MINORITY RIGHTS AND DISSOLUTION

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BUSINESS ORGANIZATIONS:
Tax and Legal Aspects Compared
LLCs, S Corporations and C Corporations

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MINORITY RIGHTS AND DISSOLUTION

I. INTRODUCTION

In many respects, the rights of minority owners under New York law governing limited liability companies differs from the rights afforded to minority shareholders under New York's Business Corporation Law.

This outline addresses: (1) the protections afforded to minority shareholders under the Business Corporation Law ("BCL"); (2) corporate dissolution under the BCL; (3) the protections afforded to minority members under New York's Limited Liability Company Law ("LLCL"); and (4) the dissolution of LLCs under the LLCL. Recent cases and comparisons to Delaware laws are addressed throughout.

II. MINORITY SHAREHOLDER PROTECTIONS UNDER THE BUSINESS CORPORATION LAW

Several BCL provisions provide minority shareholders with statutory rights under circumstances where minority shareholders are excluded from participation in corporate affairs.

A. Fiduciary Duty of Majority Shareholders

In closely held corporations, majority shareholders owe a fiduciary duty to minority shareholders to treat them fairly and in good faith. In re Kemp & Beatley (Gardstein), 64 N.Y.2d 63, 69-70 (1984). "Predicated on the majority shareholders' fiduciary obligation to treat all shareholders fairly and equally, to preserve corporate assets, and to fulfill their responsibilities of corporate management with 'scrupulous good faith,' the courts' equitable power can be invoked when 'it appears that the directors and majority shareholders have so palpably breached the

fiduciary duty they owe to the minority shareholders that they are disqualified from exercising the exclusive discretion and the dissolution power given to them by statute.'" Id.

B. Preemptive Rights

Under the concept of preemptive rights, majority shareholders may not issue new shares in the corporation if it dilutes the voting power of the minority, without giving the minority shareholders the first right to purchase the issued shares. BCL § 622(b)(1); Katzowitz v. Sidler, 24 N.Y.2d 512, 518 (1969). This enables minority shareholders to maintain their ownership percentage. Preemptive rights apply to voting shares and equity shares for companies incorporated before February 22, 1998. For entities incorporated after February 22, 1998, there is no statutory preemptive right unless provided for in the certificate of incorporation. BCL § 622(b)(2).

C. Shareholder Derivative Suits

Any shareholder may bring a derivative suit on behalf of the corporation against its officers and directors. BCL § 626(a); Marx v. Akers, 88 N.Y.2d 189, 193 (1996). "By their very nature, shareholder derivative actions infringe upon the managerial discretion of corporate boards." Marx, 88 N.Y.2d at 194. In general, prior to filing suit, the plaintiff must first make a demand upon the corporation's board to take action against the officers or directors. Id. If, however, such a demand would be futile, the plaintiff may proceed without placing the demand. Id. at 198. "[T]he object is for the court to chart the course for the corporation which the directors should have selected, and which it is presumed that they would have chosen if they had not been actuated by fraud or bad faith." Id. at 194. If the shareholder succeeds, the proceeds belong to the corporation. BCL § 626(e). However, the shareholder may be awarded reasonable expenses, including attorney's fees. BCL § 626(e).

D. Rights of Appraisal and Payment

Minority shareholders can require the corporation to buy back their stock at fair value in a number of situations. Shareholders are entitled to a buy-out if the certificate of incorporation is amended in such a way that: (1) alters or abolishes any preferential right of preferred shares; (2) creates, alters or abolishes any provision or right in respect to the redemption of such shares or any sinking fund for the redemption or purchase of such shares; (3) alters or abolishes preemptive rights; or (4) excludes or limits voting rights. BCL § 806(b)(6).

A shareholder can also require a corporation to buy back the stock in the event of a merger, consolidation, sale, lease, exchange or other disposition of all or substantially all of the corporation's assets. BCL § 910.

III. CORPORATE DISSOLUTION UNDER THE BUSINESS CORPORATION LAW

A. Dissolution Under BCL § 1103: Shareholder's Petition

Under BCL § 1103, the holders of shares representing at least ten percent of the votes of the outstanding shares may call a meeting to consider a resolution for involuntary dissolution. BCL § 1103(b); In re Bernfeld, 86 A.D.3d 244, 255 (2d Dep't 2011). The certificate of incorporation may authorize a lesser proportion of shares. BCL § 1103(b). The resolution may be adopted by a majority vote at a meeting of shareholders, if the shareholders find that the corporation's "assets are not sufficient to discharge its liabilities, or that they deem a dissolution to be beneficial to the shareholders." BCL § 1103(a) and (c). The shareholders may then present a petition for corporate dissolution. BCL § 1103(a).

B. Dissolution Under BCL § 1104: Shareholder or Director Deadlock

Under BCL § 1104, the holders of one-half of the outstanding shares may present a petition for dissolution on the basis of shareholder or director deadlock. BCL § 1104(a). The three grounds for such dissolution are as follows:

> (1) That the directors are so divided respecting the management of the corporation's affairs that the votes required for action by the board cannot be obtained.
> (2) That the shareholders are so divided that the votes required for the election of directors cannot be obtained.
> (3) That there is internal dissension and two or more factions of shareholders are so divided that dissolution would be beneficial to the shareholders.

BCL § 1104(a).

"In determining whether dissolution is in order, the issue is not who is at fault for a deadlock, but whether a deadlock exists." In re Dream Weaver Realty, Inc., 70 A.D.3d 941, 942 (2d Dep't 2010). "Rather, the critical consideration is the fact that dissension exists and has resulted in a deadlock precluding the successful and profitable conduct of the corporation's affairs." Id. (holding that dissolution was proper when the dissension between two shareholders "posed an irreconcilable barrier to the continued functioning and prosperity of the corporation").

Additionally, under § 1104(c), any shareholder entitled to vote "may present a petition for dissolution on the ground that the shareholders are so divided that they have failed, for a period which includes at least two consecutive annual meetings, to elect successors to directors whose terms have expired." BCL § 1104(c); Nelkin v. H. J. R. Realty Corp., 25 N.Y.2d 543, 549 (1969) (holding that the failure to hold shareholders' meetings was not sufficient grounds for dissolution unless the shareholders are so divided that they cannot elect directors).

C. Dissolution Under BCL § 1104-a: Special Circumstances

BCL § 1104-a "provides minority shareholders in close corporations with protection from oppressive conduct by majority interests." In re Seagroatt Floral Co., Inc., 78 N.Y.2d 439, 444 (1991). Under this provision, the holders of at least twenty percent of all outstanding shares may petition for judicial dissolution in special circumstances, such as oppressive acts by the majority shareholders. BCL § 1104-a; Seagroatt, 78 N.Y.2d at 444. A shareholder vote is not required. BCL § 1104-a. The grounds for dissolution are: (1) the directors or officers have committed illegal, fraudulent or oppressive actions towards the complaining shareholders, or (2) the corporate assets are being looted, wasted or diverted for non-corporate purposes by its directors, officers or those in control of the corporation. BCL § 1104-a(a).

The court will consider whether dissolution is the only feasible way to achieve a fair return for the minority shareholders. BCL § 1104-a(b). In doing so, the courts take into account: "(1) whether liquidation of the corporation is the only feasible means whereby the petitioners may reasonably expect to obtain a fair return on their investment; and (2) whether liquidation of the corporation is reasonably necessary for the protection of the rights and interests of any substantial number of shareholders or of the petitioners." BCL § 1104-a(b).

"The purpose of this involuntary dissolution statute is to provide protection to the minority shareholder whose reasonable expectations in undertaking the venture have been frustrated and who has no adequate means of recovering his or her investment." Kemp & Beatley, 64 N.Y.2d at 74.

Oppression includes conduct by a majority shareholder that "substantially defeats expectations that, objectively viewed, were both reasonable under the circumstances and were central to the [oppressed shareholder's] decision to join the venture.'" Id. at 73. Reasonable

expectations in a closely held corporation include continued employment and input in the management of the company. Id. at 71, 74.

Following the commencement of a § 1104-a dissolution proceeding, if the majority shareholders wish to continue operating the business and avoid dissolution, they may elect, within 90 days, to buy-out the minority shareholders by paying fair value for their shares. BCL § 1118(a); In re Penepent Corp., Inc., 96 N.Y.2d 186, 191 (2001).

1. Determining the Fair Value of the Oppressed Shareholder's Interest

Many shareholder agreements include a provision setting forth the price to be paid in the event of a buy-out. See, In re of Pace Photographers, 71 N.Y.2d 737, 741 (1988). In dissolution proceedings brought under § 1104-a, "the terms of a shareholders' agreement governing a voluntary sale of stock by a shareholder to the corporation *do not* dictate the 'fair value' of a minority interest" under § 1118. Pace, 71 N.Y.2d at 741 (emphasis added). Instead, the court will "fix the fair value of petitioner's shares as of the day prior to the filing of the petition" under § 1104-a. Pace, 71 N.Y.2d at 748.

Minority shareholder's stock must be treated equally. Penepent, 96 N.Y.2d at 194. A minority shareholder's stock must not be discounted because of its minority status. Id. "To impose upon petitioning minority shareholders a penalty because they lack control would violate two 'central equitable principles of corporate governance.' First, a minority discount would deprive minority shareholders of their proportionate interest in the corporation as a going concern. Second, it would result in shares of the same class being treated unequally." Id. (quotation omitted).

In the event of a disagreement over the determination of the fair value of the shares, "the court, upon the application of such prospective purchaser or purchasers or the petitioner, may

stay the proceedings brought pursuant to section 1104-a of this chapter and determine the fair value of the petitioner's shares as of the day prior to the date on which such petition was filed." BCL § 1118(b). The petitioner may be awarded interest from "the date the petition is filed to the date of payment for the petitioner's share." Id.

However, BCL § 1118 neither defines fair value, nor sets forth criteria to determine fair value. Seagroatt, 78 N.Y.2d at 445. Fair value depends on the circumstances of each case. Id. "The objective in calculating 'fair value' is to determine 'what a willing purchaser in an arm's length transaction would offer for petitioners' interest in the company as an operating business." Penepent, 96 N.Y.2d at 193 (quotation omitted).

Additionally, "[t]he court may order stock valuations be adjusted and may provide for a surcharge upon the directors or those in control of the corporation upon a finding of willful or reckless dissipation or transfer of assets or corporate property without just or adequate compensation therefore." BCL § 1104-a(d).

The petitioner remains a shareholder until his or her shares are purchased. In re Davis, 174 A.D.2d 449, 452 (1st Dep't 1991). See also, In re Spiefogel, 237 B.R. 555, 560-61 (E.D.N.Y. 1999) (holding that the petitioning shareholder was entitled to collect dividends until his shares were actually paid for).

D. Common Law Corporate Dissolution

There is also a common law right of judicial dissolution of a corporation. A corporation may be dissolved under the common law when the officers or directors breach their fiduciary duty to the minority shareholders. In re Dubonnet Scarfs, Inc., 105 A.D.2d 339, 341 (1st Dep't 1985). Dissolution may be ordered when "majority shareholders engage in egregious breaches of fiduciary duties" owed to minority shareholders. White v. Fee, No. 57828/11, 2012 WL

2360934, at *3 (Sup. Ct. Westchester County June 7, 2012). "[T]o obtain a common law dissolution, the plaintiff must demonstrate 'that the majority of the corporation seek to carry it on for the purpose of enriching themselves at the expense of the minority.'" Id. at *15 (quoting Fontheim v. Walker, 282 A.D. 373, 375–376 (1st Dep't 1953)).

The court may order dissolution if "the directors or those in control of the corporation are looting the corporate assets to enrich themselves at the expense of the minority shareholders; continuing the corporation solely to benefit those in control; or that the actions of the directors or those in control has been calculated to depress the capital of the corporation in order to coerce the minority shareholders to sell their stock at a depressed price." Shapiro v. Rockville Country Club, Inc., No. 15308-02, 2004 WL 398980, at *5 (Sup. Ct. Nassau County Feb. 23, 2004). The court may order dissolution even if the corporation is operating profitably. White, No. 57828/11, 2012 WL 2360934, at *15.

A minority shareholder holding less than twenty percent of outstanding shares may bring an action for dissolution under the common law. Lewis v. Jones, 107 A.D.2d 931, 933-34 (3d Dep't 1985) (holding that a minority shareholder who only owned 19% of the shares could bring action seeking common law dissolution of the corporation based on allegations of fraud, misappropriation and use of corporate assets for personal gain).

E. Dissolution Under the Delaware General Corporation Law

In Delaware, the board of directors may authorize dissolution as follows:

> If it should be deemed advisable in the judgment of the board of directors of any corporation that it should be dissolved, the board, after the adoption of a resolution to that effect by a majority of the whole board at any meeting called for that purpose, shall cause notice of the adoption of the resolution and of a meeting of stockholders to take action upon the resolution to be mailed to each stockholder entitled to vote thereon as of the record date for determining the stockholders entitled to notice of the meeting.

8 Del. C. § 275. If the majority of shareholders vote for in favor of dissolution, the corporation will be dissolved. Id. The shareholders may also authorize dissolution without action by the directors. Id.

For close corporations, the certificate of incorporation may include a provision granting to any stockholder "an option to have the corporation dissolved at will or upon the occurrence of any specified event or contingency." 8 Del. C. § 355.

If there are only two stockholders, each of whom own 50% of the stock, and they are "unable to agree upon the desirability of discontinuing such joint venture and disposing of the assets used in such venture," either stockholder may petition the court for dissolution. 8 Del. C. § 273(a).

IV. MINORITY SHAREHOLDER PROTECTIONS UNDER THE LIMITED LIABILITY COMPANY ACT

A. LLCs Generally

The New York Limited Liability Company Law ("LLCL") was enacted in 1994. LLCL § 101. An LLC is a "business form combining corporate-type limited liability with partnership tax advantages and organizational characteristics." Tzolis v. Wolff, 10 N.Y.3d 100, 118 (2008). The advantages of the LLC form may "render the partnership, limited partnership and closely held corporation obsolete." Peter A. Mahler, When Limited Liability Companies Seek Judicial Dissolution, Will the Statute Be Up to the Task?, N.Y. St. B.J. at 8 (2002).

However, the LLC statute lacks many of the protections available to minority shareholders under the BCL. Douglas K. Moll, Minority Oppression & the Limited Liability Company: Learning (or Not) from Close Corporation History, 40 Wake Forest L. Rev. 883, 887 (2005). Thus, if there are not provisions protecting minority shareholders in the operating agreement, in many cases there will not be a default remedy under the LLC statute.

The only remedy codified in the LLC statute is dissolution, either by the consent of a majority or by a court order when it is not reasonably practicable to carry on the business. LLCL §§ 701 and 702. Thus, a court can refuse to grant dissolution if the business is profitable and can continue to be run by majority rule, even if the minority members are being oppressed. See e.g., Horning v. Horning Const., LLC, 12 Misc. 3d 402, 412-13 (Sup. Ct. Monroe County 2006) (dismissing a dissolution proceeding because the LLC was still turning a profit, despite continued in-fighting and animosity among the members which resulted in lower profits).

B. Fiduciary Duties of Managing Members

Managing members of LLCs owe a fiduciary duty to the non-managing members. Pokoik v. Pokoik, 115 A.D.3d 428, 429 (1st Dep't 2014). Under LLCL § 409, a "manager shall perform his or her duties as a manager . . . in good faith and with that degree of care that an ordinarily prudent person in a like position would use under similar circumstances." LLCL § 409. This "is the same fiduciary standard applied to corporate directors." In re Die Fliedermaus LLC, 323 B.R. 101, 110 (S.D.N.Y. 2005). "It is elemental that a fiduciary owes a duty of undivided and undiluted loyalty to those whose interests the fiduciary is to protect. This is a sensitive and inflexible rule of fidelity, barring not only blatant self-dealing, but also requiring avoidance of situations in which a fiduciary's personal interest possibly conflicts with the interest of those owed a fiduciary duty." Pokoik v. Pokoik, 115 A.D.3d 428, 429 (1st Dep't 2014) (quoting Birnbaum v. Birnbaum, 73 N.Y.2d 461, 466 (1989)).

The following elements must be established in an action for breach of fiduciary duty: (1) the existence of a fiduciary relationship; (2) misconduct by the defendant; (3) and damages directly caused by the defendant's misconduct. Pokoik v. Pokoik, 115 A.D.3d 428, 429 (1st Dep't 2014) (holding that a managing member breached his fiduciary duty by unilaterally

depleting non-managing member's capital accounts in order to address a tax situation, where the managing member had an interest in reducing the non-managing member's capital accounts). See also Nathanson v. Nathanson, 20 A.D.3d 403, 404 (2d Dep't 2005) (finding that allegations of self-dealing by a managing member of an LLC were sufficient to state a cause of action for breach of fiduciary duty).

C. Shareholder Derivative Suits

Derivative suits by LLC members are not explicitly available under the LLCL. However, the Court of Appeals has interpreted the LLCL to allow for derivative suits. Tzolis v. Wolff, 10 N.Y.3d 100, 102, 105 (2008) ("To hold that there is no remedy when corporate fiduciaries use corporate assets to enrich themselves was unacceptable in 1742 and in 1832, and it is still unacceptable today"). An LLC member may bring a derivative action on the LLC's behalf even though the LLC statute does not provide for this. Id. at 118, 121. "Courts have repeatedly recognized derivative suits in the absence of express statutory authorization . . . In light of this, it could hardly be argued that the mere absence of authorizing language in the Limited Liability Law bars the courts from entertaining derivative suits by LLC members." Id. at 106.

The pre-suit demand required by BCL § 626(c) is also a condition precedent to a derivative action involving an LLC, unless it can be shown that such a demand would be futile. Barone v. Sowers, 128 A.D.3d 484, 484 (1st Dep't 2015).

D. Equitable Accounting

An LLC member also has a common law right to seek an equitable accounting even though the LLC statute does not provide for that remedy. Gottlieb v. Northriver Trading Co., LLC, 58 A.D.3d 550, 550 (1st Dep't 2009).

E. Right of Inspection

Members of LLCs have a statutory right to inspect the LLC's books and records. LLCL § 1102; Gartner v. Cardio Ventures, LLC, 121 A.D.3d 609, 610 (1st Dep't 2014).

F. Fair Value Appraisal

Upon withdrawal as a member of an LLC, the "withdrawing member is entitled to receive any distribution to which he or she is entitled under the operating agreement and, if not otherwise provided in the operating agreement, he or she is entitled to receive, within a reasonable time after withdrawal, the fair value of his or her membership interest in the limited liability company as of the date of withdrawal based upon his or her right to share in distributions from the limited liability company." LLCL § 509. The member has the right to commence an action to determine the fair value of his membership interest in the LLC. Man Choi Chiu v. Chiu, 125 A.D.3d 824, 825 (2d Dep't 2015) leave to appeal denied sub nom. Chiu v. Chiu, 26 N.Y.3d 905 (2015).

V. DISSOLUTION OF LIMITED LIABILITY COMPANIES

A. Dissolution Under LLCL § 701

An LLC may be dissolved upon the first of the following to occur: (1) the latest date on which the LLC is to dissolve, provided in the articles of organization, or at a time specified in the operating agreement; (2) the happening of events specified in the operating agreement; (3) the vote or written consent of at least a majority of the members or a greater or lesser percentage as required in the operating agreement; (4) when there are no members; or (5) the entry of a decree of judicial dissolution under LLCL § 702. LLCL § 701(a). The "death, retirement, resignation, expulsion, bankruptcy or dissolution of any member or the occurrence of any other event that

terminates the continued membership of any member shall not cause the limited liability company to be dissolved or its affairs to be wound up." LLCL § 701(b).

"Absent written consent or formal vote of a majority of members, the only means of dissolution recognized by the operating agreement and applicable statute was by judicial dissolution." Matter of Beverwyck Abstract, LLC, 53 A.D.3d 903, 904 (3d Dep't 2008) (holding that the only way to dissolve the LLC was through judicial dissolution because there was no formal vote or written consent of the majority of the members as required to dissolve the LLC under § 701).

B. Dissolution Under LLCL § 702

"Dissolution under the Limited Liability Law is not as easy as dissolution under the Business Corporation Law." Horning v. Horning Const., LLC, 12 Misc. 3d 402 (Sup. Ct. Monroe County 2006). Under LLCL § 702,

> [o]n the application by or for a member, the supreme court in the judicial district in which the office of the limited liability company is located may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement.

LLCL § 702. Even if the statutory standard is met, the court has discretion whether to dissolve an LLC. Horning, 12 Misc. 3d at 410.

"[T]he dissolution of a limited liability company under LLCL 702 is initially a contract-based analysis." In re 1545 Ocean Ave., LLC, 72 A.D.3d 121, 128 (2d Dep't 2010). "[U]nlike the judicial dissolution standards in the Business Corporation Law and the Partnership Law, the court must first examine the limited liability company's operating agreement to determine, in light of the circumstances presented, whether it is or is not reasonably practicable

for the limited liability company to continue to carry on its business in conformity with the operating agreement." Id.

The absence of a dissolution provision in the operating agreement "leaves the court with no choice but to apply the strict Limited Liability Company Law § 702 standard." Horning, 12 Misc. 3d at 410. Thus, without a robust operating agreement, judicial dissolution is only possible "whenever it is not reasonably practicable to carry on the business" even if minority members are oppressed and even if there is extreme animosity between the members. Id. See also, Spires v. Casterline, 4 Misc. 3d 428, 433 (Sup. Ct. Monroe County 2004) (refusing to dissolve an LLC because the operating agreement failed to provide a basis for its dissolution upon the request of one of its members. Rather, the agreement only stated that the company was to be managed by one or more members, and any one of the members could have managed the company).

1. The Risk of Insolvency is a Proper Ground for Judicial Dissolution

If continued operation of the LLC would lead to insolvency, the courts will allow dissolution. Mizrahi v. Cohen, 104 A.D.3d 917, 920 (2d Dep't 2013), leave to appeal dismissed, 21 N.Y.3d 968, 992 N.E.2d 421 (2013). In Mizrahi, two equal members formed an LLC, and they initially made equal capital contributions. Id. at 918. Over time, however, the contributions by the plaintiff greatly exceeded those of the defendant, with the plaintiff contributing $1.4 million, and the defendant contributing only $317,000. Id. at 919. The LLC experienced net operating losses every year and would have failed were it not for the capital infusions by the plaintiff. Id. The court granted the application for judicial dissolution because continuing to operate the LLC was financial unfeasible. Id. at 920.

The court in Mizrahi also ordered a buy-out of the defendant's interest upon the dissolution of the LLC, even though the LLC law "does not expressly authorize a buyout in a dissolution proceeding" because a buy-out was an appropriate equitable remedy in this circumstance. Id. at 920.

2. Breach of Fiduciary Duty by Majority Members is not a Proper Ground for Judicial Dissolution

Breaches of the majority shareholders' fiduciary duties or oppressive acts by the majority shareholders are insufficient grounds for judicial dissolution of LLCs. Widewaters Herkimer Co., LLC v. Aiello, 28 A.D.3d 1107, 1107-08 (4th Dep't 2006) (dismissing a dissolution action alleging that the majority members breached their fiduciary duty to the minority shareholders and engaged in oppressive conduct towards them because those are not proper grounds for dissolution of an LLC).

The expulsion of a member has been found to be an insufficient ground for judicial dissolution. Doyle v. Icon, LLC, 103 A.D.3d 440, 440 (1st Dep't 2013). In Doyle, the plaintiff alleged that he has been systematically excluded from the operation and affairs of the company by defendants. Id. The court held that the expulsion of a member is insufficient to establish that it is no longer "reasonably practicable" for the company to carry on its business. Id. The court reasoned that the stated purpose of the entity could still be achieved, and that continuing the entity was financially feasible because the company was profitable. Id. Instead of dissolving the LLC, the court stated that plaintiff must reply upon his other (presumably non-statutory) causes of action. Id. at 441.

3. Shareholder Deadlock is an Insufficient Basis for Judicial Dissolution

Even though the Court of Appeals created the right of derivative suits for LLCs in 2008 (see Tzolis v. Wolff, 10 N.Y.3d 100, 102, 105 (2008)), New York courts have refused to extend

to LLCs the dissolution protections found in the BCL. See, e.g., In re 1545 Ocean Ave., LLC, 72 A.D.3d 121, 131 (2d Dep't 2010). To prevail in a judicial dissolution action, the plaintiff must show that "the management of the entity is unable or unwilling to reasonably permit or promote the stated purpose of the entity to be realized or achieved, or that continuing the entity is financially unfeasible." Doyle v. Icon, LLC, 103 A.D.3d 440, 440 (1st Dep't 2013).

In 1545 Ocean, the managers of an LLC disagreed about construction work performed on the LLC property and about the hiring of one of the manager's construction businesses to perform the work. 1545 Ocean, 72 A.D.3d at 131. The Second Department refused to apply concepts from the BCL and limited the available remedies to those found in the LLC Act. Id. The court stated that dissolution standards for corporations do not apply to LLCs in the determination of whether it is not reasonably practicable to carry on the business, because the legislature chose not to adopt the corporate standard when it enacted LLC statute in 1994 and left the standard unchanged when it enacted amendments in 1999. Id. The court held that dissolution of an LLC requires a showing of either a failed purpose or financial unfeasibility. Id.

Thus, although shareholder deadlock is a basis, by itself, for judicial dissolution under BCL § 1104, no such independent ground for dissolution exits under LLCL § 702. 1545 Ocean, 72 A.D.3d at 131. "The court will not dissolve an LLC merely because the LLC has not experienced a smooth glide to profitability or because events have not turned out exactly as the LLC's owners originally envisioned . . . . [D]issolution is reserved for situations in which the LLC's management has become so dysfunctional or its business purpose so thwarted that it is no longer practicable to operate the business, such as in the case of a voting deadlock or where the defined purpose of the entity has become impossible to fulfill." Id. (quotation omitted).

4. Extreme Animosity Between the Members is an Insufficient Basis for Judicial Dissolution

Even if there is extreme hostility and animosity between the members, as long as the company if profitable, the court will not dissolve the LLC. Horning v. Horning Const., LLC, 12 Misc. 3d 402 (Sup. Ct. Monroe County 2006) (refusing to dissolve a profitable company doing business without an operating agreement [because the members had disagreed about the proposed terms] even though the animosity between the members had negatively impacted its profitability); Natanel v. Cohen, 43 Misc. 3d 1217(A), 988 N.Y.S.2d 524 (Sup. Ct. 2014) (refusing to dissolve an LLC on the basis of animosity between the members).

C. Dissolution by Arbitration

Many operating agreements contain provisions requiring arbitration of disputes. There is case law indicating that an application for judicial dissolution of an LLC can – and in some cases must – be made in an arbitration proceeding if the operating agreement provides for arbitration. In Cusimano, the Second Department affirmed a motion to stay a § 702 dissolution proceeding and compel arbitration because there was a "valid agreement to arbitrate that expressly and unequivocally encompassed" dissolution of the LLC. Cusimano v. Berita Realty, LLC, 103 A.D.3d 720, 721 (2013). See also, Hoffman v. Finger Lakes Instrumentation, LLC, 7 Misc.3d 179, 186-87 (Sup. Ct. Monroe County 2005) (holding that the disaffected members of an LLC were required to arbitrate their claims for dissolution because there was a broad arbitration provision in the LLC's operating agreement). But see Mizrahi v. Cohen, No. 3865/10, 2012 WL 104775, at *5 (Sup. Ct. Kings County Jan. 12, 2012), aff'd as modified, 104 A.D.3d 917 (2d Dep't 2013), leave to appeal denied, 21 N.Y.3d 968 (2013) (noting that an application for "judicial dissolution of the LLC can only be determined by the court" (i.e., not an arbitration panel)).

D. Delaware Limited Liability Company Act

The Delaware LLC Act is firmly grounded on principles of freedom of contract. 6 Del. C. § 18-1101(b); Haley v. Talcott, 864 A.2d 86, 96 (Del. Ch. 2004).

Delaware law provides for an LLC to be dissolved upon any of the following events occurring: (1) at a time specified in a limited liability company agreement; (2) upon the happening of events specified in the LLC agreement; (3) upon the vote or written consent of members who own more than two-thirds of the interest in the profits of the LLC; (4) if there are no members; or (5) the entry of a decree of judicial dissolution under § 18-802. 6 Del. C. § 18-801.

Under § 18-802, the court may dissolve a limited liability company "whenever it is not reasonably practicable to carry on the business in conformity with a limited liability company agreement." 6 Del. C. § 18-802. In Delaware, as in New York, even if "there are no facts under which the LLC could carry on business in conformity with the LLC Agreement, the remedy of dissolution . . . remains discretionary." Haley, 864 A.2d at 93 (Del. Ch. 2004). Like New York courts, Delaware courts "will not dissolve an LLC merely because the LLC has not experienced a smooth glide to profitability." Matter of Arrow Inv. Advisors, LLC, 2009 WL 1101682, at *1-2 (Del. Ch. Apr. 23, 2009).

However, unlike New York courts, the Delaware courts have found dissolution to be appropriate in situations of member deadlock. Delaware courts will order dissolution when: "(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." Fisk Ventures, LLC v. Segal, 2009 WL 73957, at *4 (Del. Ch. Jan. 13, 2009) aff'd, 984 A.2d 124 (Del. 2009) (holding that dissolution was

appropriate because there was a member deadlock and no mechanism in the operating agreement to circumvent the stalemate). See also Haley, 864 A.2d at 93 (dissolving an LLC because the two members were hopelessly deadlocked, despite the existence of a detailed exit remedy in the LLC agreement, because the exit mechanism did not "equitably effect the separation of the parties.").