



Robert Shapiro, Plaintiff - Appellant
v.
Gabriel Ettenson, Defendant - Respondent.

NYS AD (1st Dept) 2017

FACTS:

This case involves three founding members who formed and began operating an LLC in January 2012 with no operating agreement. They subsequently negotiated and exchanged draft agreements but none was executed. In December 2013, two members acting by written consents and majority vote executed and adopted an operating agreement and filed amended articles of organization designating the LLC as manager-managed. The operating agreement authorized the members to approve, by majority vote, requests to members for additional capital contributions and the reduction of a member's percentage interest upon failure to contribute.

The third member, who never signed or otherwise approved the operating agreement and who claimed the members at inception orally agreed to act only by unanimous consent, sued to invalidate the operating agreement after the two other members approved a capital call and resolved to eliminate the third member's salary.

The lower court agreed with the majority members that LLC Law § 402(c)(3) ("except as provided in the operating agreement ... the vote of a majority in interest of the members entitled to vote thereon shall be required to ... adopt, amend, restate or revoke the articles of organization or operating agreement") authorizes the adoption of an operating agreement by vote of a majority in interest, and disagreed with the plaintiff member that LLC Law § 417 ("the members of a limited liability company shall adopt a written operating agreement ... before, at the time of or within ninety days after the filing of the articles of organization") requires the members' unanimous consent to adopt an operating agreement.

ISSUE:

1. May an operating agreement be adopted by the vote of a majority in interest of the members entitled to vote thereon?
2. Is an oral agreement regarding unanimity on this issue enforceable?
3. Can an operating agreement explicitly provide that a member's participating interest may be reduced proportionally if the member fails to make a requested additional capital contribution?

DECISION:

1. Yes
2. No, not in light of a written agreement.
3. Yes.

CONCLUSION:

Plaintiff argued that the LLC's operating agreement was invalid because its adoption was not unanimous.

However, New York Limited Liability Company Law § 402(c) provides that the operating agreement may be adopted by "the vote of a majority in interest of the members entitled to vote thereon."

Plaintiff further contended that the parties had an oral agreement regarding unanimity on this issue.

However, Limited Liability Company Law § 417 requires a written operating agreement, and where there is no operating agreement or the operating agreement fails to address issues in dispute, the default provisions under the Limited Liability Company Law govern.

Additionally, as such adopted operating agreement explicitly provided that a member's participating interest may be reduced proportionally if the member fails to make a requested additional capital contribution, defendants were acting in accordance with the agreement when they issued their "Notice of Call for Additional Capital Contributions from Members."

It should be noted that ironically, the same operating agreement that the plaintiff hoped to invalidate also provided him with a small measure of relief based on the agreement's provision stating that no compensation shall be paid to managers for their services, prompting the court to vacate the portion of the lower court's order declaring that the defendants were authorized to set their own salaries and reduce plaintiff's salary by majority vote.

Such relief may be fleeting, however, as the operating agreement also provides that it can be amended by written approval "in accordance with this Agreement and the LLC Law", which means there's apparently nothing to stop the majority members from again relying on § 402 (c) (3) to amend the agreement as they desire, to change the it's provision governing manager compensation.

All this means that if there isn't an operating agreement signed by all members when the LLC is formed, at any time thereafter, those holding a majority of the voting interests may adopt an operating agreement without the signature or consent of minority members.