LAW SEMINARS INTERNATIONAL

An Advanced One-Day Workshop on
Easements and CCRs

September 3, 2008
Seattle, WA

Dissolution of a Real Estate Limited Liability Company as a Technique to Avoid Liability After Ballard Square

Joseph P. McCarthy, Esq.
Stoel Rives LLP
Seattle, WA

DISSOLUTION OF A REAL ESTATE LIMITED LIABILITY COMPANY AS A TECHNIQUE TO AVOID LIABILITY AFTER BALLARD SQUARE

I. INTRODUCTION

This paper examines the risks faced by a real estate developer who attempts to limit exposure to construction defect claims by dissolving its development entity. Three cases decided by the Court of Appeals in 2007 make it clear that dissolving a limited liability company in order to avoid construction defect claims is a very risky strategy.

Residential real estate development is a risk-intensive business. Developers must manage a number of significant risks to create a successful project. Those risks include entitlement risks, construction cost risk, market risks, and construction quality and warranty risk. A developer who does not or cannot control or mitigate these risks is rolling the dice.

There has been significant condominium construction defect litigation in the past seven years in the Pacific Northwest. The litigation has fueled a string of appellate decisions that gave expansive interpretations to the implied warranties under the Washington Condominium Act.[1] As a result, by 2004 or so, the insurance industry stopped insuring developers and contractors for claims arising from condominiums. The legislature subsequently amended the Condominium Act to restore some balance to the Condominium Act[2] and the insurance crisis, as well as the amount of defect litigation, has abated somewhat. All of this activity, however, has caused developers to look at various ways to manage the risks of defect litigation and liability.

It goes without saying that the most basic technique for limiting liability in real property development is to use a limited liability company.[3] In the author's experience, many attorneys have counseled their clients to dissolve their limited liability entity prior to the expiration of the relevant statute of limitations for defect claims. The author and some others believe this strategy to be dangerous due to provisions of the Limited Liability Company Act relating to creditors rights. In 2005, however, Division I of the Court of Appeals published its opinion in Ballard Square Condominium Association v. Dynasty Constr. Co.[4] holding that claims against a corporation arising after its dissolution were barred. Afterwards, the advocates of dissolution seemed vindicated.

Less than a year after publication of the Ballard Square opinion, however, the legislature amended the Business Corporation Act and the Limited Liability Company Act to create

[1] Marina Cove Condominium Owners Association v. Isabella Estates, 109 WA.App.230,34P.3d 870(Div I, 2001); Park Avenue Condominium Owners Association v. Buchan Developments, LLC, 117 Wn.App.369, 71 P. 3d 692 (Div I, 2003).

[2] SSB 5556; HB 1848.

[3] The Limited Liability Company Act is found at Chapter 25.15 RCW. Liability protection is also available through the use of a business corporation. A corporation, for various reasons including the lack of pass-through tax attributes, is generally a poor vehicle for development of real estate. Therefore, this paper will focus on limited liability companies and will not discuss corporations. For a discussion of choice of entity in real estate development see Washington Real Property Desk book, Section 5.3.

[4] Ballard Square Condo. Owners Ass'n v. Dynasty Constr. Co., 126 Wash. App. 285, 108 P.3d 818 (Div. 1, 2005), aff'd Ballard Square 158 Wash2d 603, 146 P.3d 914 (2006).

a survival period for post-dissolution claims.[5] Then, in June of 2007, Division I of the Court of Appeals published a trio of cases[6] in which it combined the creditors' rights provisions of the Limited Liability Company Act with the new survival statute to assist home owners in bringing claims against condominium developers. These cases make it clear how disastrous a strategy of dissolution can be for a developer.

We will begin with an overview of the liability protections that are afforded to and withheld from individuals under the Limited Liability Company Act. We will then review the holding of Ballard Square. Finally, we will review the holdings in the three recent cases.

II. THE PROTECTIONS OFFERED (AND NOT OFFERED) BY LIMITED LIABILITY COMPANIES.

A. The Statutory Insulation from Liability To Third Parties is Limited in Scope

The Limited Liability Company Act generally, but not completely, insulates its members and managers from liability for the obligations of the entity. Section 125 of the Limited Liability Company Act states:

> (1) Except as otherwise provided by this chapter, the debts, obligations, and liabilities of a limited liability company, whether arising in contract, tort or otherwise, shall be solely the debts, obligations, and liabilities of the limited liability company; and no member or manager of a limited liability company shall be obligated personally for any such debt, obligation, or liability of the limited liability company solely by reason of being a member or acting as a manager of the limited liability company.

There are two exceptions to the elimination of personal liability. First, Section 125 is expressly subject to the other sections of the Limited Liability Company Act. For instance, the provisions dealing with dissolution and winding up a company's affairs contain a separate liability protection scheme for members and managers. This paper reviews those provisions in detail below. Second, the liability shield only operates to eliminate liability arising from the mere fact of being a member or manager. For instance, a member or manager is liable for its own torts under RCW 25.15.125(b). This concept is also found in the corporate context.[7]

---

[5] See RCW 25.15.303. See RCW 23B.14.340; S.B. 6596, 59th Leg., Reg. Sess. (Wash 2006).

[6] Chadwick Farms Owners Association v FHC, LLC, 160 P.3d 1061 (Div I, 2007); Maple Court Condominium Association v. Roosevelt, LLC, 160 P.3d 1068 (Div I, 2007); Emily Lane Homeowners Association v. Colonial Development, L.L.C., 160 P.3d 1073 (Div I 2007).

[7] See Grayson v. Nordic Constr. Co., 92 Wn.2d 548, 552-53, 599 P.2d 1271, 1273 (1979).

B. The Law of Fraudulent Conveyances Applies to Limited Liability Companies

The Limited Liability Company Act applies "fraudulent conveyance" principles to limited liability companies. The Limited Liability Company Act states:

> (1) A limited liability company shall not make a distribution to a member to the extent that at the time of the distribution, after giving effect to the distribution (a) the limited liability company would not be able to pay its debts as they became due in the usual course of business, or (b) all liabilities of the limited liability company, other than liabilities to members on account of their limited liability company interests and liabilities for which the recourse of creditors is limited to specified property of the limited liability company, exceed the fair value of the assets of the limited liability company, except that the fair value of property that is subject to a liability for which the recourse of creditors is limited shall be included in the assets of the limited liability company only to the extent that the fair value of that property exceeds that liability.
>
> (2) A member who receives a distribution in violation of subsection (1) of this section, and who knew at the time of the distribution that the distribution violated subsection (1) of this section, shall be liable to a limited liability company for the amount of the distribution. A member who receives a distribution in violation of subsection (1) of this section, and who did not know at the time of the distribution that the distribution violated subsection (1) of this section, shall not be liable for the amount of the distribution. Subject to subsection (3) of this section, this subsection (2) shall not affect any obligation or liability of a member under a limited liability company agreement or other applicable law for the amount of a distribution.
>
> (3) Unless otherwise agreed, a member who receives a distribution from a limited liability company shall have no liability under this chapter or other applicable law for the amount of the distribution after the expiration of three years from the date of the distribution unless an action to recover the distribution from such member is commenced prior to the expiration of the said three-year period and an adjudication of liability against such member is made in the said action.[8]

[8] RCW 25.15.235.

Thus, a limited liability company can claw back a distribution wrongfully received. The Limited Liability Company Act imposes, however, a three year statute of repose on actions for recovery. It is not clear from the statute whether commencement of an action within three years is sufficient or whether an adjudication of liability must be made within that period.

C. Piercing the Veil Applies to Limited Liability Companies

The concept of "piercing the veil" is also expressly incorporated in the Limited Liability Company Act. The Limited Liability Company Act states:

> Members of a limited liability company shall be personally liable for any act, debt, obligation, or liability of the limited liability company to the extent that shareholders of a Washington business corporation would be liable in analogous circumstances. In this regard, the court may consider the factors and policies set forth in established case law with regard to piercing the corporate veil, except that the failure to hold meetings of members or managers or the failure to observe formalities pertaining to the calling or conduct of meetings shall not be considered a factor tending to establish that the members have personal liability for any act, debt, obligation, or liability of the limited liability company if the certificate of formation and limited liability company agreement do not expressly require the holding of meetings of members or managers.[9]

Our courts have issued a number of opinions regarding "piercing the veil", or the "doctrine of disregard" as our courts seem to prefer to call it. Generally speaking, a corporate entity will be disregarded if two elements have been proven: (i) that there is such a commingling of property rights or interests to make it apparent that the corporation and some other entity (or person) were intended to function as one, and (ii) that to regard the corporation and the other entity as separate would aid the consummation of a fraud or wrong upon an other.[10] The first element involves shareholder abuse of the corporation. The second looks at whether the conduct has caused inequity or harm to third parties.

Piercing the veil is an equitable doctrine of great longevity and ubiquity in American law.[11] It is the perception of inequity in wrongful entity dissolutions that opens members and managers of a limited liability company to personal liability. It was also the

[9] RCW 25.15.060.
[10] Morgan v Burks, 93 Wn.2d 580, 585, 611 P.2d 751 (1980)
[11] See Matheson and Eby, The Doctrine of Piercing The Veil In An Era of Multiple Limited Liability Entities: An Opportunity To Codify The Test For Waiving Owners' Limited-Liability Protection, 75 Wash. L. Rev. 147 (2000).

perceived inequity of Ballard Square that caused the legislature to amend the Business Corporation Act and the Limited Liability Company Act.

D. Members and Managers Have Limited Protection From Creditors During Wind Up.

The Limited Liability Company Act provides a three step scheme for terminating a Limited Liability Company's existence. The first step is dissolution of the Limited Liability Company, the second step is winding up and the third step is cancellation. Each step is distinct and has distinct legal consequences.

1. Dissolution. Dissolution occurs upon (i) the termination date set forth in the certificate of formation, (ii) the happening of events specified in the operating agreement, (iii) the written consent of all members, (iv) ninety days after the dissociation of the last member, (v) the entry of a judicial decree of dissolution, or (vi) two years after an administrative dissolution by the Secretary of State.[12] Note that, except for the last two items, these dissolution events are private events for which there is no public notice.

Dissolution triggers an affirmative obligation to wind up the affairs of the entity. RCW 25.15.270 states:

> A limited liability company is dissolved and its affairs shall be wound up upon the first to occur of the following . . . .

2. Winding Up. Winding up may be conducted by the manager, members, the court or a receiver. The Limited Liability Company Act grants broad powers to the persons conducting the wind up. The statute lists those powers:

> Upon dissolution of a limited liability company and until the filing of a certificate of cancellation as provided in RCW 25.14.080 the persons winding up the limited liability company's affairs may, in the name of, and for and on behalf of, the limited liability company, prosecute and defend suits, whether civil, criminal, or administrative, gradually settle and close the limited liability company's business, dispose of and convey the limited liability company's property, discharge or make reasonable provision for the limited liability company's liabilities, and distribute to the members any remaining assets of the limited liability company.[13]

The Limited Liability Company Act also imposes duties on those persons to make provisions for creditors. Those duties include paying or providing for third party creditors before paying members or manager. They also include the affirmative duty to pay or provide for all known claims, whether conditional, contingent or un-matured. The statute states:

[12] RCW 25.15.270.
[13] RCW 25.15.295(2).

> A limited liability company which has dissolved shall pay or make reasonable provision to pay all claims and obligations, including all contingent, conditional, or unmatured claims and obligations, known to the limited liability company and all claims and obligations which are known to the limited liability company but for which the identity of the claimant is unknown. If there are sufficient assets, such claims and obligations shall be paid in full and any such provision for payment made shall be made in full. If there are insufficient assets, such claims and obligations shall be paid or provided for according to their priority and, among claims and obligations of equal priority, ratably to the extent of assets available therefore. Unless otherwise provided in a limited liability company agreement, any remaining assets shall be distributed as provided in this chapter. Any person winding up a limited liability company's affairs who has complied with this section is not personally liable to the claimants of the dissolved limited liability company by reason of such person's actions in winding up the limited liability company.[14]

The last section of the statute implies that a person who does not pay or provide for all claims is personally liable to the claimants. In other words, to keep the liability protections of the Limited Liability Company, the members and managers must properly wind up the company's affairs by making provision for unmatured claims.

3. Cancellation. The final step of the process is cancellation of the company. Upon the completion of the dissolution and wind-up, a "Certificate of Cancellation" must be filed with or by the Secretary of State. Under the Limited Liability Company Act:

> A certificate of cancellation shall be filed in the office of the secretary of state to accomplish the cancellation of a certificate of formation upon the dissolution and the completion of winding up of a limited liability company and shall set forth: (1) The name of the limited liability company; (2) The date of filing of its certificate of formation; (3) The reason for filing the certificate of cancellation; (4) The future effective date (which shall be a date not later than the ninetieth day after the date it is filed) of cancellation if it is not to be effective upon the filing of the certificate; and (5) Any other information the person filing the certificate of cancellation determines.[15]

Cancellation terminates the existence of a limited liability company as a "person" under the law. When the company is cancelled, it ceases to exist and no longer has the ability to act.

[14] RCW 25.15.300.
[15] RCW 15.15.080.

> A limited liability company formed under this chapter shall be a separate legal entity, the existence of which as a separate legal entity shall continue until cancellation of the limited liability company's certificate of formation.

These sections of the Limited Liability Company Act make it clear that the liability limitation of an Limited Liability Company depends on successful formation of the company, proper treatment of the company, property treatment of the company's creditors, and a healthy respect for equity.

III. THE BALLARD SQUARE DECISION: A GLIMMER OF OPPORTUNITY AND A LEGISLATIVE REACTION.

In Ballard Square the developer was a corporation. It built and sold all the units in a condominium by the end of 1992. The developer dissolved in 1995. In 1997, the condominium owners filed an insurance claim due to water intrusion problems. In 2002, the condominium association sued the developer for breach of contract.[16] The trial court dismissed the association's claims as untimely. The Court of Appeals was required to interpret the dissolution and survival provisions of the Business Corporation Act. It held that the statute provided a two-year period (commencing on dissolution) to bring actions against a corporation for causes of action accruing before dissolution. It held that the Business Corporation Act did not provide a survival period for claims that arose after dissolution. In the absence of a statute, the issue was governed by common law. The common law provided no such remedy. Therefore, the association's claims against the developer, which arose after dissolution, were barred.[17] The court recognized the inequity of its result and invited the legislature to revise the statute, Id. at 296, but the result was in.

Some attorneys argued that the Ballard Square holding should apply to limited liability companies as well. This argument was problematic because the Limited Liability Company Act did not contain a survival provision like the Business Corporation Act and because limited liability companies are not creatures of the common law and there is no common law to apply to them. Nevertheless, Ballard Square emboldened the advocates for aggressive dissolution as a liability management device since its result might tend to eliminate the risk of personal liability otherwise lurking in the Limited Liability Company Act.

Our Supreme Court took review of Ballard Square and affirmed the result in an opinion published in November of 2006.[18] Before that, however, the legislature amended the Business Corporation Act.[19] It also amended the Limited Liability Company Act to

[16] The cause of action was breach of a contractual provision to construct the condominium in accordance with the plans and specifications. 126 Wn. App. 285, 286. This cause of action was apparently chosen because claims for breach of implied and express warranties under the Condominium Act were time barred. See RCW 64.32.452.
[17] 126 Wn. App. 285 at 286-297.
[18] Ballard Square 158 Wash2d 603, 146 P.3d 914 (2006).
[19] RCW 23B.14.340.

provide a three year period for survival of claims against dissolved limited liability companies. The new section of the Limited Liability Company Act, RCW 25.15.303, became effective in June of 2006. It states:

> The dissolution of a limited liability company does not take away or impair any remedy available against that limited liability company, its managers, or its members for any right or claim existing, or any liability incurred at any time, whether prior to or after dissolution, unless an action or other proceeding thereon is not commenced within three years after the effective date of dissolution. Such an action or proceeding against the limited liability company may be defended by the limited liability company in its own name.

Note that the statute preserves actions against the company, its managers and its members. Note also that the statute preserves claims that arise both before and after dissolution. Finally, note the phrase "effective date of dissolution." Dissolution can occur

The legislative history makes it clear that the purpose of the bill is to protect homeowners from developers who dissolve their LLCs.[20] The bill passed the Senate and House without a single "no" vote.[21]

IV. THE PROBLEMS THAT CONFRONT A DEVELOPER FROM IMPROVIDENT DISSOLUTION OF AN LLC.

On June 18, 2007, our Court of Appeals published three opinions dealing with the survival of defect claims by condominium associations against dissolved limited liability companies.

A. Chadwick Farms: The Plaintiffs' Trifecta.

In Chadwick Farms, supra, FHC, LLC constructed the Chadwick Farms Condominiums. When the project was completed and the units sold, it ceased operations and did not submit its annual report or renewal fee to the Secretary of State. The Secretary issued a notice of administrative dissolution in March of 2003. In August of 2004, the condominium association brought a construction defect suit against FHC. Seven months later, in March of 2005, the Secretary of State cancelled FHC's certificate of formation.

In May of 2005, FHC filed third party claims against several contractors. FHC then moved for dismissal of the association's claims based on the fact that FHC was no longer a legal entity. The association moved to amend its complaint to include the members of the LLC. The trial court dismissed the action without addressing the motion to amend.

[20] Washington House Bill Report, 2006 Regular Session, Senate Bill 6531, Feb. 28, 2006; Washington Senate Bill Report, 2006, Regular Session, Senate Bill 6531, February 11, 2006.
[21] Washington Final Bill Report, 2006 Regular Session, Senate Bill 6531.

The Court of Appeals held that the 2006 amendment to the Limited Liability Company Act was remedial and was therefore retroactive. It held that the association therefore had three years from the date of dissolution to file the suit.[22] FHC argued that the 2006 amendment did not deal with claims against cancelled companies. It argued that since its legal existence ceased upon cancellation, it could not be sued. Therefore, upon cancellation any claims against it were abated. This argument finds support in Section 070(c) of the Limited Liability Company Act, which states that the company ceases to exist upon cancellation. The court rejected this argument. It stated that the amendments were remedial and should not be interpreted to allow cancellation to defeat the legislative intent.[23] The court therefore reversed the dismissal of the association's claims.

It went on, however, to rule that since FHC had been cancelled before it brought the third party claims against its contractors, it could not prosecute those claims. Under Section 295(2) of the Limited Liability Company Act, a company has power to sue and be sued after dissolution. Upon cancellation, however, it ceases to exist. The court also pointed out that Section 303, if it did anything to abate the effect of cancellation, only preserved claims against the company. By failing to reinstate itself after its dissolution, FHC lost its ability to bring claims, even though it was still subject to being sued.

Finally, the court held that the association should have been allowed to amend its complaint. The association argued that the members had failed to properly wind up FHC's affairs and were personally liable to FHC's creditors under RCW 25.15.300. The court agreed that the association had a colorable legal claim. It stated:

> While cancellation marks the end of a limited liability company as a separate legal entity, it does not necessarily follow that claims against the LLC or its managers or members also abate. Chadwick should have been permitted to amend its complaint. Thus, the trial court's failure to do so was an abuse of its discretion.[24]

FHC suffered the worst result imaginable. The claims against it were allowed. It was denied the ability to bring third party claims and its members were subjected to potential personal liability by creditors for failing to wind up the affairs of the entity during the dissolution period. Under Chadwick Farms, cancellation terminates a company's existence, sort of.

B. Emily Lane: Taking a Clear Stand on Personal Liability under Section 300.

In Emily Lane, supra, the developer LLC dissolved itself in December of 2004 and filed a certificate of cancellation (signed by all members) two weeks later. The opinion does not disclose anything about winding up of the business. The LLC apparently argued that it had completed the winding up.[25] The association argued that it had not properly

[22] Chadwick Farms, 160 P.3d 1061 at 1066.
[23] Id. at 1066.
[24] Id. at 1068.
[25] Emily Lane, supra at 1074.

conducted the winding up.[26] The condominium association filed suit against the LLC in July of 2005, seven months after cancellation and eight months after dissolution.[27] The trial court allowed the suit against the LLC to proceed, but dismissed the claims against the members of the LLC.[28]

On appeal, the court held that the claims against the LLC could proceed because the 2006 amendments were retroactive. It stated that the 2006 amendment:

> Applies retroactively and permits actions against that LLC even if the LLC maintains it completed the winding up process and cancelled its certificate of formation.[29]

This statement makes it clear that neither the winding up nor cancellation of an LLC bars claims during the three years.

The court also reversed the dismissal of the claims against the members and managers of the LLC. The court did not have a well-developed record on the dismissal so it did not know the basis for the dismissal. It held, however, that a dismissal based solely on the LLC structure was improper. The court noted that members and managers can be personally liable under the equitable principles of piercing the veil and for improperly winding up the company's affairs. The court stated:

> As noted in *Chadwick*, other provisions of the Act provide that it is only when the members carry out a *proper* dissolution in winding up the company, that they are not personally liable. Thus, the converse would necessarily be true. That is, any person winding up an LLC's affairs who has not complied with RCW 25.15.300 may be personally liable to claimants. The members of Colonial may be liable for their failure to properly wind up the company.
>
> The possibility of piercing the veil of an LLC (thus permitting personal liability of its members) was envisioned at the time the statute was enacted. Perceiving such an eventuality, the Washington State Trial Lawyers Association was instrumental in requiring that the LLCA provide a statutory vehicle for piercing the LLC veil. Because case law did not create such a vehicle, a section was added to the legislation that permitted courts to consider factors and policies set forth in established case

[26] Id. at 1076.
[27] Emily Lane, supra. at 1077
[28] Id. at 1074.
[29] Id.

> law with regard to piercing the corporate veil in the context of an LLC.[30]
>
> The court accepted the implication of liability in Section 300. Its decision confirms that both the statute and the common law doctrine of piercing provide grounds for personal liability of members and managers to third parties.

IN reaching this result, the court appears to have been influenced by the conduct of the Limited Liability Company's members. The following excerpt from the opinion is revealing:

"In June 2005, Colonial's bookkeeper notified the insurance carrier of a possible claim against the LLC:

'The Notice of Claim to the insurance company may be a moot point. The LLC was dissolved effective 1/21/05 and therefore there is nothing to sue! We did not receive the Notice of Claim prior to the dissolution so we should be clear according to our attorney. Rejoice!
Pat'

Emily Lane argues that Colonial's aggressive pursuit of litigation after it was cancelled precludes Colonial from cloaking itself in the limited liability cloak afforded to it by the LLCA. Emily Lane provided this court with examples of letters, discovery and affirmative defenses that Colonial pursued even while it was rejoicing over being clear of liability."[31]

C. Maple Court: In Case There Was Any Doubt . . . .

In Maple Court Seattle Condominium Association v. Roosevelt, LLC, supra, the development LLC was administratively dissolved by the Secretary of State in September of 2002. Fifteen months later, in December of 2003, the condominium owners filed suit against the LLC. In July of 2004, the LLC filed a third-party complaint against its construction manager, Steinvall, and a number of subcontractors. Two months later, in September of 2004, the LLC was cancelled by the Secretary of State. Six months after being cancelled, the LLC and Steinvall settled with the owners. They then sought to recover from the subcontractors, the settlement amounts they had paid to the owners. The trial court dismissed their claims against the subcontractors.[32]

The company was sued and it filed its own suit while it was in "wind-up" mode. The company settled the lawsuit against it after it had been cancelled. The Court of Appeals held that upon cancellation, the company lost the ability to pursue the lawsuit against the subcontractors. . The LLC argued that it should be allowed to wind up its affairs even

[30] Id. at 1076.
[31] Emily Lane, 100 P.2d 1973 at _____.
[32] Maple Court, 160 P.3d 1068 at 1070.

though it was a cancelled company. Essentially, its argument was that cancellation precludes reinstatement but does not preclude completion of the winding up. The court disagreed with this argument. It looked to the language of Section 295, which states:

> Upon dissolution of a limited liability company and until the filing of a certificate of cancellation as provided in RCW 25.14.080 the persons winding up the limited liability company's affairs may . . . prosecute and defend suits, whether civil, criminal, or administrative, gradually settle and close the limited liability company's business, dispose of and convey the limited liability company's property, discharge or make reasonable provision for the limited liability company's liabilities, and distribute to the members any remaining assets of the limited liability company.

The language of Section 295 by itself would also appear to prevent payment of the settlement amount after cancellation. After all, the ability to defend, as well as pursue, lawsuits ceases upon cancellation. The court did not address that issue, however. The court did note, however, that the company could have applied for reinstatement at any time and would have been free to continue business as normal.[33]

The Court of Appeals also affirmed the dismissal of Steinvall's claims against the subcontractors. The condominium owners did not sue Steinvall. The only claims against Steinvall were those of the Limited Liability Company. Once the Limited Liability Company was cancelled, it was not a legal entity and had no valid claims against Steinvall. Since Steinvall's claims were derivative, it also had no valid claims.[34]

> None of this matters, however, because the homeowners association never filed a claim against Steinvall. Thus, any settlement that Steinvall made was on behalf of Roosevelt and was gratuitous since Roosevelt was not a legal entity and could not pursue a claim against Steinvall. Since Roosevelt could not maintain an action against Steinvall, there was no duty for Steinvall to pay Roosevelt. Since Steinvall had no duty to pay Roosevelt, none of the subcontractors had a duty to pay Steinvall. Steinvall's payment to Roosevelt for its share of the settlement is nothing more than a volunteer payment.[35]

Since Steinvall failed to recognize Roosevelt's disability, it wasted its money. Those who deal with cancelled Limited Liability Companies, do so at their own peril.

V. CONCLUSION

Chadwick Farms, Emily Lane and Maple Court make the following points clear. First, upon dissolution of a Limited Liability Company, the members or managers must wind

[33] Id. at 1072.
[34] Id. at 1072.
[35] Id. at 1072-73.

up the affairs of the company. Failure to do so violates the Limited Liability Company Act. Second, cancellation of the company's existence does not terminate claims pending against it. Claims may be brought against a non-existent Limited Liability Company. Cancellation does, however terminate the company's ability to bring claims against others because the Limited Liability Company no longer exists. Third, a member or manager who fails to properly wind up the affairs of a dissolved Limited Liability Company is personally liable to the creditors of the Limited Liability Company for its conduct in winding up the business.

It is clear that terminating a Limited Liability Company —whether affirmatively or passively—as a strategy for avoiding claims is extremely risky. The Limited Liability Company will still be subject to suit during the three year survival period but it may be unable to take action to protect its interests. It could have both hands tied behind its back. Moreover, the members of the Limited Liability Company may face personal liability for failing to properly wind down the business.

The guidance that these cases offer to the developer's attorney is simple. If a Limited Liability Company will be dissolved, the members or manager must make reasonable provision for conditional, contingent and unmatured claims. This means estimating the likelihood of payment and setting aside funds or other sources of payment, to the extent available to pay those claims. There is very little guidance on what constitutes "reasonable provision" for these claims or when a claim is "known". Developers should consider insurance, reserve funds, warranty funds and holdbacks as tools to use during wind up. The fundamental question presented, however, is whether setting aside such reserves or insurance actually constitutes a winding up or whether winding up requires settlement or other resolution of all known claims.

Without settlement or other resolution of claims, a winding up does not prevent a homeowners association from suing the Limited Liability Company. A properly wound up Limited Liability Company —whether cancelled or not—would theoretically present whatever assets it still had to the creditor. The members and managers of the Limited Liability Company would not, however, be in a secure position for two reasons. First, the Limited Liability Company could not bring third-party claims if it had been cancelled. Its ability to defend itself is thus limited. Second, the members and managers face the risk of personal liability for improperly winding up the business. It seems better to avoid dissolution entirely. Prior to dissolution, there is no duty to wind up or make provision for claims, and the members avoid the risk of personal liability from an improper wind up. The members then only face the risks of piercing the veil and fraudulent conveyance—the ordinary risks they face every day that they conduct through the limited liability company form.