

NEWS ALERT**CONSTRUCTION****Your corporate real estate is held by a separate LLC,
so it's protected, right? Maybe not ...**

By Anthony R. Leone

Your business real estate may not be safe from a separate, but related, company's bankruptcy.

In a shot across the bow to the Massachusetts construction community, a Massachusetts bankruptcy court has determined that in certain circumstances a bankruptcy trustee may seize a non-bankrupt company's assets to satisfy a related bankrupt company's creditors. The bankruptcy case of In re Cameron Construction & Roofing Co., Adv. P.No. 15-1121, 2016 WL 7241337 (Bankr. D. Mass. December 14, 2016), involved a bankrupt roofing contractor and a "property management" company, both founded and owned by the same individual. The contractor was incorporated as a roofing company with limited assets, namely roofing equipment and vehicles. Years before filing for bankruptcy, the owner had created the separate limited liability "property management" company, which owned the real property from which the contractor operated its business. The bankruptcy trustee filed the case seeking to disregard the separate corporate structures of the two companies and "consolidate" the assets of the non-bankrupt property management company with those of the bankrupt contractor to satisfy the latter's creditors.

The two companies appeared to be separate corporate entities, but in assessing the relationship between the two the Court determined that despite the fact that the contractor and the non-bankrupt company filed separate tax returns, maintained separate articles of incorporation, issued separate W-2s, and filed separate annual reports, there was a "substantial identity between the entities to be consolidated."

In particular, the Court focused on the following factors:

- The individual owner had an ownership interest in both the bankrupt contractor and the property management company
- The bankrupt contractor only owned 1% of the property management company despite contributing 10% of the capital, whereas the individual owner received a 99% ownership interest in the property management company for contributing 90% of the capital
- The property management company operated beyond its stated business purpose, which was "the ownership, management and development of real estate"
- The property management company did not have a formal lease agreement with the bankrupt contractor and received varied amounts for "rent" that sometimes exceeded the fair market rental value and which the property management company booked as payment for work performed by its employees

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- The bankrupt contractor and non-bankrupt property management company did not enter into subcontracts between them, nor did the property management company send invoices to the bankrupt contractor even though its employees worked exclusively for the bankrupt contractor

Relying on these facts, the Court determined that assets of the non-bankrupt company could be “consolidated” into the bankrupt estate of the contractor. The result is that the trustee can use the assets of the related property management company, which did not file for bankruptcy, as if they were assets of the contractor.¹

TAKEAWAYS

Many Massachusetts contractors operate under this two-company structure and this case serves as notice that companies must be careful and strategic to ensure that the corporate structure will protect the assets in the event of a bankruptcy of the contractor entity. Merely following “minimal corporate formalities” while disregarding the distinction of the companies in operation could expose interrelated companies facing financial difficulties to a much broader reach of creditors than would otherwise be expected. If you have any questions or concerns based upon this recent development, you should discuss your corporate structure and operations with counsel to ensure that you are positioned to maximize the protection of your assets.

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¹ Here, the bankruptcy trustee was not attempting to hold the manager and owner of the companies liable under a more traditional piercing of the corporate veil argument, but rather reach the assets of the non-bankrupt company.

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