



LLC Operating Agreement Overrides Fiduciary Duty

It has long been the law in Massachusetts that an owner of a closely held company owes a fiduciary duty of “utmost good faith and loyalty” to the company and his or her fellow owners. Generally speaking, if an owner learns about a business opportunity for the company, the owner must bring that opportunity to the company and afford the company the chance to pursue the opportunity.

Butts v. Freedman involved an investment banking firm named Boston Equity Advisors (BEA), of which Freedman and Butts were the co-owners. When the relationship between Butts and Freedman deteriorated, Freedman met with a competing firm and discussed a possible merger of the two companies. He did not disclose the potential merger to Butts. Instead, he left BEA to join the competitor and did not invite Butts. Butts then sued, alleging that Freedman breached his fiduciary duty by failing to bring the merger opportunity to him and BEA.

The problem for Butts, however, was that the BEA Operating Agreement expressly stated:

“Other Activities. The Members . . . may engage in . . . other business ventures and investment opportunities of every kind . . . , including serving as managers, members and general or limited partners of corporations . . . with purposes similar to or the same as those of [BEA]. Neither [BEA], nor any other Member or Manager, shall have any rights in or to such . . . opportunities, or the income or profits therefrom.”

After a bench trial in the Business Litigation Session, the court found in Freedman’s favor. The judge reasoned that the “Other Activities” provision limited the scope of Freedman’s fiduciary duty such that he could not be held liable for engaging in conduct permitted by that provision. The Appeals Court affirmed. The Court recognized that while the Operating Agreement’s provision may be inconsistent with the corporate opportunity doctrine, the trial judge properly “gave effect to the broad language of the parties’ agreement.”

This case is an important reminder – for small business owners and lawyers as well – to pay careful attention to what otherwise may seem like boilerplate language. Fiduciary duties can be overridden by contract, and limitations on fiduciary duties can have serious repercussions down the road if the relationship deteriorates.

About OCM

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