

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM SOUTH CAROLINA
WORKERS' COMPENSATION COMMISSION

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SC Court of Appeals

WCC Case No.: 1316470
Appellate Case No.: 2016-000617

Elias Reyna Respondent,

v.

Fenerly Inc. / Tony's Place of Sumter LLC, Employer, and
Foremost Signature Insurance Co., Carrier Appellants.

FINAL REPLY BRIEF OF APPELLANTS

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At the core of this appeal is an uncomplicated but important matter of statutory interpretation: Under the South Carolina Workers' Compensation Act ("Act"), is a limited liability company ("LLC") treated as a partnership or a corporation? Resolution of this threshold question of law defines the proper track of analysis – the lens through which the facts of this case must be viewed. If an LLC is to be treated as a partnership, its members must affirmatively opt in to be covered, regardless of whether they are working members or merely members in name only. But if an LLC is to be treated as a corporation, its members are covered under the Act unless they reject coverage and do not otherwise fall within the Act's definition of "employee." There is no dispute that Claimant Elias Reyna's employer Tony's Place of Sumter, LLC ("Tony's Place LLC") is a registered LLC created by South Carolina statute. (Respondent's Brief p. 7). The only dispute, therefore, is which of the two tracks of analysis the Commission should have followed.

I. Reversal is warranted because the Commission failed to even consider the threshold question of how to treat an LLC under the Act.

As outlined in Appellants' Final Brief, the Commission's view of the facts was infected by application of the wrong paradigm and must be reversed in its entirety. The Commission never engaged in the seminal analysis of whether an LLC – an entity created by South Carolina's Uniform Limited Liability Company Act of 1996, S.C. Code Ann. § 33-44-101, which became law after the passage of the Workers' Compensation Act – should be treated as a corporation or a partnership. This error of omission, standing alone, requires reversal. *See, e.g., Brayboy v. Clark Heating Co., Inc.*, 306 S.C. 56, 58-59, 409 S.E.2d 767, 768 (1991)(finding that "[t]he findings of fact of an administrative body must be sufficiently detailed to enable the reviewing court to determine whether the

findings are supported by the evidence and whether the law has been properly applied to those findings” and determining that “a recital of conflicting testimony followed by a general conclusion is patently insufficient to enable a reviewing court to address the issues”). The result of bypassing this threshold question is an inherently contradictory analysis by the Commission – one that cites to § 42-1-130 of the Act (specifying that working business partners must opt-in to be covered) yet relies on corporation-specific terminology that is nowhere to be found in the LLC lexicon. The incongruity of the Commission’s opinion demonstrates why this omission was reversible error.¹

II. Reversal is warranted because the Commission found “Tony’s Place LLC is a corporation” and erroneously treated it as such under the Act.

It is apparent that the Commission, despite citation to conflicting support, ultimately chose the “corporation track” as its paradigm, as evidenced by the Commission’s reliance on Reyna’s opt-out form and consideration of alternate coverage under the definition of “employee.” This too was reversible error. Although the Act has never been amended to address the later creation of the LLC entity, both this Court and the Commission previously have opined that the partnership track is the correct paradigm for determining workers’ compensation coverage in the LLC context. *See Hartzell v. Palmetto Collision, LLC*, 406 S.C. 233, 244 n.5, 750 S.E.2d 97, 103 n.5 (Ct. App. 2013)(“We exclude Stallings from this analysis because, although he worked for

¹ Given this inherent conflict in the Commission’s analysis, it is not surprising that Respondent’s Brief fails to explain how § 42-1-130 provides any support for the Commission’s finding that Tony’s Place LLC “is a corporation.” (R. p. 27; *see also* R. p. 10)(“Under § 42-1-130 Tony’s Place of Sumter LLC is a corporation.”). There is no dispute that Tony’s Place LLC is a limited liability company. The question at issue in this appeal is not whether Tony’s Place LLC is a corporation or a partnership (because it is neither), but whether Tony’s Place LLC should be *treated* as a corporation or partnership under the Act. To the extent Respondent’s Brief suggests this appeal concerns the former rather than the latter, it misapprehends Appellants’ argument.

Employer as well as being the sole member of its limited liability company, the record does not indicate he *elected to be included* as an employee for workers' compensation purposes.”)(emphasis added); *Nitin Shah v. Satya, LLC & Selective Ins. Co.*, 2003 SC Wrk. Comp. LEXIS 666, at *13-14; 2003 WL 23335132, at *4 (SCWCC Full Commission Panel).²

In *Nitin Shah*, the Commission held that an LLC member must elect to be included as a covered employee under the entity’s policy, lest he be automatically excluded. 2003 SC Wrk. Comp. LEXIS 666, at *13-14; 2003 WL 23335132, at *4. The Full Commission reached this conclusion after hearing testimony from an employee in the Commission’s Coverage and Compliance Division, who “explained her opinion and the Commission’s position concerning owners of L.L.C.s . . . [and] testified that owners or members of L.L.C.s are not considered employees but are considered similar to partners in a business.” 2003 SC Wrk. Comp. LEXIS 666, at *9-11; 2003 WL 23335132, at *4. After affording weight to that interpretive guidance, the Commission found, in pertinent part:

5. That Nitin Shah did not elect to be included as a covered employee under the workers' compensation policy of Satya, L.L.C. and as a member of the L.L.C. (co-owner of the company), he must make such an election to be included or he is automatically excluded from coverage.

6. That Nitin Shah was not a covered employee under Satya, L.L.C.'s workers' compensation policy because no notification was given to the carrier under Section 42-1-130 indicating his desire to be included in coverage. Therefore, benefits in this case are denied.

7. That Defendants are not responsible for any of the Claimant's medical bills as a result of his accident of April 30, 2001 due to the fact that the

² Although not binding, the Commission’s treatment of LLC members is persuasive and consistent with the approach adopted by this Court in *Hartzell*.

Claimant was not a covered employee under the workers' compensation policy of Satya, L.L.C.

Id.

Respondent fails to address Appellants' citation to *Nitin Shah*, but nevertheless urges this Court to “defer to the Commission’s interpretation of the statute as ‘[t]he construction of a statute by the agency charged with its administration will be accorded the most respectful consideration and will not be overruled absent compelling reasons.’” (Respondent’s Brief p. 5)(quoting *Sparks v. Palmetto Hardwood, Inc.*, 406 S.C. 124, 750 S.E.2d 61 (2013)). Appellants submit that *Nitin Shah*’s well-reasoned, well-supported analysis of how LLC members are viewed under the Act presents a far clearer Commission interpretation for this Court to consider than the underlying opinion in this case, which muddles the terminology and fails to address the differences between LLCs and corporations.³

Although Respondent makes much of the fact that the Commission found in this case that Reyna was a “shareholder” in the LLC, (Respondent’s Brief, pp. 1-3), that purported “factual finding” is of no import to this appeal. As previously explained in Appellants’ Final Brief, the Commission conflated the “shareholder” designation of a

³ Because both this Court and the Commission have already addressed the issue of how LLCs are viewed under the Act, this Court need not even consider Respondent’s argument that “LLC shareholders receive the protection of limited liability – the same protection enjoyed by shareholders of traditional corporations . . . [and i]n virtually every aspect, our courts describe an LLC [outside of the Workers Compensation context] as a ‘corporate entity’ and treat it as a corporation.” (Respondent’s Brief, p. 9). Nevertheless, Appellants would be remiss not to reference the Supreme Court’s opinion in *16 Jade St., LLC v. R. Design Constr. Co., LLC*, 405 S.C. 384, 747 S.E.2d 770 (2013), which appears to have recognized a difference between the personal liability of LLC members and corporation shareholders by declining “to reach the novel issue of whether the LLC Act absolves an LLC member of personal liability for negligence committed while acting in furtherance of the company business.” 405 S.C. at 390, 747 S.E.2d at 773.

corporation with the “member” designation of a limited liability company, presumably because the underlying testimony used those terms interchangeably without regard to their legal significance. (Appellants’ Final Brief, p. 13, n.5 (citing R. p. 144, line 15-p. 151, line 12; R. p. 152, lines 4-5; R. p. 153, lines 9-10; R. p. 154, line 14-p. 155, line 9)).⁴ This confusion was compounded by Claimant Reyna’s almost-complete lack of any memory about his pre-assault circumstances. (*Id.* (citing R. p. 134, line 11-p. 136, line 18)).

It is a misnomer to call an owner of a limited liability company a “shareholder.” An LLC does not issue shares, and its owners are members not shareholders. *See* S.C. Code Ann. § 33-44-908(a)-(f)(discussing the procedure for converting a limited liability company to a corporation and noting “[a] member *who becomes a shareholder of a corporation as a result of a conversion* remains liable as a member for an obligation incurred by the limited liability company before the conversion takes effect and for which a member would be personally liable”); S.C. Code Ann. § 33-44-909(b)(6)(defining the liability that takes place after the aforementioned conversion and noting “a member's liability for all obligations of the corporation incurred after the conversion takes effect *is*

⁴ Respondent’s suggestion that the Commission’s “finding” that “Reyna is a shareholder was not appealed and is the law of the case” mischaracterizes the issues on appeal. As explained in Appellants’ Final Brief, the Commission may have erroneously transposed the terminology, but it cannot convert an LLC into a corporation by using corporation-specific terminology, i.e., calling Reyna a “shareholder” rather than a “member.” Moreover, Respondent does not dispute that the issue before the Court on appeal is a purely jurisdictional one, and this Court is not bound by the Commission's findings of fact on which jurisdiction is based. *Canady v. Charleston County Sch. Dist.*, 265 S.C. 21, 25, 216 S.E.2d 755, 757 (1975). This Court “has both the power and duty to review the entire record, find jurisdictional facts without regard to conclusions of the Commission on the issue, and decide the jurisdictional question in accord with the preponderance of evidence.” *Hernandez-Zuniga v. Tickle*, 374 S.C. 235, 243; 647 S.E.2d 691, 695 (Ct. App. 2007).

that of a shareholder of the corporation”)(emphasis added in both parentheses). It does not matter how many times the parties and/or the Commission invoke incorrect terminology when referencing Reyna’s ownership in the LLC, there can be no purported “factual finding” in the record that converts Tony’s Place LLC to an entity that it was not.⁵

Nor can Reyna circumvent his failure to opt in to coverage by suggesting that coverage still lies due to “the practical reality that while Reyna was nominally a shareholder and officer in the LLC, he actually worked as a cook at Tony’s Pizza, LLC.” (Respondent’s Brief, p. 3). Because an LLC is treated like a partnership under the Act, an LLC member cannot make an end run around the opt-in requirement by arguing that he is an “employee” standing apart from his partner status. As the South Carolina Supreme Court has held, “[w]orking partners are not employees.” *Marlow v. E. L. Jones & Son, Inc.*, 248 S.C. 568, 571, 151 S.E.2d 747, 748 (1966) (quoting Larson’s Workers’ Compensation Law §§ 54.30-54.32)(“However, we find no support in the evidence for the commission’s conclusion that claimant was an employee of either or both of his associates. While Brown was the contact man with Jones, as between themselves the three roofers were on an equal basis and regarded each other as

⁵ It is for this reason that Respondent again misapprehends Appellants’ argument that referred to the tax status of Tony’s Place LLC. (Appellants’ Final Brief, p. 15). This citation was not, as Respondent suggests, a “mix up [of] the distinction between a legal entity (LLC and corporation) and a tax entity (sole proprietor/partnership versus C-corporation versus S-corporation).” (Respondent’s Brief p. 8-9). Appellants noted that Tony’s Place LLC is classified as a partnership for federal income tax purposes only to debunk any suggestion that “Tony’s Place LLC was operating as a corporation contrary to its registered designation as a ‘limited liability company’ with the Secretary of State.” (Appellants’ Final Brief, p. 15)(citing R. pp. 187-196)).

partners.”). Any suggestion that Reyna could be both a member/owner of the LLC and an employee is pretermitted by *Marlow* and § 42-1-130.

III. Reyna’s purported additional sustaining ground lacks merit.

There is no merit to Respondent’s suggestion that as an additional sustaining ground, the Court should consider that Reyna was “a Spanish speaker with limited English and minimal business sophistication” – the implication being he could not possibly have known his status with Tony’s Place would change when he went from cook in a restaurant to part-owner of the restaurant. (Respondent’s Brief p. 10). The LLC formation documents reveal a very different set of circumstances than Respondent’s Brief portrays. While it is true that Reyna began working in 1999 as a cook in the Tony’s Place restaurant Peidis opened on Hwy 15 South (the companion restaurant to the Tony’s Pizza restaurant Peidis already owned on North Main Street), there can be no doubt that Reyna’s role at Tony’s Place changed dramatically in April 2012.

In April 2012, Tony’s Place went from being a restaurant solely owned by Peidis to a restaurant *co-owned by Peidis and Reyna* under the umbrella of an LLC *that Reyna helped form*. As a result of the 2012 Business Purchase Agreement between Peidis and Reyna, Reyna became an LLC member, and for that membership, he paid an amount equal to 30 percent of the value of Tony’s Place on Hwy 15 South. (R. p. 101, lines 9-25; R. p. 121, lines 18-25; R. pp. 190-196). In return, Reyna became a co-owner of Tony’s Place, to include ownership in the restaurant’s “[f]urniture, fixtures, furnishings, inventory and other equipment . . . [and g]oodwill.” (R. p. 191). That ownership Reyna purchased included the right “to use the name Tony’s Place of Sumter, LLC, in

connection with the business hereby sold for so long as the Seller [Peidis] and Buyer [Reyna] are co-owners of the business. . . .” (R. p. 194).

Reyna did not – as Respondent’s Brief suggests – just incidentally “buy into” the LLC. (Respondent’s Brief p. 11). Reyna *formed* the LLC as a co-organizer with Peidis in 2012 to become a co-owner of the restaurant where he worked. Although Tony’s Place (the restaurant) existed prior to 2012, Tony’s Place LLC (the entity) did not. Moreover, the Business Purchase Agreement signed by Reyna provided that the actual “Purchase Price” of his ownership would be adjusted on the day of closing for several items, including “[i]nsurance premiums.” (R. p. 192).

It is hard to imagine a set of circumstances that provided greater notice of a change in employment status than this – transitioning after 13 years of working as a restaurant cook to becoming a co-owner of the restaurant and organizing an LLC to do so.⁶ That Reyna continued to be a working member of the LLC – a cook and operational manager – does not nullify the change in his employment status that occurred when he became part-owner of the restaurant in which he had previously only worked. Contrary to Respondent’s suggestion, there is nothing about “the position in which Reyna was placed” (Respondent’s Brief, p. 10) that supports the Commission’s conclusions.

⁶ It is for this reason that Reyna’s citation to *Chavis v. Watkins*, 256 S.C. 30, 34, 180 S.E.2d 648, 650 (1971) is inapposite. In that case, Chavis, a painter, was injured while helping to renovate a newly purchased parsonage belonging to a Columbia church. Chavis was an employee of Watkins Construction Company,¹ a sole proprietorship of John T. Watkins, and worked on the church project at Watkins’ insistence. *Chavis*, 256 S.C. at 31-32, 180 S.E.2d at 649. The Court rejected the argument that the church was Chavis’ employer on that project because it found no evidence that Watkins informed Chavis the church would step into the employer shoes, and “Chavis disclaims any knowledge that Watkins had stepped out of the role in which he customarily did business as Watkins Construction Company.” *Chavis*, 256 S.C. at 34, 180 S.E.2d at 650. Chavis was initially a painter, and he remained a painter throughout the applicable time period. He did not transition from an employee role to a working-owner role as Reyna did.

CONCLUSION

This Court should reverse the erroneous findings and conclusions of the Workers' Compensation Commission which held that Claimant Elias Reyna is an employee covered under his Employer's workers' compensation policy. At both the Single Commissioner and Appellate Panel levels, the analysis of this threshold jurisdictional question was infected by assumptions lacking any validity in law or fact, *to wit*: that the Employer limited liability company is a "corporation" and that Claimant Reyna, a member of the LLC, was covered unless he "opted out." South Carolina law does not support the Commission's treatment of Employer Tony's Place of Sumter, LLC as a corporation, nor the presumption that an LLC member must opt out rather than opt in to coverage. As this Court has previously indicated, South Carolina law treats LLC members as business partners who must affirmatively *opt in* to coverage in accordance with the provisions of S.C. Code Ann. § 42-1-130.

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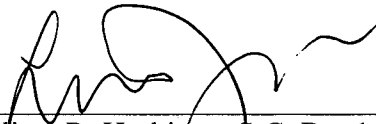
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CERTIFICATE OF COMPLIANCE

The undersigned counsel hereby certifies that Appellants' Final Reply Brief complies
with Rule 211(b) of the South Carolina Appellate Court Rules.

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