

In A Limited Liability Company, Ownership Doesn't Necessarily Include Control Of Any Decisions

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Joshua Stein

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Dividing up a limited liability company can require careful identification and allocation of "economic" and "control" rights.

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Family businesses large and small, whether involving real estate or anything else, often use a limited liability company as the ownership vehicle for the business. The founder of the business will often maintain a controlling position in the LLC, while other family members receive only an “economic interest”—the right to receive money and enough information to file their taxes, but not much more.

When the founder dies and LLC interests go to the various family members, or if the founder gets divorced, it can become crucially important to define exactly who gets what types of rights in the LLC. If a surviving family member or spouse receives only an economic interest,

then they cannot make decisions for the company or even know very much about what's happening in the company. Most importantly, they cannot decide how much money the LLC should distribute to its members and when.

Instead, any holder of a mere economic interest just gets money—if and when the LLC management decides the time is right—and a bit of information. Often that's precisely what the founder wanted. For example, the founder might not have confidence in the business judgment or sophistication of a particular family member or of future generations more generally. The founder might not want one family member to second-guess the decisions of another family member or group.

Recent litigation involving assets of the Bich family underscored the importance of these distinctions. A family LLC owned hundreds of thousands of shares in the Bic company, an international manufacturer of pens, lighters, and other products. Bruno Bich, husband and father, owned a 99% economic interest in the company. The LLC agreement also gave him the right to designate the manager of the company, i.e., the person who could manage and control the company and make all its decisions.

Bruno and his wife, Veronique, at some point entered into a post-nuptial agreement, an agreement between spouses who are already married but want to resolve future disputes about division of assets if they separate or divorce. That agreement said that if the parties separated, Bruno would transfer to Veronique his 99% "interest" in the LLC. It didn't mention his right to designate the manager of the company.

Eventually, the parties did separate. After that, Bruno died. At some point along the way Bruno and his three sons, who owned the other 1% of the LLC, made an agreement transferring to the sons Bruno's right to designate the manager of the LLC.

Veronique sued, demanding that she receive not only Bruno's 99% economic interest, but also his right to appoint the manager of the LLC. Presumably, she would have used that right to appoint herself or a trusted third party to run the LLC, thus assuring that the LLC distributed money. This was a crucially important agenda item for her since she would receive 99% of those distributions as a 99% economic interest owner. On the other hand, if she couldn't directly or indirectly control the LLC then it might never distribute a penny to her. She argued that the reference to Bruno's "interest" ought to include all his rights under the LLC agreement as they existed when he signed the post-nuptial agreement or perhaps at some later point. Those rights would have included his right to designate the LLC's manager.

The court rejected her broad reading of "interest," concluding that she could recover only Bruno's 99% economic interest, and had no claim to his right to designate the manager of the LLC and hence initiate distributions by the LLC.

As part of the basis for decision, the court noted that Delaware law governed the LLC. Delaware law defined “interest” in an LLC as nothing more than an economic interest. More generally, the court noted that the post-nuptial agreement referred only to Bruno’s 99% “interest,” specifying the percentage at issue. It said nothing about any of his other rights under the LLC agreement. As a result, the post-nuptial agreement didn’t require Bruno to transfer those rights to her. He could do whatever he wanted with them.

She ended up owning almost the entire LLC but without the ability to initiate distributions. The control of distributions resided indirectly with the happy couple’s three sons.

In negotiating any LLC agreement and planning for the death or divorce of any of the members, or any other transfers within the family, the Bich saga underscores the important of understanding exactly what rights exist within the LLC. Then the business understanding and the documents themselves must carefully distinguish between economic rights and managerial rights. Sometimes those rights should end up in the same place. Sometimes they shouldn’t.

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