EXAMINERS' ANALYSIS OF QUESTION NO. 10

Before distributing assets to shareholders upon dissolution, a corporation is required to pay or make provisions for its debts, obligations, and liabilities. MCL 450.1855a. After payment or adequate provision has been made for the corporation's debts, the remaining assets are required to be distributed to shareholders according to their respective rights and interests. *Id*. Thus, AWC was legally obligated to pay its debts (here, delinquent property taxes) before Sid and Frank received their respective distributions.

Barney

If a director votes for, or concurs in, making distributions to shareholders during or after dissolution of the corporation without paying the debts of the corporation as required by section 1855a, the director is "jointly and severally liable to the corporation for the benefit of its creditors or shareholders, to the extent of any legally recoverable injury suffered by its creditors or shareholders as a result of the action ..." MCL 450.1551(1); 450.1551(1)(b). The liability is limited to the "difference between the amount paid or distributed and the amount that lawfully could have been paid or distributed". MCL 450.1551(1).

Here, the legally recoverable injury suffered by the City of Springfield is the $50,000 in delinquent property taxes. Barney's liability is limited to the difference between the amount distributed to Sid and Frank ($100,000, or $50,000 each), and the amount that could have been lawfully distributed to Sid and Frank ($50,000, or $25,000 each). Thus, without considering any offsets for the liability of the shareholders, Barney would be liable to the corporation for $50,000.

Under MCL 450.1551(2), Barney would not be liable had he otherwise complied with the business judgment rule, MCL 450.1541a. Under MCL 450.1541a, directors are required to discharge their duties: "(a) In good faith. (b) With the care an ordinarily prudent person in a like position would exercise under similar circumstances. (c) In a manner he or she reasonably believes to be in the best interests of the corporation." Here, there really is no claim that Barney's actions were done in good faith. He deliberately chose to benefit Sid and Frank rather than pay the delinquent property taxes. Thus, the business judgment rule will provide no defense to Barney.

It could be argued that the debt was owed by the corporation and, because the corporation dissolved, the debt is uncollectable. However, a creditor may bring an action directly "against the directors of a corporation for the dissipation of corporate assets during the process of dissolution in the face of known debts." *City of Muskegon v Amec, Inc*, 62 Mich App 644, 647 (1975).

Sid

Pursuant to MCL 450.1551(3), a shareholder who accepts or receives a share dividend with knowledge of facts indicating it is contrary to MCL 450.1551(1) is liable to the corporation for the amount received in excess of the shareholder's share of the amount that lawfully could have been distributed.

The facts indicate the Sid was aware that Barney issued larger dividends in lieu of paying the delinquent property taxes. Because he had knowledge that Barney made distributions without paying the debts of the corporation, he is liable for excess amount. Since he was lawfully entitled to $25,000, but received $50,000, Sid is liable for $25,000.

Frank

Because the facts specifically state that Frank had no knowledge that Barney issued larger dividends rather than satisfy the debts of the corporation, Frank is not liable to the corporation.