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SUPREME COURT

COMMONWEALTH OF KENTUCKY
KENTUCKY SUPREME COURT
CASE NO. 2011-SC-000587

RICK PANNELL **APPELLANT**

v.

APPEAL FROM
COURT OF APPEALS
CASE NO. 2010-CA-001172
and
FAYETTE CIRCUIT COURT
CIVIL ACTION NO. 06-CI-03131

ANN SHANNON AND
ELEGANT INTERIORS, LLC **APPELLEES**

BRIEF OF APPELLEES ANN SHANNON AND ELEGANT INTERIORS, LLC

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned does hereby certify that copies of this Brief were served upon the following named individuals by United States Mail, first class, postage prepaid on this the 11th day of December, 2012: Carroll M. Redford, III, Susan Y.W. Chun, and Michelle L. Hurley, Miller, Griffin & Marks, P.S.C., 271 West Short Street, Suite 600, Lexington, Kentucky 40507; Hon. Kimberly N. Bunnell, Judge, Fayette Circuit Court, 521 Robert F. Stephens Courthouse, 120 N. Limestone Street, Lexington, Kentucky 40507; Hon. Samuel P. Givens, Jr., Clerk of Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, Kentucky 40601. The undersigned does certify that the record on appeal was not withdrawn by the undersigned from the Fayette Circuit Court Clerk.

Christopher L. Thacker

STATEMENT CONCERNING ORAL ARGUMENT

The issues on appeal are matters solely of law. Appellees Ann Shannon and Elegant Interiors, LLC therefore do not believe oral argument is necessary. This is especially true given that the General Assembly has now supplemented the language of the controlling statute in a manner that clearly ratifies the holding of the lower courts in this case.

COUNTERSTATEMENT OF POINTS AND AUTHORITIES

COUNTERSTATEMENT OF THE CASE

Appellee/Defendant Ann Shannon established her home furnishings and decoration business,[1] Elegant Interiors, LLC, as a limited liability company in January 2000.[2] On or about March 4, 2004, Plaintiff/Appellant Rick Pannell, a commercial landlord, entered into a written commercial lease agreement with Elegant Interiors, LLC.[3] As reflected by his preprinted name on the cover, which contained a blank for the "Tenant" and other details, the Lease was executed using a form provided by Plaintiff/Appellant.[4]

"Elegant Interiors, LLC" is written into the blank for "Tenant" on the cover page of the Lease.[5] The very first paragraph of the Lease also expressly identified Elegant Interiors, LLC as the sole tenant under the Lease. That paragraph states as follows (bold emphasis added):

> THIS LEASE AGREEMENT ("Lease"), made this 4th day of Feb., 2004 between Rick Pannell, landlord, having his principal office at 2200 Brannon Road, Nicholasville, Kentucky 40356 ("Landlord"), and **Elegant Interiors, a LLC corporation,** with offices at 198 Moore Dr., Suite 104 Lex, Ky 40503 **("Tenant")**.[6]

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[1] *See* Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), p.10, R.A. 346.

[2] *See* Certificate of Existence, Exhibit A to Defendant's Motion for Summary Judgment, R.A. 344, attached hereto as Exhibit A.

[3] The "Lease", attached hereto as Exhibit B, R.A. 10.

[4] *Id.*

[5] *Id.*

[6] *Id.*, p. 1, R.A. 13.

Additionally, Shannon signed the Lease on the last page in a signature block below the heading containing the defined term "TENANT" on a line with the pre-printed preface "By:".[7]

A separate bank account was maintained by and for Elegant Interiors, LLC, and rents due under the Lease between Elegant Interiors, LLC and Plaintiff/Appellant were paid with checks drawn from Elegant Interiors, LLC's corporate account.[8]

Sometime after Elegant Interiors, LLC had begun operating in the premises, the parties observed that foot traffic at this location was not as large as they had anticipated; the parties therefore agreed to divide the premises into two leasable units and to find a second tenant for part of the space.[9] And in early 2006, the parties found a chiropractor who was interested in leasing part of the space that had been leased to Elegant Interiors, LLC.[10]

Shannon prepared a short "release" setting forth the basic agreement regarding the division of the premises and agreeing to agree on a "new lease." This document was not a new lease, or itself an amendment to the prior Lease, but rather explicitly states that "upon acceptance of this document, a new lease will be signed."[11] Furthermore, the

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[7] *Id.* at 16, R.A. 28.

[8] *See* Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), pp. 21-24, R.A. 347.

[9] *Id.* at pp. 47- 48, R.A. 348.

[10] *Id.* at p. 50, lines 10 – 14, R.A. 349.

[11] The "Release", attached hereto as Exhibit C, R.A. 69.

Release stated that apart from the specific space and rent changes to be agreed to by the parties, "all other stipulations will remain the same as in the initial lease."[12]

The "new lease" anticipated by the Release was in effect an amendment to the Lease to reduce the amount of space rented to Elegant Interiors, LLC. This amendment was accomplished on or about March 2, 2006, by inserting the changes to the terms of the Lease into the original lease form—the parties took the original Lease and crossed-out the changed amended terms and wrote in the new terms by hand. Thus the original Lease and the "new lease" are the same document, which is attached as Exhibit B.

The amended terms included editing the date of execution in the initial paragraph quoted above; altering the term of the Lease from 36 months to "13 months, 9 days"; and altering the amount of square footage and the amount of the rent.[13] No other terms in the Lease were altered or amended, and the Lease as amended retained a "Complete Agreement" provision stating that "[t]his writing contains the entire agreement between the parties hereto[.]"[14]

No amendment or alteration was made to the portion of the Lease defining the "Tenant" as Elegant Interiors, LLC; and the amended Lease was executed with new signatures immediately above the original ones in the signature blocks. At no time did

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[12] *Id.*

[13] Lease, page 1-2, R.A. 13-14 (Exhibit B hereto).

[14] *Id.*, p. 16, ¶ 46, R.A. 28.

Shannon ever agree to be personally liable for the debts of Elegant Interiors, LLC generally or for the Lease between Elegant Interiors, LLC and Rick Pannell specifically.[15]

Elegant Interiors, LLC continued to operate out of the leased premises after the amendments to the Lease in March 2006, and to pay rent from its corporate account, just has it had before, until June 20, 2006.[16]

Elegant Interiors, LLC was administratively dissolved in the fall of 2005 for the inadvertent failure to file the LLC's annual report and pay the annual report fee of $15.00, which was a result of Shannon's failure to update the mailing address for Elegant Interiors, LLC with the Secretary of State.[17] That dissolution was "canceled" by the Secretary of State, and Elegant Interiors, LLC was reinstated in August 2006.[18] Elegant

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[15] *See* Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), pp. 79-80, R.A. 350.

[16] *See, e.g.*, Complaint ¶ 6 (alleging that Elegant Interiors, LLC, breached the Lease by, *inter alia*, "failing to pay rent for the months of June and July, 2006"), R.A. 2; Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), pp. 77, R.A. 350 (Elegant Interior, LLC conducted business "right up until a couple of days right before" vacating the premises).

[17] Notices for Elegant Interiors, LLC, were sent to Shannon as its sole member. Shannon had changed her residential address the previous year. As a result, the notices regarding Elegant Interiors LLC's annual report and dissolution were sent to the wrong address and ultimately not delivered. *See* Notice Envelope marked "return to sender" R.A. 9 and Certificate of Dissolution, attached to Appellant's Brief as Exhibit "7", R.A. 8 (containing Shannon's previous mailing address). *See also* Statement of Change updating the address filed with the Application for Reinstatement on August 11, 2006, https://app.sos.ky.gov/corpscans/33/0486433-06-99999-20060811-SCG-1076069-PU.pdf

[18] *See* Certificate of Existence, Exhibit A to Defendant's Motion for Summary Judgment, R.A. 344, attached hereto as Exhibit A.

Interiors, LLC vacated the premises on June 20, 2006,[19] after a dispute with Plaintiff/Appellant regarding the pace and disruption caused by renovations to divide the premises pursuant to the Lease amendments in March 2006.[20]

In the action below, the Circuit Court granted Plaintiff/Appellant summary judgment against Elegant Interiors, LLC for breach of the Lease, as amended on March 2, 2006, while holding that Shannon was not personally liable for the breach by Elegant Interiors, LLC. In denying Plaintiff/Appellant's motion to alter, amend, or vacate, the Circuit Court explained:

> The Court holds that, as a matter of law, the final and controlling lease agreement between the parties was the lease agreement with amendments made and dated March 2, 2006. The first paragraph of this amend lease defines the "Tenant" as "Elegant Interiors, a LLC corporation" [sic]. Accordingly, the Tenant, and the party assuming the obligations of Tenant, under the amended lease remained the Limited Liability Company.
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> Further, the Court holds that regardless of the administrative dissolution of the LLC on November 1, 2005, pursuant to KRS 275.295(3) the reinstatement of Elegant Interiors, LLC, on August 11, 2006 (before the entry of any judgment in this matter), related back to the time of its administrative dissolution. Accordingly, the amendments to the lease on behalf of the LLC are effective "as if the administrative dissolution had never occurred." *See Fairbanks Arctic Co. v. Prather & Assoc., Inc.*, 198 S.W.3d 143, 146 (Ky. App. 2005). Therefore, the Court declines to vacate its previous ruling which held that

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[19] The Plaintiff/Appellant's forcible detainer action was unopposed, and, in fact, neither Shannon nor Elegant Interiors were served with the Complaint in that action because it was sent to Shannon's previous home address. *See* Forcible Detainer Petition, Exhibit C to Plaintiff's Motion to Alter, Amend, or Vacate, R.A. 526; and Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), p. 77, R.A. 350.

[20] S*ee, e.g.,* May 2006 Letter from Counsel for Elegant Interiors, LLC describing disruption and declaring "constructive eviction." R.A. 33.

> Defendant Ann Shannon is not personally liable for any of Plaintiff's claimed damages.[21]

The Plaintiff/Appellant appealed from the Circuit Court's holding that Appellee/Defendant Shannon "is not personally liable for any of Plaintiff's claimed damages" for breach of the Lease.

On appeal the Kentucky Court of Appeals affirmed by its opinion dated August 26, 2011. This Court subsequently granted Plaintiff/Appellant's Motion for Discretionary Review.

ARGUMENT

The Lease upon which Plaintiff/Appellant bases his claims was always between himself and Elegant Interiors, LLC, a Kentucky limited liability company. The Lease, in both its original and amended form, unambiguously defines Elegant Interiors, LLC as the "Tenant." Defendant/Appellee Ann Shannon was never a party to the Lease, nor did she ever personally guarantee the obligations of Elegant Interiors, LLC under the Lease. Because a member of a limited liability company may not be held liable for the debts of the company unless the member has ***unequivocally*** agreed to such liability in writing, and because reinstatement of an administratively dissolved limited liability company "relates

[21] Order entered April 20, 2009, R.A. 618-619.

back" "as if the administrative dissolution ... had never occurred,"[22] the Circuit Court correctly held that Shannon is not personally liable for any damages claimed by Plaintiff/Appellant under the Lease.

I. SHANNON IS NOT LIABLE FOR ELEGANT INTERIORS, LLC'S OBLIGATIONS UNDER THE LEASE.

The fundamental benefit of operating a business as a LLC, a limited liability company, is that the LLC status shields the individual member or members of the LLC from personal liability for the business's debts. "An LLC is an unincorporated business structure that combines the business advantages of a corporation with the income tax advantages of a partnership. The centerpiece of the LLC is its provision for limited liability for its members and managers in regard to the debts and obligations of the LLC[.]"[23]

The liability shield applies regardless of how the LLC's obligations arise. As KRS 275.150 explains, there is no personal liability unless the member agrees in writing to be liable for the LLC's debt:

> no member, manager, employee, or agent of a limited liability company [] shall be personally liable by reason of being a member, manager, employee, or agent of the limited liability company, under a judgment, decree, or

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[22] At all relevant times to this appeal, the controlling statute was KRS 275.295(3)(c) ("[T]he reinstatement [of a limited liability company] shall relate back to and take effect as of the effective date of the administrative dissolution, and the limited liability company shall resume carrying on business as if the administrative dissolution had never occurred."). The statute has since been repealed and re-enacted as KRS 14A.7-030(3). As discussed below, the statute was revised in 2012 in part to reaffirm the holdings of *Fairbanks Arctic Co. v. Prather & Assoc., Inc.*, 198 S.W.3d 143, (Ky. App. 2005) and of the Court of Appeals in this case.

[23] Rutledge and Booth, "The Limited Liability Company Act: Understanding Kentucky's New Organizational Option", 83 Ky. L.J. 1, 6 -7 (1995).

> order of a court, agency, or tribunal of any type, or in any other manner, in this or any other state, or on any other basis, for a debt, obligation, or liability of the limited liability company, whether arising in contract, tort, or otherwise.

This Court recently reaffirmed that "KRS 275.150 emphatically rejects personal liability for an LLC's debt unless the member or members, as the case may be, have agreed through the operating agreement or another written agreement to assume personal liability. ***Any such assumption of personal liability, which is contrary to the very business advantage reflected in the name 'limited liability company', must be stated clearly in unequivocal language which leaves no room for doubt about the parties' intent.***"[24]

When forming her business, Elegant Interiors, LLC, Ann Shannon consciously chose to form it as a limited liability company in order to protect herself from the possibility of personal liability for the business's obligations.[25] She observed all "corporate" formalities relevant to this case. In particular, in the very fist paragraph of the Lease—the form of which was provided by the Plaintiff/Appellant as Landlord—the agreement clearly identified Elegant Interiors, LLC as the sole Tenant assuming the obligations under the Lease. Similarly, the signature block in the Lease indicated that the signature "by" Ann Shannon was on behalf of the "Tenant," which the first paragraph defined as Elegant Interiors, LLC.[26] There is no mention whatsoever of a personal

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[24] *Racing Inv. Fund 2000 v. Clay Ward Agency*, 320 S.W.3d 654, 659 (Ky. 2010).

[25] *See* Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), p. 11, R.A. 346.

[26] Lease, pages 1 & 16, R.A. 13 & 28 (Exhibit B hereto).

guaranty by Shannon. Accordingly, as the Circuit Court recognized, there is no basis for holding Shannon liable for damages caused by the breach the Lease.

II. PURSUANT TO KRS 275.295(3)(C)'S PLAIN LANGUAGE, ELEGANT INTERIORS, LLC'S REINSTATEMENT "RELATES BACK" TO ALL ACTIONS TAKEN ON BEHALF OF THE LLC DURING THE PERIOD OF ADMINISTRATIVE DISSOLUTION.

In this Appeal, Plaintiff/Appellant does not argue directly that the "corporate veil" should be pierced,[27] but rather tries to reach the same result by arguing that because Elegant Interiors, LLC was administratively dissolved for a period due to the inadvertent failure to file an annual report, Shannon as its managing-member is therefore exposed to personal liability for the LLC's obligations during the period of administrative dissolution. But, by statute, administrative dissolution, which is a mere administrative act,

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[27] Plaintiff did make a direct piercing argument below to no avail. Under Kentucky law, two elements must be proven before the corporate veil will be pierced pursuant to the alter ego theory:

> (1) that the corporation is not only influenced by the owners, but also that there is such unity of ownership and interest that their separateness has ceased; *and* (2) that the facts are such that adherence to the normal attributes, viz, treatment as a separate entity, of separate corporate existence would sanction a fraud or promote injustice.

White v. Winchester Land Dev. Corp., 584 S.W.2d 56, 61-62 (Ky. App. 1979) (citations omitted) (emphasis added).

There is no evidence whatsoever supporting either element in this case. While the first element is difficult to apply in the context of a member-managed LLC, the evidence shows that Elegant Interiors, LLC was a separate entity conducting business apart from Ann Shannon's personal affairs. *See* Rutledge and Booth, 83 Ky. L.J. 1, 6-7 ("[T[he LLC permits all owners to participate in management without waiving liability protection."). For instance, Elegant Interiors, LLC had its own bank account. As to the second element, there is nothing to suggest that Shannon created or used Elegant Interiors, LLC for any fraudulent purpose. Furthermore, given the fact that by the terms of the Lease he himself drafted, Plaintiff/Appellant was always aware of the fact that his Lease was with the limited liability company, adherence to the normal rules of limited liability in this case does not promote injustice, but rather furthers the public policy embodied in the LLC statutes.

does not result in any such loss of liability protection. KRS 275.295(3)(c) provided that, "the reinstatement [of a limited liability company] shall relate back to and take effect as of the effective date of the administrative dissolution, and the limited liability company shall resume carrying on business **as if the administrative dissolution had never occurred**." Elegant Interiors, LLC was reinstated in 2006.[28] The administrative dissolution relied upon by Plaintiff/Appellant is therefore a nonevent under Kentucky law.

A. Because after reinstatement it is "as if the administrative dissolution ... had never occurred" ordinary limited liability principles apply in this case.

Elegant Interiors, LLC admittedly was temporarily administratively dissolved. However, it was reinstated on August 11, 2006 and that reinstatement, and the plain language of KRS 275.295(3)(c), established that Shannon cannot be held personally liable for actions taken in the name of Elegant Interiors, LLC.

Immunity from personal liability is one of the hallmarks of corporate or limited liability company law. Indeed, KRS 275.150, "Immunity from personal liability," establishes that:

> (1) ... [N]o member, manager, employee, or agent of a limited liability company ... shall be personally liable by reason of being a member, manager, employee, or agent of the limited liability company ... for a debt, obligation, or liability of the limited liability company, whether arising in contract, tort, or otherwise.

Plaintiff/Appellant claims that Shannon is not entitled to KRS 275.150 immunity simply because Elegant Interiors, LLC was temporarily administratively dissolved. Yet that was cured when the Kentucky Secretary of State reinstated Elegant Interiors, LLC on

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[28] *See* Certificate of Existence, Exhibit A to Defendant's Motion for Summary Judgment, R.A. 344, attached hereto as Exhibit A.

August 11, 2006. The plain language of the reinstatement statute, KRS 275.295, shows that reinstatement of Elegant Interiors, LLC relates back to, and takes effect as of, the date of administrative dissolution. In other words, the statute itself states that the limited liability company is to be treated as having never been dissolved in the first place. Specifically, KRS 275.295 provided, in pertinent part:

> (3) A limited liability company administratively dissolved under subsection (2) of this section ... may apply to the Secretary of State for reinstatement at any time after the effective date of dissolution ...
>
> (c) When the reinstatement is effective, the reinstatement shall relate back to and take effect as of the effective date of the administrative dissolution, and the limited liability company shall resume carrying on business as if the administrative dissolution had never occurred.

Thus, as the Court of Appeals held in *Fairbanks Arctic Blind Co. v. Prather & Associates, Inc.*, the General Assembly "intended for reinstatement to restore a corporation to the same position it would have occupied had it not been dissolved and that reinstatement validates any action taken by a corporation between the time it was administratively dissolved and the date of its reinstatement."[29]

1. The overwhelming weight of authority interpreting KRS 275.295 support the Circuit Court's holding in this case.

Relying on the reasoning of *Fairbanks,* the United States District Court for the Eastern District of Kentucky rejected the very argument that Plaintiff/Appellant now relies on, to wit, that individual LLC members are personally liable for acts undertaken on the LLC's behalf during a period of administrative dissolution later cured by reinstatement:

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[29] 198 S.W.3d 143, 146 (Ky. App. 2005).

> At oral argument, Plaintiff emphasized the language of the statute that provides that, upon reinstatement, the limited liability company shall resume carrying on business, thereby implying that the Kentucky legislature only intended that LLC members receive LLC protection after the reinstatement. The Court rejects Plaintiff's tortured reading of the statute for a couple of reasons. First, if the legislature wanted to include that caveat in the statute, they could have done so, and second, the Court believes the plain and ordinary meaning of the statute controls. **By including the language that the reinstatement relates back to the date of the administrative dissolution, the Court believes the legislature meant what it said, to wit, that a § 275.295 reinstatement cures the dissolution, and that cure is effective as of the date of dissolution.**
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> * * *
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> The situation herein is similar [to that in *Fairbanks*], where the alleged tortious conduct occurred while the LLC was administratively dissolved but then reinstated later. **If contracts that were entered into on behalf of the dissolved corporation in *Fairbanks* were deemed valid by the Kentucky Court of Appeals, the Court believes Kentucky courts would similarly conclude when asked to interpret the LLC statute. As a result, Cosmo's LLC and its members will be able to take advantage of the limited liability that K.R.S. § 275.150(1) provides.**[30]

This Memorandum Order in the case of *Eve v. Cosmo's LLC, et al.*, is highly instructive, as it deals with the very issue and statute at issue in this case. It also further evidences that, based on the plain language of KRS 275.295, the Circuit Court correctly determined that immunity from personal liability should be available to Shannon for actions taken on behalf of the LLC during the period of administrative dissolution because Elegant Interiors, LLC had been reinstated.

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[30] *Eve v. Cosmo's LLC, et al.*, Case No. 06-188-DLB, Memorandum Order at pp. 9-10 (E.D. Ky. Mar. 27, 2008)(emphasis added), attached hereto at tab 1.

Plaintiff/Appellant relies heavily on the unpublished opinion in the case of *Forleo v. American Products of Kentucky*,[31] to argue that "relating back" does not include the statutory right of "immunity." That opinion reasoned that the corporation law equivalent of KRS 275.295(3)(c) was "silent" on the issue of personal liability, and focused on the "shall resume" language, without effectively addressing the "relate back to" and "take effect as of the effective date" language of the statute. The *Forleo* court also did not address the 2005 published opinion in *Fairbanks Arctic Co. v. Prather & Assoc., Inc.*,[32] which rejected focusing on the "resume" language, and instead, recognized that "**[s]imply put, the General Assembly meant what it said, that upon reinstatement, "it is 'as if the administrative dissolution ... had never occurred.'**"[33]

Forleo is also factually distinguishable from the present case. In *Forleo*, the corporation was not reinstated until after the trial court had already entered judgment against the individual defendants.[34] Then, the reinstatement was raised for the first time in a motion to alter or amend.[35] Here, Elegant Interiors, LLC was reinstated in August

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[31] 2005-CA-000196, 2006 WL 2788429 (Ky. App. 2006) (unpublished). The *Forleo* opinion is attached here to under tab 2.

[32] 198 S.W.3d 143 (Ky. App.).

[33] *Id.*, 198 S.W.3d at 146 (quoting KRS 271B.14-220(3)) (emphasis added).

[34] *Forleo* at 2.

[35] *Id.*

2006,[36] nearly four years before the Circuit Court entered its order of summary judgment against Elegant Interiors, LLC, on May 25, 2010.[37]

In any event, to the extent that *Forleo* conflicts with the rule as announced in *Fairbanks*, and with express statutory authority, it is unpersuasive. As explained by United States District Judge Jennifer Coffman in *eServices, LLC v. Energy Purchasing, Inc.*,[38] an opinion specifically addressing the apparent conflict between the two cases, *Fairbanks* correctly reflects Kentucky law regarding the effect of reinstatement. Judge Coffman specifically addressed and rejected Plaintiff/Appellant's suggestion that *Forleo* should apply when an obligation arising during the period of administrative dissolution is sought to be enforced against a reinstated entity and its members, while *Fairbanks* applies when it is the reinstated entity that is seeking to enforce the obligation.

As Judge Coffman explained, pursuant to the rule announced in *Fairbanks*, "the reinstatement statute, as applied, grants amnesty for business actions taken by the corporation during the dissolution, which is inconsistent with *Forleo*'s punitive application of the [dissolution] statute."[39] Therefore, Judge Coffman rejected eServices' argument (which is identical to Plaintiff/Appellant's argument here) "that both

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[36] *See* Certificate of Existence, Exhibit A to Defendant's Motion for Summary Judgment, R.A. 344, attached hereto as Exhibit A.

[37] R.A. 626.

[38] No. 11-198-JBC, 2012 WL 404957 (E.D. Ky. Feb. 6, 2012) (holding that under Kentucky law "administrative reinstatement also reinstates limited liability for acts taken during the period of dissolution" so that corporate officer was not personally liable on contracts signed while corporation was administratively dissolved) attached hereto at tab 3.

[39] *Id.* at 6.

interpretations can exist simultaneously, with the *Fairbanks* decision applying only to actions taken by the corporate entity and thereby entitling eServices to sue Energy Purchasing, and the *Forleo* decision applying only to actions taken by individual officers, directors, or shareholders and thereby entitling eServices to sue [an officer] in his individual capacity, is inconsistent with Kentucky law and attempts to insert a distinction into the statute that is not present on its face."[40]

The considerably less well-reasoned opinion of the United States District Court for the Eastern District of Tennessee to the contrary in the case of *Dolphin Offshore Partners., L.P. v. Indus. Res. Corp.*[41] appears to have been largely driven by that federal court's belief that it was bound to apply *Forleo*, "whether unpublished or not" as "the best indicant of Kentucky law on this point."[42]

However, the federal court in *Dolphin* lacked the benefit of either the Court of Appeal's opinion in this case, Judge Coffman's analysis in *eServices*, or the holding of the Kentucky Court of Appeals earlier this year in in *Harshman Constr. & Elec., Inc. v. Witte*.[43] In *Harshman*, the Court of Appeals again expressly applied *Fairbanks* to hold

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[40] *Id.*

[41] 499 F. Supp. 2d 1025 (E.D. Tenn. 2007).

[42] *Id.* at 1027.

[43] 2011–CA–000609–MR, 2012 WL 2471445 (Ky. App., June 29, 2012) (unpublished). Copy attached hereto at tab 4.

that shareholders and officers of a corporation are not liable for corporate obligations that are undertaken between administrative dissolution and reinstatement.[44]

The other Kentucky Court of Appeals opinion relied upon by Plaintiff/Appellant is clearly distinguished from the facts in this case. In the case of *Ed Martin v. Pack's, Inc.*,[45] the legal issue was ***not*** whether reinstatement "relates back" to actions taken on behalf of an entity during the period of the entity's administrative dissolution. In fact, the *Martin* opinion expressly states that *Fairbanks* was not relevant in that case because **in *Martin* there had never been any reinstatement**. As the Court of Appeals explains:

> After reviewing the *Fairbanks* decision, we fail to see how it was applicable to the facts of the instant case. The *Fairbanks* decision simply holds that a company's reinstatement restores it to the "same position it would have occupied had it not been dissolved and that reinstatement validates any action taken by a corporation between the time it was administratively dissolved and the date of its reinstatement." *Id.* at 146. **In the instant case, the *Fairbanks* decision has no application because Southeastern has not been reinstated in Kentucky.** Thus, Martin remains personally liable for his own actions, not Southeastern.[46]

Accordingly, in *Martin*, the Court of Appeals did *not* rely on *Forleo* for its holding on the reinstatement issue, but only for the distinct issue of whether "shareholders, officers, and directors of a dissolved corporate entity can be held

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[44] *Id.* at 6. ("Therefore, we conclude that the trial court erred in determining that Anthony and David could be held individually liable for any actions undertaken on behalf of Harshman Construction solely because it had been administratively dissolved.").

[45] 358 S.W.3d 481 (Ky. App. 2011).

[46] *Martin v. Pack's Inc.*, 358 S.W.3d 481, 485 (Ky. App. 2011) (emphasis added).

personally liable for non-winding up of debts after the dissolution",[47] where there has never been any reinstatement. *Martin* is there for not relevant to this case.

Finally, the Circuit Court and the Court of Appeals interpretation of KRS 275.295 in this case is in accord the law of the majority of other states with similar "relates back" statutes.

As explained in a leading treatise on corporation law:

> In most jurisdictions, the reinstatement of a corporation following dissolution by administrative action of the state relates back to the effective date of dissolution, and ***directors or officers are not personally liable for actions undertaken during the period of dissolution or suspension. Such matters become the exclusive liability of the corporation.***[48]

Thus, for example, the case of *Amoco Oil Co. v. Hembree*[49] addressed the issue under Missouri law, but on facts that are materially indistinguishable from this case. In *Hembree*, the plaintiff entered into a lease agreement with a corporation that in fact had been administratively dissolved at the time the lease agreement was executed.[50] After the termination of the lease agreement, plaintiff realized that the corporation had been dissolved and sued the president and sole stockholder for amounts due under the terminated lease. The individual defendant's corporation was reinstated after litigation began, and after its reinstatement the corporation was also made a defendant in the

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[47] *Id.* at p. 484.

[48] 16A JENNIFER L. BERGER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 8117, p. 228 (perm. ed., 2003 rev. vol. Cum. Supp. 2010), available through Westlaw online, 16A Fletcher Cyc. Corp. § 8117.

[49] 776 S.W.2d 68 (Mo. App. 1989), attached at tab 5.

[50] *Id.* at 69.

action.[51] The trial court granted summary judgment against the defendant corporation on the lease obligation, but held that the president and sole stockholder was not personally liable.[52] The Missouri Court of Appeals affirmed, holding that reinstatement "closed the gap between the revocation and the reinstatement. ***Looking back from the time of reinstatement it was as if the corporate existence had never been interrupted.***"[53]

Likewise, in *Asha Distributing of K.C., Inc. v. Sani-Kem Corp.*,[54] the federal district court applying Missouri law granted a motion to dismiss claims against two corporate officers for alleged negligence related to a fire that occurred while the corporate owner was administratively dissolved. The court held that where reinstatement had occurred before a judgment in the action, "the effect of filing the certificate of renewal is to revive the corporation as if its charter had never been forfeited" and the entity's officers "are relieved of personal liability."[55]

In *Rocky Mountain Sales & Service, Inc. v. Havana RV, Inc.*,[56] the Colorado Court of Appeals held that the president of a corporation was not personally liable in a suit brought by a seller to recover for a debt which arose as result of a generator being ordered in name of the buyer corporation while the corporation was administratively dissolved. The court noted that the president had "continued to operate the business under its

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[51] *Id.*

[52] *Id.*

[53] *Id.* at 70.

[54] 1989 WL 106718, *1 (D. Kan. 1989) (unpublished), attached at tab 6.

[55] *Id.* at *2.

[56] 635 P.2d 935 (Colo. App. 1981), attached at tab 7.

corporate name at the same location and with the same personnel during the period of its suspension,"[57] and held that after the restatement the corporation "was regarded as having had continuous existence." Therefore, the corporations "powers are retroactive to the date of its suspension, and ***the effect is the same as if the suspension had never occurred***," and the president was not liable for the obligation incurred by the corporation during the period of administrative dissolution.[58]

Similarly in this case, Elegant Interiors, LLC, operated under its own name and in the same manner during the period of administrative dissolution as it had before, accordingly after its reinstatement, as a matter of law, it is "as if the administrative dissolution … had never occurred."[59]

The contrary foreign authorities cited by Plaintiff/Appellant for the most part merely demonstrate that not all jurisdictions have the same "relate-back" rule embodied in KRS 275.295(3)(c). And it is telling that it is the *dissent* in the recent Vermont Supreme Court case of *Daniels v. Elks Club of Hartford* (which is discussed extensively in the Plaintiff/Appellant's brief) that relies upon Kentucky law.[60]

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[57] *Id.* at 936.

[58] *Id.* at 937.

[59] KRS 275.295(3)(c).

[60] 2012 VT 55, P100 (Vt. 2012) (dissent relying on *Fairbanks Arctic Blind Co. v. Prather & Assocs.*, 198 S.W.3d 143 (Ky. App. 2005); *Pannell v. Shannon*, No. 2010-CA-001172-MR (Ky. Ct. App. Aug. 26, 2011); *eServices, LLC v. Energy Purchasing, Inc.*, No. 11-198-JBC, 2012 WL 404957 (E.D. Ky. Feb. 6, 2012) for the proposition that "under Kentucky law 'administrative reinstatement also reinstates limited liability for acts taken during the period of dissolution' so that corporate officer was not personally liable on contracts signed while corporation was administratively dissolved"). Attached at tab 8.

2. The General Assembly's amendment of KRS 275.295(3)(c) / KRS 14A.7-030(3) specifically ratifies the rule articulated by the Court of Appeals in *Fairbanks* and the holding of the Court of Appeals in this case.

In the 2010 Session, the Kentucky General Assembly repealed and replaced the language of KRS 275.295(3)(c) with a materially identical provision now codified as KRS 14A.7–030(3)(c).[61] Then, in 2012, the Generally Assembly amended KRS 14A.7–030(3)(c) to provide as follows:

> When the reinstatement is effective:
> (a) It shall relate back to and take effect as of the effective date of the administrative dissolution:
> (b) The entity shall continue carrying on its business as if the administrative dissolution or revocation had never occurred; and
> (c) The liability of any agent shall be determined as if the administrative dissolution or revocation had never occurred.[62]

The General Assembly made two material changes to the statute. First, the term "resume" was changed to "continue" in subpart (b). And new language was added as subpart (c) to make more explicit the implications of the provision that after reinstatement it is as if "administrative dissolution or revocation had never occurred." These revisions were not intended to change the law, but rather to repudiate any general application of *Forleo* and to ratify the court holdings in *Fairbanks*, *Eve v. Cosmo's LLC, et al.*, *eServices, LLC v. Energy Purchasing*, and of the Court of Appeals in this case.

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[61] Ky. Acts 2010, Ch. 151, § 37 and Ch. 151, § 151. Copy attached at tab 9.

[62] Ky. Acts 2012, Ch. 81, § 83. Copy attached at tab 10.

In his article "*The 2012 Amendments to Kentucky's Business Entity Statutes*" Thomas E. Rutledge explains the General Assembly's reason for making these amendments as follows:

> In continuation of the effort to strip the *Forleo* decision of continuing viability, the statute has been supplemented to state that upon reinstatement, the liability of any agent shall be determined as if the administrative dissolution "had never occurred." This new language responds to *Forleo*'s suggestion that the reinstatement language "is silent as to the issue of personal liability." Further addressing the *Forleo* decision, the "resume" upon which the court relied has been replaced with "continue."[63]

Thus, these most recent amendments confirm that the law in Kentucky is, and has been, that after reinstatement the entity "is treated as having been in existence [during the period of administrative dissolution], complete with the corporate shield against personal liability."[64] That is simply to say, in the words of the statute both before and after the most recent amendments to KRS 275.295(3)(c) / KRS 14A.7-030(3), after reinstatement for all legal purposes it is as if the administrative dissolution "had never occurred."

B. Application of the "relates-back" rule is consistent with the purposes and policy underlying administrative dissolutions and reinstatement.

Absent any actual allegation of fraud or misuse of the corporate form (which could be addressed by seeking to pierce the corporate veil), Plaintiff/Appellant's argument that the lower courts' interpretation of KRS 275.295(3)(c) "would promote fraud and abuse" is a red herring. The Supreme Court of Delaware explained the

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[63] Thomas E. Rutledge, *The 2012 Amendments to Kentucky's Business Entity Statutes*, 101 Ky. L.J. Online 1, p. 11 (2012), http://www.kentuckylawjournal.org/the-2012-amendments-to-kentuckys-business-entity-statutes.

[64] *eServices, LLC v. Energy Purchasing, Inc.*, 2012 WL 404957, No. 11-CV-00198-JBC, 4 (E.D. Ky. Feb. 6, 2012), attached at tab 3.

reasoning behind the relates-back rule as it applies to the limited liability shield in the case of *Frederic G. Krapf & Son, Inc. v. Gorson*:

> We are of the opinion that failure to pay franchise taxes is an issue solely between the corporation and the State since the franchise tax statutes are for revenue raising purposes alone. This being so, if the creditor dealt in good faith with the corporation as a corporation, and if no fraud or bad faith on the part of the corporate officers is involved, the creditor's remedy is against the corporation.
>
> ***
>
> **We think it clear that in the absence of fraud or bad faith a corporate officer may enter into a contract binding on the corporation, even after forfeiture of the charter, particularly when, as at bar, the forfeiture came about by inadvertence.** We think it equally clear that the corporate creditor has a remedy against the corporation. **It follows, therefore, that summary judgment was properly entered for Gorson who was sued in his individual capacity.**[65]

The Supreme Court of Michigan reached the same conclusion in *Bergy Bros., Inc. v. Zeeland Feeder Pig, Inc.*[66] Commenting on that state's version of the "relates-back" provision, the court explained that:

> The forfeiture statute is obviously an attempt to bring to an end corporations which have ceased to conduct business as corporations. The statutory scheme calls for the winding up of corporations whose charters have been forfeited. **The Legislature also recognized, however, that the failure to file reports and pay fees may be the result of inadvertence or neglect rather than an indication that the corporation is defunct. Thus, it provided for the**

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[65] *Frederic G. Krapf & Son, Inc. v. Gorson*, 243 A.2d 713, 715 (Del. 1968) (holding that president and owner of corporation was not personally liable for obligations of corporation incurred during period of corporate dissolution where corporation was later reinstated) (emphasis added), attached at tab 11.

[66] 415 Mich. 286, 297, 327 N.W.2d 305, 309 (Mich. 1982) (reversing personal judgment against president of reinstated corporation), attached at tab 12.

> **reinstatement of the corporate charter upon paying back fees, filing back reports, and paying a penalty.** [...] Michigan law expressly made the reinstatement retroactive by providing that reinstatement operated to validate all contracts entered into during the period of forfeiture. **Where, as here, the corporate charter has been reinstated pursuant to the statute, the corporation should be considered to have had at least de facto existence during the period of forfeiture, which would preclude application of the partnership theory of liability.**[67]

In light of the basic purpose of the "forfeiture" or dissolution provisions, and in light of the express provision for retroactive reinstatement, the Michigan court observed that "we see no reason to infer that the forfeiture statute was intended to have a separate penal effect on officers. Its basic purpose was to terminate defunct corporations and to encourage the payment of fees and the filing of reports."[68]

Like the Court of Appeals in *Fairbanks*,[69] these courts have recognized that administrative dissolution results from the failure to file a form and pay a fee imposed by the state. Generally, as in this case, this failure has no effect on third-parties dealing with a corporation or LLC.

The Plaintiff/Appellant was on notice that he was dealing with a limited liability entity when he entered into the Lease and when he revised it on March 2, 2008. The Lease states that the "Tenant" was Elegant Interiors, a LLC corporation [sic]."[70]

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[67] *Id.* 308-309 (emphasis added).

[68] *Id.* at 309.

[69] 198 S.W.3d at 144-45 (quoting opinion explaining that "[t]he object of [corporate dissolution and reinstatement statutes] [is] solely the raising of revenue").

[70] Lease, p. 1, R.A. 13. Attached hereto as Exhibit B.

Furthermore, both before and after the amendment the rent was paid on checks drawn from the Elegant Interiors, LLC's corporate account.[71] The Plaintiff/Appellant was not prejudiced by the administrative dissolution, and there is nothing in the record to suggest that either he or the Defendant/Appellee even knew about the administrative dissolution until well after the Lease was amended.[72] To allow Plaintiff/Appellant to exploit this technical deficiency after the fact would be contrary to the express terms of KRS 275.295(3)(c) and would undermine the limited liability policy that is the very reason LLC's exist.[73]

III. SHANNON, INDIVIDUALLY, IS SIMPLY NOT A PARTY TO THE LEASE, AND THEREFORE, CANNOT BE HELD PERSONALLY LIABLE AS A MATTER OF LAW.

Plaintiff/Appellant also suggests that by having him sign a statement (the "Release") agreeing to ***reduce obligations under the Lease***, somehow Shannon became personally liable for the amended Lease with Elegant Interiors, LLC. By it terms, however, this separate writing was an agreement to execute a new lease, and not itself a

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[71] *See* Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), pp. 21-24, R.A. 347.

[72] There is no evidence in the record that either party in fact discovered the dissolution until July 26, 2006, when the Complaint was filed in this action. R.A. 1, 7. Shannon was not previously aware of the dissolution because she had neglected to update the mailing address listed for Elegant Interiors, LLC with the Secretary of State after she had moved to a new residence the year before the administrative dissolution. *See* Notice Envelope marked "return to sender," R.A. 9; and Certificate of Dissolution, R.A. 8 (containing Shannon's previous mailing address). *See also* Statement of Change updating the address filed with the Application for Reinstatement on August 11, 2006, https://app.sos.ky.gov/corpscans/33/0486433-06-99999-20060811-SCG-1076069-PU.pdf

[73] *Racing Inv. Fund 2000 v. Clay Ward Agency*, 320 S.W.3d 654, 659 (Ky. 2010); Rutledge and Booth, "The Limited Liability Company Act: Understanding Kentucky's New Organizational Option", 83 Ky. L.J. 1, 6-7 (1995).

lease. This document states: "Upon acceptance of this document, a new lease will be signed . . . . All other stipulations will remain the same as in the initial Lease."[74] And, in fact, the parties did execute the promised "new lease" by amending the original Lease to (1) reduce the space leased to Elegant Interiors, LLC, and (2) reduce the amount of rent owed by Elegant Interiors, LLC.

Accordingly, in his Complaint and throughout the Circuit Court proceedings below, Plaintiff/Appellant necessarily relied upon the terms in the Lease agreement, and not the separate Release prepared by Shannon, as the basis of his substantive claims for breach of the Lease.[75] In fact, the Release is not even mentioned in the Complaint.[76] This is because the Release simply does not purport to create any new obligation on the part of Shannon or Elegant Interiors, LLC, and therefore does not constitute an agreement by Shannon to be personally liable for the LLC's debts.

Furthermore, there is absolutely no evidence in the record to support Plaintiff/Appellant's contention that he asked for or was ever told that Shannon was assuming any personal liability as "consideration" for the execution of the amended Lease. No such allegation appears in any pleading or affidavit filed with the Circuit

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[74] *See* Release, R.A. 69. Attached hereto as Exhibit C.

[75] *See, e.g.*, Complaint ¶ 6 ("Defendant, Elegant Interiors, LLC, has breached the Lease by attempting to terminate the Lease without cause[.]"); ¶ 7 ("Pursuant to Paragraph 23 of the Lease, Plaintiff has accelerated and declared all rent and additional rent for the remaining term of the Lease to be due [.]"); ¶ 8 ("Paragraph 23 of the Lease obligates the Defendant to pay attorney's fees[.]"), R.A. 2. Paragraphs 13, 15, 16 make the same claims against Shannon citing the same provisions of the Lease. R.A. 3-4.

[76] *See* R.A. 1-6.

Court in this action. And, of course, no new consideration was legally required for the mutually agreed amendment of the Lease going forward.[77]

Plaintiff/Appellant also argues that Shannon signed the Lease in her personal capacity, as opposed to her corporate capacity. Plaintiff/Appellant bases this argument on the document cover page reading "Lease Agreement for Ann Shannon" and the fact that Shannon signed them "Ann Shannon." Even a cursory review of the Lease, drafted by Plaintiff/Appellant, shows that "Tenant" is a defined term—and defined as "Elegant Interiors, LLC"—as noted in the cover page and the opening recitals of the Lease itself. When amending the lease terms, the parties kept these original terms of the Lease in place.[78] Hence, the Court should recognize Plaintiff/Appellant's argument as a hollow one. Here, every indication—and especially the Lease document itself—indicated that Shannon signed the Lease in her representative capacity, with Elegant Interiors, LLC as the "Tenant."

Finally, Plaintiff/Appellants assertions that extrinsic evidence shows that the parties' intended for Shannon to be personally bound under the Lease is contradicted by

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[77] *See, e.g., Kentucky Home Mut. Life Ins. Co. v. Leitner*, 196 S.W.2d 421, 424 (Ky. 1946) ("Any executory contract which is bilateral in the advantages and obligations given and assumed may at any time after it has been made and before a breach thereof has occurred be changed or modified in one or more of its details by a new agreement also bilateral by the mutual consent of the parties without any other consideration.").

[78] *See* Release, R.A. 69. Attached hereto as Exhibit C.

the only germane evidence in the record[79] and, more importantly, is irrelevant. When construing or interpreting a contract, a court must determine the intention of the parties to the contract.[80] However, for an unambiguous contract, no construction is necessary, and the parties' intentions must be gathered from the four corners of the contract without resort to extrinsic evidence.[81] "It is well settled in Kentucky that, in the absence of ambiguity, a contract will be enforced according to its terms."[82]

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[79] *See* Exhibit B to Defendant's Motion for Summary Judgment, (Deposition of Shannon), p.79-80, R.A. 350:

> Q What was your understanding of your Obligations with respect to the March 2006 lease?
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> A My understanding is and always has been that Elegant Interiors is Elegant Interiors.
>
> Q And that understanding comes from what?
>
> A The way I set my company up.
>
> * * *
>
> Q Did you have any discussions with Mr. Pannell about the fact that because he was agreeing to accommodate you and reduce your space, that he wanted you personally to be obligated?
>
> A No.
>
> Q Okay. Did you all have any discussions about a personal guarantee or executing any similar type document at any time?
>
> A No.

[80] *See 3D Enters. Contracting Corp. v. Louisville & Jefferson County Metro. Sewer Dist.*, 174 S.W.3d 440, 448 (Ky. 2005).

[81] *Id.*

[82] *Codell Constr. Co. v. Commonwealth*, 566 S.W.2d 161, 164 (Ky. App. 1977); *see also Veech v. Deposit Bank of Shelbyville*, 278 Ky. 542, 128 S.W.2d 907, 911 (1939) ("If the contract is so clear and free from ambiguity as to be self-interpretative, no construction is necessary but it should stand as it is written and should be enforced according to its express terms …").

The language of the Lease defining the "Tenant" here is plain and unambiguous. There is no provision in the Lease imposing any liability upon Shannon for the obligations arising from the Lease. There is absolutely no mention of or reference to a personal guaranty anywhere in the Lease. Furthermore, Paragraph 46 of the Lease provides that ***"[t]his writing contains the entire agreement between the parties hereto[.]"*** Thus, the intention of the parties from the four corners of the Lease could not be clearer:

> THIS LEASE AGREEMENT ("Lease"), made this 4th day of Feb., 2004 between Rick Pannell, landlord, having his principal office at 2200 Brannon Road, Nicholasville, Kentucky 40356 ("Landlord"), and **Elegant Interiors, a LLC corporation,** with offices at 198 Moore Dr., Suite 104 Lex, Ky 40503 (**"Tenant"**).[83]

The Court cannot read additional language into the contract but must construe the contract as made.[84] In this matter, the Circuit Court construed and interpreted the Lease according to its plain and unambiguous terms and held that the sole "Tenant" under the lease was Elegant Interiors, LLC. And if Lease were ambiguous it would be construed

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[83] Lease, p. 1, R.A. 13. (bold emphasis added). Attached hereto as Exhibit B.

[84] *See Alexander v. Theatre Realty Corp.*, 253 Ky. 674, 70 S.W.2d 380, 387-88 (1934). *See also Perry v. Perry*, 143 S.W.3d 632, 633 (Ky. App. 2004) ("The Court cannot read words into the contract which it does not contain.").

against Plaintiff/Appellant as the drafter of the agreement.[85] Here there is no dispute that the Lease was executed using a pre-printed form provided by the Plaintiff/Appellant.[86]

Finally, the result of any ambiguity as to the question of personal liability would be that Shannon could not be held liable. As this Court has previously held, "assumption of personal liability by a member of an LLC is so antithetical to the purpose of a limited liability company that ***any such assumption must be stated in unequivocal terms leaving no doubt that the member or members intended to forego a principal advantage of this form of business entity.***"[87]

This is no such unequivocal statement that Shannon intended to forego "a principal advantage" of doing business through a limited liability company in this case. The Circuit Court therefore correctly held that only Elegant Interiors, LLC, was liable for damages resulting from the breach of the Lease.

CONCLUSION

Because Plaintiff/Appellant's claims are based on a Lease agreement that by its express terms was entered into with a limited liability company, the Circuit Court correctly held that Defendant/Appellee Ann Shannon is not personally liable for the

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[85] *See Perry,* 143 S.W.3d at 633 (Ky. App. 2004); *Wiggins v. Schubert Realty & Invest. Co.*, 854 S.W.2d 794, 796 (Ky. App. 1993).

[86] *See* Lease, R.A. 10, attached as Exhibit B. As might be expected in this context, the Lease terms generally favor the Landlord. Perhaps the starkest example of that fact in this case is the provision at the end of paragraph 45 of the Lease ("End of the World"), providing: "Landlord shall be deemed allied with the Forces of Light and Tenant shall be deemed allied with the Powers of Darkness notwithstanding either party's final ordered placement." *Id.* at 16, R.A. 28.

[87] *Racing Inv. Fund 2000 v. Clay Ward Agency*, 320 S.W.3d 654, 659 (Ky. 2010).

judgment against Elegant Interiors, LLC. Accordingly, the Circuit Court's judgment should be affirmed.

Respectfully Submitted,

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