No. 331148

COURT OF APPEALS, DIVISION III
OF THE STATE OF WASHINGTON

RICK A. HOLMAN, individually and on behalf of WOLF CREEK HOLDINGS OF SPOKANE, LLC, a Washington Limited Liability Company,

Respondents

v.

BRIAN W. BRADY and MOUNTAIN BROADCASTING, LLC, a Washington Limited Liability Company,

Appellants

BRIEF OF APPELLANTS

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I. INTRODUCTION

Rick Holman and Brian Brady are co-owners of Wolf Creek Holdings, LLC ("Wolf Creek"), which owns a building leased to a television station in Spokane. The television station is owned by Mountain Broadcasting, LLC ("Mountain Broadcasting"), a company indirectly owned by Brady. After its several requests for relief from the unfairly high rent in the 1993 Lease were rebuffed, Mountain Broadcasting notified Wolf Creek that it would not be renewing its 1998 Lease by a letter to Brady dated September 21, 2012 ("Non-Renewal Notice"). Thereafter, Mountain Broadcasting negotiated a new lease with Wolf Creek (through negotiations with Brady) ("New Lease").

Holman individually, and derivatively on behalf of Wolf Creek, brought this lawsuit against both Brady and Mountain Broadcasting, asserting five causes of action premised on allegations that (1) the Non-Renewal Notice was ineffective (meaning the original 1998 Lease is still in place) and/or (2) Brady lacked authority to execute the New Lease. Holman asserts that the Non-Renewal Notice was invalid because it was not sent via registered or certified mail and that Brady lacked authority under the Wolf Creek LLC Agreement to bind the company to the New Lease. Both contentions are founded on erroneous readings of the expired 1998 Lease and Wolf Creek LLC Agreement.

Holman's derivative claims fail to satisfy CR 23.1, which sets forth the requirements for asserting claims derivatively on behalf of a limited liability company. It is undisputed that Holman did not comply with CR 23.1; therefore, the trial court erred in not dismissing his derivative claims. Holman's derivative action also fails because he impermissibly joined personal claims with his purported derivative claims, which created a fatal conflict of interest.

The derivative claims against Mountain Broadcasting allege that the Non-Renewal Notice had to be sent to Wolf Creek via certified or registered mail. The 1998 Lease, however, required only timely written notice; it is not disputed this was sent to and received by Wolf Creek. The now-terminated lease provided that written notices, if sent via certified or registered United States mail, would be conclusively "deemed" delivered. It did not preclude other methods of delivery. The lower court erroneously treated this provision as a "requirement" that the notice ***must*** have been sent via certified or registered mail. The 1998 Lease did not require notice by registered or certified mail. The undisputed evidence presented to the trial court established actual delivery. Because the Non-Renewal Notice was effective, the 1998 Lease did not automatically renew, and the trial court committed reversible error in not granting summary judgment to the contrary.

Holman also erroneously claims that Brady lacked authorization to enter into the New Lease. The Wolf Creek LLC Agreement specifically authorized either Holman or Brady to execute leases on Wolf Creek's behalf, so long as the terms were fair to Wolf Creek. Holman presented no evidence below, nor does he even contend, that the New Lease was unfair to Wolf Creek, although he does have a desire to continue with the grossly inflated lease rates under the now expired 1998 Lease. Nothing in the Wolf Creek LLC Agreement required Holman's consent to the New Lease or restricted Brady from acting on behalf of the Wolf Creek in this regard. The trial court erred in invalidating the New Lease because Holman did not consent to it.

II. ASSIGNMENTS OF ERROR

1. The trial court erred in not dismissing Holman's derivative claims against Mountain Broadcasting.[1]

2. The trial court erred in denying Brady and Mountain Broadcasting's Motion for Summary Judgment.[2]

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[1] CP 153-155.

[2] CP 370-372.

3. The trial court erred in granting Holman's Motion for Partial Summary Judgment against Mountain Broadcasting.[3]

4. The trial court erred in entering judgment against Mountain Broadcasting in favor of Holman personally.[4]

III. ISSUES PERTAINING TO ASSIGNMENTS OF ERROR

1. Whether CR 23.1 or RCW 25.15 sets forth the applicable standard for assessing if Holman can assert derivative claims against Mountain Broadcasting on behalf of Wolf Creek. (Assignment of Error 1).

2. Whether Holman's derivative claims fail where:

   a. it is undisputed that Holman did not comply with CR 23.1 because his Complaint did not contain a verified statement that his derivative action was not brought collusively to confer personal jurisdiction over Brady;

   b. Holman did not establish under CR 23.1 that he could fairly and adequately represent the interests of Wolf Creek (and Brady) in a derivative action against Mountain Broadcasting; and

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[3] CP 370-372.

[4] CP 385-387.

c. Holman created a conflict of interest by impermissibly joining personal claims against Brady and derivative claims against Mountain Broadcasting on behalf of Wolf Creek.

(Assignment of Error 1).

3. Whether the trial court erred in finding that Mountain Broadcasting's Non-Renewal Notice was required to be sent via certified or registered mail to be effective to cancel the lease between Mountain Broadcasting and Wolf Creek when the Lease Agreement did not impose that requirement and where it is undisputed that the Non-Renewal Notice was actually received by Wolf Creek. (Assignments of Error 2-3).

4. Whether the trial court erred in finding that Mountain Broadcasting's Non-Renewal Notice was required to be delivered to Holman personally to be effective to cancel the lease between Mountain Broadcasting and Wolf Creek when the Lease Agreement did not impose that requirement and where it is undisputed that the Non-Renewal Notice was received by Wolf Creek. (Assignments of Error 2-3).

5. Whether the Wolf Creek LLC Agreement authorized Brady, on behalf of Wolf Creek, to enter into the New Lease with Mountain Broadcasting. (Assignments of Error 2-3).

6. Whether the trial court erred in entering judgment against Mountain Broadcasting in favor of Holman, personally,

instead of in favor of Wolf Creek where Holman has no personal claims. (Assignment of Error 4).

IV. STATEMENT OF THE CASE

A. Background facts.

Rick Holman and Brian Brady are the co-owners of Wolf Creek LLC, each having a 50% member interest.[5] Wolf Creek owns commercial real estate in Spokane, Washington, which it leases to Mountain Broadcasting, owner of Spokane's KAYU-TV.[6] The sole member of Mountain Broadcasting is Northwest Broadcasting, Inc., which is owned by entities in which Brady has ownership interests.[7]

The initial term of the lease between Wolf Creek and Mountain Broadcasting was 15 years, commencing on January 12, 1998.[8] The original lease ("1998 Lease") was to be automatically extended for successive 5-year terms "unless Tenant shall give notice to the Landlord at least ninety (90) days prior to the Extension Date that the Tenant elects that the term of this Lease not be extended."[9]

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[5] CP 5-66 (Complaint at ¶¶ 1.2, 1.3, and 3.2).

[6] *Id.* (Complaint at ¶¶ 3.5 and 3.6).

[7] *Id.* (Complaint at ¶¶ 3.6 and 3.7).

[8] CP 187 (1998 Lease, Article II).

[9] *Id.*

Article XXIII of the 1998 Lease specified how notice was to be provided, stating that "[a]ll notices or demands of any kind required or desired to be given by the Landlord or Tenant hereunder shall be in writing and shall be deemed delivered 48 hours after depositing the notice or demand in the United States mail, certified or registered, postage prepaid, addressed to landlord or tenant respectively at the addresses set forth after their signature at the end of this Lease."[10] Of note, there is no address listed under the Landlord's name at the end of the 1998 Lease.[11] Brady was identified in the 1998 Lease under the "Landlord" signature block as the person to sign on behalf of Wolf Creek LLC; Holman was not.[12]

It is undisputed that for years prior to the expiration of the original Lease term, Mountain Broadcasting had advised Wolf Creek that the lease rent (which under the 1998 Lease was increased each year without reference to local real estate market conditions) had reached an amount that was far in excess of market. For example, in a letter dated November 8, 2005, Wolf Creek was advised that the lease rate "is completely out of step

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[10] CP 208 (1998 Lease, Article XXIII).

[11] CP 211.

[12] *Id.*

with comparable office rents on Spokane's South Hill."[13] Again on March 19, 2009, more than three years before the 1998 Lease was set to expire, Mountain Broadcasting notified Wolf Creek that the lease rate was "completely out of sync with the current commercial market on Spokane's South Hill.[14] In response, as it did every year, Wolf Creek, acting through Holman, responded by raising the rent.[15]

As a consequence of these serial lease rate increases, by September 2012, Mountain Broadcast was paying $23.52/square foot on a triple net basis, and the lease rate was scheduled to increase to $24.35/square foot if the 1998 Lease was extended in 2013.[16] Based on Mountain Broadcasting's market surveys in 2012, the market for similar property was a fraction of this price.[17] Had Mountain Broadcasting elected to renew the 1998 Lease in 2013, the lease rate would have been about 300% above

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[13] CP 216 – 170 (November 8, 2005, letter).

[14] CP 219-220 (March 19, 2009, letter).

[15] CP 222 (December 9, 2008, letter); CP 223 (December 14, 2009, letter); CP 224 (December 6, 2010, letter); and CP 225 (December 2, 2011 letter). Of note, there is no evidence that Holman sent any of these rent increase notices via registered or certified U.S. Mail.

[16] CP 178.

[17] *Id.*

market.[18] Not surprisingly, Mountain Broadcasting was not interested in extending the lease at this rate.

To prevent the automatic renewal of the 1998 Lease, Mountain Broadcasting was required to give written notice of its intent not to extend the lease at least 90 days before the 15th anniversary of the Lease.[19] As the lease commenced on January 12, 1998, written notice of non-renewal was required on or before October 12, 2012. Given Mountain Broadcasting's dissatisfaction with the lease terms, it was not at all surprising that on September 20, 2012, well within the time period for notice non-renewal set forth in the 1998 Lease, Mountain Broadcasting sent Brady of Wolf Creek a Non-Renewal Notice via overnight delivery.[20] The Non-Renewal Notice was sent to Brady in his "position as a member of Wolf Creek Holdings of Spokane LLC," and stated: "This letter shall constitute notice that Mountain is electing that the term of the Lease not be extended as provided in said Article II."[21]

It is not disputed that Wolf Creek timely received the Non-Renewal Notice through Brady: Jon Rand, General

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[18] *Id.*, CP 178.

[19] CP 39

[20] CP 227

[21] CP 227 (September 21, 2012, letter); CP 172-176, and CP 178; and CP 284-291.

Manager of Mountain Broadcasting, testified that he authorized and directed Mountain Broadcasting's counsel (Fred Levy of Brown Rudnick in Washington, D.C.) to send the Non-Renewal Notice to Brady over a facsimile of his (Mr. Rand's) signature.[22] Diane M. Palacios, legal assistant to Mr. Levy, testified that on September 20, 2012,[23] she sent the Non-Renewal Notice via Federal Express overnight delivery to Brady.[24] Ms. Palacios received written confirmation from Federal Express that the envelope containing the Non-Renewal Notice was, in fact, delivered to Brady on September 21, 2012, at 1:58 p.m., and had been signed for by "P Billingsley."[25]

Pamela Billingsley, Brady's administrative assistant, confirmed she received a copy of the Non-Renewal Notice on behalf of Brady via overnight delivery on or about September 24, 2012.[26] Brady testified that he received the Non-Renewal Notice shortly after it was sent.[27] What is more, Brady

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[22] CP 268-283 and CP 254-264 (Deposition of Jon D. Rand, pages 96, 97, 125).

[23] While the Non-Renewal Notice was sent on September 20, 2012, it is dated September 21, 2012. Ms. Palacios testified that the letter was dated September 21, 2012, but was ready to be sent mid-day on September 20, 2012. CP 285 (Palacios Decl. at ¶ 4).

[24] CP 285 (Palacios Decl. at ¶¶ 3-5).

[25] CP 285-286 (Palacios Decl. at ¶¶ 6-7).

[26] CP 172 and 178. It should be noted that September 21, 2012, was a Friday and September 24, 2012, was a Monday.

[27] CP 182 (Brady Decl. at ¶ 7).

contemporaneously confirmed receipt of the Non-Renewal Notice via a return letter dated October 4, 2012, acknowledging, on behalf of Wolf Creek, that Mountain Broadcasting "was electing not to extend the terms of its Lease with Wolf Creek Holdings of Spokane, LLC."[28]

After the 1998 Lease expired, Mountain Broadcasting and Wolf Creek entered into a New Lease.[29] The New Lease was negotiated between Jon Rand of Mountain Broadcasting and Brady on behalf of Wolf Creek.[30] Mountain Broadcasting originally proposed a new lease rate of $9/square foot for a three year term, which it claimed was "at the very high end of the rental market."[31] In response, Brady (on behalf of Wolf Creek), acknowledged receipt of the Non-Renewal Notice, but indicated that $9/square foot was not an acceptable rate.[32] Based on market data, Brady countered with a lease rate of $15/square foot for a three-year term, with annual CPI adjustments. [33]

On October 10, 2012, Rand (on behalf of Mountain Broadcasting), asserted that the proposed $15/square foot rate

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[28] CP 229 (October 4, 2012, letter) and CP 131.

[29] CP 9 (Complaint at ¶ 3.14).

[30] CP 178, 131-133.

[31] CP 178.

[32] CP 131-133 (October 4, 2012 letter).

[33] *Id.*

was still 200% of the comparable market properties.[34] However, "To put these negotiations to bed," Mountain Broadcasting proposed a three year lease term at $14/square foot.[35] As Brady notified Holman in November 2012, this $14/square foot rate in the New Lease "is more than 150% of the average market rate of approximately $8.30/sq. ft. which is reflected in the market survey."[36]

Holman has never asserted that the terms of the New Lease are not fair to Wolf Creek, nor could he, as the new lease rate is still more than 150% above market. Rather, Holman desires to continue with the inflated lease rate under the expired 1998 Lease, which would have been more than 300% above market if it was extended. Desiring to keep the above-market lease rates embodied in the 1998 Lease, Holman only claims that his consent was required on behalf of Wolf Creek to enter into the New Lease – a proposition that contradicts the unambiguous terms of Wolf Creek's LLC Agreement.

B. Holman's Complaint.

In February 2013, Holman, both individually and on behalf of Wolf Creek, brought this lawsuit against Brady and

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[34] CP 134.

[35] CP 134.

[36] CP 124 and 127.

Mountain Broadcasting. In five separate causes of actions[37], Holman claims that the Non-Renewal Notice and New Lease were invalid:

First Cause of Action:[38] Holman alleges that the Non-Renewal Notice was ineffective because it was not sent to Wolf Creek via certified or registered mail and, therefore, the 1998 Lease was automatically extended for an additional 5 years until January 11, 2018. Holman claims that Mountain Broadcasting breached the extended term of the 1998 Lease, as it was not making payments thereunder, but instead was paying under the terms of the New Lease.

Second Cause of Action:[39] In the alternative, if the Non-Renewal Notice was proper, Holman claims that Brady lacked authority to bind Wolf Creek to the New Lease. It is alleged that Mountain Broadcasting is a Holdover Tenant under the 1998 Lease, and was in breach of the 1998 Lease by not making the required holdover payments.

Third Cause of Action:[40] Holman also alleges that Brady breached the Wolf Creek LLC Agreement "by unilaterally accepting a deficient notice of non-renewal of the January 12,

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[37] CP 5-66 (Complaint).

[38] CP 10-11.

[39] CP 11-12.

[40] CP 12.

1998 Lease Agreement from Mountain Broadcasting and by entering into a new Lease Agreement with Mountain Broadcasting without disclosing the Lease Agreement terms to Holman and without obtaining his consent." Holman also alleges that Brady further breached the Wolf Creek LLC Agreement "by directing and participating in Mountain's breach of the existing Lease Agreement for defendant Brady's own personal gain."[41]

Fourth Cause of Action:[42] Holman further alleges that Brady breached his implied covenant of good faith and fair dealing under the Wolf Creek LLC Agreement. The allegations supporting this cause of action are identical to those supporting the Third Cause of Action quoted above.

Fifth Cause of Action:[43] Holman's final allegation is that Brady breached his fiduciary duties to Wolf Creek and Holman. The allegations in the Complaint supporting this cause of action are identical to those supporting the Third and Fourth Causes of Action quoted above.

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[41] *Id.*

[42] CP 13.

[43] CP 14.

C. Procedural history.

Brady and Mountain Broadcasting moved to dismiss Holman's Complaint based on the lack of personal jurisdiction over Brady (a resident of Michigan), Holman's failure to comply with the rules governing pleading derivative claims (CR 23.1), and Holman's improper joinder of personal claims against Brady and derivative claims on behalf of Mountain Broadcasting.[44] The trial court denied this motion, finding it had personal jurisdiction over Brady and that Holman's derivative claims and personal claims were appropriate.[45]

Thereafter, Brady filed a summary judgment motion seeking to dismiss all claims in Holman's Complaint based on undisputed evidence that the Non-Renewal Notice was effective and that Brady was authorized to enter the New Lease with Mountain Broadcasting.[46] Holman filed a cross-motion for partial summary judgment, arguing the Non-Renewal Notice was ineffective in preventing the 1998 Lease from automatically renewing, and that Brady lacked authority to enter into the New Lease on behalf of Wolf Creek.[47] The trial court denied Brady's motion and granted Holman's motion, finding that Mountain

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[44] CP 79-89.

[45] CP 153-155.

[46] CP 292-308.

[47] CP 311-336.

Broadcasting breached the 1998 Lease "for the failure to give timely notice to Wolf Creek by certified or registered mail of its intent not to renew the Lease Agreement, and because notice was not sent to the Landlord" (First Cause of Action) and that Brady breached the Wolf Creek LLC Agreement (Third Cause of Action) by "unilaterally accepting a deficient notice of non-renewal of Lease Agreement from Mountain, and by entering into a new Lease Agreement with Mountain without disclosing the Lease Agreement terms to Mr. Holman and without obtaining his consent."[48]

Brady and Mountain sought discretionary review of the trial court's summary judgment ruling.[49] Subsequently, the trial court entered a judgment against Mountain Broadcasting in favor of Holman and Wolf Creek on his claim for attorney fees, costs and interest ("Judgment").[50] On the same date, the trial court entered an order granting CR 54(b) Certification and Entry of Final Judgment as to Mountain Broadcasting, LLC on Plaintiffs' Attorney's Fees and Costs and Interest, with the issue of unpaid rent to Wolf Creek reserved to a later date.[51] Brady

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[48] CP 370-372.

[49] CP 373-378.

[50] CP 385-387.

[51] CP 379-384.

and Mountain Broadcasting then timely filed a Notice of Appeal of the Judgment against Mountain Broadcasting.[52]

The parties then stipulated to entry of an order staying the remaining proceedings pending appellate review, and that Holman would dismiss his breach of fiduciary claim against Brady without prejudice, and would not refile the claim except under specified conditions.[53] The parties also agreed to dissolve Wolf Creek upon entry of final judgment in this matter.[54] Pursuant to that stipulation, the parties filed a Stipulated Motion and Order of Dismissal of Breach of Fiduciary Duty Claim Without Prejudice, which was entered by the trial court.[55] The trial court then granted the parties' Stipulated Motion to Stay Proceedings pending appellate review.[56]

V. SUMMARY OF ARGUMENT

The trial court erred in failing to dismiss Holman's Complaint for three primary reasons. First, Holman lacked standing to assert derivative claims on behalf of Wolf Creek under CR 23.1, and impermissibly joined with his derivative claims, personal claims against Brady. Second, Mountain

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[52] CP 388-392 (CP 393-398 – Notice of Supersedeas Bond).

[53] CP 399-400.

[54] *Id. at* CP 400.

[55] CP 401-402.

[56] CP 403-404.

Broadcasting's Non-Renewal Notice was effective to terminate the 1998 Lease. Third, Brady possessed the authority under the Wolf Creek LLC Agreement to enter into the New Lease with Mountain Broadcasting.

CR 23.1 required a verified Complaint, attesting that the proposed derivative claims were not a collusive mechanism to confer personal jurisdiction over Brady and that Holman could fairly and adequately represent Wolf Creek (and Brady's) interests. Holman failed to allege, let alone prove, these requirements. His derivative claims, therefore, fail as a matter of law and should have been dismissed. They also fail because he impermissibly joined personal claims with his derivative claims, creating a conflict of interest (when summary judgment was granted on two of the derivative claims, Holman took judgment personally and resisted Brady's argument that judgment on the claims relating to the lease should be solely in favor of Wolf Creek).

Ignoring the plain meaning of the 1998 Lease, the trial court concluded that the Non-Renewal Notice had to be delivered to Holman via registered or certified mail. The 1998 Lease required notice to the Landlord (Wolf Creek), not any individual member. Brady is a member of Wolf Creek, authorized to act on behalf of the entity, and actual delivery of the Non-Renewal Notice to him satisfied Mountain Broadcasting's contractual notice duty.

The 1998 Lease states that written notices, if sent via certified or registered United States mail, would be conclusively "deemed" delivered. It did not preclude other methods of delivery. It is undisputed that Mountain Broadcasting timely sent the required notice of non-renewal, and that it was received by Brady via overnight delivery as a member of Wolf Creek. Mountain Broadcasting's Non-Renewal Notice was effective, and the 1998 Lease terminated at the expiration of the initial 15-year term.

The trial court also failed to apply the operative provisions of the Wolf Creek, LLC Agreement in ruling that Brady lacked authority to enter into the New Lease, even though both Brady and Holman were expressly granted the authority under the Wolf Creek LLC Agreement to execute leases on the entities' behalf.[57] Wolf Creek is a member-managed LLC (as opposed to run by a manager), thus "all members" possessed the "authority to obligate or bind the

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[57] This authority is expressly extended to executing leases per Article XIII, section 1, which confirms that "**any member** ... shall have the power to execute and deliver proxies, stock powers, deeds, **leases**, contracts ..... for and in the name of the Company.... CP 248 (Article XIII, Section 1, Wolf Creek, LLC Agreement) (emphasis added).

company in connection with any matter,"[58] so long as the transaction is "fair" to Wolf Creek. Holman offered no evidence, nor did he contend, that the New Lease was unfair, but only claimed his consent to it was required. As Holman's consent to the New Lease was not required, the trial court erred in not entering summary judgment in favor of Mountain Broadcasting on this issue.

VI. ARGUMENT

A. The trial court's rulings on summary judgment are subject to *de novo* review.

An order granting summary judgment is subject to review *de novo*, and the appellate court engages in the same inquiry as the trial. *See Folsom v. Burger King*, 135 Wn.2d 658, 663, 958 P.2d 301 (1998). Summary judgment is only warranted when "there is no genuine issue as to any material fact" and "the moving party is entitled to judgment as a matter of law." CR 56(c). The burden is on the party seeking summary judgment to demonstrate the absence of a genuine issue of material fact. *Folsom*, 135 Wn.2d at 663. All of the facts and reasonable inferences must be viewed in the light most favorable to the nonmoving party. *See Ruvalcaba v. Kwang Ho Baek*, 175 Wn.2d 1, 6, 282 P.3d 1083 (2012). Even where the evidentiary facts are

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[58] CP 181-185 and CP 235 (Article V, Section 2, Wolf Creek, LLC Agreement).

undisputed, if reasonable minds could draw different inferences from those facts, then summary judgment is not warranted. *See Chelan Cnty. Deputy Sheriffs' Ass'n v. Chelan Cnty.*, 109 Wn.2d 282, 294-95, 745 P.2d 1 (1987).

For purposes of determining whether there is a genuine issue of material fact for trial, materiality is based on the governing substantive law. *See Rossiter v. Moore*, 59 Wn.2d 722, 724, 370 P.2d 250 (1962) (indicating "material facts" are determined "under applicable principles of substantive law"; quotation omitted); *Morris v. McNicol*, 83 Wn.2d 491, 494, 519 P.2d 7 (1974) (indicating "a 'material fact' is a fact upon which the outcome of the litigation depends").

B. Holman's derivative claims fail under CR 23.1.

In his Complaint, Holman asserts both a personal claim against Brady (breach of fiduciary duty) and derivative claims against Mountain Broadcasting on behalf of Wolf Creek. Since the only claims against Mountain Broadcasting are those asserted derivatively by Holman, Holman's failure to assert valid derivative claims mandates dismissal of Mountain Broadcasting from the lawsuit.[59]

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[59] Given that Holman is a citizen of California, and Brady is a citizen of Michigan, the assertion of jurisdiction here over Brady must ultimately fall with the dismissal of Wolf Creek.

Wolf Creek is a third person, being a distinct legal entity, having its own rights and duties (even if Holman owns part of it), and Holman cannot assert Wolf Creek's rights on his own, individual behalf. *See Gustafson v. Gustafson*, 47 Wn. App. 272, 276, 734 P.2d 949 (1987); *Sabey v. Howard Johnson Co.*, 101 Wn. App. 575, 584, 5 P.3d 730 (2000). Through his derivative claim, Holman seeks to pursue an exception, by invoking the right of certain owners or beneficiaries to bring suit derivatively on behalf of an entity that is not pursuing its own claims. That claim should have been dismissed by the trial court, because Holman has not followed the rules governing the pleading of derivative actions, and because the essential conditions for a derivative action have not, and cannot be met.

Standing is a common law doctrine that prohibits a litigant from raising another's legal right. *Grant Cnty. Fire Prot. Dist. No. 5 v. City of Moses Lake,* 150 Wn.2d 791, 802, 83 P.3d 419 (2004). An exception to this rule exists when a shareholder or member of a limited liability company attempts to bring a derivative action, but to do so the standing and pleading requirements in CR 23.1 must first be met:

> In a derivative action brought by one or more shareholders or members to enforce a right of a

> corporation or of an unincorporated association,[60] the corporation or association having failed to enforce a right which may be properly asserted by it, the complaint shall be verified and shall allege (a) that the plaintiff was a shareholder or member at the time of the transaction of which he complains. . . and (b) that the action is not a collusive one to confer jurisdiction on a court of this state which it would not otherwise have. . . . The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association.

CR 23.1 imposes four requirements upon a party who wishes to bring derivative actions, all of which must be alleged in a verified complaint: (1) the claimant must be a shareholder at the time of the complained of transaction, (2) the action must not simply be collusive in order to confer jurisdiction on the court, (3) the complaint must allege what attempts the claimant made to have the directors or company bring the suit, and (4) the claimant bringing suit must fairly and adequately represent the interests of the other shareholders or members. *Gustafson,*

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[60] RCW 1.16.080 states that "Unless the context clearly indicates otherwise, the terms "association," "unincorporated association," and "person, firm, or corporation" or substantially identical terms shall, without limiting the application of any term to any other type of legal entity, be construed to include a limited liability company." Thus, CR 23.1 applies equally to shareholders and members of limited liability companies; *see also Taylor v. Moskow*, No. 13–10802–FDS, 2013 WL 5508157 at *4 (D. Mass. Oct. 1, 2013); *In re Weeks Landing, LLC*, 439 B.R. 897, 913 (2010).

47 Wn. App. at 276-77, 734 P.2d at 953. Holman's Complaint fails to comply with CR 23.1 in several key respects.

1. Holman's Complaint was not verified.

CR 23.1 specifically demands that a derivative complaint be verified: "the complaint ***shall*** be verified ...". CR 23.1 (emphasis added). The mandatory verification requirement requires a plaintiff, at the time the complaint is filed, to attest to the veracity of the factual assertions under penalty of perjury. *State v. Heyes*, 44 Wn.2d 579, 587, 269 P.2d 577, 582 (1954) (*citing People v. Godines*, 17 Cal.App.2d 721, 62 P.2d 787 (1936) (a first degree perjury prosecution may be based on a verified complaint containing false allegations regarding material matters)).

Several critical allegations must be attested to under CR 23.1 when requesting derivative relief. Holman's failure to comply with those mandatory pleading requirement commands dismissal of his derivative claims against Mountain Broadcasting.

2. Holman did not verify that his derivative claims were not merely collusive to confer jurisdiction over Brady.

Holman's Complaint is independently deficient because it does not contain a verified statement that Holman did not bring the complaint against Mountain Broadcasting collusively for the sake of obtaining jurisdiction in Washington over Brady. Holman was understandably unwilling to make that sworn statement, since this case is really only brought as a derivative action in order to obtain jurisdiction in Washington because there is no personal jurisdiction over Brady (a citizen of Michigan) in Washington. Holman (a citizen of California) sought to create jurisdiction by alleging wrongs on Wolf Creek's behalf against Brady, where Wolf Creek is a Washington LLC that owns real estate in Spokane. Holman is bound to swear, under penalty of perjury, that was not his intention, and he has failed to do so. Holman's derivative claims should be dismissed for that reason alone.[61]

3. Holman's lawsuit is not in the best interest of Wolf Creek and his assertion of individual claims presents an impermissible conflict.

CR 23.1 further requires that: "The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association." Holman's Complaint is deficient

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[61] In his Motion to Dismiss, Brady sought dismissal of the claims against him for lack of personal jurisdiction. Brady believes this ruling was in error. However, there is no final judgment on claims against Brady (the trial court's CR 54(b) certification pertained to the judgment against Mountain Broadcasting). Should a final judgment be entered against Brady, he intends to further contest personal jurisdiction by appeal.

under this part of CR 23.1 for two reasons: (1) his claim, which is really a restatement of his personal claim against Brady, cannot be in the best interest of Wolf Creek, and (2) by also asserting personal claims against Brady, along with the derivative claims, Holman created an impermissible conflict, because the real purpose of his claim is to benefit himself at the expense of the other member of Wolf Creek LLC, Brady.

a. Holman's derivative claims are disguised claims against Brady.

There are only two members of Wolf Creek LLC: Holman and Brady. Holman cannot, therefore, satisfy any test requiring him to fairly represent the interest of the members of Wolf Creek as a class. Holman's proper remedy is a direct action against Brady for declaratory relief (as to the members' rights and responsibilities vis-a-vis Wolf Creek), and for damages to the extent he alleges financial harm. Wolf Creek is neither a necessary nor appropriate party to such an action; it was added merely to assist in obtaining jurisdiction in an inconvenient forum.

Further, the court is entitled to judge, from the allegations within Holman's complaint, whether the action is truly in the best interests of Wolf Creek and <u>all</u> members of Wolf Creek LLC. Holman alleges that Brady breached both contractual and alleged fiduciary duties to Holman by receiving notice of termination of a lease between Wolf Creek and Mountain. The claim is highly dubious on its face; Holman has articulated no basis on which to understand how a party might properly refuse to receive notice duly sent by another party, or why a court should recognize a duty to do so. Wolf Creek entered the New Lease with Mountain Broadcasting; Holman has not shown how the New Lease is either unfair or how it is in the interest of Wolf Creek to invalidate the New Lease.

The entire purpose of this lawsuit is for Holman to gain advantage over Brady, the only other member of the LLC, not to advocate for both members' interests on a common footing. The case should have been brought as a suit for declaratory judgment as to control of the LLC, or for asserted breach of the LLC agreement to the extent Holman may believe the New Lease with Mountain Broadcasting is somehow unfair. It wasn't brought that way, however, because Holman required Wolf Creek to support jurisdiction in a forum that is inconvenient to Brady. There is no basis for a derivative action, except as a forbidden aid to personal jurisdiction that otherwise does not exist.

b. Holman improperly joined derivative and personal claims.

Holman also has a conflict of interest because he cannot fairly and adequately represent Wolf Creek in a derivative action, as required by Rule 23.1, while pursuing his own direct claims. The "general rule [is that] a plaintiff cannot join in the same suit a [derivative] claim on behalf of the corporation and an individual, personal claim against the defendants." 3A Tegland, Washington Practice: Rules Practice at 518 (5th Ed. 2006) (*citing Hames v. Spokane-Benton Cnty. Nat. Gas Co.*, 118 Wash. 156 (1922)). The rationale underlying this rule is that joinder of these type of claims also creates a conflict of interest. *See St. Clair Shores Gen. Emp. Ret. Sys. v. Eibeler*, No. 06–CV–688, 2006 WL 2849783, at *7 (S.D.N.Y. Oct. 4, 2006) ("Courts in this Circuit have long found that plaintiffs attempting to advance derivative and direct claims in the same action face an impermissible conflict of interest."). In light of this, courts "have applied a strict standard in scrutinizing simultaneous direct and derivative actions for signs of conflict." *Ryan v. Aetna Life,* 765 F. Supp. 133, 135 (S.D.N.Y.1991); *see also Cordts-Auth v. Crunk,* LLC, 815 F. Supp. 2d 778, 793-94 (S.D.N.Y. 2011) aff'd, 479 F. App'x 375 (2d Cir. 2012).

This case presents what in reality is a personal financial dispute between the two owners of Wolf Creek. This is not the type of matter suited for resolution by derivative action, as a conflict exists between the financial interests of the two Wolf Creek members. Holman's real complaint centers on Brady's actions, as a member, in executing the New Lease. He claims these actions were in breach of a fiduciary duty from Brady to Holman personally, which injured him because Wolf Creek now produces less income than it did formerly under its unfair, over-market lease. The proper procedural mechanism for Holman to have utilized was a direct claim against Brady, seeking declaratory relief – not a derivative action. The trial court erred in not dismissing the derivative claims.

4. CR 23.1 trumps RCW 25.15 to the extent they conflict.

In his Complaint, Holman relies exclusively on RCW 25.15.370 and 25.15.380 to justify his derivative claims. He makes no mention of CR 23.1, nor makes any attempt to show compliance with its mandatory requirements.

While there are some similarities between CR 23.1 and RCW 25.15, in several key respects, they are in conflict. Unlike RCW 25.15, CR 23.1 requires that the derivative complaint be verified and attest that the derivative claims are not asserted in a collusive fashion to confer jurisdiction on the court. Under CR 23.1, Holman was required to articulate how he could fairly and adequately represent the other member's interests (Brady) in enforcing the rights of Wolf Creek.

The Washington Supreme Court has held that "if a statute appears to conflict with a court rule, this court will first attempt to harmonize them and give effect to both, but if they cannot be harmonized, the court rule will prevail in procedural matters and the statute will prevail in substantive matters." *City of Fircrest v. Jensen,* 158 Wn.2d 384, 393–94, 143 P.3d 776 (2006), *cert. denied,* 549 U.S. 1254 (2007). Substantive law "creates, defines, and regulates primary rights", while procedures involve the "operations of the courts by which substantive law, rights, and remedies are effectuated." *Id.* (internal quotations and citation omitted). *See Putman v. Wenatchee Valley Med. Ctr., P.S.,* 166 Wn.2d 974, 216 P.3d 374 (2009) (holding that RCW 7.70.150 is procedural because it addresses how to file a claim to enforce a right provided by law.) RCW 25.15 et seq. is a procedural statute, and because it conflicts with CR 23.1 and cannot be harmonized, CR 23.1 controls.

Holman made no attempt below to show compliance with CR 23.1. This deficiency is fatal to Holman's purported derivative claims.

C. Mountain Broadcasting's Non-Renewal Notice complied with the 1998 Lease.

Even assuming Holman is permitted to assert derivative claims on behalf of Wolf Creek and it was proper to join them with his personal claims, the judgment against Mountain Broadcasting must still be vacated because the trial court erred in holding that Mountain Broadcasting's Non-Renewal Notice was deficient.

It is undisputed that Mountain Broadcasting timely sent a written Non-Renewal Notice to Wolf Creek via Federal Express, and it was received by Brady. It is also undisputed that if this notice was effective, the 1998 Lease was terminated.

Holman claims that the Non-Renewal Notice was deficient both because it was not sent via certified or registered mail and because it was not sent to him. The trial court erroneously agreed with both contentions, in contravention of the unambiguous language in the 1998 Lease. Mountain Broadcasting, therefore, is not bound by the terms of the 1998 Lease, and the trial court's Order and Judgment to the contrary should be reversed.

1. 1998 Lease did not *require* notice be sent via registered or certified mail.

The trial court misapplied the 1998 Lease, which requires written notices, but does not mandate delivery of notices by registered or certified mail. Rather, under the 1998 Lease, written notice was required and ***if*** the required written notice was effectuated by certified or registered mail, it would be "deemed delivered 48 hours after depositing the notice or demand in the United States mail."[62] Thus, if notice was sent by registered or certified mail, the sender would be afforded a presumption that the notice was delivered 48 hours after it was sent. But this delivery presumption was not required in instances (like here) where the sender uses an alternative form of delivery and therefore must independently establish proof of actual delivery.

The parties are in accord that the notice requirement is a contractual provision that must be interpreted in accordance with the objectively expressed intent of the parties.[63] The question is whether Mountain Broadcasting complied with the notice provision by using Federal Express as a delivery mechanism. The Non-Renewal Notice provided by Mountain Broadcasting was in writing, as required, and the undisputed evidence shows it was timely delivered via Federal Express to Wolf Creek. Mountain Broadcasting does not seek the delivery presumption afforded by notice delivered by registered or certified mail, as timely delivery was independently established.

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[62] CP 208 -- Article XXIII of the 1998 Lease provided:

All notices or demands of any kind required or desired to be given by the Landlord or Tenant hereunder **shall be in writing** and **shall be deemed delivered 48 hours after depositing** the notice or demand in the United States mail, certified or registered, postage prepaid, addressed to landlord or tenant respectively at the addresses set forth after their signature at the end of this Lease. (Emphasis added).

[63] CP 321.

The efficacy of the Non-Renewal Notice turns on the terms of Article XXIII of the 1998 Lease, as the facts surrounding the content, timing, mode of delivery and receipt are all undisputed. Effective notice was given by Mountain Broadcasting to Wolf Creek.

2. Alternatively, Mountain Broadcasting substantially performed the notice requirement in the 1998 Lease.

The doctrine of substantial compliance or substantial performance is well-established in contract law, dating back to Justice Cardozo's holding that a deficiency in performance may not be considered a breach as long as it is not "so dominant or pervasive as in any real or substantial measure to frustrate the purpose of the contract." *Jacob & Youngs v. Kent,* 230 N.Y. 239, 129 N.E. 889, 891 (N.Y. 1921).

Even if the trial court correctly determined that the 1998 Lease required notice be delivered by certified or registered mail, Mountain Broadcasting's delivery of notice by Federal Express substantially complied with that requirement. Federal Express serves all the functions of certified mail. That is, it involves documented receipt by the carrier and documented delivery by the carrier to the addressee. As a matter of law, where actual delivery is not disputed, case law supports that

Mountain Broadcasting substantially performed the notice requirements in the 1998 Lease.

In *Fleisher Engineering & Construction Co. v. U.S.*, 311 U.S. 15 (1940), the United States Supreme Court examined the adequacy of notice required by statute. The statute (40 U.S.C. § 270b) addressed a materialman's right to sue, granting such a right "upon giving written notice" and (unlike the 1998 Lease) further mandated that such "notice shall be served by mailing the same by registered mail, postage prepaid or in any manner in which the U.S. marshal is authorized to serve summons." *Fleisher Eng'g*, at 19. It was admitted that the notice at issue was in writing and was sent by mail to the correct persons, who actually received the notice. *Id.* at 18. Thus, the sole issue was whether the notice was deficient because it was not sent via registered mail, even though it was actually received.

In resolving the issue, the Court held that "a distinction should be drawn between the provision explicitly stating the condition precedent to the right to sue and the provision as to the manner of serving notice." *Id.* The Court found that the first proviso, which defined the condition precedent to suit, was "fully met" by confirmed receipt of the written notice by the designated persons. *Id.* at 19. The Court then turned to the mode of service of the notice, which was required by registered mail, holding:

> We think that the purpose of this provision as to the manner of service was to assure the receipt of the notice, not to make the described method mandatory so as to deny right of suit when the required written notice within the specified time had actually been given and received. **In the face of such receipt, the reason for a particular mode of service fails**. It is not reasonable to suppose that Congress intended to insist upon an idle form. Rather, we think that Congress intended to provide a method which would afford sufficient proof of service when receipt of the required written notice was not shown.

Id. at 19 (emphasis added).

Like the statute in *Fleisher Engineering*, here the 1998 Lease contained two provisos in the notice section (though unlike the statute, the 1998 Lease contained no language – "shall" – mandating a specific mode of delivery).[64] The first requires that all notices be in writing to either the Landlord or Tenant.[65] The notice provision in the statute then indicates the effect of a specific mode of service, stating that notice "shall be deemed delivered 48 hours after depositing the notice or demand in the United States mail, certified or registered, postage prepaid...."[66] Even though the statute made the specified mode of delivery mandatory (which the 1998 Lease did not), the Supreme Court rejected the argument that notice failed where the specified mode of delivery was not employed. *Fleisher Eng'g,*

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[64] CP 60.
[65] CP 60.
[66] CP 60.

311 U.S. 15. Thus, even if the 1998 Lease *did require* a specified mode of delivery (it does not), the reasoning employed by the Supreme Court would apply squarely here. The purpose of the notice provision in the 1998 Lease "was to assure the receipt of the notice, not to make the described method mandatory." In *Fleisher Engineering*, and in this case, the required written notice was unquestionably received in a timely fashion, supporting in both instances the logical holding that "[i]n the face of such receipt, the reason for a particular mode of service fails." *Id.* at 18.

Korey v. Sheff, 3 Mass.App.Ct. 266, 327 N.E.2d 896 (1975), presented an issue of whether a lease could only be renewed if notice was served by registered mail. The lease in question (which unlike the statute in *Fleischer*, was similar to the language of the 1998 Lease) provided, in part, that "the lessee shall have the option to renew this lease if notice is given in writing to the lessor . . . and . . . any such notice to the Lessor shall be deemed duly given if and when mailed by registered mail. . . ." *Korey*, 327 N.E.2d at 897. In construing the lease, the *Korey* Court held that "[t]hese provisions do not require that written notice be sent by registered mail, to the exclusion of other modes of transmission, in order effectively to exercise the option to renew." *Id.* Actual receipt of written notice would fulfill the notice requirement of the renewal provision of the lease...." *Id.*

Here, both members of Wolf Creek (Holman and Brady) knew Mountain Broadcasting was unhappy with the lease rate and intended to provide notice of non-renewal. Well before the 90-day deadline, Mountain Broadcasting provided written notice to Wolf Creek (via letter to Brady) that it intended to terminate the 1998 Lease. The Non-Renewal Notice was sent by Mountain Broadcasting's attorney to Brady on September 20, 2012, via overnight Federal Express delivery.[67] There is no dispute that the Non-Renewal Notice was received the next day, as established by a written delivery confirmation from Federal Express.[68] Moreover, Brady's administrative assistant confirmed she received the Non-Renewal Notice, on behalf of Brady, via overnight delivery.[69] Brady also testified that he received the Non-Renewal Notice, and sent a response letter to Mountain Broadcasting on or about October 4, 2012.[70]

Holman claims that despite this undisputed evidence that Wolf Creek actually received the Non-Renewal Notice, it was nonetheless deficient because it was not sent by registered or

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[67] CP 285 (Palacios Decl. at ¶¶ 5-6).

[68] CP 286 (Palacios Decl. at ¶ 7).

[69] CP 172 (Billingsley Decl. at ¶ 3).

[70] CP 182 (Brady Decl. at ¶¶ 7-9).

certified mail. However, as the Supreme Court held, in the face of actual receipt of notice "the reason for a particular mode of service fails." *Fleisher Eng'g*, 311 U.S. at 19. Additionally, accepting Holman's position would produce an absurd result of finding non-compliance with the notice provision when actual notice was unquestionably provided. Such an absurdity must be avoided. "The contract must be read as the average person would read it; it should be given a practical and reasonable rather than a literal interpretation, and not a strained or forced construction leading to absurd results." *Eurick v. Pemco Ins. Co.*, 108 Wn.2d 338, 341, 738 P.2d 251 (1987) (internal quotations and citation omitted).

The undisputed evidence is that Wolf Creek actually received Mountain Broadcasting's non-renewal notice within the time period prescribed in the 1998 Lease. No evidence to the contrary exists. The Non-Renewal Notice sent to Brady as a member of Wolf Creek served the intended purpose of the notice requirement in the 1998 Lease, warranting entry of summary judgment in favor of Mountain Broadcasting. The trial court's ruling to the contrary should, therefore, be reversed.

3. 1998 Lease Required Notice to the "Landlord" (Wolf Creek), not Holman.

The trial court also ruled on summary judgment that the Non-Renewal Notice was deficient because it was not also simultaneously sent to Holman. This ruling impermissibly modifies the parties' contract, as the 1998 Lease required only that notice be provided to the "Landlord" (Wolf Creek) and not to Holman individually as a member of the Wolf Creek. The trial court lacked authority to rewrite the parties' contract.

In Article II of the 1998 Lease, entitled "Lease Term," the parties agreed that the initial term of the lease would be extended "unless the Tenant shall give notice to the **Landlord** at least ninety (90) days prior to the Extension Date that the Tenant elects that the term of this Lease not be extended."[71] Article XXIII of the 1998 Lease expressly provided that notices should be "addressed to the Landlord or Tenant respectively at the addresses set forth after their signature at the end of this Lease."[72] While there are no addresses identified following the1998 Lease signature blocks, Brady was identified under the "Landlord" signature block as the person to sign on behalf of Wolf Creek LLC; Holman was not.[73] This makes sense, as Wolf Creek is a member-managed LLC: "The Company will be operated by its members and no manager will be appointed."[74]

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[71] CP 181 (Brady Decl. at ¶ 3) and CP 187.

[72] CP 208.

[73] CP 211.

[74] CP 235 (Article V, Section 1, Wolf Creek, LLC Agreement).

As a member-managed LLC, "All members of the Company shall have the authority to obligate or bind the Company in connection with any matter."[75]

Because Wolf Creek is a member-managed LLC, notice to Brady unquestionably constituted notice to Wolf Creek (the "Landlord"). Thus, notice to Brady at his address was *exactly* compliant with the notice requirements of the 1998 Lease. The trial court's ruling to the contrary constituted an impermissible judicial rewriting of the Wolf Creek LLC Agreement.[76]

It is settled law in Washington that courts do not have the power, under the guise of interpretation, to rewrite contracts the parties have deliberately made for themselves. *Clements v. Olsen,* 46 Wn.2d 445, 448, 282 P.2d 266 (1955). Courts may not interfere with the freedom of contract or substitute their judgment for that of the parties to rewrite the contract or interfere with the internal affairs of corporate management. *Id.* at 449–50.

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[75] CP 235 (Article V, Section 2, Wolf Creek, LLC Agreement).

[76] 1998 Lease provides that any changes or modifications to the Lease could only be effectuated by a written agreement signed by all parties. Article XXVI ("Entire Agreement") (1998 Lease reflects the entire agreement between the parties and could only be amended or altered "by an instrument in writing signed by both Landlord and Tenant.") CP 209-210. It is undisputed that the notice provision in the 1998 Lease was never amended or modified.

By requiring the Non-Renewal Notice be sent to Holman, individually, the trial court disregarded the clear and unambiguous language of the 1998 Lease and effectively rewrote the parties' contract, in violation of Washington law. The 1998 Lease required that the Non-Renewal Notice be sent to Wolf Creek as "Landlord." The undisputed facts establish that the Non-Renewal Notice was sent by Mountain Broadcasting to Brady within the 90-day non-renewal notice period. The undisputed evidence below also proved that Brady received and responded to this letter within the 90-day non-renewal notice period. The 1998 Lease only required notice to Wolf Creek, which occurred. The fact that notice was not also sent to Holman is irrelevant[77], and the trial court's ruling to the contrary constituted reversible error.

D. The Wolf Creek LLC Agreement authorized Brady (as a member of Wolf Creek) to execute the New Lease with Mountain Broadcasting.

The trial court also erred in ruling that Brady lacked authority under the Wolf Creek LLC Agreement to enter into the New Lease with Mountain Broadcasting without Holman's consent. This contention is asserted in Holman's **Second** Cause

[77] Neither Holman nor the trial court offered any explanation of why the timely written notice delivered to Wolf Creek (via Brady) should be ineffective if delivered to the only two members of the LLC. This is not a situation in which the LLC, or any member, could have taken any action on the notice. It was effective to terminate the 1998 Lease upon delivery.

of Action and, together with the notice issue, is also raised in the **Third, Fourth** and **Fifth** Causes of Action. Holman's Complaint does not allege that the terms of the New Lease are unfair to Wolf Creek, but only that Brady lacked authority to enter the New Lease. This is a fatal omission, not only because the derivative claim is exposed as Holman's personal claim (*supra* pp.25-27), but also because the LLC Agreement expressly says either member of the LLC may enter a Lease on behalf of the LLC, so long as it is fair.

Instead of electing to have Wolf Creek run by a manager, Holman and Brady agreed to a member-managed structure. Article V, section 2, of the LLC Agreement describes the authority of members: "all members of the Company shall have the authority to obligate or bind the Company in connection with any matter."[78] This authority is expressly extended to executing leases per Article XIII, section 1, which confirms that "**any member** ... shall have the power to execute and deliver proxies, stock powers, deeds, **leases**, contracts ..... for and in the name of the Company....[79] (emphasis added.)

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[78] CP 235 (Article V, Section 2, Wolf Creek, LLC Agreement).

[79] CP 248 (Article XIII, Section 1, Wolf Creek, LLC Agreement) (emphasis added).

Under this structure, Holman and Brady were each empowered with authority to act on behalf of Wolf Creek. Holman's claim that all members, acting collectively, must reach unanimous agreement to execute managerial decisions is absolutely at odds with other provisions of the LLC Agreement.[80] Such a construction would render Article V, section superfluous. The import of Section 2 is that each LLC member, individually, is empowered to bind the company.

The parties did agree that agreement of both members would be required for some decisions. Entering a lease was not among them, as the parties had expressly agreed "any member" could enter a Lease. Article IV, Section 2(b), sets forth 5 types of company action requiring approval of both Holman and Brady. This section does not reference managerial decisions, nor does it limit the authority of members to execute contracts or leases. Rather, it requires majority approval (which is unanimous approval, in a two-member LLC) to (1) amend the LLC Agreement; (2) authorize action changing the purpose of the company; (3) require additional capital from members; (4) reduce or limit member contribution obligations, or (5) issue new membership interests; none of which are at issue here.

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[80] It would also be impractical, which is why the parties did not insist on agreement by members as a condition of the LLC being enabled to do business.

While Brady and Holman agreed that each had broad ranging authority to bind Wolf Creek to a new lease, this authority was not unlimited. In fact, Brady and Holman both ***expressly contemplated*** the possibility of a transaction between Wolf Creek and an entity personally controlled by one of them, as was the case with the New Lease executed by Brady on behalf of Wolf Creek.

The Wolf Creek LLC Agreement provides that no contract shall be void or voidable if an "interested member" executes the contract for the LLC, so long as the contract "is fair to the Company as of the time it is authorized, approved or ratified by the members or the committee thereof."[81] Holman has never claimed that the New Lease was unfair to Wolf Creek, nor could he as the new lease rate is above market, although he does have a desire to continue with the inflated lease rates under the expired 1998 Lease.

Rather, Holman claims Brady "lacked authority to bind Wolf Creek to a new 1998 Lease" (Second Cause of Action) and that he breached the Wolf Creek LLC Agreement by entering into a New Lease "without disclosing the 1998 Lease terms to Mr. Holman and without obtaining his consent." (Third, Fourth and Fifth Causes of Action). As discussed above, the Wolf Creek

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[81] CP 234-235 (Article VI, Section 2(b), Wolf Creek, LLC Agreement).

LLC Agreement clearly states that all members possess authority to enter leases on behalf of Wolf Creek, without previewing the terms of the same to other members or obtaining their consent, and any such lease is valid so long as it is fair to Wolf Creek LLC.

The restriction on member authority imposed by the trial court (at the request of Holman) simply does not exist in the Wolf Creek LLC Agreement. The trial court's acceptance of Holman's view amounted to impermissible judicial rewriting of the parties' LLC Agreement. *See Clements,* 46 Wn.2d at 449–50 (courts may not interfere with the freedom of contract, or substitute their judgment for that of the parties to rewrite the contract or interfere with the internal affairs of corporate management.)

Brady had the clearly defined right under the LLC Agreement to enter into the New Lease with Mountain Broadcasting. Holman agreed to this when he executed the Wolf Creek LLC Agreement. Given Brady's ownership interest in Mountain Broadcasting, the New Lease had to be fair to Wolf Creek at the time of its execution. This was the express mechanism contractually agreed to by Holman and Brady to safeguard Wolf Creek's interests if either of them, acting as "interested members," entered into a contract with Wolf Creek. Because the Non-Renewal Notice was delivered in a timely fashion and Brady did not have a contractual duty under the LLC Agreement to obtain Holman's consent prior to entering into the New Lease, Holman's **Second**, **Third, Fourth** and **Fifth** Causes of Action fail as a matter of law, and the trial court committed reversible error in not so holding.

E. The Trial Court erred in entering judgment in favor of Holman on Wolf Creek's claims.

As discussed above, judgment against Mountain Broadcasting was erroneously entered for a number of reasons. However, assuming it was proper to enter any judgment against Mountain Broadcasting, it would have to run in favor of the other party to the 1998 Lease – Wolf Creek – not Holman personally.

Inexplicably, the trial court granted Holman's request to have the judgment against Mountain Broadcasting entered in his favor personally.[82] Holman possesses NO personal claims against Mountain Broadcasting and there is absolutely no justification to have entered judgment in his favor against Mountain Broadcasting. The trial court committed reversible error in entering judgment in favor of Holman personally.

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[82] CP 385-387 (listing the Judgment Creditor as Rick Holman, Individually and on behalf of Wolf Creek Holdings of Spokane LLC).

VII. CONCLUSION

The trial court should be reversed because (1) Holman's derivative claims against Mountain Broadcasting brought on behalf Wolf Creek were defective, (2) Mountain Broadcasting's Non-Renewal Notice was timely and properly delivered to Wolf Creek, and (3) Brady properly entered into the New Lease with Mountain Broadcasting on behalf of Wolf Creek. Further, the matter should be remanded, with instructions to the trial court to grant Brady and Mountain Broadcasting's Motion for Summary Judgment, and enter judgment in their favor.

DATED this 15th day of October, 2015.

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By ______________________________

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APPENDIX

APPENDIX A

2006 WL 2849783
Only the Westlaw citation is currently available.
United States District Court,
S.D. New York.

ST. CLAIR SHORES GENERAL EMPLOYEES RETIREMENT SYSTEM, Plaintiff,
v.
Paul EIBELER, et al., Defendants.

No. 06 Civ. 688(SWK). | Oct. 4, 2006.

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OPINION AND ORDER

SHIRLEY WOHL KRAM, U.S.D.J.

*1 This litigation comes before the Court on a motion filed by the Special Litigation Committee (the "SLC") of the board of directors of Take Two Interactive Software, Inc. ("Take Two"), a Delaware corporation headquartered in New York. The Amended Complaint (the "Complaint") filed by the plaintiff, St. Clair Shores General Employees Retirement System ("St. Clair" or "Plaintiff"), avers three basic causes of action. First, the Complaint asserts derivative claims against various officers and directors in connection with alleged insider trading (the "Derivative Insider Trading Claims"). Second, the Complaint advances derivative claims against several officers and directors who allegedly issued materially misleading proxy statements in the years 2003, 2004, and 2005, in violation of Section 14(a) of the Exchange Act and Rule 14a-9 (the "Derivative Section 14(a) Disclosure Claims"). Third, the Complaint sets forth direct, class action claims for injuries suffered by St. Clair and other holders of Take Two common stock as a result of the allegedly misleading proxy statements of the years 2003, 2004, and 2005 (the "Direct Common Law Disclosure Claims"). The SLC has moved to stay these three causes of action while it considers whether this litigation is in the best interests of Take Two.

For the reasons that follow, this court grants the SLC's motion and stays this litigation in its entirety for a period of 150 days.

I. The Allegations of the Complaint

The Complaint names Take Two and eleven of its officers and directors as defendants. The Complaint alleges that the officer and director defendants: (A) engaged in insider trading and (B) violated disclosure requirements under Exchange Act Section 14(a), Rule 14a-9, and Delaware law.

A. The Derivative Insider Trading Claims

Plaintiff avers two separate episodes of insider trading. In both instances, directors and officers of Take Two allegedly sold shares of Take Two while in possession of material nonpublic information concerning the corporation.

The first alleged episode of insider trading involved the sale of Take Two common stock by certain officer and director defendants between June and November 2003. The Complaint alleges that these defendants sold 465,000 shares of Take Two stock at a time when they knew that the SEC would likely bring an enforcement action for Take Two's revenue overstatements in the years 2000 and 2001.

The second alleged episode of insider trading involved the sale of Take Two common stock by certain officer and director defendants between March and July 2005. The Complaint alleges that these defendants sold 573,000 shares of Take Two common stock while aware that Take Two's best selling video game, Grand Theft Auto San Andreas ("San Andreas"), contained hidden, sexually explicit content, which would negatively impact its marketability.

In order to remedy these alleged instances of insider trading, the Complaint seeks disgorgement of profits realized by the defendants through their sale of Take Two stock at inflated values.

B. The Disclosure Claims

*2 In addition to the Derivative Insider Trading Claims, Plaintiff asserts that the defendants violated their disclosure duties by filing materially misleading proxy statements over the past several years (the "Disclosure Claims"). The crux of these claims is that certain defendants caused proxy statements to be filed in February 2003, May 2004, and May 2005, while failing to disclose material information to the shareholders. In connection with these allegedly misleading proxy statements, Take Two shareholders approved the issuance of five million additional shares for Take Two's employee stock option plans.

In order to remedy the harm caused by the proxy statements in question, Plaintiff asserts two types of claims. First, in its Derivative Section 14(a) Disclosure Claims, Plaintiff seeks an award of compensatory damages for Take Two. Second, in its Direct Common Law Disclosure Claims, Plaintiff seeks an award of damages to the class for any harm caused by the allegedly misleading proxy statements.

II. Discussion

After this litigation was commenced, Take Two's board of directors appointed the SLC to investigate whether litigation was in Take Two's best interests. The SLC now moves the Court to stay all proceedings for a period of 150 days in order to facilitate the conduct of its investigation.

A. Choice of Law

Regardless of whether the underlying cause of action arises under federal or state law, "federal courts should apply state law governing the authority of independent directors to discontinue derivative suits to the extent such law is consistent with [federal law]."*Burks v. Lasker,* 441 U.S. 471, 486 (1979). Therefore, the appropriateness of the SLC's motion for a stay is a question to be resolved under the law of Take Two's state of incorporation, Delaware. *See, e.g. Stein v. Bailey,* 531 F.Supp. 684, 691-93 (S.D.N.Y.1982) (applying Delaware law in determining whether to defer to special litigation committee's decision not to pursue derivative litigation).

B. The SLC's Entitlement to a Stay of Derivative Litigation

Under Delaware law, a properly formed special litigation committee of the board of directors is generally entitled to a stay of derivative litigation for the reasonable period of time necessary to complete its investigation. *See Biondi v. Scrushy,* 820 A.2d 1148, 1163-64 (Del. Ch.2003); *Kaplan v. Wyatt,* 484 A.2d 501, 510 (Del. Ch.1984); *Abbey v. Computer & Commc'ns* Tech., 457 A.2d 368, 375-76 (Del. Ch.1983). In fact, Delaware courts have declined to grant such a stay only in unusual circumstances. *See, e.g., Biondi,* 820 A.2d at 1165-66 (refusing to grant stay because special litigation committee in question was obviously biased and thus its decision seeking termination of action could not command respect); *Carlton Invs. v. TLC Beatrice Int'l Holdings, Inc.,* No. CIV.A. 13950, 1996 WL 33167168, at *2, *9 (Del. Ch. June 6, 1996) (refusing to grant stay because substantial discovery and motion practice had already occurred).

*3 Therefore, to the extent that Plaintiff advances derivative claims *(see* Compl. ¶¶ 104-26), the SLC's motion for a stay is well supported by Delaware law. Specifically, St. Clair does not allege the type of unusual circumstances in which a stay of discovery is inappropriate. *See Biondi,* 820 A.2d at 1165-66; *Carlton Invs.,* 1996 WL 33167168, at *2, *9. Moreover, contrary to St. Clair's assertions, the SLC need not meet any special burden of proof before a stay of derivative proceedings is warranted. Rather, the propriety of a stay is presumed under Delaware law. *Abbey,* 457 A.2d at 375; *Kaplan,* 484 A.2d at 510. Consequently, the Derivative Insider Trading Claims must be stayed.

Nonetheless, St. Clair argues that the SLC lacks standing to seek a stay of the Disclosure Claims. In doing so, St. Clair correctly notes that a special litigation committee's authority derives directly from the board's authority to decide whether derivative litigation should be pursued on behalf of the corporation. *See Zapata Corp. v. Maldonado,* 430 A.2d 779, 786 (Del.1981). St. Clair reasons that where a given suit is not subject to the demand requirement or is otherwise outside the purview of the board's managerial power, *see Aronson v. Lewis,* 473 A.2d 805, 814 (Del.1984), *overruled on other grounds by Brehm v. Eisner,* 746 A .2d 244, 253-54 (Del.2000), a special litigation committee is similarly powerless to affect the progression of that suit. With this reasoning in mind, St. Clair argues that the Derivative Section 14(a) Disclosure Claims are not within the SLC's power to investigate because derivative claims brought under Section 14(a) are a species of derivative claim not subject to the demand requirement and business judgment rule. In addition, St. Clair contends that the Direct Common Law Disclosure Claims are outside the bounds of the SLC's investigatory powers because they are not derivative in nature, and are thus not governed by the demand requirement and business judgment rule.

The merits of these contentions are addressed in the following sections. In the first instance, the Court finds that the Derivative Section 14(a) Disclosure Claims are subject to the demand requirement and within the SLC's power to investigate, and thus Delaware law requires that such claims be stayed while the SLC conducts its investigations. [1] In the second instance, the Court reasons that there is a significant doubt as to whether St. Clair can bring derivative and direct claims arising out of the same alleged wrongdoing in the same action. As a result, there is no need to address whether the Direct Common Law Disclosure Claims are within the SLC's investigatory reach. Rather, for the purposes of Plaintiff's motion for a stay the Complaint will be read as if it only avers derivative claims, all of which are within the reach of the SLC's investigation.

1. The SLC's Standing to Investigate Derivative Section 14(a) Disclosure Claims

***4** As a general matter, the board of directors has primary authority to decide whether a corporation should pursue derivative litigation. *See Kamen v. Kemper Fin. Servs., Inc.,* 500 U.S. 90, 101 (1991); *Spiegel v. Buntrock,* 571 A.2d 767, 773 (Del.1990). In order to ensure that the board can exercise its primary authority to control derivative litigation, Delaware law requires that shareholders make a demand on the board before initiating a derivative suit. *Spiegel,* 571 A.2d at 773. Furthermore, in recognition of the board's primary authority, Delaware law applies the business judgment rule to board decisions concerning the initiation of derivative litigation, presuming that the board acted on an informed basis, in good faith, and in the honest belief that the decisions were in the corporation's best interests. *Id.* at 773-74.

There is nothing on the face of Delaware's demand requirement and business judgment rule that precludes their application to derivative claims brought under Section 14(a).*See id.;*Chancery Court R. 23.1. Nonetheless, some courts have deviated from tradition when considering derivative suits that allege Section 14(a) claims, with the result that there is some controversy regarding the applicability of the demand requirement and business judgment rule to Section 14(a) claims. [2]

While acknowledging the existence of this controversy, the Court is not persuaded that Section 14(a) claims should be treated as a special species of derivative claim not subject to the demand requirement and business judgment rule. Specifically, arguments in favor of the special treatment of derivative Section 14(a) claims generally rest on two lines of reasoning with which the Court disagrees. First, one court in this district has concluded that Second Circuit case law precludes the application of the demand requirement and business judgment rule to claims brought under Section 14(a).*See, e.g., Vides v. Amelio,* 265 F.Supp.2d 273, 276 (S.D.N.Y.2003). Second, working from the premise that the materiality of proxy statement disclosures is largely a legal issue, some courts have drawn the unwarranted conclusion that the pursuit of derivative Section 14(a) litigation is not within the board's business judgment. *See, e.g., id.* at 275-76; *In re Tri-Star Pictures, Inc., Litig.,* CIV. A. No. 9477, 1990 WL 82734, at *8 (Del. Ch. June 14, 1990).

In the following sections, the Court will set forth the reasons for its disagreement with these two general arguments. The Court will then conclude that Section 14(a) derivative claims are, like other derivative claims, subject to the demand requirement and business judgment rule. Consequently, the Derivative Section 14(a) Disclosure Claims must be stayed while the SLC conducts its investigation.

a. Second Circuit Case Law on Demand Requirement and Business Judgment Rule in Section 14(a) Litigation

The Second Circuit's most extensive treatment of the applicability of traditional rules of derivative litigation to Section 14(a) claims occurred in *Galef v. Alexander,* 615 F.2d 51 (2d Cir.1980).*Galef* considered the narrow issue of whether the directors of a corporation were entitled to summary judgment on claims brought under Section 14(a) where the board, all of whose members were named defendants in the suit, decided that the suit was not in the corporation's best interests. *Id.* at 64.Not surprisingly, the Second Circuit held that where a claim has been stated against directors under Section 14(a), federal policy precludes the application of the business judgment rule to the decision of those very same directors to terminate litigation. *Id* . This ruling is consistent with traditional rules governing derivative litigation, under which no deference is owed to board decisions concerning the termination of litigation if a majority of board members are interested in the litigation. *See, e.g., Zapata,* 430 A.2d at 784. However, *Galef* explicitly reserved judgment on the general question of whether the business judgment rule would apply to decisions to dismiss made by a disinterested board or an independent committee of the board. 615 F.2d at 64 n. 20. [3] Therefore, *Galef* does require the modification of traditional understandings of the demand requirement and business judgment rule in the context of Section 14(a) litigation.

***5** Moreover, subsequent Second Circuit jurisprudence belies the claim that such modification is compelled by federal policy. Specifically, in *Lewis v. Graves,* the Second Circuit dismissed Section 14(a) claims for failure to make a demand, which makes clear that demand is required in this context. 701 F.2d 245, 249 (2d. Cir .1983). Since "[t]he purpose of the demand requirement is to afford the directors an opportunity to exercise their reasonable business judgment,"*Kamen,* 500 U.S. at 96 (quotations omitted), the holding in *Lewis v. Graves* suggests that the business judgment rule is equally applicable to board decisions regarding the pursuit of Section 14(a) claims. In fact, if board decisions on the pursuit of litigation did not enjoy the benefit of the business judgment rule, the rationales underlying the demand requirement would be largely undermined. Specifically, the board would be given an initial decision-making opportunity by operation of the demand requirement, but, in the absence of the business judgment rule, this initial decision-making opportunity would be of little significance because courts and shareholders could conduct a de novo review of the propriety of board decisions.

Consequently, Second Circuit jurisprudence has clearly held the demand requirement applicable to derivative Section 14(a) litigation, which implies that the business judgment rule should be similarly applicable. *See also In re Par Pharm. Inc. Derivative Litig.,* 750 F.Supp. 641, 645-47 (S.D.N.Y.1990); *Stein v. Bailey,* 531 F.Supp. at 695-96; *Abramowitz v. Posner,* 513 F.Supp. 120, 130 (S.D.N.Y.1981). Thus, Second Circuit case law supports the SLC's request for a stay.[4]

b. Compliance or Noncompliance with Disclosure Requirements Is a Matter of Law But Decision to Litigate Is a Business Decision

It may be accepted that a director's decision concerning what information should be included in a proxy statement is not entirely protected by the business judgment rule. *See In re Anderson, Clayton S'holders' Litig.,* 519 A.2d 669, 675 (Del. Ch.1986). For example, a director's decision to include materially misleading declarations or omissions in a proxy statement in contravention of federal and state law would presumably be evaluated without the presumption of propriety afforded by the business judgment rule. *See id.*In addition, a board's decision as to whether a particular statement or omission was materially misleading would also be denied the protection of the business judgment rule because this decision involves a question of materiality, which courts are well suited to answer on their own. *Vides,* 265 F.Supp.2d at 275. In sum, a board's decision that a particular proxy statement did or did not satisfy federal and state disclosure requirements is presumably not entitled to any special respect in a court of law. However, this is no reason to conclude, as some courts have, that a board's decision as to whether the corporation should pursue derivative litigation to vindicate violations of federal and state disclosure requirements is not entitled to the protection of the business judgment rule. *See id.* at 275; *In re Tri-Star Pictures, Inc. Litig.,* 1990 WL 82734, at *8.

***6** To the contrary, it is axiomatic that "decisions of a corporation-including the decision to initiate litigation-should be made by the board of directors."*Kamen,* 500 U.S. at 101 (quotations omitted); *see also Spiegel,* 571 A.2d at 773. So, although the board may not be best positioned to determine whether Section 14(a) has been violated, the law regards the board as best positioned to make the *business* decision as to whether derivative litigation should be initiated to remedy such a potential violation. In fact, even if Section 14(a) has been violated, the board might reasonably determine that it is not in the best interests of the corporation to pursue derivative litigation. For example, it might cost the corporation more to enforce its rights under Section 14(a) than the corporation could possibly recover through the successful prosecution of a lawsuit. On the other hand, should the board find that Section 14(a) litigation is in the best interests of the corporation, the law regards the board as best situated to determine how resources should be spent on that litigation. The business judgment rule is simply a means to acknowledge that the board is better positioned to weigh the comparative risks and benefits of the initiation and conduct of litigation than is a court. *See Spiegel,* 571 A.2d at 773 ("The purpose of pre-suit demand is to assure that the stockholder affords the corporation the opportunity to address an alleged wrong without litigation, to decide whether to invest the resources of the corporation in litigation, and to control any litigation which does occur.").

Therefore, the business judgment rule should apply to board decisions regarding the pursuit of derivative Section 14(a) litigation, provided the relevant decision makers are not interested in the transaction in question. Moreover, since the demand requirement merely recognizes the board's privileged position by providing it with an initial decision-making opportunity, *Kamen,* 500 U.S. at 96, the demand requirement should also be applied to Section 14(a) litigation. *See Lewis,* 701 F.2d at 249.

c. The SLC Has Standing to Investigate the Derivative Section 14(a) Disclosure Claims

In consequence, the Court declines Plaintiff's invitation to deviate from traditional rules governing derivative litigation by holding the demand requirement and business judgment rule inapplicable in the specific context of Section

14(a) litigation. Specifically, as the foregoing discussion demonstrates, the Court finds unpersuasive the reasoning that has been used to justify such deviation from tradition.

As a result, this Court concludes that derivative claims brought under Section 14(a) are subject to the demand requirement and the decision as to whether to bring such claims is within the board's business judgment. *Cf. Lewis,* 701 F.2d at 249; *Fink v. Weill,* No. 02 Civ. 10250(LTS), 2005 WL 2298224, at *4 (S.D.N.Y. Sep. 19, 2005); *In re Trump Hotels S'Holder Derivative Litig.,* Nos. 96 Civ. 7820 DAB, 96 Civ. 8527 DAB, 2000 WL 1371317, at *10 n. 5. Furthermore, where demand is excused because the plaintiff alleges with particularity that a majority of the board is tainted by self-interest, the board may appoint a committee of independent directors to determine whether derivative Section 14(a) litigation is in the corporation's best interests. *See Zapata,* 430 A.2d at 786.

*7 In the instant case, the Derivative Section 14(a) Disclosure Claims are indisputably derivative in nature and thus are subject to the demand requirement and business judgment rule. Moreover, the SLC is allegedly an independent committee established to investigate the desirability of pursuing such Claims. Therefore, Plaintiff's Derivative Section 14(a) Disclosure Claims are within the SLC's investigatory reach, and these Claims must be stayed while the SLC conducts its investigations. *Abbey,* 457 A.2d at 375; *Kaplan,* 484 A.2d at 510.

2. The SLC's Standing to Investigate St. Clair's Direct Common Law Disclosure Claims

The Direct Common Law Disclosure Claims are mirror images of the Derivative Section 14(a) Disclosure Claims. In fact, the only differences between these Claims are the labels St. Clair attaches to them and the entity identified as the injured party.[5] The underlying wrongful conduct pleaded by St. Clair, i.e., the presence of material omissions in the 2003, 2004, and 2005 proxy statements, is exactly identical. Essentially, then, St. Clair seeks to vindicate its own interests by demanding recovery for the Class, while also attempting to represent the interests of Take Two by requesting damages for the corporation in connection with the same alleged wrongdoing. The Court finds significant cause to doubt that St. Clair can adequately advance these dual interests, and thus concludes that the Direct Common Law Disclosure Claims should be treated as derivative claims for the purposes of this motion.

Courts in this Circuit have long found that plaintiffs attempting to advance derivative and direct claims in the same action face an impermissible conflict of interest. *See, e.g., Tuscano v. Tuscano,* 403 F.Supp.2d 214, 223 (E.D.N.Y.2005); *Wall Street Sys., Inc. v. Lemence,* No. 04 Civ. 5299(JSR), 2005 WL 292744, at *3 (S.D.N.Y. Feb. 8, 2005); *Ryan v. Aetna Life Ins. Co.,* 765 F.Supp. 133, 136 (S.D.N.Y.1991); *Brickman v. Tyco Toys, Inc.,* 731 F.Supp. 101, 108 (S.D.N.Y.1990); *Kamerman v. Steinberg,* 113 F.R .D. 511, 515-16 (S.D.N.Y.1986). As a result of this impermissible conflict, some courts have refused to certify a plaintiff as a class representative, while others have refused to allow the derivative action to proceed. *Compare Brickman,* 731 F.Supp. at 109,*with Ryan,* 765 F.Supp. at 137.

In deciding whether to eliminate the conflict of interest by treating the claims as exclusively derivative or exclusively direct, courts have scrutinized the plaintiff's allegations. *See Tuscano,* 403 F.Supp.2d at 223; *Moran v. Household Intn'l., Inc .,* 490 A.2d 1059, 1069 (Del. Ch.1985) ("In determining whether a complaint states an individual or a derivative cause of action, the Court is not bound by the designation employed by the plaintiff."), *abrogated on other grounds by Tooley v. Donaldson, Lufkin & Jenrette, Inc.,* 845 A.2d 1031, 1035-40 (Del.2004); *Dieterich v. Harrer,* 857 A.2d 1017, 1027 (Del. Ch.2004) ("[T]he court must look to all the facts of the complaint and determine for itself whether a direct claim exists.").

*8 In the instant case, the Direct Common Law Disclosure Claims fundamentally allege that the defendants issued materially misleading proxy statements in violation of Section 14(a) of the Exchange Act. Although such claims may be brought both derivatively and directly, *see Katz v. Pels,* 774 F.Supp. 121, 127 (S.D.N.Y.1991), the Supreme Court has stated that "[t]he injury which a stockholder suffers from corporate action pursuant to a deceptive proxy solicitation ordinarily flows from the damage done the corporation, rather than from the damage inflicted directly upon the stockholder."*J.I. Case Co. v. Borak,* 377 U.S. 426, 432 (1964). In accord with the Supreme Court's generalization, Take Two is the entity that has suffered the primary injury in this case-the addition of a combined five million shares to Take Two's 2002 Stock Option Plan. (Compl.¶¶ 116, 121, 126.) Indeed, even if St. Clair successfully prosecuted its direct claim for injuries to its right to cast an informed vote, St. Clair might only be entitled to nominal damages. *See In* *re Tri-Star Pictures, Inc., Litig.*, 634 A.2d 319, 334 n. 18 (Del.1993).

Moreover, a direct claim for failure to disclose material information in connection with the solicitation of shareholder action can only succeed if the solicited corporate transaction "in turn caused impairment to the economic or voting rights of stockholders."*Loudon v. Archer-Daniels-Midland Co.*, 700 A.2d 135, 142 (Del.1997). Since the addition of five million shares to the Stock Option Plan does not clearly affect Plaintiff's economic or voting rights, it may be difficult for Plaintiff to maintain a direct action for the alleged material omissions in the 2003, 2004, and 2005 proxy statements. *See id.;Paskowitz v. Wohlstadter,* 822 A.2d 1272, 1280 (Md.App.2003). Therefore, Plaintiff's Disclosure Claims are primarily derivative in nature.*See Tooley,* 845 A.2d at 1033 (indicating that the classification of a suit as derivative or direct turns on "who suffered the alleged harm ..." and "who would receive the benefit of any recovery or other remedy").

Given that an impermissible conflict of interest may prevent Plaintiff from advancing its derivative and direct disclosure claims in the same action, and that Plaintiff's Direct Common Law Disclosure Claims are primarily derivative in nature, the Court will treat these disclosure claims as derivative for the purposes of the present motion to stay. *Cf. Tuscano,* 403 F.Supp.2d at 223. For the reasons stated in the preceding section concerning the Derivative Section 14(a) Disclosure Claims, the SLC has standing to investigate these additional disclosure claims.

Therefore, although it is improper at this juncture to dismiss the Direct Common Law Disclosure Claims outright, *cf. Brickman,* 731 F.Supp. at 104, the Court finds that all of the Disclosure Claims should be stayed while the SLC conducts its investigations. *Abbey,* 457 A.2d at 375-76; *Kaplan,* 484 A.2d at 510.

III. Conclusion

*9 The Court grants the SLC's motion to stay this litigation in its entirety. Although the SLC is entitled to a stay for the reasonable period of time necessary to complete its investigation, *Abbey,* 457 A.2d at 375-76, the SLC has requested a stay of 150 days. The Court has no reason to conclude that this period of time is unreasonable, and thus finds that a stay of 150 days dating from the entry of this Order is warranted.

However, when the SLC has terminated its investigation, the stay must be lifted. *Id.* at 375.Thus, should the SLC finish its investigation before 150 days have expired, proceedings in this case must commence. On the other hand, should the SLC desire an additional stay of the proceedings in this case, the SLC must make a showing of cause in a future application to the Court.

In any event, when the stay in these proceedings has been lifted or has otherwise expired, the defendants will have thirty days to respond to the Complaint, absent any agreement to the contrary between the parties.

SO ORDERED.

All Citations

Not Reported in F.Supp.2d, 2006 WL 2849783

Footnotes

1 In finding that the Derivative Section 14(a) Disclosure Claims are subject to the demand requirement, the Court does not pass judgment on whether Plaintiff has adequately pleaded demand futility or, in the alternative, its efforts to make a demand on the board. Instead, the Court merely concludes that Plaintiff would have to show either demand futility or adequate efforts to make a demand on the board, in order to proceed with its Derivative Section 14(a) Disclosure Claims, and thus a stay of the instant litigation is warrant. Plaintiff's position is that a stay is not warrant because no such showing is required.

2 *Compare Lewis v. Graves,* 701 F.2d 245, 247-50 (2d Cir.1983) (dismissing derivative suits brought under Sections 10(b) and 14(a) of the Exchange Act due to plaintiff's failure to make demand on board); *Fink v. Weill,* No. 02 Civ. 10250(LTS), 2005 WL 2298224, at *4 (S.D.N.Y. Sep. 19, 2005) (dismissing derivative suit brought under Section 14(a) for failure to make demand); *In re Trump Hotels S'Holder Derivative Litig.,* Nos. 96 Civ. 7820 DAB, 96 Civ. 8527 DAB, 2000 WL 1371317, at *10 n. 5 (S.D.N.Y. Sep. 21, 2000) (reasoning that demand requirement applies to Section 14(a) claims that are brought derivatively), *with Vides v. Amelio,* 265 F.Supp.2d 273, 275-76 (S.D.N.Y.2003) (holding that demand requirement does not apply to Section 14(a) claims because content of proxy-statement disclosures is not within board's

business judgment); *Katz v. Pels*, 774 F.Supp. 121, 127 (S.D.N.Y.1991)(holding that "demand is not required, nor required shown futile" in Section 14(a) case).

3 In reserving judgment, the Second Circuit cited *Lewis v. Anderson*, 615 F.2d 778, 784 (9th Cir.1979) ("So long as those accused of manipulating the proxy vote are excluded from deciding whether or not to pursue the claim there is no conflict between the business judgment rule and § 14(a).").

4 The Second Circuit has noted one reason why demand might be required in a given case even if the business judgment rule would not apply. In particular, requiring demand in such situations preserves the board's opportunity to take control of litigation brought on behalf of the corporation, *see Galef*, 615 F.2d at 59, even if no deference will be paid to board decisions to dismiss. Although this reasoning suggests that there might be limited circumstances in which demand is required but the business judgment rule does not apply, it nonetheless supports the conclusion reached by this Court that the SLC is entitled to a stay. Specifically, in requesting a stay, the SLC is asking for an initial opportunity to determine whether the board should take over the instant litigation, not demanding that the Court defer to its eventual decision, whatever that may be. The SLC is entitled to this initial decision-making opportunity under the logic of *Lewis*, which held the demand requirement applicable to Section 14(a) litigation, and *Zapata*, which held that the board may delegate its decision-making authority to an independent committee where the board is interested. Thus, even if the Second Circuit were to find subsequently that the business judgment rule is inapplicable to Section 14(a) claims, Second Circuit case law supports the SLC's request for a stay.

Nonetheless, as the following sections demonstrate, there is ample reason to conclude, as this Court does, that the business judgment rule applies to Section 14(a) litigation, even if Second Circuit case law is silent on this matter.*See Galef*, 615 F.2d at 64 n. 20.

5 St. Clair refers to the Direct Common Law Disclosure Claims as "Class Claim[s] for Breach of Fiduciary Duty", while referring to the Derivative Section 14(a) Disclosure Claims as "Derivative Action[s] for Violation[s] of Section 14(a)". Similarly, St. Clair identifies the Class as the injured party in connection with the former Claims, while identifying Take Two as the injured party in relation to the latter.

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APPENDIX B

2013 WL 5508157
Only the Westlaw citation is currently available.
United States District Court,
D. Massachusetts.

Jane E. TAYLOR, Plaintiff,
v.
James M. MOSKOW, JMB Group, LLC,
and Black Oak Realty, LLC, Defendants.

Civil Action No. 13–10802–FDS. | Oct. 1, 2013.

Attorneys and Law Firms

Donald J. Bertrand, Alford & Bertrand, LLC, Watertown, MA, for Plaintiff.

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MEMORANDUM AND ORDER ON DEFENDANTS' MOTION TO DISMISS

SAYLOR, District Judge.

*1 This is an action brought by a beneficiary of various trusts against persons and entities that rent and manage real property owned by LLCs of which the trusts are members. Plaintiff Jane Taylor asserts claims for fraud, misrepresentation, conversion, unjust enrichment, and negligent infliction of emotional distress against defendants James Moskow, JMB Group, LLC, and Black Oak Realty, LLC, and an additional claim of breach of fiduciary duty against defendant James Moskow. Jurisdiction is based on diversity of citizenship.

James Moskow is the manager of Coolidge Properties, LLC, and Stearnwood Properties, LLC, each of which owns various properties, and a trustee of trusts that are members of those LLCs. Moskow is a one-half owner of JMB Group and of Black Oak Realty. The complaint alleges that James Moskow, JMB Group, and Black Oak Realty engaged in self-dealing by overcharging Coolidge Properties and Stearnwood Properties for the services of JMB Group and Black Oak Realty and failed to disclose those overcharges, to the detriment of Jane Taylor, who is a beneficiary of the trusts.

Defendants have moved to dismiss the action pursuant to Fed.R.Civ.P. 12(b)(6) for failure to state a claim upon which relief can be granted. For the reasons set forth below, the motion will be granted.

I. *Background*

Unless otherwise noted, the facts are stated as alleged in the complaint.

A. *The Parties and Relevant Entities*

Plaintiff Jane E. Taylor is a resident of Florida. She is a beneficiary of the Jay I. Moskow Irrevocable Real Estate Trust, the Jane E. Taylor GST Exempt Trust, and the Jane E. Taylor Non–Exempt Trust. (Compl.¶¶ 1, 9, 13, 16). She is also a trustee of the Jane E. Taylor GST Exempt Trust. (*Id.* ¶ 13).

Defendant James M. Moskow is Taylor's brother. (Def.'s Opp. Mot. Remand Ex. A). He is a resident of California. (*Id.*) Moskow is a trustee of the Jay I. Moskow Irrevocable Real Estate Trust and of the Jane E. Taylor GST Exempt Trust. He is also a manager of Coolidge Properties, LLC, and Stearnwood Properties, LLC. (Compl.¶¶ 5, 12). He asserts that he and his wife, Linda Moskow, are the only members of JMB Group, LLC, and Black Oak Realty, LLC, and that he is the sole manager of those companies as well. (Def's Opp. Mot. Remand Ex. A; *see* Compl. ¶ 14).

Defendant JMB Group, LLC, is a limited liability company organized under the laws of Massachusetts. (Compl.¶ 3). JMB Group manages the properties controlled by Coolidge Properties, LLC, and Stearnwood Properties, LLC. (*Id.* ¶ 15).

Defendant Black Oak Realty, LLC, is a limited liability company organized under the laws of Massachusetts. (*Id.* ¶ 4). Black Oak Realty arranges rentals for the properties controlled by Coolidge Properties, LLC, and Stearnwood Properties, LLC. (*Id.* ¶ 14).

Coolidge Properties, LLC, is a limited liability company. It controls the real estate at 9 Sewall Avenue, Brookline, Massachusetts, containing 64 apartments.(*Id.* ¶ 6). The Jay I. Moskow Irrevocable Real Estate Trust, the Jane E. Taylor GST Exempt Trust, and the Jane E. Taylor Non–Exempt Trust are members of Coolidge. James Moskow is the manager. (*Id.* ¶ 5).

*2 Stearnwood Properties, LLC, is a limited liability company. It controls the real estate at 27 Longwood Avenue, 29 Longwood Avenue, 31 Longwood Avenue, and 12–14

Stearns Road, Brookline, Massachusetts, containing, in total, 19 apartments. (*Id.* ¶ 10). The Jane E. Taylor GST Exempt Trust is a member of Stearnwood. James Moskow is the manager. (*Id.* ¶¶ 11, 13).

The Jay I. Moskow Irrevocable Real Estate Trust has as a trustee James Moskow, and has as beneficiaries Jane Taylor, the Jane E. Taylor GST Exempt Trust, and the Jane E. Taylor NonExempt Trust. It is a member of Coolidge Properties.(*Id.* ¶¶ 9, 16).

The Jane E. Taylor GST Exempt Trust has as trustees James Moskow and Jane Taylor, and has as a beneficiary Jane Taylor. (*Id.* ¶ 13). It is a member of Coolidge Properties and Stearnwood Properties. (*Id.* ¶ 16).

The Jane E. Taylor Non-Exempt Trust has as a beneficiary Jane Taylor. (*Id.* ¶ 16). It is a member of Coolidge Properties. (*Id.*). The complaint does not list a trustee. (*See generally id.*).

B. *The Claims*

The complaint asserts claims against all three defendants for fraud, misrepresentation, conversion, unjust enrichment, and negligent infliction of emotional distress. In addition, it asserts against defendant Moskow a claim for breach of fiduciary duty concerning his management of Coolidge Properties and Stearnwood Properties. The central allegation of the complaint is that defendants submitted inflated billing statements to Coolidge and Stearnwood, thereby profiting themselves and taking benefits from the member trusts that own Coolidge and Stearnwood and, indirectly, from the beneficiaries of those trusts.

Specifically, the complaint alleges that, at an unspecified time, defendants submitted inflated billing statements to Coolidge and Stearnwood, setting up a scheme to funnel funds out of Coolidge and Stearnwood. It alleges that Moskow willfully failed to disclose his self-dealing to the member trusts or to Taylor, that he misappropriated her funds, and that he willfully misled her. It further alleges that Moskow owed a fiduciary duty to Taylor in his role as manager of Coolidge and Stearnwood. And it alleges that defendants made material and intentional misrepresentations of fact to Taylor, knowing that she would rely on them, which she did to her detriment. Finally, it alleges that, as a result, Taylor suffered financial loss and other damages, and that she suffered emotional distress and physical harm manifested by objective symptoms.

C. *Procedural Background*

On February 14, 2013, plaintiff filed this action in Norfolk County Superior Court. On April 8, defendants removed this action to federal court on the basis of diversity of citizenship. *See*28 U.S.C. §§ 1332(d), 1441(b). Defendants have moved to dismiss the action pursuant to Fed.R.Civ.P. 12(b)(6).

II. *Legal Standard*

On a motion to dismiss, the Court "must assume the truth of all well-plead[ed] facts and give plaintiff the benefit of all reasonable inferences therefrom."*Ruiz v. Bally Total Fitness Holding Corp.,* 496 F.3d 1, 5 (1st Cir.2007) (citing *Rogan v. Menino,* 175 F.3d 75, 77 (1st Cir.1999)). To survive a motion to dismiss, the complaint must state a claim that is plausible on its face. *Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 570, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007). That is, "[f]actual allegations must be enough to raise a right to relief above the speculative level, ... on the assumption that all the allegations in the complaint are true (even if doubtful in fact)."*Id.* at 555 (citations omitted)."The plausibility standard is not akin to a 'probability requirement,' but it asks for more than a sheer possibility that a defendant has acted unlawfully."*Ashcroft v. Iqbal,* 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009) (quoting Twombly, 550 U.S. at 556). Dismissal is appropriate if plaintiff's well-pleaded facts do not "possess enough heft to show that plaintiff is entitled to relief."*Ruiz Rivera v. Pfizer Pharm., LLC,* 521 F.3d 76, 84 (1 st Cir.2008) (quotations and original alterations omitted).

III. *Analysis*

A. *Standing*

*3 Defendants first contend that plaintiff cannot sue individually for harms that were suffered by Coolidge and Stearnwood, which are LLCs. Instead, they assert that plaintiff could assert a claim, if at all, only derivatively.

The complaint provides little detail about the alleged injuries caused by defendants' conduct. As to the claims for fraud, misrepresentation, conversion, and breach of fiduciary duty, plaintiff lists as the harms personal financial loss, consequential damages, and deprivation of her property rights. (Compl.¶¶ 24, 30, 34, 37). As to the unjust enrichment claim, plaintiff asserts that defendants obtained funds from defrauding her and that she (personally) is entitled to the funds "unlawfully transferred" from Stearnwood and Coolidge to defendants. (*Id.* ¶ 42). Although plaintiff frames these harms as personal, the complaint as written makes clear that Steamwood and Coolidge (which are LLCs) directly suffered the losses. The trusts (which are members of the LLCs) and plaintiff (who is a beneficiary and/or trustee of the trusts) indirectly suffered the losses. In other words, the complaint in substance alleges that defendants misappropriated the funds of various certain entities—not those of plaintiff.

As a general rule, "a mere shareholder, officer, director, or member does not have standing to assert a claim on behalf of a business entity" for injuries suffered by the entity. *Laverty v. Massad,* 661 F.Supp.2d 55, 61 (D.Mass.2009) (citing *Diva's Inc. v. City of Bangor,* 411 F.3d 30 (1st Cir.2005)). Thus, "a member of an LLC cannot bring an action *in his own name* to enforce the rights or redress the injuries of the LLC."*Id.*(citing *First Taunton Fin. Corp. v. Arlington Land Acquisition–99, LLC,* 20 Mass. L. Rep. 556 (Mass.Super.Ct.2006)) (emphasis added). Plaintiff here does not have standing to assert a claim for injuries suffered by an LLC. Such a claim must be brought by the LLC itself, or derivatively on its behalf.

As a general matter, a member of an LLC can assert a claim on its behalf either (1) when authorized by the LLC to do so or (2) when the entity has failed to assert its own rights, as a derivative action. *See*Mass. Gen. Laws ch. 156C, § 56 (providing that a member or manager of a limited liability company can bring a suit on its behalf when authorized by a vote or a written operating agreement); *Billings v. GTFM, LLC,* 449 Mass. 281, 289, 867 N.E.2d 714 (2007) (stating that "members of a limited liability company [may] bring suits on its behalf"). Plaintiff here is not a member or manager of the LLCs, and therefore cannot bring a derivative action. *Diamond v. Pappathanasi,* 78 Mass.App.Ct. 77, 93, 935 N.E.2d 340 (2010) ("[I]n order to maintain a derivative action, one must strictly retain an ownership interest in the company on whose behalf the action is brought").

Certain of the trusts named in the complaint, however, are members of the LLCs. A member trust could thus bring a derivative claim on behalf of the LLCs for injuries suffered by the LLCs. And even though plaintiff is not herself a member trust, she might be able, in her capacity as a trustee or beneficiary, to assert a derivative claim on behalf of the trust seeking damages for harm to the LLCs. *See*Mass. Gen. Laws ch. 203E, § 811 ("A trustee shall take reasonable steps to enforce claims of the trust...."); *Demoulas v. Demoulas Super Markets, Inc.,* 424 Mass. 501, 677 N.E.2d 159 (1997) (holding that a beneficiary, rather than a trustee, of a trust that owned shares of a corporation could bring a shareholder's derivative action against the corporate directors based on their usurpation of corporate opportunities, noting that "the trustee may very well be the director whose operation of the corporation is being challenged" and that therefore "the beneficiary is not required to depend on the trustee to bring such an action"); *see also Zoppo v. Zoppo,* 453 F.Supp.2d 232, 234 (D.Mass.2006) ("[A] trustee has the power to bring claims on behalf of beneficiaries."); *cf. Diamond,* 78 Mass.App.Ct. at 93–94, 935 N.E.2d 340 (holding that a trust beneficiary had not "established her standing to maintain a derivative action" because she did not "hold a direct interest in the entity on whose behalf she is purporting to sue").

*4 In any event, plaintiff here has not attempted to bring these claims derivatively. And, even if she had, a derivative suit is subject to the procedural requirements of Rule 23.1, which do not appear to have been satisfied. *See*Fed R. Civ. P. 23.1; *First Taunton Fin. Corp.,* 20 Mass. L. Rep. 556, 2006 WL 696689, at *4 (holding that Mass. R. Civ. P. 23.1 applies to limited liability companies); *Mastromatteo v. Mastromatteo,* 21 Mass. L. Rep. 705, 2006 WL 3759512, at *2 (Mass.Super.Ct.2006) (same).

Finally, plaintiff conceivably could assert a claim against Moskow for breach of fiduciary duty in his role as trustee. But the complaint alleges only a breach of his duties "[a]s a manager of Steamwood Properties, LLC and Coolidge Properties, LLC." (Compl.¶ 35); *cf.*Mass. Gen. Laws ch. 203E, § 1001(b) (identifying beneficiary's remedies for breach of trust by trustee); Bogert, *The Law of Trusts and Trustees* § 543 ("The trustee must not place himself in a position where his own interests or that of another enters into conflict, or may possibly conflict, with the interest of the trust or its beneficiary."). By framing the breach as stemming from Moskow's role as a manager of the LLCs, any injury caused by that breach was suffered by the LLCs, not plaintiff. Therefore, any such claims must be brought derivatively by a representative of the trusts, not individually.

In short, plaintiff's claims against defendants for injuries to the LLCs that caused damage to her financial interests must fail. As a general proposition, the law provides remedies for fraud, misrepresentation, and self-dealing, even in family enterprises, and even in enterprises with complex ownership and management structures. But the law also ordinarily requires that those structures be respected, except in a few, narrowly-defined circumstances that the complaint here has not alleged. Defendants' motion to dismiss Counts One through Five will therefore be granted.[1]

B. *Negligent Infliction of Emotional Distress*

The sixth claim, negligent infliction of emotional distress, does allege a harm that plaintiff herself suffered—namely, that she experienced physical harm due to defendants' alleged negligence. (Compl.¶ 45).

To state a claim for negligent infliction of emotional distress, and party needs to assert: "(1) negligence; (2) emotional distress; (3) causation; (4) physical harm manifested by objective symptomatology; and (5) that a reasonable person would have suffered emotional distress under the circumstances of the case."*Payton v. Abbott Labs,* 386 Mass. 540, 557, 437 N.E.2d 171 (1982); *see Sullivan v. Boston Gas Co.,* 414 Mass. 129, 132, 605 N.E.2d 805 (1993). The complaint here alleges that defendants "negligently inflicted emotional distress upon the Plaintiff," that defendants' actions "were the cause of" her distress, that as a result she "reasonably suffered physical harm manifested by objective symptomatology," and that as a result of defendants' negligence she "suffered emotional distress, and has been caused to suffer financial hardship, costs, and attorney fees."(Compl.¶¶ 44–47).

*5 Although "the pleading standard Rule 8 announces does not require 'detailed factual allegations,' " the Rule "demands more than an unadorned, the-defendant-unlawfully-harmed-me accusation."*Iqbal,* 556 U.S. at 678 (citing *Twombly,* 550 U.S. at 555). The principles of Rule 8 apply with special force in a context such as this, where plaintiff is essentially attempting to graft a negligence claim onto a family business dispute, and where issues such as duty, breach, causation, and injury are murky at best. For example, the reasonableness and foreseeability of any severe emotional distress stemming from the facts alleged in the complaint-which, again, essentially allege financial injury to LLCs—are questionable at best. *See, e.g., Smith v. Jenkins,* 718 F.Supp.2d 155, 172 (D.Mass.2010) (finding that it was not reasonably foreseeable that borrower would suffer severe emotional distress due to alleged fraud by lenders, mortgage brokers, and real estate firms, and thus that they were not liable for negligent infliction of emotional distress). Under the circumstances, and at a minimum, a claim for negligent infliction of emotional distress requires something more than a "formulaic recitation of the elements." *Iqbal,* 556 U.S. at 678. The complaint here does not meet that standard. Accordingly, defendants' motion to dismiss will be granted.

IV. *Conclusion*

For the foregoing reasons, the defendants' motion to dismiss is GRANTED.

So Ordered.

All Citations

Slip Copy, 2013 WL 5508157

Footnotes

1 Defendants further contend that the complaint is insufficient to state claims for fraud, misrepresentation, conversion, breach of fiduciary duty, unjust enrichment, and negligent infliction of emotional distress. Because Counts One through Five will be dismissed for lack of standing, the sufficiency of those pleadings need not be addressed.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 15th day of October, 2015, I caused to be served a true and correct copy of the foregoing document as follows:

Kammi Mencke-Smith Kevin J. Curtis Winston & Cashatt, Lawyers, PS 601 W. Riverside Ave., Ste 1900 Spokane, WA 99201	___ Hand Delivery ✓ U.S. Mail ___ Overnight Delivery ___ Fax Transmission
Division III Court of Appeals State of Washington 500 N Cedar St Spokane, WA 99201	___ Hand Delivery ✓ U.S. Mail ___ Overnight Delivery ___ Fax Transmission

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