

STATE OF MICHIGAN
COURT OF APPEALS

VENKATA KRISHNA NALLABALLI,

Plaintiff-Appellant,

UNPUBLISHED
June 28, 2011

v

ESWARI ACHANTA, AND GMGT
TECHNOLOGIES, INC.,

No. 298042
Washtenaw Circuit Court
LC No. 09-001362-CK

Defendant-Appellee.

Before: WHITBECK, P.J., and MARKEY and K. F. KELLY, JJ.

PER CURIAM.

Plaintiff Venkata Nallaballi appeals as of right from the circuit court order granting summary disposition in favor of defendants Eswari Achanta and GMGT Technologies, Inc. The circuit court determined that Nallaballi had no currently enforceable rights under a contract between Nallaballi, Achanta, and GMGT because enforcement would violate federal law. We affirm.

I. FACTS

Nallaballi is an Indian citizen and was, at the time he commenced the underlying litigation, working in the United States pursuant to an H-1B visa. The term H-1B visa is derived from 8 USC 1101(a)(15)(H)(i)(b), which describes the term immigrant to include “an alien . . . who is coming temporarily to the United States to perform services . . . in a specialty occupation” The H-1B visa program is designed to allow professionals from other countries who are employed in “specialty occupations” to work in the United States on a temporary basis.¹ As an alien admitted to this county under an H-1B visa, Nallaballi can only perform services for an employer who has petitioned for an H-1B visa on his behalf.² At all

¹ 20 CFR 655.700.

² 8 USC 1184(n)(1) provides:

A nonimmigrant alien described in paragraph (2) who was previously issued a visa or otherwise provided nonimmigrant status under section 101(a)(15)(H)(i)(b) is authorized to accept new employment upon the filing by the prospective

relevant times during this litigation, Nallaballi was employed by LimoLink Corporation, an Iowa-based corporation.

On January 30, 2009, Achanta filed articles of incorporation for GMGT. GMGT is a Michigan corporation in the business of software development and strategic consulting. GMGT's operating agreement was prepared and signed by Achanta, Kalyani Gopalam, and Suneetha Nallaballi. Pursuant to the terms of the operating agreement, Achanta, Gopalam, and Suneetha Nallaballi were equal shareholders in GMGT. Suneetha Nallaballi signed the agreement on behalf of plaintiff Nallaballi, her husband.

In April 2009, Gopalam resigned from GMGT and renounced her interest in the company. Gopalam's resignation was accomplished through a stock redemption agreement. Pursuant to the agreement, both Gopalam and Suneetha Nallaballi transferred their stock certificates to GMGT in exchange for \$25,000 each. Suneetha Nallaballi, however, did not cash the \$25,000 check that GMGT gave her.

After executing the stock redemption agreement, GMGT, Achanta, Nallaballi, and Suneetha Nallaballi entered into an amended agreement voiding the stock redemption agreement between GMGT, Achanta, and Suneetha Nallaballi. The purpose of the amended agreement was for Nallaballi to assume his wife's interest in GMGT as a 50 percent shareholder. Nallaballi, however, possessed an H-1B visa at the time the amended agreement was executed. Therefore, Nallaballi could not own stock in GMGT because it had elected to be an S-corporation for federal tax purposes³. Thus, the amended agreement provided:

2. **Clarification.** The purpose of this Amended Agreement is to effectuate an agreement between GMGT, Achanta, and Nallaballi concerning their respective roles in the operation of GMGT. GMGT, Achanta, and Nallaballi agree that Nallaballi currently possesses an H-1B Visa and is working in the United States pursuant to the same. Further, [] GMGT, Achanta, and Nallaballi agree that Nallaballi intends to obtain his Green Card and, upon obtaining the same, that GMGT will promptly enter into a subsequent agreement making Nallaballi an equal legal partner in GMGT.

3. **Operation.** This Amended Agreement shall operate until such time as Nallaballi has obtained his valid Green Card and has entered into a subsequent agreement with GMGT and Achanta, at which time Nallaballi will be made a full

employer of a new petition on behalf of such nonimmigrant as provided under subsection (a).

See also 8 CFR 214.2(h)(1)(i) ("Under section 101(a)(15)(H) of the Act, an alien may be authorized to come to the United States temporarily to perform services or labor for, or to receive training from, an employer, if petitioned for by that employer.").

³ 26 USC 1361(b)(1)(C) ("For purposes of this subchapter, the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not . . . have a nonresident alien as a shareholder.").

legal partner, director, and/or officer of GMGT. This Amended Agreement will operate from the date of its signing until such time as the aforementioned subsequent agreement is entered into between the parties. Under this Amended Agreement Nallaballi shall enjoy the status of a full partner, director, and/or officer of GMGT. Accordingly, Nallaballi shall enjoy an equal fifty percent (50%) share in the following:

GMGT's profits after taxes;

GMGT's liabilities;

All decisions concerning the operation of GMGT, unless otherwise agreed to in writing and signed by the parties;

All decisions concerning the management of GMGT, unless otherwise agreed to in writing and signed by the parties;

All remaining business decisions concerning GMGT not otherwise addressed supra, unless otherwise agreed to in writing and signed by the parties; and

GMGT's outstanding common shares, 60,000 of which were listed at the time of GMGT's incorporation.

According to Nallaballi, Achanta refused to comply with the terms of the amended agreement after it was executed. Therefore, Nallaballi filed a complaint against Achanta and GMGT on November 19, 2009. In his complaint, Nallaballi alleged that Achanta refused to provide Nallaballi with account information from GMGT. Also, Nallaballi alleged that Achanta was funneling business from GMGT to another business that Achanta owned. Further, Nallaballi stated that Achanta was not consulting Nallaballi regarding GMGT's business decisions. Nallaballi's complaint included three counts: (1) breach of the amended agreement, (2) request for accounting, and (3) breach of fiduciary duty.

Achanta and GMGT moved for summary disposition pursuant to MCR 2.116(C)(8). Achanta and GMGT argued that Nallaballi lacked standing because he was not a shareholder under the terms of the amended agreement. Additionally, Achanta and GMGT argued that Nallaballi had no right to participate in the day-to-day operations and management of GMGT. Achanta and GMGT argued that allowing Nallaballi to participate in the operations of GMGT would subject GMGT to liability with the federal government because Nallaballi did not have an H-1B visa with GMGT.

After hearing arguments, the circuit court granted Achanta and GMGT's summary disposition motion from the bench, explaining as follows:

[T]he only way that I can interpret this contract so as to not make it illegal is to interpret it to say that when he gets his Green Card those will be the rights that he will exceed to.

As it is, he has by his own admission not obtained the Green Card. And at this point, he has no status, no standing to seek any remedies that are sought in this complaint. Motion is granted.

Nallaballi now appeals the circuit court's decision.

II. ENFORCEMENT OF AMENDED AGREEMENT

A. STANDARD OF REVIEW

Nallaballi argues that the circuit court erred in granting Achanta and GMGT's motion for summary disposition based on its determination that the amended agreement was unenforceable.

A motion under "MCR 2.116(C)(8) tests the legal sufficiency of the complaint by the allegations of the pleadings alone."⁴ However, when an action is based on a written contract, the plaintiff must attach a copy of the contract to the complaint.⁵ The contract then becomes part of the pleadings, and the trial court may consider it in deciding a motion for summary disposition based on the failure to state a claim.⁶ When deciding a motion under MCR 2.116(C)(8), the "trial court, and this Court must accept all well-pleaded factual allegations as true, construing them in a light most favorable to the nonmoving party."⁷ The trial court should only grant the motion "if no factual development could possibly justify recovery."⁸ This Court reviews de novo a circuit court's decision granting a motion for summary disposition brought under MCR 2.116(C)(8).⁹ To the extent that this case involves interpretation of the parties' amended agreement, this Court will review de novo the contract interpretation as a question of law.¹⁰

B. LEGAL PRINCIPLES

When interpreting a contract, the primary goal is to determine and honor the intent of the parties.¹¹ However, courts may not enforce a contract if enforcement would violate a statute.¹² Therefore, courts must determine whether a contract violates the law before enforcing it.¹³

⁴ *Feyz v Mercy Mem Hosp*, 475 Mich 663, 672; 719 NW2d 1 (2006).

⁵ *Laurel Woods Apts v Roumayah*, 274 Mich App 631, 635; 734 NW2d 217 (2007).

⁶ *Id.*

⁷ *Cummins v Robinson Twp*, 283 Mich App 677, 689; 770 NW2d 421 (2009).

⁸ *Feyz*, 475 Mich at 672.

⁹ See *Adair v Michigan*, 470 Mich 105, 119; 680 NW2d 386 (2004).

¹⁰ *Sweebe v Sweebe*, 474 Mich 151, 154; 712 NW2d 708 (2006).

¹¹ *UAW-GM Human Resource Ctr v KSL Rec Corp*, 228 Mich App 486, 491; 579 NW2d 411 (1998).

C. INTERPRETATION OF THE AGREEMENT

In this case, it is clear that the parties intended that Nallaballi have the rights of a shareholder and director/officer of GMGT. However, the parties' amended agreement was also clearly an attempt to circumvent federal tax law. GMGT elected to be treated as a subchapter S-corporation for federal tax purposes. Thus, GMGT is not taxed as a separate entity. Instead, its profits flow through to the shareholders, who then report it on their individual income tax returns.¹⁴ There are, however, several requirements for a business to qualify as a subchapter S-corporation.¹⁵ One such requirement is that a business may not have a nonresident alien as a shareholder.¹⁶ Nallaballi is a nonresident alien. Therefore, he could not be a shareholder in GMGT or it would lose its subchapter-S status.¹⁷

Nallaballi contends that his status as a shareholder does not violate federal law because a nonresident alien is permitted to be a shareholder in a C-corporation. This argument, however, ignores the parties' amended agreement. Section 2 of the amended agreement provides that "GMGT will promptly enter into a subsequent agreement making Nallaballi an equal legal partner in GMGT" *after* he has obtained his Green Card. Subsection 3 further provides: "This Amended Agreement shall operate until such time as Nallaballi has obtained his valid Green Card and has entered into a subsequent agreement with GMGT and Achanta, at which time Nallaballi will be made a full legal partner, director, and/or officer of GMGT." Subsection 3(f) goes on to state: "Under this Amended Agreement Nallaballi shall enjoy the status of full partner, officer, and/or director of GMGT. Accordingly, Nallaballi shall enjoy an equal fifty percent (50%) share in . . . GMGT's outstanding shares"

Nallaballi argues that he is a shareholder under Subsection 3(f). However, when construing the language of sections 2, 3, and 3(f) together, it is clear that the parties did not intend for Nallaballi to become a shareholder in GMGT until after he obtained his Green Card. Otherwise, GMGT would lose its S-corporation status. By his own admission, Nallaballi has not obtained a Green Card. Therefore, despite Nallaballi's arguments to the contrary, he is not a shareholder in GMGT.

Additionally, the provisions of the amended agreement providing Nallaballi with an equal share in all management and business decisions of GMGT are unenforceable. Under federal law,

¹² *Sands Appliance Servs v Wilson*, 463 Mich 231, 239; 615 NW2d 241 (2000); see also *Kukla v Perry*, 361 Mich 311, 325; 105 NW2d 176 (1960) ("[W]here an illegal contract is involved, the court will not enforce it or grant relief thereunder[.]").

¹³ See *Kaiser Steel Corp v Mullins*, 455 US 72, 77; 70 L Ed 2d 833; 102 S Ct 851 (1982) ("It is also well established . . . that a federal court has a duty to determine whether a contract violates federal law before enforcing it.").

¹⁴ 26 USC 1363(a); 26 USC 1366(a).

¹⁵ 26 USC 1361(b).

¹⁶ 26 USC 1361(b)(1)(C).

¹⁷ See 26 US 1362(c-d).

an alien admitted to the United States under an H-1B visa is only permitted to work for the employer who petitioned for the alien's H-1B visa.¹⁸ By Nallaballi's own admission, he is present in the United States under an H-1B visa. And his H-1B visa was not obtained through GMGT. Therefore, he cannot be employed by GMGT unless GMGT first files a new petition for an H-1B visa on his behalf,¹⁹ or his residency status changes. Neither has happened.

Because Nallaballi does not have an H-1B visa with GMGT, the amended agreement's provisions stating that Nallaballi will enjoy the benefits of an equal partner and director/officer of GMGT are unenforceable. For this Court to interpret the provisions otherwise would be in direct contravention of federal law. It is unlawful for an employer to hire or recruit an unauthorized alien for employment in the United States.²⁰ And any person or entity that employs an unauthorized alien is subject to criminal penalty.²¹ Therefore, until his residency status changes, Nallaballi may not participate in business operations of GMGT.

D. NALLABALLI'S EMPLOYMENT STATUS

Nallaballi, however, argues that he was not a GMGT employee. Nallaballi relies on 20 CFR 656.3, which defines "employment" as follows: "Permanent, full-time work by an employee for an employer other than oneself. For purposes of this definition, an investor is not an employee." Nallaballi argues that because he already had full-time employment with LimoLink, he was not a GMGT employee. We are not persuaded. Nallaballi seeks to participate in the management and operations of GMGT. Involvement of this nature rises above that of a passive investor and would require Nallaballi to perform the functions of an employee. That Nallaballi has an H-1B visa and full-time employment with LimoLink does not change this. The only way Nallaballi may be employed by another employer is for that employer to file a new petition on his behalf.²² As previously discussed, this has not happened.

E. SEVERABILITY

Nallaballi argues that even if some of the provisions of the amended agreement are unenforceable, others remain effective because the agreement includes a severability clause. Specifically, Nallaballi argues that subsections 3(a), (b), and (f) are enforceable and entitle him to a 50 percent share in GMGT's profits, liabilities, and outstanding common stock. We disagree that these subsections are enforceable.

¹⁸ 8 CFR 214.2(h)(1)(i).

¹⁹ 8 USC 1184(n)(1).

²⁰ 8 USC 1324a(a)(1)(A).

²¹ 8 USC 1324a(f).

²² See 8 USC 1184(n)(1).

As a general rule, if a portion of a contract is invalid or unenforceable, that does not void other valid provisions if the provisions are severable.²³ “The primary consideration in determining whether a contractual provision is severable is the intent of the parties.”²⁴ In this case, the amended agreement includes a severability clause:

10. Severability. Every provision of this Amended Agreement is intended to be severable unless otherwise noted. In the event that any term or provision hereof is declared to be illegal or invalid for any reason whatsoever by a court of competent jurisdiction, such illegality or invalidity shall not affect the balance of the terms and provisions hereof, which terms and provisions shall remain binding and enforceable. [Amended agreement, p 4.]

Based on this language, it is clear that the parties intended that all provisions of the amended agreement be severable and enforceable in the event that any other provisions were deemed unenforceable. The severability provision, however, cannot save subsections 3(a), (b), and (f) because they are not enforceable in their own right.

As previously discussed, GMGT has elected to be treated as a subchapter S-corporation for federal tax purposes. One of the requirements for a business to qualify as a subchapter S-corporation is that it may not have a nonresident alien as a shareholder.²⁵ Although Nallaballi is not the legal or record owner of shares in GMGT, allowing him a 50 percent share in the profits, liabilities, and outstanding common stock would make him the shareholder for federal tax purposes. 26 CFR 1.1361-1(e) provides in part:

(e) Number of shareholders—(1) General rule. A corporation does not qualify as a small business corporation if it has more than the number of shareholders provided in section 1361(b)(1)(A). Ordinarily, the person who would have to include in gross income dividends distributed with respect to the stock of the corporation (if the corporation were a C corporation) is considered to be the shareholder of the corporation.

* * *

The person for whom stock of a corporation is held by a nominee, guardian, custodian, or an agent is considered to be the shareholder of the corporation for purposes of this paragraph (e) and paragraphs (f) and (g) of this section.

As applied to this case, 26 CFR 1.1361-1(e) does not allow Nallaballi to share equally in the profits, liability, and outstanding stock of GMGT. If subsections 3(a), (b), and (f) of the

²³ *Professional Rehabilitation Assoc v State Farm Mut Automobile Ins Co*, 228 Mich App 167, 174; 577 NW2d 909 (1998).

²⁴ *Id.*

²⁵ 26 USC 1361(b)(1)(C).

amended agreement are enforced, Nallaballi would be required to include the dividends distributed by GMGT in his gross income. Therefore, he would be considered the shareholder of GMGT despite the fact that the shares are not held in his name. As such, enforcement of these provisions would violate 26 USC 1361(b)(1)(C) by allowing a nonresident alien to be a shareholder in an S-corporation.

F. CONCLUSION

In sum, Nallaballi has no currently enforceable rights under the terms of the amended agreement. The only way to interpret the amended agreement without violating federal law is to interpret it as if it were an executory contract or contract subject to a condition precedent. When Nallaballi obtains his Green Card, but only at that time, he will have the rights listed in the amended agreement. Any other interpretation would violate federal law.

We affirm.

/s/ William C. Whitbeck

/s/ Jane E. Markey

/s/ Kirsten Frank Kelly