



Don't Put Your Head in the Sand

The Appeals Court's recent decision in *People's United Bank v. B&B Fire Protection, Inc.* ([see the decision here](#)) illustrates the consequences of staying silent and hoping an issue just fizzles out. The case involved a company, B&B Fire Protection, Inc. ("B&B"), owned by two men: Barnes, who owned 51%, and Berry, who owned 49%. Barnes also owned 100% of the shares of two other companies. Barnes took out a line of credit for his other companies and caused B&B to guaranty the debt. Barnes did not tell Berry of this loan or, more importantly, of B&B's Guaranty. Under G.L. c. 156D, § 8.31 ([see the statute here](#)) the Guaranty was a "conflict of interest transaction" because Barnes caused B&B to guaranty the debt of his companies, and the disinterested B&B owner (Berry) did not approve it. These transactions are voidable unless "authorized, approved or ratified."

The two men had a falling out (unrelated to the loan), which led to Berry buying out Barnes' interest in B&B. When Berry took over B&B's operations, he discovered B&B's Guaranty. Berry emailed the bank, and even instructed the bank to freeze the line of credit until he and Barnes sorted out the situation. Berry, however, did not specifically repudiate B&B's Guaranty. The loan officer responded with an email suggesting that they meet to discuss the company's (B&B's) options. Berry then effectively let the issue die and never followed up with the bank. Barnes' companies defaulted on the loan, and the bank sought to enforce the Guaranty against B&B.

After a bench trial, the trial court held that although the Guaranty was voidable, Berry ratified the Guaranty through his inaction and silence. The Appeals Court affirmed, and held that the trial judge correctly concluded that Berry "did nothing to exercise [B&B's repudiation right] and instead purposefully shut his eyes to means of information within his own possession and control, having only that knowledge which he cared to have."

An important lesson: if you discover a "conflict of interest transaction," you better repudiate it clearly and promptly. Don't close your eyes and hope it goes away. This case also demonstrates how a business operator can compound the problem. The trial court appeared to be influenced by how Berry tried to avoid the liability through a corporate restructuring in which he tried to siphon off the company's assets to a new entity.

This case is discussed in more detail in the Jan. 10, 2019 edition of *Massachusetts Lawyers' Weekly*, in which OCM Partner David Mack is quoted. [MLW Subscribers can view the article here.](#)

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