

HEFFERNAN LAW FIRM, PLLC

1201 MARKET STREET

KIRKLAND, WASHINGTON 98033-5440

PHONE 425.284.1150 • FAX 425.284.1147

www.heffernanlawfirm.com

T. DANIEL HEFFERNAN

DEVON M. THURTLÉ

EMAIL
dan@heffernanlawfirm.com

EMAIL
devon@heffernanlawfirm.com

MEMORANDUM

Date: June 13, 2008

Surviving Liability of Dissolved LLCs

In 2007, Division 1 of the Washington Court of Appeals decided three cases that may have significant ramifications regarding the continuing liability of single-project LLCs. These cases are: (1) *Chadwick Farms Owners Ass'n v. FHC, LLC*, 139 Wn. App. 300, 160 P.3d 1061 (2007); (2) *Maple Court Seattle Condo. Ass'n v. Roosevelt, LLC*, 139 Wn. App. 257, 160 P.3d 1068 (2007); (3) *Emily Lane Homeowners Ass'n v. Colonial Dev., L.L.C.*, 139 Wn. App. 315, 160 P.3d 1073 (2007). These cases hold that a dissolved and cancelled LLC has no standing to sue its contractors, but that due to recent revisions in the Limited Liability Companies Act,¹ the developer LLC could nevertheless remain liable to the HOA. It is thus important for developers using single-project LLCs to dissolve and cancel its LLCs in such a way to preserve its rights against its contractors.

Surviving Liability of an Administratively Dissolved LLC

In Washington, where an LLC is administratively dissolved by the Secretary of State, the LLC is provided with a period of two years in which it may apply to be reinstated. RCW 25.15.290. If no application for reinstatement is filed within those two years, the Secretary of State “shall” cancel the certificate of formation. *Id.* Once the certificate of formation is cancelled, an LLC is no longer a separate legal entity. RCW 25.15.070. Thus, an LLC does not have standing to bring claims after it has been cancelled, two years after dissolution. Nevertheless, it can be sued for up to three years after dissolution under RCW 25.15.303.

This was the problem for the developers in *Chadwick Farms* and *Maplecourt Seattle*. In each of those cases, the LLC was administratively dissolved for failure to pay fees and file an annual report. During the two-year period for reinstatement, the HOA brought claims against the LLCs for construction defects. The developers attempted to bring third-party claims against contractors and subcontractors, but those claims were barred because the LLCs failed to apply for reinstatement within two years of dissolution, and the certificates of formation had been cancelled. Thus, the court reasoned, the LLCs did not have standing to bring third-party claims.

¹ RCW 25.15. *et seq.*

July 10, 2008

Page 2

However, the HOA's claims against the LLC could continue because they were brought within the three-year period under RCW 25.15.303. The LLC statute necessarily leaves an LLC exposed to claims for a period of one year where it cannot pass those claims through to contractors, because the statute provides a two-year cancellation period and a three-year suit limitations period.

Surviving Liability of a Member-Dissolved LLC

A member-dissolved LLC is different, as the court in *Emily Lane* observed. There, the members dissolved the LLC, wound it up, and ten days after dissolution the members cancelled the LLC. It was not until eight months after the dissolution that the HOA filed suit. The court of appeals held that the rule in *Chadwick* and *Maplecourt* controlled, and the LLC could be sued but it could not assert claims against subcontractors.

The lack of standing to sue in *Emily Lane* arises out of similar statutes as the liability in the *Chadwick* and *Maplecourt* decisions with only minor variations. Where an LLC is dissolved by its members, the members then proceed to wind-up the LLC. The winding-up period continues until the members file a cancellation of the certificate of formation. RCW 25.15.080. During this winding up period, the LLC has standing to prosecute and defend suits. RCW 25.15.295. Upon filing of the cancellation of the certificate of formation, the LLC ceases to exist as a separate legal entity and does not have standing to bring claims. So, RCW 25.15.303 leaves a member-dissolved LLC exposed to claims for up to three years after dissolution, regardless of when the LLC is cancelled.

The winding-up and cancellation statutes do not provide a limit on the period of time that an LLC may wind-up its affairs. Therefore, an LLC may be able to protect against the situation that arose in *Chadwick Farms*, *Maplecourt Seattle*, and *Emily Lane* by immediately dissolving the LLC and extending its wind-up period for three years. The LLC should not be cancelled until at least three years from dissolution, at which time RCW 25.15.303 cuts off claims against it.

Surviving Liability of Members of a Dissolved LLC

Regardless of the method or date of dissolution and cancellation of an LLC, individual members remain personally liable for actions that constitute grounds to pierce the corporate veil. In other words, termination of the LLC generally does not affect – either positively or negatively – the personal liability of its members.

However, Washington Law does limit somewhat the personal liability of members conducting a proper winding-up. RCW 25.15.300 provides that, where an LLC has been properly wound-up and cancelled pursuant to that statute, including providing for all of the LLC's known liabilities, the members of the LLC cannot be individually liable for claims "by

July 10, 2008

Page 3

reason of such person's actions in winding up the limited liability company." In other words, an HOA cannot make a claim personally against LLC members simply because the LLC no longer exists. Independent grounds for piercing the corporate veil must be established. The converse is also true, that a person who does not properly wind up an LLC, including providing for known liabilities, may be personally liable for those claims against the LLC. *Emily Lane*, 139 Wn. App. at 314. Thus, a proper winding-up of the company is crucial to protect the members of the LLC.