

Winding Up a Construction Company in Minnesota

Unlike your typical company that may sell a product or services, Minnesota construction companies that provide residential services are licensed by the Minnesota Department of Labor and Industry (“DLI”)ⁱ. This licensing adds an additional level to the typical steps utilized in shutting down a business and winding up its affairs. While most Minnesota corporations and limited liability companies that choose to dissolve as provided by statute receive protection from most further claims against the companyⁱⁱ, claims made under the Minnesota statutory warranty for residential construction survive dissolutionⁱⁱⁱ. Whether the dissolved construction company maintains continuing reserves to fund such post-dissolution claims, a successful claimant who obtains a final judgment arising out of a residential construction related claim may recover from the contractor’s recovery fund administered by DLI^{iv}. Because of the survival of such claims, consideration must be given to the future effects on licensing.

For each licensed residential construction company, the contractor’s recovery fund may pay out an aggregate amount among all claimants of up to \$75,000^v. Should any owner, officer, qualifying person, managing employee or affiliate of the dissolved residential construction company desire to hold a subsequent residential construction license going forward, DLI requires the subsequent residential construction company to pay the contractor’s recovery fund double the amount paid out because of the dissolved residential construction company plus twelve percent interest per year for each year the fund has not been repaid from the date of its payout^{vi}. If a person wants to hold a residential construction license after dissolution of their prior construction company, consideration must be given on how statutory warranty claims against the dissolved company are handled before the company is dissolved.

Because the claims that survive dissolution are those of the Minnesota statutory warranty for residential construction, a brief overview of those warranties is needed. Minnesota Statutes chapter 327A provides for warranties for every residential new construction and home improvement work from the warranty date of one year that the work is free from defects caused by faulty workmanship or defective materials; two years that installed mechanical systems are free from defects caused by faulty installation; and ten years that the work is free from defects caused by major construction defects due to noncompliance with building standards^{vii}. Essentially the warranty date is the date the work is delivered to the customer^{viii}. As this statute has been interpreted by various Minnesota case law, the one-year warranty only requires that the defect had to occur in the first year. Because most construction defects exist at the time of installation, the one-year requirement is satisfied. The claimant may make such a one-year warranty claim up to ten or twelve years after the warranty date. For a more thorough discussion of this issue, see my article “Minnesota Construction Workmanship Warranty – Why a 1-year warranty is really a 10/12-year warranty^{ix}”

Because of all of this, I recommend a Minnesota residential construction company take the following action steps (not necessarily in a specific order) in dissolving the company:

1. Identify whether a future residential construction license may be desired by any owner, officer, qualifying person or managing employee of the company. If it is, then consideration must be given to how future warranty claims are handled for the dissolving company. While there are many ways to handle this issue, common solutions are keeping a warranty reserve in place after dissolution, having another residential licensed construction company contractually agree to service such claims (and likely fees are involved), or have one or more of the individuals from the dissolving residential construction company contractually agree to be financially responsible for such claims (with an indemnification and hold harmless agreement).
2. Determine what form of dissolution to pursue. Statutory dissolution comes in two general flavors, with notice to creditors and without notice to creditors^x. While dissolution with notice shortens the time a claim may be made against the dissolving company more than dissolution without notice, for dissolution with notice to be effective all potential claimants must receive notice. That likely includes all prior customers, vendors, subcontractors, employees, etc. O
3. Identify all personally guaranteed accounts, gather the guaranties, and consider notifying the account holders that the company is dissolving, the account holders should extend no further credit to the company and the guarantor will not honor any claims on the guaranty for extensions made after a specified date. Such a notice may or may not be effective against a claim on the guaranty, and such guaranties should be reviewed with the assistance of legal counsel to determine their ongoing effect.
4. Determine the end date of contractual agreements such as leases (real property, equipment and automobile), service contracts (vendor and customer), and other contractual obligations and whether any of them may be terminated early without penalty and what termination penalties apply. Notify contracted parties, as appropriate, of the pending dissolution and termination of contract.
5. Determine how the company shall dispose of its assets. Dissolution generally requires that the dissolving company pay or make arrangements with third-party creditors first, then inside creditors (often owner loans), then disburse remaining amounts to the owners^{xi}. Dissolution is additionally dictated by the company's governing legal documents (such as buy-sell agreement, shareholder or member control agreement, operating agreement, etc.). Identify work in progress and when such work may be complete, especially those involving open construction permits. Dissolution should be timed so that work is completed and all permits are closed before final dissolution.
6. Identify all known potential claims that may survive dissolution and how such claims, should they arise, are to be handled.
7. Preparing for filing final tax returns after dissolution is completed.

Often legal and accounting professional help is needed before, during and after completion of the above action steps. These action steps are not a comprehensive list of things to be done in dissolving a residential construction company; however, they are a good “first steps” list to prepare an actual plan of dissolution so that the dissolution progresses with less surprises, risks are minimized, and dissolution may be completed in a reasonable manner and time.

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ⁱ Minn. Stat. Chpt. 326B.

ⁱⁱ Minn. Stat. § 302A.781; Minn. Stat. §§ 322C.0703 and 322C.0704;

ⁱⁱⁱ Minn. Stat. § 327A.02, subd. 2a.

^{iv} Minn. Stat. § 326B.89.

^v Minn. Stat. § 326B.89.

^{vi} Minn. Stat. § 326B.84(9)(i).

^{vii} Minn. Stat. § 327A.02, subd. 1-3.

^{viii} Minn. Stat. § 327A.91m subd. 8.

^{ix} <http://www.acumenlegaladvisors.com/minnesota-construction-workmanship-warranty-why-a-1-year-warranty-is-really-a-1012-year-warranty/>

^x Minn. Stat. §§ 302A.727 and 302A.7291; Minn. Stat. §§ 322C.0703 and 322C.0704.

^{xi} Minn. Stat. § 302A.725; Minn. Stat. § 322C.0707.