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No. 67772-1

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION I

CONLEY PROPERTY RESOURCES, L.L.C., a Washington limited liability company; and A. Bernard Conley, a married man,

Appellants,

v.

JAMES A. GODFREY, a married man; and CHATEAU RETIREMENT COMMUNITIES, LLC, a Washington limited liability company,

Respondents.

BRIEF OF APPELLANTS

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I. INTRODUCTION & PROCEDURAL BACKGROUND

The issue before this Court is whether the following arbitration-clause language limits arbitration to disputes between Members of a company:

Any claim between the Members arising out of or relating to this Agreement, including any claim based on or arising from an alleged tort, shall be determined by arbitration (emphasis supplied) (CP 145)

The Conley plaintiffs (now appellants) contend that the trial court erred by ruling that this “claim between the Members” arbitration clause bound them to arbitrate their claims in this case. The Conley plaintiffs’ claims were not between members, but were specifically against non-member managers of a limited liability company. The Conley plaintiffs seek reversal of the trial court’s decision and remand of this case to the trial court for further proceedings.

This case arises as a management-deadlock dispute between non-member managers. The Conley plaintiffs pleaded claims, not between the Members, but by (1) one Manager (Bernie Conley) against another Manager (Jim Godfrey) and his managerial agent in a management-deadlock dispute and (2) one Member (Conley Property Resources, L.L.C.) against that same defendant Manager (Godfrey) and that same managerial agent who caused monetary damage to that Member due to that management-deadlock dispute.

The above-quoted “claim between the Members” arbitration clause is found at Section 19.2 of a limited liability operating agreement. The Members and the Managers are each a distinct party to that operating agreement. That operating agreement further distinguishes the differing rights, responsibilities, and remedies of Members and Managers, including the carve out of specific “Default” and “Alternative Dispute Resolution” Sections that address only Members within the narrow scope of those Sections.

In sum, the gravamen of the Conley plaintiffs’ claims is not one “between the Members”. Instead, as will be detailed in the Statement of the Case section of this brief, their claims arise out of a management deadlock within an equally co-managed and co-owned limited liability company named LBL Associates, LLC (“LBL”).

The co-Managers of LBL are plaintiff Bernie Conley and defendant Jim Godfrey. However, Managers Conley and Godfrey are not the Members (owners) of LBL. Instead, the co-equal Members of LBL are separate legal entities: plaintiff Conley Property Resources, L.L.C. and non-party Godfrey Resources, LLC. These eponymous Members are respectively owned by the Conley and Godfrey families.

Plaintiff Bernie Conley, as a Manager, and plaintiff Conley Property Resources, as a Member, brought their claims to stop defendant Godfrey and his managerial agent, defendant Chateau Retirement Centers, LLC, (1) from silencing Bernie Conley's management voice in the operations of LBL, (2) from disenfranchising Bernie Conley's management vote in the operations of LBL, and (3) to recover damages and obtain equitable relief, such as access to business records, timely material information, and an accounting, due to defendants' management breaches and to prevent defendants from obtaining payment defense costs from LBL during the pendency of the action. (CP 5-23)

In response to the Conley plaintiff's management-breach claims, defendant Godfrey filed a CR 12(b)(6) motion (CP 24-48) accompanied by his seven-page declaration reciting his version of the parties' management disputes and attaching the LBL operating agreement (CP 49-83).

It is critical to point out that defendant Godfrey's motion was to dismiss, on the substantive merits, the Conley plaintiffs' management-breach claims. Godfrey's dismissal motion was not a motion seeking to dismiss plaintiffs' complaint on the ground that the management dispute involved arbitrable claims. Defendant Godfrey stated on the first two pages of his motion:

In this case, the Complaint fails to state a claim because (1) the plaintiffs have sued the wrong parties; (2) by written agreement of the parties, the breach of contract claim is not allowed; (3) the plaintiffs' Complaint utterly fails to allege a valid claim for breach of fiduciary duty; and (4) the claim for declaratory relief is not justiciable, is entirely hypothetical, and thus is nothing more than an impermissible request for an advisory opinion. (CP 24 I. 23, CP 25 II. 1-4)

The only reference to arbitrable disputes, a forum issue, found within the Godfrey dismissal motion was a hypothetical reason as to why the Conley plaintiffs allegedly "sued the wrong parties" (Godfrey Argument No. 1, above). Godfrey argued that the complaint should be dismissed because LBL was an unnamed necessary party defendant. However, LBL is the company and by definition is not a Manager or Member of itself. Defendant Godfrey then posited a hypothetical reason that the Conley plaintiffs did not name LBL as a defendant in order to avoid arbitration even though arbitration is appropriate only for the limited circumstances of "any claim between the Members" according to Section 19.2 of the operating agreement. (CP 33 II. 22-25, CP 34 II. 1-6)

Following up on that misplaced hypothetical reason, defendant Godfrey then asked for attorneys' fees under the discretionary attorneys'-fee clause found within the limited "between Members" arbitration clause. (CP 45 II. 22-23, CP 46 II. 1-2, II.21-23)

In sum, it is critical, again, to point out that defendant Godfrey was not seeking to have the Conley plaintiffs'

management-breach claims heard by an arbitrator. Instead, defendant Godfrey wanted the complaint dismissed on the merits.

The Conley plaintiffs responded to the merits. Within their response, the Conley plaintiffs also pointed out that the LBL operating agreement Section 19.2 arbitration was to limited to claims “between the Members” and that there were no claims between the Members asserted within the Conley plaintiffs’ management-breach complaint. (CP 107, 145 (Section 19.2))

Defendant Godfrey’s reply and his six-page reply declaration addressed only the merits of the dispute. Defendant failed to rebut the Conley plaintiff’s observation that Section 19.2 arbitration was solely for claims “between the Members” and that there were no such claims in the complaint. (CP 264-70, CP 271-77)

At oral argument there was colloquy between counsel and the trial court about the merits of the case based upon the facts, identified in the two Godfrey and one Conley declarations, and about arbitrating plaintiffs’ claims against LBL. (RP 1-28)

The trial court chose not to rule on the merits, but instead stated that the entirety of the dispute was arbitrable as stated in its oral decision:

. . . I am going to grant the motion. I think that this is the wrong court, the wrong place, it needs to be in arbitration. I’m not going to award attorney’s fees, but I . . . will dismiss the lawsuit under [CR] 12(b)(6). This . . . case should be arbitrated rather pursuant to the arbitration provision of the

agreement rather than . . . being here in court. (RP 28, ll. 12-17)

The Conley plaintiffs bring this appeal so that they may have their day in court, where they are entitled to seek redress of defendants' management breaches. In a nutshell, they want (1) Bernie Conley's management voice restored in the operations of LBL, (2) Bernie Conley's management vote re-enfranchised in the operations of LBL, and (3) to recover damages and obtain equitable relief, such as access to business records and an accounting, due to defendants' management breaches and to prevent defendants from obtaining indemnity from LBL. (CP 5-23)

The grounds for this appeal are narrow, but the consequences are vast given the Conley plaintiff's right to have their day in court. Namely, is the arbitration clause found at Section 19.2 limited to claims "between the Members"? Or may a trial court disregard the right of parties to contract freely and choose specific language, and then undo the parties' bargain by rewriting Section 19.2 to impose arbitration upon certain parties to the LBL operating agreement who chose not to consent to arbitration?

II. ASSIGNMENTS OF ERROR & ISSUES PERTAINING TO SAME

Appellants Conley Property Resources, L.L.C. and A. Bernard Conley (hereinafter collectively referred to as “Conley plaintiffs”) make the following assignments of error:

A. Assignments of Error

1. The trial court erred by not treating defendant Godfrey’s CR 12(b)(6) motion to dismiss the Conley plaintiffs’ claims as a motion for summary judgment as mandated by the last sentence of CR 12(b)(6). (CP 279-80)

2. The trial court erred in granting defendant Godfrey’s CR 12(b)(6) motion to dismiss the Conley plaintiffs’ claims on the ground that each management-breach claim is an arbitrable dispute. (RP p.28, ll. 12-17; CP 280)

3. The trial court erred in entering the order as one for dismissal with prejudice since the court’s accompanying oral decision treated the Conley plaintiffs’ claims as being subject to arbitration. (RP p. 28, ll. 12-17; CP 280)

B. Issues Pertaining to Assignments of Error

1. Did the trial court err by ignoring the last sentence of CR 12(b)(6) by not treating defendant Godfrey’s CR 12(b)(6) motion as a motion for summary judgment because

matters outside the pleading were presented to and not excluded by the trial court? (Assignment of Error 1).

2. Do the Conley plaintiffs' claims against defendant Godfrey as a company manager and against defendant Chateau Retirement Communities (as Godfrey's managerial agent), solely for breaches of management duties and where no company member is named as a defendant, constitute an arbitrable "claim between the Members [of the LBL company]" under the limited-party arbitration clause found at Section 19.2 of the LBL operating agreement? (Assignment of Error 2)

3. Should the trial court's order of dismissal be treated as an order staying arbitration pursuant to RCW 7.04A.070(6)? (Assignment of Error 3)

III. STATEMENT OF THE CASE

The narrow issue on appeal is about the identity of the parties subject to an arbitrable “claim between the Members” arbitration clause. That narrow issue is set in the context of the LBL operating agreement, a management-deadlock dispute, and the Conley plaintiffs’ claims.

A. Relevant Terms of The LBL Operating Agreement

1. The parties to the LBL operating agreement are identified in the first sentence of that document:

is made effective as of the 10th day of August 2004 (the “Effective Date”) by Conley Property Resources L.L.C. . . . (“CPR”), Godfrey Resources LLC . . . (“GR”), CPR-GR LLC . . . (“CPR-GR”), and A. Bernard Conley and James A. Godfrey as managers (the “Managers”). CPR, CPR-GR, and GR and any new admitted member shall be sometimes referred to herein as “Member” (CP 130)

2. The terms of the LBL operating agreement identify plaintiff Bernie Conley and defendant Godfrey as co-equal Managers and their respective family companies are co-equal Members (owners) of LBL. In other words, the Managers and the Members are different persons. No Manager is a Member. No Member is a Manager. (CP 85 II. 2-4; CP 112 II. 22-25, CP 112 II. 1-10, 130-32, 134)

3. The duties of the Managers are different from the duties of a Member under the operating agreement. Under

Section 10.1 of the operating agreement, and subject to limited exceptions, a Manager has the:

exclusive right and power to manage . . . [LBL] and to do all things and make all decisions necessary . . . to carry on the business . . . of [LBL]. The authority of each Manager shall include, but shall not be limited to the following: [describing ten actions such as operating LBL, selling LBL property, employing persons, leasing, executing binding documents, entering into agreements, borrowing money, and suing on behalf of LBL]. (CP 136-37)

4. Other duties of the Managers include a determination of surplus cash of LBL, denominated as “Cash Available From Operations” under Section 1.5 that is to be distributed to Members under Section 9.1 (last sentence); a determination of tax distributions under Section 9.2; and a fiduciary duty under Section 10.5 to safekeep and use funds and assets of LBL and to use such funds and assets in accordance with the operating agreement. (CP 130-31, 136-37, 139)

5. By contrast, Section 11.1 states that:

No Member shall take part in the conduct or control of [LBL] business or the management of [LBL], or have any right or authority to act for or on behalf of, or otherwise bind, [LBL] (except as specifically provided herein, and except a Member who may also be the Manager [which is not the case here] (CP 139) (emphasis supplied)

6. Further, by way of contrast to a Manager’s duties, the Members’ duties are different and limited to those expected of investors owning a valuable equity interest. Those

duties include the terms of raising additional capital under Section 6.3 and transfers of valuable membership interests under Section 13. (CP 71-74, 134-35)

7. Last, the LBL operating agreement contains a detailed “Default” Section 14 and a detailed “Alternative Dispute Resolution” Section 19 that are limited only to Member defaults and Member dispute resolution. The parties chose not to include, within these two Sections, language defining what constituted defaults by a Manager and language providing for Manager dispute resolution. (CP 141-45)

8. As to “Default” Section 14, the parties chose language that identified: six separate events that constitute a Member default at Section 14.1; four separate actions that a Non-Defaulting Member could take against another Member, including purchasing the Defaulting Member’s interest and suspending a Manager, at Section 14.2; and the terms by which a Non-Defaulting Member could purchase a Defaulting Member’s interest at Section 14.3. (CP 141-43) Again, for purposes of clarity, the parties chose not to include a default section within the operating agreement for alleged Manager defaults.

9. As to “Alternative Dispute Resolution” Section 19, the parties further chose language that provided alternative dispute resolution for disputes limited to those between the Members. Section 19 is composed of four subsections. The first

subsection is Subsection 19.1, and it opens with the prefatory comment that “The Members hope there will be no disputes arising out of their relationship”. Nothing in the remainder of this Subsection 19.1 addresses any dispute with a Manager. To the contrary all activity to resolve disputes within that subsection is performed only by a Member or Members, including resolving their disputes by binding arbitration and trying to resolve matters by non-binding mediation. (CP 144)

10. Similarly, the language of the arbitration clause, at issue in this appeal and found at Section 19.2, does not include Managers. It reads in full:

Any claim between the Members arising out of or relating to this Agreement, including any claim based on or arising from an alleged tort, shall be determined by arbitration in Seattle commenced in accordance with RCW 7.04.060, provided that the total award by a single arbitrator (as opposed to a majority of the arbitrators) shall not exceed \$250,000, including interest, attorneys’ fees and costs. If any Member demands a total award greater than \$250,000, there shall be three neutral arbitrators. If the Members cannot agree on the identity of the arbitrator(s) within 10 days of the arbitration demand, the arbitrator(s) shall be selected by the administrator of the American Arbitration Association (AAA) office in Seattle from its Large, Complex Case Panel (or have similar professional credentials). Each arbitrator shall be an attorney with at least 15 years’ experience in commercial or planning law and shall reside in the Seattle metropolitan area. Whether a claim is covered by this Agreement shall be determined by the arbitrator(s). All statutes of limitations which would otherwise be applicable shall apply to any arbitration proceeding hereunder. (CP 145) (emphasis supplied)

11. Finally, remaining Subsections 19.3 and 19.4 address the Procedures and Hearing aspect of the “claim between the Members” arbitration. Under Subsection 19.3, it is Members who may be required to provide some or all of their case by written declaration and that the “Members intend to limit live testimony and cross-examination to the extent necessary to ensure a fair hearing on material issues”. (CP 145)

12. Subsection 19.4 then addresses the arbitration hearing and refers to time limits that the Members, alone, have set for the hearing and decision, and that Members, alone, may be joined to this arbitration and that this arbitration may be consolidated with another arbitration. Again, the parties chose the language of this carefully crafted four-part Alternative Dispute Resolution Section not to include Managers in the procedures and the arbitration hearing. (CP 145)

B. The Management-Deadlock Dispute

13. LBL is the ground lessor of the Chateau at Bothell Landing Retirement Community (the “Project”), which is a 102-unit retirement and assisted-living community located in Bothell. LBL’s operations are extremely limited. LBL’s operations as a ground lessor are confined to the receipt of monthly rents from the tenant that operates the Project, the monthly payment of a mortgage (with a 2041 maturity date) and payments of entity-

specific expenses from those rents. The balance is surplus cash to be paid to the Members, as if they were “coupon clippers” receiving a steady stream of income, pursuant to Section 9.1 of the operating agreement (last paragraph as “Cash Available From Operations”, a defined term at Section 1.5 and determined by a Manager). The operations for the retirement community are conducted, not by LBL, but by the ground-lease tenant and a related management company. The ground-lease tenant is obligated to pay all operating expenses, including real property taxes and insurance, and to pay for all repairs and improvements (CP 85 ll. 5-15; CP 113, ll. 19-25, 114, 115 ll. 1-10, 116 ll. 17-21, 130-31, 136, 155, 160, 164-65, 169-74, 177-78)

14. Defendant Godfrey, and by acting through defendant Chateau Retirement Communities, LLC (“CRC”), violated the parties’ operating agreement for LBL and his fiduciary duties to both plaintiffs in at least two respects. First, defendant Godfrey unilaterally loaned or contributed the surplus cash (“Cash Available From Operations”) of LBL to other Conley-Godfrey co-managed companies without first informing Bernie Conley and without obtaining Bernie Conley’s consent. It is undisputed that this was surplus cash because if it were necessary for LBL operations, then it would not have been so loaned or contributed. Second, defendant Godfrey unilaterally reduced the amount of rents that LBL’s ground-lease tenant, a co-managed company that operates

the Project, was obligated to pay LBL without first informing and without obtaining Bernie Conley's consent. This unilateral action deprived LBL of additional surplus cash. (CP 85 ll. 16-25; CP 115 ll. 11-24, 116-17, 118, ll. 1-19, 119 ll. 9-14, 161, 169-70, 199-204, 205, 208, 212, 216, 229-30, 232-36, 237-40, 254 -58)

15. As to operating-agreement violations of management duties, the Conley plaintiffs first contend that defendant Godfrey's unilateral loans and contributions of surplus cash (a) violate Section 9.1 of the operating agreement because the surplus cash is to be distributed to the Members and (b) violate Sections 5 and 10.2(d) because making such loans and contributions is not a primary purpose of LBL and a change in the nature of LBL, (CP 130, 133-34, 136, 138). Related to that is the refusal to provide access to business records under Section 12.2. (CP 140) The Conley plaintiffs next contend that defendant Godfrey's unilateral decision to reduce the receipt of rents of the ground lease (a) violate Section 9.1 of the operating agreement because it diminishes surplus cash to be distributed to the Members and (b) violate Section 10.2(a) as an improper attempt to modify the lease giving rise to the rents, and (c) violate Section 10.6(a) because it is an improper attempt to modify that lease via an affiliate. (CP 136, 138, 139)

16. As to breaches of management-fiduciary duties, the Conley plaintiffs first contend that defendant Godfrey

breached his fiduciary duty as a manager set forth at Section 10.5, which requires him, as a manager to “have a fiduciary responsibility for the safekeeping of all funds and assets of [LBL], and all such funds and assets shall be used in accordance with the terms of this Agreement”, which defendant Godfrey did not do as described in the prior paragraph. The Conley plaintiffs next contend that defendant Godfrey breached the fiduciary duties of care, loyalty, and the obligation to act in good faith and with fair dealing due to the actions described in the prior paragraph. The Conley plaintiffs next contend that these fiduciary duties were breached due to defendant Godfrey’s failure to provide timely and material information (such as the loans, contributions, and rent reductions discovered after the fact) to them. (CP 92-104, 139)

17. The effect of defendant Godfrey’s undisclosed and unconsented actions was to silence Bernie Conley’s management voice and disenfranchise his management vote as to these two surplus cash actions and any other actions that defendant Godfrey has failed to disclose. Effectively there were no longer two co-equal managers, but one: defendant Godfrey. The Conley plaintiffs contend that by his unilateral undisclosed and unconsented actions, defendant Godfrey became a “majority of one” manager as part of his efforts to freeze Bernie Conley out of management and Conley Property Resources out of its ownership rights. (CP 86 II. 1-8; CP 117 II. 3-25, 118, 119 II. 1-14, 121 II. 20-

25, 122 II. 1-17, 124 II. 3-25, 125 II. 1-7, 237-40, 241-42, 252, 259-61, 262-63)

18. The Conley plaintiffs contend that Bernie Conley's loss of his management rights, which were designed to protect Conley Property Resources, due to defendant Godfrey's unilateral management actions then damaged plaintiff Conley Property Resources. Defendant Godfrey damaged plaintiff Conley Property Resources by putting distributable surplus cash out of reach of LBL in two ways: (a) by the unilateral LBL loans or cash contributions to other co-managed companies and (b) by depriving LBL of rents that would have added surplus cash available for distribution to all of the Members, including Conley Property Resource's share. (CP 86 II. 9-16; CP 115 II. 11-24, 116-17, 118 II. 1-19, 119 II. 9-26, 120, 121 II. 1-2, 161, 169-70, 199-204, 205, 208, 212, 216, 229-30, 232-36, 237-40, 254-58)

19. Defendant Godfrey attempted to justify his unilateral actions on the grounds that the surplus cash of LBL was necessary to pay for the bills of other Conley-Godfrey co-managed companies. The Conley plaintiffs contend that this justification is nothing more than a variant of taking money from Peter to pay the debts of Paul. Defendant Godfrey's attempted justification to take the surplus cash of "Peter [here, LBL]" to pay for the debts of "Paul [other companies]" violates the express terms of the LBL operating agreement, at Section 9.1, that mandate the payment of surplus

cash directly to all of its members, including Conley Property Resource's share. Godfrey's attempted justification is not true and not well thought out as it would expose LBL to claims by creditors of other co-managed companies that LBL and the other co-managed companies lack a separate corporate existence. (CP 86 II. 17-24, 91 II. 5-8, 22-25; CP 125 II. 20-25, 126 II.1-3, 128)

20. Defendant Godfrey's unilateral action to reduce rents also violated the lease obligation to pay stipulated rents to LBL. That unilateral Godfrey action then violated the conditions of the LBL mortgage, which is insured by the federal department of Housing and Urban Development ("HUD"). Those HUD conditions mandate the payment of the stipulated rents rather than the Godfrey-induced reduced rent amounts. Defendant Godfrey's unilateral action threatened to place the HUD-insured LBL mortgage in default. (CP 86 I. 25, 87 II. 1-5; CP 118 II. 20-24, 119 II. 1-8, 241-42, 252)

C. The Claims

21. The facts identified in the prior "LBL operating agreement" and "The Management-Deadlock Dispute" sections gave rise to the Conley plaintiffs' complaint that contained three causes of action. (CP 5-22)

22. The Conley plaintiffs' first cause of action is against defendant Godfrey for management breaches of the LBL

operating agreement. (CP 15-16). The first cause of action seeks injunctive relief for plaintiff Conley Property Resources to get access to business records and to reinstate the proper rent payments. (CP 15-16) The first cause of action seeks damages for plaintiff Conley Property Resources for its share of the surplus cash that defendant Godfrey put out of reach by his unilateral loans, cash contributions, and rent reductions to co-managed companies. (CP 15-16)

23. The Conley plaintiffs' second cause of action is for management breaches of fiduciary duties against defendant Godfrey and defendant Chateau Retirement Communities, LLC ("CRC") acting as Godfrey's managerial agent. (CP 16-18) Ironically, defendant CRC is supposed to be co-managed by Bernie Conley. The second cause of action seeks injunctive relief for each of the Conley plaintiffs, including the right to obtain timely, material information about the operations of LBL, for participation in material decisions, and for an accounting of LBL funds, and to reinstate proper rent payments. (CP 17-18) The second cause of action seeks damages for plaintiff Conley Property Resources for its share of the surplus cash that defendants put out of reach by their unilateral loans, cash contributions, and rent reductions to co-managed companies. (CP 16-18)

24. The Conley plaintiffs' third cause of action is for a declaratory judgment to declare that defendants Godfrey and his

managerial agent CRC are not entitled to indemnification as managers under Section 10.4 for LBL to pay their attorneys' fees for the defense of this case. The Conley plaintiff's third cause of action is due to the acts of defendants to take unilateral actions without consent where surplus cash was put out of reach by their unilateral loans, cash contributions, and rent reductions to co-managed companies. (CP 18-19)

IV. ARGUMENT

A. De Novo Standard of Review of All Issues on This Appeal

This Court's review of a trial court's decision to grant summary judgment (although couched as a CR 12(b)(6) ruling in the dismissal order) is based on a *de novo* standard of review. In a nutshell, it is a standard of review where this Court gives no deference to the trial court's decision. Instead, this Court engages in the same inquiry as a trial court may when considering the motion for summary judgment.¹ (Related to Assignment of Error No. 1)

Here, the threshold substantive question is interpretation of an unambiguous contract is a question of law. Interpretation of an unambiguous contract is a question of law even if the parties dispute the legal effect of a certain provision. Thus, this Court

¹ Smith v. Sea Ventures, Inc., 93 Wn. App. 613, 615, 969 P.2d 1090, 1091 (1999)

reviews questions of law on a *de novo* standard of review.²
(Related to Assignment of Error No. 2)

Last, there is the interpretation of RCW 7.04A.070(6), as he applied to the dismissal order in the case, as a stay of the case pending arbitration. The interpretation of that statute is a legal question similarly subject to a *de novo* standard of review.³
(Related to Assignment of Error No. 3)

In sum, this appeal of a very narrow issue about whether Managers are parties to arbitrate “[a]ny claim between the Members” is subject to *de novo* review given its procedural posture before this Court and this Court’s interpretation of an unambiguous contract term regarding the parties bound to arbitrate of “any claim between the Members”.

B. The Trial Court Erred Where It Failed To Consider Defendant’s CR 12(b)(6) Motion As One For Summary Judgment Because Matters Outside Of The Pleadings Were Presented And Not Excluded By The Trial Court

Under Washington law, a CR 12(b)(6) motion to dismiss that is supported by materials outside the complaint shall be treated as a motion for summary judgment. Since defendant Godfrey provided a seven-page declaration detailing his view of the

² Absher Constr. Co. v. Kent Sch. Dist. No. 415, 77 Wn. App. 137, 141-42, 890 P.2d 1071 (1995)

³ Optimer Int’l, Inc. v. RP Bellevue, LLC, 170 Wn.2d 768, 771, 246 P.3d 785, 787 (2011)

management disputes, and then recited those declaration facts in detail at pages two to five of his opening brief, then his motion to dismiss must be treated as one for summary judgment.⁴

Furthermore, Washington law mandates that if the trial court did not exclude Bernie Conley's response declaration or the two Godfrey declarations (opening and reply), then dismissal of this action under CR 12(b)(6) was error. Because the trial court did not exclude that extrinsic evidence, then it was mandated to treat defendant Godfrey's motion to dismiss as a summary judgment.⁵

The consideration of defendant's motion as one for summary judgment is important because the extrinsic evidence submitted by the respective parties demonstrates the context of the management-deadlock dispute, and its consequences, in which the Conley plaintiffs pleaded their claims rather than viewing those claims in a vacuum.

C. The Conley Plaintiffs Brought Claims Against Defendants as Managers for Breach of Management Duties. Therefore It Was Reversible Error for The Trial Court To Dismiss The Conley Plaintiffs' Claims On The Grounds That They Were "Between The Members" Arbitrable Disputes Pursuant to Section 19.2 Of The Operating Agreement

⁴ CR 12(b)(6) (Last sentence); Hope v. Larry's Markets, 108 Wn. App. 185, 191-92, 29 P.3d 1268 (2001) (dismissal for failure to state a claim was error)

⁵ St. Yves v. Mid State Bank, 111 Wn.2d 374, 377, 757 P.2d 1384 (1988) (CR 12(b)(6) motion treated as summary judgment)

1. **Role of the Trial Court Is To Respect The Parties' Agreement and Not Rewrite It.**

This Court's recent decision of Rimov v. Schultz addresses the role of the trial court when considering whether a particular party agreed to arbitrate a dispute.⁶

Amy Rimov and Mary Schultz were respectively an associate and a principal at Ms. Schultz's law firm and they were lovers. During their relationship, they executed a release of claims, ostensibly due to the fact that one served as an employee and the other as employer during their relationship.⁷

When their relationship ended, Ms. Rimov claimed that the release was invalid. She then retained counsel to represent her in a potential claim against Ms. Schultz. Both parties agreed to put the issue of the validity of the release before a retired superior court judge as a non-binding arbitration. The retired judge ultimately rendered a decision that Rimov-Schultz release was valid and binding.⁸

Nearly a year after the judge's decision, Ms. Rimov filed a complaint against Ms. Schultz and her law firm seeking an equitable distribution of property accumulated during their relationship and claims related to her employment. Ms. Schultz

⁶ Rimov v. Schultz, 162 Wn. App. 274, 253 P.3d 462 (2011)

⁷ Id. at 277, 253 P.3d at 464

⁸ Id.

countered that the retired judge's decision was binding because non-binding arbitration is not recognized as a matter of law.⁹

On appeal, this Court ruled in Rimov that parties to an arbitration agreement were free to seek an advisory opinion from the retired judge.¹⁰

Relevant to this appeal, is that in rendering its Rimov opinion, this Court recognized the right of the parties to bargain as to what who is and who is not subject to a binding arbitration. In doing so, the Rimov opinion elucidated certain legal rules that will guide this Court in this appeal, the crux of which is whether claims against a manager for management breaches become an arbitrable "claim between the Members" under Section 19.2 of the LBL operating agreement.

2. Rules That The Trial Court Failed To Observe.

The Rimov court first stated the bargained-for nature of arbitration:

Arbitration traces its existence and jurisdiction first to the parties' contract and then to the arbitration statute itself. [citation omitted] Parties are free to decide if they want to arbitrate. [citation omitted] The parties may also decided the issues to be submitted to arbitration. [citation omitted] Once, an issue is submitted to arbitration, [then] the statute controls. [citation omitted]¹¹

⁹ Id. at 277-78, 253 P.3d at 464

¹⁰ Id. at 288-89, 253 P.3d at 469-70

¹¹ Id. at 465, 253 P.3d at 280

The Rimov court then addressed the specific language of the purported arbitration clause between Rimov and Schultz, and stated the following rules of contract interpretation:

A contract exists when there is mutual assent to its essential terms. [citation omitted] In determining the mutual intention of the contracting parties, the unexpressed subjective intentions of the parties are irrelevant; the assent of the parties must be gleaned from their outward manifestations. [citation and footnote omitted] When construing an agreement, we give effect to every word so as not to render any word superfluous. [citation omitted]¹²

The Rimov court then applied the “ordinary meaning” rule of interpretation to the word “nonbinding”. This Court found that meaning was not inadvertent given the language of the clause at issue. In sum, “nonbinding” meant what it said: the Rimov-Schultz arbitration was not binding.¹³

Last, the Rimov court concluded that the parties’ plain meaning of the arbitration clause governs whether or not a party agreed to arbitrate, and trumps public-policy considerations:

Although public policy strongly favors arbitration as a remedy for settling disputes, arbitration should not be invoked to resolve disputes that the parties have not agreed to arbitrate. [citations omitted] The parties cannot be compelled to arbitrate unless they have agreed to do so. [citation omitted] The presumptions referenced above do not overcome the plain meaning of the contract that a nonbinding procedure

¹² Id. at 466, 253 P.3d at 282

¹³ Id. at 466-67, 253 P.3d at 282-83

was chosen. No agreement to arbitrate was made.
(emphasis supplied)¹⁴

3. The Parties to the LBL Operating Agreement Knew the Difference Between Managers and Members for Non-Section 19 Parts of That Agreement.

The “claim between the Members” clause is a contract term found within a contract, which is the LBL operating agreement. The LBL operating agreement, as stated at paragraphs 1-8 of the Statement of the Case portion of this brief, recognizes that the non-Section 19 parts of that agreement recognize that:

1. Each Manager and Member is a party to that agreement,
2. Each Manager and Member is a distinct person or entity,
3. No Manager is a Member and no Member is a Manager,
4. A Manager owes management duties unlike a Member,
5. The parties provided for a Member Default section, but not for a Manager default section in the agreement.

Recognizing the distinctions that the parties made in their choice of language, to distinguish between Managers and Members as to their duties and their identity, and to create a Member Default section limited to Member disputes, the parties then created Section 19.

¹⁴ Id. at 468, 253 P.3d at 285

4. The Parties Did Not Include Disputes Against Managers As Part of the Member-Member Arbitration.

The parties created Section 19 to resolve disputes between the Members as stated at paragraphs 9-12 of the Statement of the Case portion of this brief. The word “Manager” never appears once in each of the four subsections of Section 19. Only a Member or Members are identified in each of those subsections. Only a Member or Members are the motive force or forces acting under that Section, be it for mediation, arbitration, procedures, or the hearing.

In sum, the choice of words at Section 19.2, that binding arbitration is for “Any claim between the Members”, means what it says. The plain meaning of “between” is “by the common action of: jointly engaging” or “in common to: shared by”.¹⁵ The only ones identified in a Section 19.2 arbitration involved “by the common action of jointly engaging” or “in common to: shared by” are Members.

In sum, a Section 19.2 arbitrable “claim between the Members” is for a claim between the Members and not between the Managers or between a Member and a Manager. This is true given the differentiation between Managers and Members throughout the agreement and given the Default section that applies only to

¹⁵ <http://www.merriam-webster.com/dictionary/between> (Definitions 1a & 1b)

Members. As the Conley plaintiffs' claims are against a Manager and his agent, these claims are properly before the trial court.

D. It Was Error For The Trial Court To Dismiss With Prejudice Because The Merits of The Dispute Were Not Adjudicated and The Arbitration Statute Mandates Only Stays, Not Dismissals.

The trial court dismissed the Conley plaintiffs' claims with prejudice and with its contemporaneous oral decision that the Conley plaintiffs' claims were subject to arbitration. (RP p.28, ll. 12-17; CP 280)

Because dismissal with prejudice represents an adjudication of a final judgment on the merits with the application of *res judicata*,¹⁶ then the trial court's entry of that order was in error. The trial court did not adjudicate the merits of the Conley plaintiffs' claims arising from the management-deadlock disputes. Instead, the trial court ruled that those claims were to be arbitrated.

Therefore, the trial court should have entered an order pursuant to RCW 7.04A.070(6) to stay, not dismiss, the pending case. That statutory subsection mandates a stay of truly arbitrable disputes and reads:

(6) If the court orders arbitration, the court shall on just terms stay any judicial proceeding that involves a claim subject to the arbitration. If a claim subject to arbitration is severable, the court may sever it and limit the stay to that claim.

¹⁶ Krikava v. Webber, 43 Wn. App. 217, 219, 716 P.2d 916, 918 (1986)

V. CONCLUSION

In conclusion, the Conley plaintiffs request that this Court reverse the trial court's decision finding that the Conley plaintiffs' claims are arbitrable, based upon the summary-judgment standard and proper stay order for review, and to remand to the trial court for further proceedings in this case.

RESPECTFULLY SUBMITTED this 23rd day of January, 2012.

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CERTIFICATE OF SERVICE

Erika Trask certifies under penalty of perjury under the laws of the State of Washington that I am over the age of 18 years, and competent to be a witness herein. On January 23, 2012, I served a true and correct copy of the following documents:

- 1) BRIEF OF APPELLANTS; and
- 2) VERBATIM REPORT OF PROCEEDINGS for hearing dated September 16, 2011

to the following attorneys of record via Hand Delivery:

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SIGNED at Seattle, Washington this ^{23rd} day of January, 2012.



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