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

RYAN AND WAGES, LLC, a Washington limited liability company,
through its members, JULIA MCCORD and THE CONJUNCTIONAL
PATRIOTIC SOVERIGN PATHWAY,

Appellant/Cross-Respondent,

v.

REDDING LAKE STEVENS, LLC, an Oregon limited liability company,

Respondent.

v.

TOM WAGES, an individual,

Respondent/Cross-Appellant.

RESPONDENT/CROSS-APPELLANT'S OPENING BRIEF

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**I. ASSIGNMENTS OF ERROR AND ISSUES PERTAINING
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A. Assignments of Error.

1. The trial court erred in precluding Tom Wages from introducing evidence at trial that the \$1,250,000.00 distribution from Redding Lake Stevens, LLC to Ryan and Wages, LLC was income, and should have been distributed to the members of Ryan and Wages, LLC in accordance with their membership interest.

2. In its Finding of Fact No. 13, the trial court erred in finding that Mr. Cunningham's calculation of Tom Wages capital account balance is supported by the evidence.

3. In its Finding of Fact No. 14, the trial court erred in finding that Mr. Cunningham's calculations and testimony regarding Ryan's capital account balance is supported by the evidence.

4. In its Finding of Fact No. 17, the trial court erred in finding that Julia McCord's, and the Conjunction Patriotic Sovereign Pathway capital contribution of the Lake Stevens Property to Ryan and Wages, LLC was valued at \$4,048,000.00.

5. In its Conclusion of Law No. 6, the trial court erred in its calculation of the members of Ryan and Wages, LLC capital account balances, and its distribution of the \$1,250,000.00 to Julia McCord and the Conjunction Patriotic Sovereign Pathway.

B. Issues Pertaining to Assignments of Error.

1. Whether the trial court erred in barring Wages from introducing evidence that the \$1,250,000.00 distribution from Redding Lake Stevens, LLC to Ryan and Wages, LLC was income, and should have been distributed to the members of Ryan and Wages, LLC in accordance with their membership interest.

2. Whether the trial court erred in its calculation of the members of Ryan and Wages, LLC capital account balances, and its application of the limited liability company statutes, and its interpretation of the LLC agreements.

II. STATEMENT OF THE CASE

A. Overview.

The trial court ordered the dissolution of Ryan & Wages, LLC and distributed its assets to members Tom Wages, Julia McCord, and Floyd Ryan (Julia McCord's brother and the sole owner of the Conjunctional Patriotic Sovereign Pathway). Wages' appeals the trial court's decision

awarding everything to Julia McCord and Floyd Ryan.¹

B. Ryan & Wages, LLC is formed.

Formed in October 2004, Ryan & Wages, LLC (“R&W”) originally had two members: Doris Ryan and Tom Wages (“Wages”). After Doris Ryan’s death, her interest in the company passed to her children, Julia McCord and Floyd Ryan (collectively “Ryan”). Wages had a 51% interest in R&W, compared to Ryan’s 49% interest in the company.²

Under the R&W Operating Agreement, Wages initially agreed to contribute \$211,000.00 to R&W, and Ryan initially agreed to contribute \$100,000.00 and vacant land located in Lake Stevens, Washington (“Lake Stevens Property”) to R&W. The R&W Operating Agreement does not set a value for the Lake Stevens Property.³

In December 2005, the members of R&W executed an Addendum to the R&W Operating Agreement (“R&W Addendum”). At the time, Wages had entered into a purchase and sale agreement for vacant land in California (“California Purchase Agreement”). Under the R&W Addendum, instead of contributing \$211,000.00 to R&W, Wages

¹ Ryan initiated the lawsuit alleging Wages misappropriated funds from Ryan & Wages, LLC. Wages filed a counterclaim to dissolve Ryan & Wages, LLC. The Court found that Wages did not misappropriate funds from Ryan & Wages, LLC.

² CP 12.

³ *Id.*

contributed his California Purchase Agreement. The R&W Addendum did not change Ryan's obligation to contribute \$100,000.00 and the Lake Stevens Property to R&W. The R&W Addendum does not include a value for the Lake Stevens Property.⁴

C. Redding Lake Stevens, LLC is formed.

In December 2005, R&W became a 50% member of Redding Lake Stevens, LLC ("Redding"). Redding is governed by the Operating Agreement of Redding Lake Stevens, LLC ("Redding Operating Agreement"). The Redding Operating Agreement establishes two classes of ownership interest in Redding. R&W owns 50 Class A Units in Redding, and CMDG Investments, LLC ("CMDG") owns 50 Class B units in Redding. The members of Redding are defined in the Redding Operating Agreement as R&W and CMDG (collectively "Redding Members").⁵

Redding was formed to build two assisted living facilities. The first facility was to be constructed in California.⁶ The second facility was to be constructed on the Lake Stevens Property.⁷ Therefore, the Redding

⁴ *Id.*

⁵ CP 12-13.

⁶ CP 145.

⁷ *Id.*

Operating Agreement required R&W's to contribute the California Purchase Agreement, and the Lake Stevens Property to Redding:

Ryan & Wages LLC shall contribute: (1) The Lake Stevens Real Property, which the Members deem for purposes of this Agreement to be valued at \$4,048,000 . . . [and] (2) An assignment of its rights under that certain Vacant Land Purchase Agreement between Thomas S. Wages Ent. Inc. (or assigns) as buyer and Edward and Judy Young as sellers dated on or about June 20, 2005, as amended (the "Redding Purchase Agreement"), which assignment the Members deem for the purposes of this Agreement to be valued at \$235,312 (which equals the difference between the Members' deemed value of the Redding Real Property (\$2,235,312) and the purchase price under the Redding Purchase Agreement (\$2,000,000)).⁸

The \$4,048,000.00 value the Redding Members assigned to the Lake Stevens Property was based on the assumption that Redding would construct a 176 unit assisted living facility on the Property, and that each unit would be worth \$23,000.00 ($\$23,000.00 \times 176 \text{ units} = \$4,048,000.00$).⁹ The Redding Operating Agreement also states that if less than 176 units were built on the Lake Stevens Property the value of R&W's contribution amount to Redding would be reduced by \$23,000.00 for each unit not constructed:

If the actual number of units of the Lake Stevens Facility is less than 176, the Contribution Amount shall be decreased by

⁸ CP 145-147.

⁹ CP 170.

\$23,000 multiplied by the difference between 176 and the actual number of units.¹⁰

For instance, under this provision, if 100 units were built on the Lake Stevens Property, the value of the Lake Stevens Property contribution to Redding would be \$2,300,000.00 instead of \$4,048,000.00. In exchange for its contributions to Redding, R&W was to receive a percentage of the rents from the facility constructed on the Lake Stevens Property.¹¹

D. First Amendment to the Redding Operating Agreement.

In February 2009, Redding determined that an assisted living facility could not be constructed on the Lake Stevens Property. Therefore, R&W and CMDG executed the First Amendment to the Operating Agreement of Redding Lake Stevens, LLC (“First Amendment”).¹²

Under the First Amendment, Redding’s distributions to R&W went from a percentage of the rents received from a facility on the Lake Stevens Property to a fixed amount each month. Specifically, the First Amendment required Redding to make guaranteed distributions to R&W of \$11,000.00 per month, which the members of R&W divided in accordance with their membership interest (51% to Wages, and 49% to

¹⁰ *Id.* (emphasis added.)

¹¹ CP 171.

¹² CP 175-179.

Ryan).¹³ The First Amendment provided that Redding could stop making the \$11,000.00 monthly payments at anytime by making a lump sum payment of \$1,250,000.00 to R&W.¹⁴ The First Amendment also modified the value of R&W's capital contribution to Redding by deleting the \$4,048,000.00 value for the Lake Stevens Property as well as the provisions related to the construction of the assisted living facility on the Property:

Certain assumptions contained in the [Redding] Operating Agreement are incorrect. As a result, the first sentence of Section 2.3(a)(1) of the [Redding] Operating Agreement is hereby deleted, as are Sections 2.5(b)(2) and 2.5(b)(3) of the [Redding] Operating Agreement.¹⁵

Section 2.3(a)(1) of the Redding Operating Agreement set the value of the Lake Stevens Property at \$4,048,000.00.¹⁶ Sections 2.5(b)(2) and 2.5(b)(3) concern the construction of the 176 unit assisted living facility on the Lake Stevens Property.¹⁷ Redding never constructed an assisted living facility on the Lake Stevens Property and it remains vacant.

¹³ CP 342.

¹⁴ CP 175.

¹⁵ CP 177.

¹⁶ CP 146.

¹⁷ CP 148.

E. Ryan's lawsuits against Wages.

Ryan filed two lawsuits against Wages. In March 2009, Ryan sued Wages alleging that he misappropriated funds from R&W. Ryan's claim went to arbitration in November 2009. One issue at arbitration was the amount of each member's capital contribution to R&W.¹⁸

The Arbitrator found that Wages contributed the California Purchase Agreement with a value of \$235,312.00 to R&W, and that Ryan contributed \$100,000.00 and the Lake Stevens Property to R&W.¹⁹ However, the Arbitrator did not enter any findings as to the value of the Lake Stevens Property.²⁰

In December 2009, Ryan sued Wages a second time alleging again that he misappropriated funds from R&W.²¹ Wages denied the allegation and filed a motion for summary judgment asking the trial court to bar Ryan's claims under the doctrines of *res judicata* and *collateral estoppel*.²² The trial court granted Wages' motion in part, holding that the

¹⁸ CP 1101-1105.

¹⁹ CP 1103.

²⁰ CP 1101-1105.

²¹ CP 471.

²² CP 616.

parties were bound by the Arbitrator's decision.²³ However, the trial court allowed Ryan to pursue their claim that Wages' misappropriated funds after arbitration.²⁴ Wages answered Ryan's complaint and filed a counterclaim to dissolve R&W.²⁵

F. Redding distributes \$1,250,000.00 to R&W.

Beginning in February 2009, when the First Amendment was executed, R&W started receiving \$11,000.00 a month from Redding. Wages and Ryan divided the \$11,000.00 monthly distributions in accordance with their membership interest in R&W (51% to Wages, and 49% to Ryan).²⁶ In December 2010, Redding made the \$1,250,000.00 distribution to R&W, which stopped the \$11,000.00 monthly distributions.²⁷

²³ CP 294-295.

²⁴ The trial court found that Wages did not misappropriate funds from R&W. CP 11-20.

²⁵ CP 466-470.

²⁶ CP 1104. Ryan's first misappropriation claim went to arbitration. The Arbitrator found that Wages withdrew \$51,066.82 from R&W that should have gone to Ryan. Wages withdrew the funds contending he was entitled to a management fee. The Arbitrator found that the funds may have been deserved and earned, but they were not withdrawn in accordance with the R&W Operating Agreement. Wages was ordered to repay Ryan the funds from his portion of the \$11,000.00 monthly distributions, which he did.

²⁷ CP 1128-1137.

At the time Redding made the \$1,250,000.00 distribution, the members of R&W were a year into their second lawsuit over the operations of the company.²⁸ Nonetheless, Wages expected the \$1,250,000.00 would be distributed to the members of R&W in accordance with their membership interest. However, Ryan claimed the \$1,250,000.00 was a return of R&W's capital contribution to Redding, and that they were entitled to the entire amount because their capital account balance was over \$3,000,000.00, and Wages capital account balance was negative. Based on these arguments, Ryan filed a motion requesting that the trial court distribute the entire \$1,250,000.00 to them.²⁹

Wages opposed Ryan's motion because the \$1,250,000.00 was not a return of capital.³⁰ The \$1,250,000.00 was income, and should have been distributed to the members of R&W's in the same manner as the \$11,000.00 monthly distribution.³¹ Wages also objected to Ryan's calculation of the members' capital account balances and in particular that

²⁸ The funds were placed in Ryan's attorney's trust account.

²⁹ *Id.* Ryan contributed the Lake Stevens Property R&W which contributed the Property to Redding.

³⁰ CP 1113-1124; CP 1059-1112; RP Vol. 1, 8:7-19:19.

³¹ *Id.*

Ryan's capital account balance was over \$3,000,000.00.³² Ryan based their calculation on the incorrect \$4,048,000.00 value initially assigned to the Lake Stevens Property. The trial court denied Ryan's motion to distribute the funds, and ordered that the "\$1,250,000 shall remain in [Ryan's counsel's] trust account pending trial or arbitration in this matter."³³

Shortly after filing their first motion to release the funds, Ryan filed a second motion asking the trial court to release 49% of the \$1,250,000.00 to them, which represented their interest in R&W.³⁴ Wages did not object to Ryan's request as long as he received the remaining 51% of the \$1,250,000.00, which represented his interest in R&W. Ryan opposed any distribution to Wages, so the trial court denied Ryan's second motion to release the funds, and ordered that the "\$1,250,000.00 shall remain in the [Ryan's counsel's] trust account pending trial."³⁵

Just before trial, Ryan filed a third motion asking the trial court to distribute 10% of the \$1,250,000.00 to them in order to pay their

³² *Id.*

³³ CP 1038-1039.

³⁴ CP 1032-1037.

³⁵ CP 912-913.

attorneys' fees.³⁶ Ryan departed from their argument that the funds were a return of capital, and argued instead that the funds were "profit" and should be distributed in accordance with section 3.9 of the R&W Operating Agreement, which states, in part:

Distributions to the Members of net operating profits of the Company shall be made at least annually except that earnings may be retained by the Company and transferred to Company capital for the reasonable needs of the business.³⁷

The trial court denied Ryan's third motion to release the funds and the parties proceeded to trial.³⁸

G. Ryan's motion in limine to exclude evidence that the \$1,250,000.00 was income and should be distributed in accordance with the members' membership interest in R&W.

Wages hired expert witness Richard Toyer ("Toyer"), a certified public account, to testify at trial that the \$1,250,000.00 was income to R&W, and that it should have been distributed to the members of R&W in accordance with their membership interest. Ryan filed a motion in limine to exclude Toyer's testimony.³⁹ Ryan argued that the \$1,250,000.00 was an asset of R&W, and regardless of its character, could only be distributed

³⁶ CP 1003-1008.

³⁷ *Id.*; CP 696.

³⁸ CP 912-913.

³⁹ CP 896-911.

to the members in accordance with their capital account balances upon dissolution.⁴⁰ The trial court granted Ryan's motion, and barred Toyer's testimony regarding the character of the funds.⁴¹

Following a bench trial, the court ordered the dissolution of R&W, and relying on the incorrect \$4,048,000.00 value initially assigned to the Lake Stevens Property, awarded Ryan the entire \$1,250,000.00 upon dissolution. The trial court also awarded R&W's 50% interest in Redding to Ryan.

III. LEGAL ARGUMENT

A. **The trial court abused its discretion in excluding evidence that the \$1,250,000.00 distribution to R&W was income.**

"The meaning of a statute is a question of law reviewed de novo."⁴² Wages' filed a counterclaim to dissolve R&W under RCW 25.15 *et. al.* Therefore, this Court's review of the trial court's decision to exclude evidence regarding the character of the \$1,250,000.00 is reviewed *de novo*. The trial court should have considered Toyer's testimony regarding the character of the \$1,250,000.00 because the LLC statutes require

⁴⁰ *Id.*, RP Vol. 1, 8:7-19:19.

⁴¹ RP Vol. 1, 8:7-19:19.

⁴² *Dep't of Ecology v. Campbell & Gwinn, L.L.C.*, 146 Wn.2d 1, 9, 43 P.3d 4 (2002)

distributions of income to the members as part of the dissolution process.⁴³

Under the R&W Operating Agreement “[d]istributions to the Members of net operating profits of the Company shall be made at least annually. . .”⁴⁴ Under RCW 25.15.215, a member who was entitled to receive a distribution prior to the dissolution of the company shall receive that distribution as part of the dissolution process:

Interim Distributions. Except as provided in this article, to the extent and at the times or upon the happening of the events specified in a limited liability company agreement, a member is entitled to receive from a limited liability company distributions before the member’s dissociation from the limited liability company and before the dissolution and winding up thereof.⁴⁵

Under RCW 25.15.230, a member entitled to a distribution is treated as a creditor of the company:

Subject to RCW 25.15.235 and 25.15.300, and unless otherwise provided in a limited liability company agreement, at the time a member becomes entitled to receive a distribution, he or she has the status of, and is entitled to all remedies available to, a creditor of a limited liability company with respect to the distribution. A limited liability company agreement may provide for the establishment of a record date with respect to allocations and distributions by a limited liability company.⁴⁶

⁴³ *Medcalf v. Dep't of Licensing*, 83 Wn. App. 8, 11, 920 P.2d 228 (1996) (Holding the trial court must admit relevant evidence that tends to make the existence of a material fact more or less probable.)

⁴⁴ CP 342.

⁴⁵ RCW 25.15.215.

⁴⁶ RCW 25.15.230 (emphasis added).

Wages repeated contention throughout the case, and what he intended to present at trial, was that he was entitled to 51% of the \$1,250,000.00 at the time Redding distributed the funds in December 2010. It was only held in Ryan's attorney's trust account because Ryan claimed they were entitled to the entire amount. Under RCW 25.15.215, the trial court was required to make "interim distributions" to the members, which the members were "entitled to receive from a limited liability company . . . before the dissolution and winding up thereof." By excluding Wages' evidence as to the character of the funds, the trial court ignored the requirements of the LLC statutes, and deprived Wages of his right to present evidence that he was entitled to 51% of the \$1,250,000.00 as an interim distribution from R&W.⁴⁷

Ryan also argued in their motion in limine that evidence regarding the character of the \$1,250,000.00 should be excluded because Wages did not ask for a distribution of income as part of his counterclaim.⁴⁸ Wages' counterclaim was based on RCW 25.15 *et. al.*, which provides for the distribution of income as part of the dissolution process. Therefore,

⁴⁷ In addition, the R&W Operating Agreement specifically provides that upon the winding up and dissolution of the company distributions shall be made to members in respect to their share of profits.

⁴⁸ CP 899.

contrary to Ryan's claim, Wages' counterclaim included a request to distribute income to the members of R&W. Nonetheless, the parties litigated the character of the funds for over a year prior to trial, which clearly provided Ryan notice of Wages' claim that the funds were income.

Redding distributed the \$1,250,000.00 in December 2010, a year after Ryan filed their complaint and a year prior to trial date. When Ryan refused to distributed 51% of the funds to Wages, both parties retained expert witnesses who offered opinions as to the character of the funds and how they should be distributed. The parties' claims, defenses and the issues for trial had been briefed, argued, and litigated for over a year prior to trial. The trial court's order barring Wages' from presenting evidence as the character of the funds was contrary to Washington law that pleadings are to be liberally construed, and may be clarified in subsequent hearings:

It is well established that pleadings are to be liberally construed; their purpose is to facilitate proper decision on the merits, not to erect formal and burdensome impediments to the litigation process. If a complaint states facts entitling the plaintiff to some relief, it is immaterial by what name the action is called. Furthermore, initial pleadings which may be unclear may be clarified during the course of summary judgment proceedings.⁴⁹

The trial court abused its discretion by excluding evidence as to the

⁴⁹ *State v. Adams*, 107 Wn.2d 611, 620, 732 P.2d 149 (1987).

character of the funds.

B. The trial court erred in its calculation of the members' capital account balances.

In its Finding of Fact No. 17, the trial court valued Ryan's capital contribution to R&W at \$4,048,000.00:

The Court finds that Ryan contributed the Lake Stevens Property to R&W, which R&W subsequently contributed to Redding. Under the Redding Operating Agreement, R&W and CMDG initially deemed the value of the Lake Stevens Property at \$4,048,000. At the same time, Mr. Wages' option to purchase was valued at \$235.312. It does not make sense to the Court to value Mr. Wages' contribution at one point in time and Ryan's contribution at a different point in time. Therefore, the Court will value both contributions at the time the members agreed on the values, even though there was some evidence presented that Mr. Wages subsequently agreed to lower the value of the Lake Stevens property. The Court will value both contributions as of the time they were valued by the members of R&W and contributed to Redding. Based upon Exhibit 28, and the evidence above, the Court finds Ryan's capital account balance to be \$3,314,802.07.⁵⁰

In reaching its decision, the trial court relied on Section 2.3(a)(1) of the Redding Operating Agreement, which states that R&W shall contribute, "[t]he Lake Stevens Property, which the Members deem for the purposes of this Agreement to be valued at \$4,048,000."⁵¹ However, the trial court ignored a subsequent provision in the Redding Operating

⁵⁰ CP 539. The calculation of \$3,314,802.07 was arrived at after deducting distributions to Ryan when R&W was formed.

⁵¹ CP 722.

Agreement that requires an adjustment to the \$4,048,000.00 value under certain circumstances:

If the actual number of units on the Lake Stevens Facility is less than 176, the Contribution Amount shall be decreased by \$23,000 multiplied by the difference between 176 and the actual number of units.⁵²

The \$4,048,000.00 value for the Lake Stevens Property was based on the possible construction of a 176 unit assisted living facility on the Lake Stevens Property with a per unit value of \$23,000.00. If fewer than 176 units were built on the Lake Stevens Property, then the \$4,048,000.00 value would be adjusted down by \$23,000.00 per unit. Because there were no units constructed on the Lake Stevens Property, its value under the Redding Operating Agreement was zero. The trial court erred in applying Section 2.3(a)(1) of the Redding Operating Agreement, but not applying Section 2.5(b)(2) and 2.5(b)(3) of the same agreement.

Once the Redding Members determined that an assisted living facility could not be constructed on the Lake Stevens Property, they executed the First Amendment to the Redding Operating Agreement. Under the First Amendment, the \$4,048,000.00 value is deleted and the provisions related to the construction of the 176 unit assisted living facility

⁵² CP 746.

on the Property are also deleted.⁵³ The First Amendment does not set a new value for the Lake Stevens Property, and there was never an agreement between the members of R&W as to the value of the Lake Stevens Property. Therefore, the trial court erred in finding that Ryan's capital contribution to R&W was \$4,048,000.00, and then distributing the entire \$1,250,000.00 to Ryan based on that finding.

C. The trial court erred in finding that Wages had a negative capital account balance.

In its Finding of Fact No. 12, the trial court found that Wages withdrew "\$100,000 on December 30, 2005 as part of the Redding real estate closing" and that his capital account balance was negative \$39,215.31.⁵⁴ However, the \$100,000.00 paid to Wages was a return of his earnest money deposit, which was used to secure the purchase of the California property. Under the Redding Operating Agreement, Wages was to "receive a return of his \$100,000.00 earnest money deposit."⁵⁵ The trial court failed to credit Wages with depositing the \$100,000.00, and treated it solely as a distribution to Wages from his capital account. As a

⁵³ CP 423.

⁵⁴ CP 14.

⁵⁵ CP 154.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on June 7th, 2012, a copy of the foregoing **Respondent/Cross-Appellant's Opening Brief** was delivered at the following address via the methods indicated:

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Karrie Kelly