranties in the asset purchase agreement that "no assignment of rights in or relating to [the contracts] have been made by Seller or Shareholders." The buyer also alleged that the asset purchase agreement's representations and warranties were also breached because the financial statements did not fairly present the company's financial condition and were not prepared in accordance with generally accepted accounting principles. An expert hired by the purchaser to analyze the accuracy of the financial records of the business concluded that the sales of the contracts were improperly reflected as an "immediate recognition of revenue" instead of "deferred revenue," inflating the revenue for a given month. The expert also found that in the first half of 2004, the seller's financial statements reported as revenue the net amounts received after expenses. In the second half of 2004, however, financial statements reflected the gross amounts received as revenue without reduction for expenses. This change in accounting methods could give a "false impression of growing revenue." The Georgia Court of Appeals found that there was some evidence to support each element of fraud and reversed the trial court's grant of summary judgment.

The Court also reversed the grant of summary judgment with respect to the fraudulent transfer claim because shortly after closing, the seller distributed the proceeds of the asset sale to its four shareholders leaving the corporation with no assets.

A petition for a writ of *certiorari* in this case is currently pending in the Georgia Supreme Court.

Anti-assignment clause. Accurate Printers, Inc. v. Stark, 2008 WL 5049960 (Ga. App., Nov. 26, 2008) involved the application of an anti-assignment clause in an asset purchase agreement. API's president and sole owner purchased Oxford Printing, Inc. from the defendant. The Asset Purchase Agreement was executed between the purchaser in his individual capacity, the seller defendant and the company Oxford Printing. As part of the transaction, purchaser (also in his individual capacity), the seller defendant and the company Oxford Printing also executed a Restrictive Covenant prohibiting Oxford and Seller from involvement in "a competing business within the Area." API was not named a party to the transaction and did not execute the agreements. API did not contend that it was a third party beneficiary of any of the agreements. The purchaser himself was not a party plaintiff.

Seller agreed to work for purchaser and API to help with the business transition. Shortly thereafter, however, he went to work for Baxter Printing Co. in printing sales, where he began to compete with API, solicited API's customers, and disclosed proprietary information.

The trial court granted a directed verdict in favor of seller as to API's claims for breach of the non-compete clause and awarded attorney fees to seller, because API was not a party to the agreements it was trying to enforce. The Court of Appeals agreed, quoting Levy v. Reiner, 290 Ga. App. 471, 659 S.E.2d 848 (2008): "It is axiomatic that each corporation is a separate entity, distinct and apart from its stockholders." It affirmed the directed verdict as to the claims for breach of non-compete clause, but it reversed the award of attorney fees.

API argued that it had acquired the purchaser's rights by assignment. The Asset Purchase Agreement, however, prohibited the assignment of contract rights unless two conditions were met – the purchase price was paid in full and the seller consented. Neither of those conditions were met. API also argued that the seller had waived the anti-assignment prohibition. The Court of Appeals held that the waiver had to be "clear and unmistakable" and that the plaintiff's evidence did not satisfy those requirements. The award of attorney fees was reversed, since API as a non-party to the agreements could not breach them and had no liability for attorney's fees under them.

Corporate Conveyances of Real Estate – O.C.G.A. § 14-5-7.

Deljoo v. Suntrust Mortgage, Inc., 2008 WL 5174307 (Ga. App. Dec. 11, 2008). After financing the purchase of a residence, Suntrust and the purchaser discovered a previously unknown security deed on the property held by Shakrookh ("Daniel") Deljoo. Suntrust sued Deljoo, seeking to cancel the security deed or otherwise quiet title to the property as to the deed.

The security deed referred to the same lots of the subdivision at issue, but mistakenly identified them as being in the wrong land lot of the county district. The trial court granted summary judgment, concluding that the incorrect land lot number took the deed outside the chain of title and that the purchaser and Suntrust were bona fide purchasers without notice. The Georgia Court of Appeals affirmed that decision, 289 Ga. App. 396, 657 S.E.2d 319, but the Supreme Court reversed, 284 Ga. 438, 668 S.E.2d 245 (2008), finding that the incorrect description did not remove the deed from the chain of title.

On remand, the Court of Appeals vacated its earlier opinion, adopted the opinion of the Supreme Court, and considered the remaining enumerations of error. One of the remaining enumerations of error was that the trial court had erred in denying Deljoo summary judgment on the issue of whether the deed was properly executed. The trial court had found that there were genuine issues of material fact because: (1) the deed was signed only by the president of the corporation that had granted the property to Deljoo without any indication of his office or authority to bind the corporation and (2) the corporate seal affixed below the president's signature was illegible on the documents provided to the trial court.

The Court of Appeals affirmed the denial of summary judgment on this issue, basing its decision on O.C.G.A. § 14-5-7, a rarely cited Georgia statute on the validity of corporate conveyances of real estate, which provides that:

> "Instruments executed by a corporation conveying an interest in real property, when signed by the president or vice-president and attested or countersigned by the secretary or an assistant secretary or the cashier or assistant cashier of the corporation, shall be conclusive evidence that the president or vice-president of the corporation executing the document does in fact occupy the official position indicated; that the signature of such officer subscribed thereto is genuine; and that the execution of the document on behalf of the corporation has been duly authorized."

O.C.G.A. § 14-5-7. The Court applied the statute, noting that even if a deed is not signed by two corporate officers, the presence of an attested corporate seal could indicate authority to execute the document on a corporation's behalf. However, because the corporate seal here was illegible and because the president signed only his name with no reference to his title, the Court found that a genuine issue of fact remained as to the validity of the deed and affirmed the trial court's denial of summary judgment to Deljoo on this issue.

Article 8: Stock Owners Have No Claims Against Signature Guarantors under UCC or Common Law.

In Dudley v. Wachovia Bank, 290 Ga. App. 220, 659 S.E.2d 658 (2008), in a matter of first impression in Georgia, the Georgia Court of Appeals held that a signature guarantor is not liable to a stock owner under Article 8 of the Uniform Commercial Code.

Harold A. Dudley, Sr., executed a will bequeathing his stock to his estate to be divided among his children as executors. Years later, Mr. Dudley suffered from dementia and a stroke. Thereafter, Mr. Dudley's second wife had him sign forms that transferred the stock to her, as opposed to his estate, upon his death. One of the three issuers in which Mr. Dudley held stock (AFLAC) provided a Medallion Guarantee of his signature. Two commercial banks (Wachovia Bank, N.A. and Regions Bank) provided Medallion Guarantees as to his signature on the other two stocks (Southern Company and Regions Financial Corporation).

After Mr. Dudley's death, his executors sued Mrs. Dudley, the bank and the three corporate defendants for loss resulting from the wrongful transfer of the stock. Relying on decisions from other jurisdictions, the Court of Appeals held, as a matter of first impression in Georgia, that the warranties made by a signature guarantor under O.C.G.A. § 11-8-306 flow to those who

deal in the security in reliance on the guarantee, but not to a stock owner. Second, the Court rejected the executors' common law negligence claim, holding that claims against signature guarantors are limited to the breach of warranty remedies specified in the UCC. Thus, under neither statutory nor common law can a signature guarantor be liable to a stock owner who suffers a loss from the wrongful transfer of stock. Third, the Court did recognize the executors' claim against the three issuers, who have "absolute liability" under O.C.G.A. § 11-8-404 for a wrongful register of transfer. Finally, the Court affirmed summary judgment on the executors' equitable claims against the corporate defendants under O.C.G.A. § 13-3-24 to void the transfers, because the corporate defendants did not own or control the stock at issue.

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