



# Plop Plop, Fizz Fizz: Dissolving an Alabama Biz

By Gregory A. Brockwell

Willie Nelson tells us, "Turn out the lights, the party's over. They say that all good things must end." As it is in song, so it sometimes is in business. It is rare for a closely-held business to last forever. Odds tell us that, at some point, the business will come to an end. Even if a business is a going concern, the right of a non-controlling owner to trigger a judicial dissolution is one of the few, and sometimes most important, protections granted under current Alabama law. This article will provide an overview of dissolving an Alabama corporation or limited liability company ("LLC").

## Where to Start

When considering the end of a company, the first place to start must always be the company's governing documents. For a corporation, the lawyer needs to examine the formation document, the bylaws, any shareholder agreements, any buy-sell agreements, and any amendments of those documents. Similarly, for an LLC, the lawyer needs to examine the formation document, the company agreement, any buy-sell agreements, and any amendments of those documents. These governing documents might make significant changes to the statutory default rules, and so it is imperative to start by studying the governing documents.

The remainder of this article will discuss the statutory scheme for dissolution. But, please, first always start with governing documents.

## **Voluntary Dissolution**

If the proper procedures are followed, the proper votes obtained, or the company's governing documents otherwise provide, a company may be dissolved either voluntarily or automatically. Dissolution may thus be achieved without litigation or court intervention.

### **Voluntary Dissolution of a Corporation**

In an Alabama corporation, the decision to dissolve voluntarily may be initiated either by the board of directors or by the shareholders. The board of directors may propose dissolution for submission to the shareholders.<sup>1</sup> For the board's proposal to dissolve to be adopted, the general rule is that board of directors must recommend dissolution to the shareholders.<sup>2</sup> The board of directors must provide each shareholder (whether entitled to vote or not) notice of a proposed shareholders' meeting, and the notice must state that one of the purposes of the meeting is to consider dissolving the corporation.<sup>3</sup> At the meeting, the shareholders who are entitled to vote must then approve the proposal to dissolve.<sup>4</sup> Unless the corporation's articles of incorporation require otherwise, the vote to approve the proposal to dissolve must be at least a two-thirds majority.<sup>5</sup> The board may place conditions on the proposal to dissolve, but in no event may the board decrease the vote required for approval.<sup>6</sup>

The corporation statute also provides an alternative procedure. In lieu of the procedure described above, a corporate may be dissolved by written consent of all of its shareholders (both voting and non-voting).<sup>7</sup> The board's approval is not required under this method.<sup>8</sup>

### **Voluntary or Automatic Dissolution of an LLC**

In an Alabama limited liability company, the company is dissolved upon the occurrence of the first of the following events: (1) an event or circumstance that the company agreement (formerly known as the "operating agreement") states causes dissolution; (2) consent of all members to dissolve; or (3) when there is no remaining member.<sup>9</sup>

Under the first of these, the members may, when writing their company agreement, agree in advance on what future events or circumstances will au-

tomatically trigger a dissolution.<sup>10</sup> Such "triggering events" could be anything that the members define in the company agreement. Typical triggering events may include the death or incapacity of a key member or members, a vote of the members in such number as the agreement defines, the end of a particular purpose for which the company was formed, the insolvency or bankruptcy of the company, or the end of a particular term if the company is not intended to be perpetual.

If the company agreement does not define such triggering events, or for any other reason, the members may agree to dissolve.<sup>11</sup> Under this method, consent of all members is required. Even one "no" vote from a member can prevent a dissolution.

Finally, when the company ceases to have any remaining members, then, as a general rule, the company will automatically dissolve.<sup>12</sup> However, the company may continue in certain circumstances. First, if the holders of all transferable interests<sup>13</sup> (i.e., those holding only financial rights, but not member rights) agree in writing within 90 days to continue the company and to appoint one or more new members, then the company will continue.<sup>14</sup> Second, if the company agreement allows a manner to appoint new members and continue the company's business, the company may continue.<sup>15</sup>

### **Judicial Dissolution**

If the company cannot be dissolved voluntarily or automatically, then it may still be dissolved through litigation. Both the corporation statute and the LLC statute provide for judicial dissolution under certain circumstances.

### **Judicial Dissolution of a Corporation**

The circuit court of the county where a corporation's articles of incorporation are filed has jurisdiction to dissolve the corporation.<sup>16</sup> The Alabama Attorney General has standing to seek judicial dissolution in certain circumstances.<sup>17</sup> A creditor also has standing to seek judicial dissolution.<sup>18</sup> The much more common scenario, however, is for a shareholder to bring a proceeding for judicial dissolution.<sup>19</sup>

To file an action for judicial dissolution, the shareholder must be able to allege one of several possible grounds for dissolution.<sup>20</sup> These are: (1) that the

directors are deadlocked, the shareholders are unable to break the deadlock, and irreparable injury to the corporation is threatened or being suffered; (2) that the directors or those in control have acted, are acting, or will act in an illegal, oppressive, or fraudulent manner; (3) that the shareholders are deadlocked in voting power and have failed, for at least two consecutive annual meeting dates, to elect successors to directors whose terms have expired; or (4) that corporation assets are being misapplied or wasted.<sup>21</sup>

The Alabama Supreme Court has stated, "The law in Alabama is that dissolution of a corporation is an extreme remedy and should be ordered only where the facts clearly warrant it."<sup>22</sup> "The ultimate decision of whether to dissolve a corporation must be made by the trial court, guided by equitable principals, based on the particular facts of each case."<sup>23</sup> While the burden of proof may be high, it is not so high as to require a shareholder to prove a "willful wrecking" of the corporation.<sup>24</sup>

In a judicial dissolution proceeding, the court has discretion to issue injunctions, to appoint a receiver, and to take other action to preserve the corporate assets.<sup>25</sup> The purpose of such interim relief is to preserve the assets and carry on the corporation's business until a full hearing can be held.<sup>26</sup>

After conducting a hearing, if the court finds that one or more grounds for dissolution exist, the court may enter a decree dissolving the corporation.<sup>27</sup> After entering a decree of dissolution, the court shall direct the winding up and liquidation of the corporation's business.<sup>28</sup> The court may authorize a receiver to manage the affairs of the corporation before dissolution, or to liquidate the corporation after dissolution.<sup>29</sup>

Before filing an action for judicial dissolution, it is very important for the shareholder to consider the "election to purchase" remedy under the corporation statute. The corporation should also consider this remedy before answering the complaint. In a privately held corporation, a shareholder's filing of an action for judicial dissolution will trigger the right of the corporation or other shareholders to purchase the petitioning shareholder's shares.<sup>30</sup> For this reason, the corporation must notify all shareholders of the filing of a dissolution action within 10 days of the date of filing.<sup>31</sup> The



corporation or other shareholders are allowed 90 days from the date of filing of the dissolution action to elect to purchase the petitioning shareholder's shares.<sup>32</sup> If made, the election is irrevocable unless the court determines it is equitable to set aside.<sup>33</sup> The purchase price is the "fair value"<sup>34</sup> of the shares.<sup>35</sup> The parties are allowed 60 days from the election date to reach agreement as to the fair value and terms of purchase.<sup>36</sup> If the parties are unable to reach an agreement, then the court shall stay the dissolution proceedings and determine the fair value.<sup>37</sup> After determining the fair value, the court shall enter an order directing the purchase on such terms and conditions as the court deems appropriate.<sup>38</sup> The court will then dismiss the dissolution action, and the petitioning shareholder shall no longer have any rights or status as a shareholder except the right to receive the court-ordered payment(s).<sup>39</sup>

### **Judicial Dissolution of an LLC**

In comparison to the corporation statute, the LLC statute's provisions on judicial dissolution are much more vague. The LLC statute provides that a member may apply for judicial dissolution of the LLC "on the grounds that it is not reasonably practicable to carry on the limited liability company's activities and affairs in conformity with the limited

liability company agreement."<sup>40</sup> Such an action must be filed in the circuit court for the county in which the company's principal place of business within Alabama is located.<sup>41</sup> If the company does not have a principal place of business in Alabama, then the action must be filed in the circuit court for the county in which the company's most recent registered office is located.<sup>42</sup>

There is not much Alabama case law to explain what is meant by the standard of "not reasonably practicable."<sup>43</sup> Under the general partnership statute, the Alabama Supreme Court has held that it was "not reasonably practicable" to carry on a partnership when the partners and every witness testified that the partners could not work together, and there was also evidence that one partner was guilty of misconduct in breaching the partnership agreement.<sup>44</sup> If looking outside Alabama, Delaware is probably the best secondary resource.<sup>45</sup> In Delaware, the courts have explained:

The 'not reasonably practicable' standard does not require a petitioner to show that the purpose of the limited liability company has been completely frustrated. Rather, the standard is whether it is reasonably practicable for the company to continue to operate its business in conformity with its LLC Agree-

ment. Our law provides no blueprint for determining whether it is 'not reasonably practicable' for an LLC to continue, but several convincing factual circumstances have pervaded the case law: (1) the members' vote is deadlocked at the Board level; (2) the operating agreement gives no means of navigating around the deadlock; and (3) due to the financial condition of the company, there is effectively no business to operate. None of these factors are individually dispositive; nor must they all exist for a court to find it no longer reasonably practicable for a business to continue operating. While judicial dissolution of an LLC is a discretionary remedy that is granted sparingly, it has been granted in situations where there was 'deadlock' that prevented the entity from operating and where the defined purpose of the entity was impossible to carry out.<sup>46</sup>

What seems clear is that the meaning of the "not reasonably practicable" standard will be determined on a case-by-case basis, under the particular facts and circumstances of each case. As stated by the Delaware courts, there is no "blueprint" to follow. However, in any circumstance where there is unbreakable deadlock in the control of an LLC, there should be good grounds for judicial dissolution.

### **Effect of Dissolution**

#### **Effect of Dissolution of a Corporation**

Once dissolved, a dissolved corporation continues to exist, but its existence is solely for the purpose of winding up and liquidating its business and affairs.<sup>47</sup> Such activities may include collecting the corporation's assets, disposing of the corporation's properties, discharging the corporation's liabilities, making distributions to shareholders, and other necessary acts.<sup>48</sup> The corporation may still sue and be sued in its name.<sup>49</sup> Dissolution does not abate or suspend any pending lawsuits.<sup>50</sup>

The corporation statute provides procedures for disposing of claims against the corporation. For known claims, the corporation may dispose of the claims by providing a proper written notice to claimants and providing at least 120 days for claims to be submitted.<sup>51</sup> For unknown





claims, the corporation may publish a proper notice of its dissolution in a local newspaper of general circulation, requiring claims to be submitted within two years after the publication.<sup>52</sup>

### Effect of Dissolution of an LLC

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Winding up of an LLC may be managed by the person(s) designated in the company agreement, or, if none, by the remaining members, or, if none, by the holders of transferable interests.<sup>57</sup> On application of a member or transferee, the circuit court may supervise the winding up of the company.<sup>58</sup>

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Upon the winding up of an LLC, the company's creditors (including members who are creditors) have first priority for payment from the company's assets.<sup>61</sup> Only after creditors have been fully paid may there be any distributions to the company's members or holders of transferable interests.<sup>62</sup>

### Conclusion

When the party's over, it may be time for the business to come to an end. If all of the business's owners can agree (or have already agreed in the governing documents), then the process of a voluntary or automatic dissolution should be clear and (maybe) smooth. If that is not the case, then the law may provide a

shareholder or member the right to seek a judicial dissolution. A claim for judicial dissolution is one of the few protections that Alabama law provides to a non-controlling owner. Properly executed, a claim for judicial dissolution may allow a non-controlling owner to trigger a buy-out of his interest or a distribution by liquidation. Like climbing out the bathroom window, the disgruntled shareholder or member might find an escape from an otherwise bad party.

- 1 Ala. Code § 10A-2-14.02(a).
- 2 Ala. Code § 10A-2-14.02(b)(1).
- 3 Ala. Code § 10A-2-14.02(d).
- 4 Ala. Code § 10A-2-14.02(b)(2).
- 5 Ala. Code § 10A-2-14.02(e).
- 6 Ala. Code § 10A-2-14.02(c).
- 7 Ala. Code § 10A-2-14.02(f).
- 8 Id.
- 9 Ala. Code § 10A-5A-7.01.
- 10 Ala. Code § 10A-5A-7.01(a).
- 11 Ala. Code § 10A-5A-7.01(b).
- 12 Ala. Code § 10A-5A-7.01(c).
- 13 A "transferable interest" means a member's right to receive distributions from the LLC. Ala. Code § 10A-5A-1.02(s). A transferable interest is personal property and may be "transferred" (assigned, conveyed, gifted, etc.) from a member to a "transferee." Ala. Code §§ 10A-5A-1.02(q); 10A-5A-1.02(r); 10A-5A-5.01; 10A-5A-5.02.
- 14 Ala. Code § 10A-5A-7.01(c)(1).
- 15 Ala. Code § 10A-5A-7.01(c)(2).
- 16 Ala. Code §§ 10A-2-14.30; 10A-2-14.31.
- 17 Ala. Code § 10A-2-14.30(1).
- 18 Ala. Code § 10A-2-14.30(3).
- 19 Ala. Code § 10A-2-14.30(2).
- 20 Id.
- 21 Id.
- 22 *Abel v. Forrest Realty, Inc.*, 484 So. 2d 1069, 1072 (Ala. 1986); see also *Levine v. Beem*, 608 So. 2d 373, 374 (Ala. 1992).
- 23 Id. at 1071.
- 24 *Fulton v. Callahan*, 621 So. 2d 1235, 1253 (Ala. 1993).
- 25 Ala. Code § 10A-2-14.31(c).
- 26 Id.
- 27 Ala. Code § 10A-2-14.33.
- 28 Id.
- 29 Ala. Code § 10A-2-14.32.
- 30 Ala. Code § 10A-2-14.34.
- 31 Ala. Code § 10A-2-14.31(d).
- 32 Ala. Code § 10A-2-14.34(a).
- 33 Id.
- 34 "Fair value" is defined as "the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable." Ala. Code § 10A-2-13.01. "Fair value" is not "fair market value." Shannon P. Pratt, *Valuing a Business: The Analysis and Appraisal of Closely Held Companies* 917 (5th ed. 2008). This is an important distinction, as Alabama law will not allow the application of discounts in determining a "fair value" of shares. *Ex parte Baron Servs.*, 874 So. 2d 545, 551 (Ala. 2003).
- 35 Id.

- 36 Ala. Code § 10A-2-14.34(c).
- 37 Ala. Code § 10A-2-14.34(d).
- 38 Ala. Code § 10A-2-14.34(e).
- 39 Ala. Code § 10A-2-14.34(f).
- 40 Ala. Code § 10A-5A-7.01(d).
- 41 Id.
- 42 Id.
- 43 As of the time of writing this article, the author's search of LexisNexis for the phrase "not reasonably practicable" returned only six Alabama cases, none of which address the merits of judicial dissolution of an LLC.
- 44 *Bertolla v. Bill*, 774 So. 2d 497, 503-04 (Ala. 1999); *Cox v. F&S*, 489 So. 2d 516 (Ala. 1986); *Myrick v. Gladish*, 690 So. 2d 435 (Ala. Civ. App. 1997).
- 45 As reported by the Alabama Law Institute, many portions of Alabama's current LLC statute were derived from Delaware law. [[http://inform.alabama.gov/\\_ALI/PDF/Book/complete\\_projects/BE%202017.pdf](http://inform.alabama.gov/_ALI/PDF/Book/complete_projects/BE%202017.pdf)].
- 46 *GR Burgr, LLC v. Seibel* (In re *GR Burgr, LLC*), 2017 Del. Ch. LEXIS 156, \*11-12, 2017 WL 3669511 (Del. Ch. August 25, 2017) (internal citations and quotations omitted).
- 47 Ala. Code § 10A-2-14.05.
- 48 Id.
- 49 Id.
- 50 Id.
- 51 Ala. Code § 10A-1-9.21.
- 52 Ala. Code § 10A-1-9.22.
- 53 Ala. Code § 10A-5A-7.02.
- 54 Id.
- 55 Id.
- 56 Id.
- 57 Ala. Code § 10A-5A-7.03(a).
- 58 Ala. Code § 10A-5A-7.03(b).
- 59 Ala. Code § 10A-5A-7.04.
- 60 Ala. Code § 10A-5A-7.05.
- 61 Ala. Code § 10A-5A-7.06.
- 62 Id.



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