BUSINESS ORGANIZATIONS: MONTANA

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I. Uniform Acts

Montana has adopted a number of the Uniform Laws promulgated by the National Conference of Commissioners on Uniform State Laws. However, not all of the Montana statutes represent the most recent version of the respective Uniform Laws, and Montana has adopted variations to the uniform acts.

II. Corporations

A. **Montana Business Corporation Act.** The Montana Business Corporation Act, Mont. Code Ann. §§ 35-1-112 et seq., is derived from the Model Business Corporation Act. Whereas the Model Business Corporation Act has been amended numerous times, Montana's version of the Act has not been significantly amended since 1991. Following are some important variations between current Montana law and the most recent version of the Model Business Corporation Act.

1. Under the "de facto" corporation doctrine, persons who act on behalf of a defective corporation are protected from personal liability if they made a good faith effort to comply with the statutory requirements of incorporation, and they are unaware that the corporation was not, in fact, formed. The "de facto" corporation doctrine was eliminated in the original version of the Model Business Corporation Act, and then reinstated in more recent versions. Montana has the original version which **eliminates the "de facto" corporation doctrine**; Mont. Code Ann. § 35-1-119 imposes joint and several liability for all debts and obligations incurred by persons who act on behalf of a defective corporation. Although the Montana Supreme Court has stated that it is questionable that the de facto doctrine continues to exist in Montana, it has applied the doctrine of corporation by estoppel. Valley Victory Church v. Sandon, 326 Mont. 340 (2005).

2. Cumulative voting is the default rule in Montana. Mont. Code Ann. § 35-1-531(1). Directors will be elected by cumulative voting, unless the articles of incorporation provide otherwise. To protect against dilution of cumulative voting, directors may serve staggered terms in Montana only if the board consists of nine or more directors. Mont. Code Ann. § 35-1-422.

3. Fundamental changes to the corporation, including a merger, a sale of

substantially all of the corporation's assets outside the ordinary course of business, and dissolution, require the approval of two-thirds of the outstanding shares entitled to vote. Mont. Code Ann. §§ 35-1-815, -823. The articles of incorporation may require a greater, but not a lesser, percentage.

B. **Piercing the Corporate Veil**. A shareholder in a corporation is ordinarily not personally liable for the corporation's debts, but in rare instances a court may hold one or more shareholders in a closely held corporation liable for the corporation's debts or liabilities through application of the doctrine of "piercing the corporate veil." In Drilcon, Inc. v. Roil Energy Corp., 230, Mont. 166 (1988), the Montana Supreme Court has established a two-prong test for piercing the corporate veil that still applies today.

1. Under the first prong, the plaintiff must demonstrate that the corporation is an **alter ego**, agent, or mere instrumentality of its individual shareholders.

2. Under the second prong, the plaintiff must demonstrate that the corporation has been **used as a subterfuge** to defeat public convenience, to justify a wrong, or to perpetrate a fraud. In Peschel Family Trust v. Colonna, 317 Mont. 127 (2003), the Montana Supreme Court stated that the **undercapitalization** of a corporation from inception suggested "bad faith" which met this second prong.

3. **Both** prongs must be satisfied to pierce the corporate veil and hold one or more shareholders personally liable for the corporation's acts or debts.

4. In 2011, the Montana legislature adopted a unique provision that distinguishes between shareholders who are "active" and "not active" in the corporation. See Mont. Code Ann. §35-1-534 reprinted in Appendix A.

C. **Fiduciary Duties between Shareholders.** In stark contrast to partnership law, it is an established principle of corporate law that shareholders, as a general rule, do not have a fiduciary duty to the corporation or to each other. However, the Montana Supreme Court has ruled that majority shareholders in a closely held corporation (i.e., a corporation with a relatively small number of shareholders) owe a duty of loyalty to minority shareholders that is similar to the fiduciary duty owed by partners to each other in a partnership. Daniels v. Thomas, Dean & Hoskins, Inc., 246 Mont. 125 (1990). This duty has also been extended to minority shareholders of a closely held corporation. Sletteland v. Roberts, 304 Mont. 21 (2002).

D. **"Close" Corporations**. In 1987, prior to the adoption in Montana of the Model Business Corporation Act that allows shareholder management agreements, the Montana legislature adopted the "Montana Close Corporation Act." Mont. Code Ann. §§ 35-9-101 et seq. A corporation with 25 or fewer shareholders may elect to become a Montana "close corporation," a term that has a different legal meaning than a "closely held corporation." The Close Corporation Act imposes statutory restrictions on the transfer

of shares between shareholders, including the grant of a right of first refusal in the corporation on transfers outside of existing shareholders or their family members. Mont. Code Ann. § 35-9-202. It also allows shareholders to eliminate the board of directors. Mont. Code Ann. § 35-9-302. The failure of a Montana close corporation to observe usual corporate formalities is not a ground for piercing the corporate veil. Mont. Code Ann. § 35-9-306.

III. **Partnerships**

A. **General Partnerships.** Montana has adopted the 1993 version of the Revised Uniform Partnership Act (RUPA), Mont. Code Ann. §§ 35-10-101 et seq. Following are some important variations between current Montana law and the most recent version of the RUPA as adopted in other jurisdictions.

1. In 1995, Montana adopted a non-uniform version of the RUPA provisions relating to **limited liability partnerships**. Whereas the uniform provision provides that "[a] partner is not personally liable, directly or indirectly, by way of contribution or otherwise, for such an obligation solely by reason of being or so acting as a partner," the Montana version has unique language which, among other variations, specifically states that a partner remains liable "the partner's own negligence, wrongful act, or misconduct ... and that of any person under the partner's direct supervision and control." Mont. Code Ann. § 35-10-307.

2. The specific rules for registering a limited liability partnership are set forth at MCA §§ 35-10-701 et seq. In Montana, limited liability partnership status exists for only 5 years from registration, and must be renewed thereafter. MCA § 35-10-715.

3. In several circumstances, it is easier to dissolve a partnership in Montana than under RUPA. Whereas under RUPA it requires a majority of remaining partners to vote to dissolve a term partnership after certain acts, such as the death of a partner, under MCA § 35-10-624(2)(a) a single remaining partner has the ability to cause the dissolution of the partnership by giving notice within 90 days of such event of her intent to withdraw.

B. **Limited Partnerships**. In 2001, the National Conference of Commissioners on Uniform State Laws (NCCUSL) adopted a new and significantly revised version of the Uniform Limited Partnership Act, which Montana adopted in 2011.

1. The new Uniform Limited Partnership Act is an entirely self-contained, stand-alone act. Mont. Code Ann. §§ 35-12-501 et seq. Prior law filled gaps by referring to the general partnership act (RUPA).

2. Under prior law, limited partners were shielded from personal liability for the

debts of the partnership as long as they were not involved in management. The new Uniform Limited Partnership Act grants a full shield of limited liability to limited partners, including those limited partners who may engage in management activities, similar to the protection granted to members of a limited liability company. Mont. Code Ann. § 35-12-703.

3. Among other major features of the new Uniform Limited Partnership Act, a limited partnership may elect to be a **limited liability limited partnership** (to be distinguished from a limited liability partnership, which is governed by RUPA). Whereas general partners are generally liable for the debts and obligations of a limited partnership, a general partner of a limited liability partnership "is not personally liable, directly or indirectly, by way of contribution or otherwise, for an obligation solely by reason of being or acting as a general partner." Mont. Code Ann. § 35-12-803(3).

4. Under the new Uniform Limited Partnership Act, and absent an agreement otherwise, a limited partner does not have the right to withdraw from the partnership, Mont. Code Ann. § 35-12-1016, and is not entitled to be paid the fair value of his or her partnership interest in the event of a dissociation. Instead, the partner's interest becomes that of a transferee; as a transferee the withdrawn partner has the right to continue receiving distributions attributable to his or her interest, but has no further rights to participate in voting or management. Mont. Code Ann. § 35-12-1017.

5. The new ULPA, as adopted by Montana, has unique effective date provisions. Many of its provisions apply not only to limited partnerships formed after its effective date (October 1, 2011), but also to limited partnerships formed prior to October 1, 2011. Sec. 1, Ch. 216, L. 2011.

IV. **Limited Liability Companies**

A. **Uniform Limited Liability Company Act.** Although Montana originally enacted its own version of a limited liability company act in 1993, in 1999 it substantially adopted the Uniform Limited Liability Company Act, MCA §35-8-101 et seq. It has not yet adopted the 2006 Revised Uniform Limited Liablity Company Act.

V. **Personal Liability for Your Own Conduct**.

Regardless of the choice of entity that you choose, you always remain liable for your own negligence or wrongful conduct. For example, you cannot avoid malpractice claims by forming and operating your law practice through a professional corporation. The Montana Supreme Court recognized this principle in White v. Longley, 358 Mont. 268 (2010). In that case, Tom Longley operated a home building business through Castle Homes, LLC. Castle Homes, LLC entered into a contract to build a home for the Whites. Longley, acting on behalf of the LLC,

provided engineering and construction services under the contract. The home turned out to be a disaster, "structurally compromised from top to bottom," including a roof that could not be supported by the underlying structure. The trial court determined that Longley made misrepresentations as to his qualifications that induced the Whites to enter into the contract, and negligently performed services under the contract. The Montana Supreme Court affirmed the trial court's ruling that Longley was jointly and severally liable (along with the LLC) for the damages suffered by the Whites. The Court noted that "the Limited Liability Company Act does not offer blanket protection from liability to a member of an LLC for the member's own conduct." ¶ 37. This principle applies to any type of entity.

Appendix A
Comparison of Liability Provisions

General Partnership MCA 35-10-307(1)	Limited Liability Partnership MCA 35-10-307(2)	Limited Partnership MCA 35-10-703, -803	Limited Liability Limited Partnership MCA 35-10-703,-803	Limited Liability Company MCA 35-8-304	Corporation MCA 35-1-534(2)
"[A]ll partners are liable jointly and severally for all obligations of the partnership unless otherwise agreed by the claimant or provided by law."	"[A] partner of a limited liability partnership is not liable, directly or indirectly, including by way of indemnification, contribution, assessment, or otherwise, for: (a) any debts, obligations, or liabilities of or chargeable to the limited liability partnership... or (b) the acts or omissions of any other partner or agents, contractors, or employees of the [llp]...." Exception: a partner remains liable "for the partner's own negligence, wrongful act, or misconduct" or that of any person under the partner's direct supervision and control.	**Limited Partners**: "... A limited partner is not personally liable, directly or indirectly, by way of contribution or otherwise, for an obligation of a limited partnership solely by reason of being a limited partner even if the limited partner participates in the management and control of the limited partnership." **General Partners**: "all general partners are liable jointly and severally for all obligations of the limited partnership unless otherwise agreed by the claimant or provided by law. "	**Limited Partners**: "... A limited partner is not personally liable, directly or indirectly, by way of contribution or otherwise, for an obligation of a limited partnership solely by reason of being a limited partner even if the limited partner participates in the management and control of the limited partnership." **General Partners**: "An obligation of a limited partnership incurred while the limited partnership is a limited liability limited partnership ... is solely the obligation of the limited partnership. A general partner is not personally liable, directly or indirectly, by way of contribution or otherwise, for an obligation solely by reason of being or acting as a general partner."	(1) "... a person who is a member or manager, or both, of a limited liability company is not liable, solely by reason of being a member or manager, or both ... for a debt, obligation, or liability of the limited liability company ... or for the acts or omissions of any other member, manager, agent, or employee of the limited liability company. (2) The failure of a limited liability company to observe the usual company formalities or requirements relating to the exercise of its company powers or management of its business is not a ground for imposing personal liability on the members or managers of the limited liability company."	"Unless otherwise provided in the articles of incorporation, a shareholder who is: (a) active in a corporation is not personally liable for the acts or debts of the corporation except that a shareholder may become personally liable by reason of that shareholder's own acts or conduct; (b) not active in the corporation is not personally liable unless the corporate veil is pierced or the shareholder agrees in writing to assume personal liability."

COMPARISON OF

MONTANA MORTGAGE	v.	DEED OF TRUST (TRUST INDENTURE) UNDER SMALL TRACT FINANCING ACT
1. Mortgage only a lien		1. Trust Indenture (Deed of Trust) conveys legal title to Trustee, but only for security (Beneficiary can use a loan Servicer to handle collecting payments)
2. Is a 2-party instrument: Mortgagor & Mortgagee		2. Is a 3-party instrument: Grantor (debtor), Beneficiary & Trustee
3. No acreage limit; only security device for a lender on parcel over 40 acres (seller of large parcel can use Contract for Deed		3. Can only be used on parcel of not more than 40 acres
4. Mortgagee has private power of sale only if Mortgage so provides		4. Must say it is executed under Small Tract Financing Act. (Otherwise it is a Mortgage, with redemption & possession)
5. Upon default by Mortgagor, Mortgagee has option to foreclose either by: a. Judicial foreclosure, or b. By power of sale if Mortgage so provides		5. Power of Sale (nonjudicial foreclosure by "advertisement and sale") is read into the document; no requirement for authorization in document
6. No deficiency judgment allowed on Mortgage given directly to the vendor (not given to 3rd party lender)		6. No deficiency judgment allowed on either: a. foreclosure under power of sale, or b. foreclosure of an "occupied, single family residence: (*Chunkapurra* on rehearing)
7. Notice of Sale on Power of Sale foreclosure: a. Published for 30 days in newspaper in County or if no such newspaper, by posting on the land and in 4 other conspicuous places. (One of the places must be on front door of Courthouse); and b. Personally serving Notice of Sale 30 days before sale on: i. Occupant ii. Mortgagor iii. Every person claiming a record interest in the land		7. Upon default by Grantor (debtor) Beneficiary or Trustee can foreclose either by: a. Judicial foreclosure; or b. Power of Sale ("advertisement and sale"), but procedure not same as in Mortgage

8. No right of cure. Debtor can only pay off 100% of the debt plus foreclosure-related expenses

8. Debtor can cure default any time before sale by paying only delinquent installments of debt, plus foreclosure-related expenses.

9. Sale can occur 30 days after 1st publication of Notice of Sale

9. Notice on Power of Sale foreclosure
   a. Record with County Clerk & Recorder Notice of Sale at least 120 days before sale date
   b. At same time (120 days before sale) registered or certified mail to:
      i. Grantor at last known address
      ii. Everyone who has recorded a Request for Notice
      iii. Successor in title of Grantor
      iv. Everyone having a lien or interest subsequent to Trustee
   c. Publish copy of Notice of Sale in newspaper in the county once a week for 3 successive weeks, with last publication at least 20 days before sale date. If no such newspaper, then postinq Notice of Sale in 3 public places at least 20 days before sale date.
   d. Record before sale an Affidavit of Mailing.
   e. Sale can be postponed for no more than 15 days by public proclamation at time & place set for sale. If Bankruptcy Stay received, or stay by other court order, make multiple postponements, each not to exceed 30 days, and not for more than an aggregate of 120 days.

10. When debt paid, Mortgagee records Satisfaction of Mortgage

10. When debt paid Beneficiary or Servicer requests Reconveyance. Title Insurer or Title Insurance Producer sends Notice of Intent to Reconvey to Beneficiary or Servicer. If no objection received by certified mail within 90 days, Title Insurer or Insurance Producer records Reconveyance

11. After foreclosure sale, debtor has one-year right of redemption and if it is debtor's primary residence a one-year right of post-sale possession. See MCA § 25-13-802 re amounts payable to redeem (same as on execution)

11. No post-sale right of redemption or possession. Debtor must vacate 10 days after the sale.

Look at the statutes. Mortgages covered in MCA §§ 71-1-201 through 71-1-235 and (re redemption) §§ 25-13-801 through 25-13-825)

Look at the statute: Small Tract Financing Act covered in MCA §§ 71-1-301 through 71-1-321. *Chunkapurra* case (1987) is 226 Mont. 54; final holding at end upon rehearing