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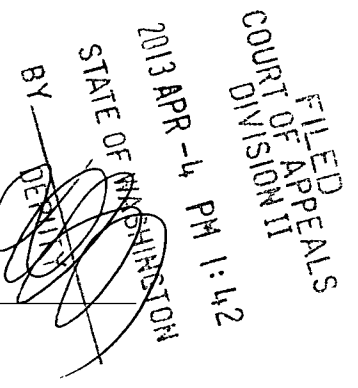

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION II

NORTHWEST CASCADE, INC.,

Appellant,

v.

UNIQUE CONSTRUCTION INC; TEMPORAL FUNDING, LLC; WILLIAM REHE; JANE DOE REHE; WILLIAM K AND MARION L LLLP; and SAHARA ENTERPRISES, LLC,

Respondents,

REPLY BRIEF OF APPELLANT/CROSS RESPONDENT NORTHWEST CASCADE, INC.

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ORIGINAL

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I. INTRODUCTION

No plaintiff is automatically entitled to a solvent defendant, but a defendant is not entitled to render itself incapable of paying a judgment by diverting its limited cash to insiders and by transferring the corporation's other assets to its shareholders for no consideration. The trial court made two fundamental errors: (1) it failed to apply the proper standards for corporate disregard by refusing to consider undisputed evidence that the Rehes gutted the corporation, and (2) it failed to segregate the Rehes' fees in connection with the corporate disregard claim.[1]

The Rehes purport to address the first error by claiming it did not happen, despite the trial court's unequivocal statements that the transfer of the 38th Avenue Lot was not before it and would not be considered. With respect to the attorney fees award, the Rehes simply ignore the lack of segregation, suggesting instead (contrary to controlling case law) that the trial court's "discretion" allows it to award a successful defendant with fees actually expended upon the unsuccessful defense of different claims by different defendants merely because the same attorney also represented the losing defendants. Setting aside the irony that this position is inconsistent with the Rehes' own defense to the corporate disregard claim,

[1] This Court need not address the fee issue as presented here if it reverses the trial court on the issue of corporate disregard. The fee award to the Rehes would simply need to be vacated as the Rehes would no longer have prevailed on that issue.

the Rehes' position is completely contrary to controlling case law and defies logic, effectively rewarding the Rehes for co-defendants Unique and Sahara Enterprises, LLC having lost on issues that consumed nearly 90% of the trial.

In their Statement of the Case at pages 5 through 8, the Rehes imply that the jury verdicts on the breach of contract and UFTA claims were wrongly decided. However, they have not appealed the jury verdict. They did not because it was supported by substantial evidence and untainted by any error in law. The Rehes nevertheless imply that they were treated unfairly by the jury, and do so in a transparent attempt to persuade this Court to disregard the trial court's errors relating to the corporate disregard claim. But the jury verdict is a verity on appeal: Unique owed NWC nearly $150,000 plus interest, and instead of paying, the Rehes transferred real property out of the corporation with actual intent to hinder, delay and defraud Unique's creditors, leaving Unique insolvent. CP 407-409.

The Rehes' cross-appeal on NWC's award of fees is devoid of substance, and amounts to nothing more than a complaint that NWC was awarded too much money. The Rehes conveniently ignore their own extensive record of deception, obstruction, delay, and refusal to comply with discovery requests and court orders that directly increased NWC's

fees and costs. NWC does not disagree with the definition of "chutzpah" cited by the Rehes (*Response* at 37), but it does disagree with the Rehes' application of it to this case: after engaging in virtually every kind of misconduct known in litigation, the Rehes now have the audacity to complain that NWC spent too much to uncover their deceit. ***That*** is chutzpah.

II. ARGUMENT ON REPLY

A. The trial court erred by failing to employ the proper legal standards in assessing NWC's cause of action for corporate disregard.

The Rehes suggest that the trial court's ruling on veil-piercing is reviewed solely for substantial evidence. *Response* at 22. This is not accurate. The standard is clear: the appellate court reviews facts underlying a trial court's decision on corporate disregard for substantial evidence, and it reviews *de novo* the legal conclusions that support corporate disregard. *Rogerson Hiller Corp. v. Port of Port Angeles*, 96 Wn. App. 918, 924, 982 P.2d 131 (1999).

The Rehes argue, without citation to any authority, that if the Court of Appeals upholds any one of five so-called "independent reasons," it must affirm the trial court's ruling. *Response* at 23. That is erroneous: if, as NWC argues, the trial court used an improper legal standard in its consideration of the evidence, and that improper standard caused it to

disregard undisputed evidence of the Rehes' corporate gutting, then this Court must reverse. Moreover, the proper benchmark for review of this case is not a random set of "reasons" that the Rehes cobbled together, but the elements of corporate disregard as set forth by Washington case law.

As set forth in NWC's *Opening Brief* at page 16, two elements are required to establish corporate disregard. First, a plaintiff must establish that the shareholder intentionally used the corporate form to evade a duty owed to a corporate creditor. Second, a plaintiff must show that this use of the corporate form caused an unjustified loss. *Morgan v. Burks*, 93 Wn.2d 580, 585, 611 P.2d 751 (1980); *Meisel v. M & N Modern Hydraulic Press Co.*, 97 Wn.2d 403, 410, 645 P.2d 689 (1982). The Rehes don't dispute these elements. Both of these elements are further refined by case law, as is discussed below.

1. The trial court erred in finding that the Rehes did not intentionally use Unique's corporate form to evade a duty owed to NWC.

As NWC explained in its *Opening Brief* at 18-30, there were two ways in which the Rehes intentionally used Unique's corporate form to evade a duty: the first was by gutting Unique of the 38th Avenue Lot, and the second was by diverting funds and assets from Unique for the Rehes' personal benefit at a time when the corporation had no cash assets and was

not paying its bills. The trial court erred in its application of the law to that evidence.

a. The trial court erred by disregarding the gutting of Unique Construction, Inc.

Bill Rehe's gutting of Unique, by transferring the 38th Avenue Lot to a Rehe-owned shell company seven months after NWC filed suit, independently justifies corporate disregard under the standard set forth in *Morgan*, 93 Wn.2d at 585.[2] The trial court's error was not that it refused to admit evidence – the evidence was admitted. The trial court's error was in ***expressly refusing to consider this evidence in connection with the corporate disregard claim***, asserting (incorrectly) that it was not asked to consider that evidence, and justifying its refusal to consider the evidence on the fact that NWC had not brought an UFTA case against transferee Winnemucca Ventures, LLC. CP 978-992; RP 4/27/12 at 10-12; RP 7/27/12 at 6-11.

The record is clear that NWC specifically asked the trial court to consider the transfer of the 38th Avenue Lot in evaluating the corporate disregard claim – in the trial brief (CP 340), in closing argument (RP

[2] Mr. Rehe subsequently lied about the transfer at his deposition, refused to provide discovery (even after being ordered to do so by the trial court), and then re-transferred the property to a Nevada shell LLC with undisclosed members. CP 735, 772-773; Ex. 269; Ex. 270; RP 3/15/12 at 123-125. Bill Rehe managed to confuse and deceive NWC long enough that NWC was unaware of the fraudulent nature of the transfer of the 38th Avenue Lot until several months before the repeatedly-delayed trial. CP 335.

3/26/12 47-48), and in a direct colloquy with the trial court (CP 984; RP 4/27/12 at 10-12). The record is equally clear that the trial court refused to do so. CP 978-992; RP 4/27/12 at 10-12; RP 7/27/12 at 6-11.

The Rehes' defense of the trial court's refusal to consider the transfer of the 38th Street Lot is predicated on the argument that a claim for corporate disregard is not available if there is a potential remedy based on fraudulent transfer. *Response* at 30 (under circumstances where shareholders "gut" a corporation, "[t]he remedy is to avoid the transfer.") The Rehes also expressly point out that the trial court's decision was based upon its opinion "that the entity holding 38th Avenue was not before the court and ***no remedy had properly been requested vis-a-vis the 38th Avenue Property***." *Response* at 2 (emphasis added). Consistent with that theme, the Rehes claim that NWC is "trying to incorrectly combine two separate legal concepts" – corporate disregard and fraudulent transfer. *Response* at 29. But the Rehes (and the trial court) are wrong, and the Washington Supreme Court has already ***explicitly rejected*** this argument in *Morgan v. Burks*.

Morgan, *supra*, was addressed extensively in NWC's *Opening Brief*, at 22-24. In *Morgan*, shareholders stripped the company of its assets after the president shot the plaintiff. The trial court refused to consider evidence of post-tort asset-stripping in assessing the plaintiff's

request for corporate disregard. In support of this decision, the defendants argued

> that post-tort wrongful activities should always be dealt with by voiding transfers...[and that] the remedy for wrongful transfers [is limited] to avoidance of the transactions.

Morgan, 93 Wn.2d at 584. The Washington Supreme Court disagreed, citing with approval a case that held:

> Equity has full power to grant relief. Ignoring the corporate entity, the court below went to the heart of the matter and did justice by granting a decree against the (otherwise not-liable defendant).... Preserving the fiction of separate legal entities, it might have accomplished the same thing by setting aside the fraudulent transfer of assets.... As the same result and the right result was reached in the direct method followed by the court below, no one may complain.

Morgan, 93 Wn.2d at 588-89 (alterations in original) (*quoting Texas Co. v. Roos*, 93 F.2d 380, 383 (5th Cir. 1937)).[3] NWC was entitled under Washington law to seek relief through an action against the Rehes on corporate disregard, particularly in light of the Rehe's active concealment of the transfers. *See* Note 2, *supra*. The trial court and the Rehes are wrong to conclude that an UFTA claim against Winnemucca Ventures was

[3] The *Morgan* court ultimately affirmed the trial court's decision for a different reason: because the bankruptcy court had already reversed the fraudulent transfers. The court held "[a]ny disregard of the corporate entity ***now*** would subject to judgment ***no funds intended to be corporate***, but only those purely individual assets of defendants." *Morgan*, 93 Wn.2d at 588 (emphasis added). Here, while the fraudulent 89th Street transfer has been reversed, the 38th Avenue Lot transfer has not, and there has been no remedy for the cash improperly diverted to the Rehes. The Rehes are still in possession

the *only* remedy Washington courts provide. The transfer of the 38th Avenue Lot was also highly relevant in the action against Rehes on corporate disregard. The trial court erred in concluding it could not be considered.

After first conceding that the trial court disregarded the transfer of the 38th Avenue lot on the belief that the issue was not properly before it, the Rehes paradoxically claim that the trial court ***did not ignore*** the 38th Avenue Lot transfer. *Response* at 10-11 and 35. The Rehes note that the trial court admitted evidence relating to the transfer and discussed it at length on the record. *Id.* The problem with the Rehes' argument is that all the discussions of the transfer on the record related to the legal question of ***whether the evidence was relevant to the issue of corporate disregard.*** CP 975-992; RP 4/27/12 at 10-12; RP 7/27/12 at 6-12. The trial court reached the wrong legal conclusion by refusing to either consider the 38th Avenue Lot transfer or make appropriate findings about that transfer.[4]

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of assets "intended to be corporate," and NWC is entitled to pursue relief through a request for corporate disregard.

[4] The trial court also wrongly suggested that the "factual question" of the transfer of the 38th Avenue Lot was the province of the jury, and that the trial court's only role in a determination on corporate disregard was in addressing strictly legal questions. RP 7/27/12 at 6-12. However, as noted above, a trial court's determination on corporate disregard is a mixed question of fact and law. Neither NWC nor the Rehes ever represented to the trial court that it would not be addressing issues of fact in its determination on corporate disregard. In fact, it was the ***Rehes*** who requested that the corporate disregard claim be tried to the court, because it is an equitable remedy proper for determination by a trial court rather than a jury. CP 363. The trial court had no problem making numerous Findings of Fact on the issue of corporate disregard, and its

Moreover, the Rehes ***expressly asked*** the trial court to disregard the evidence of the 38th Avenue Lot, and the trial court ***expressly agreed***. CP 989-991. The Rehes cannot argue that the trial court "considered" evidence of the 38th Avenue Lot transfer when they themselves successfully convinced the court to disregard that very transfer.

The Rehes also suggest that the trial court was not ***required*** to consider evidence of asset-stripping, but was merely ***permitted*** to do so. *Response* at 34. This argument deliberately misconstrues the language in *Morgan v. Burks*. The Rehes quote this passage from *Morgan*: "Thus, the Court of Appeals was correct in holding that post-tort activities ***could be considered*** in making the determination whether to disregard the corporate entity." *Morgan*, 93 Wn.2d at 585 (emphasis added). The Rehes ignore the clear meaning of that statement in the context of the immediately preceding sentence, which states

> In the latter case [of corporate "gutting"] particularly, post-tort activities ***must be considered***, and often will ***independently support disregard*** of the corporate entity, because it is only after the tort that the impetus to "gut" the corporation arises.

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statement that factual findings were the province of the jury finds no basis in the record or the law. It does, however, further confirm that trial court did not apply the proper standards in evaluating the corporate disregard claim.

Id. (emphasis added).[5] But regardless of whether consideration of corporate gutting "must" be considered, or merely "could" be considered, the Rehes argued to the trial court that the corporate gutting ***could not be considered*** because the Rehes' Nevada shell transferee was not a party to the litigation. CP 989-991. The trial court ***agreed*** that the transfer of the 38th Avenue Lot ***could not be considered.*** CP 989-990; RP 7/27/12 at 9-11. This is an error of law, even under the Rehes' incorrect interpretation of *Morgan v. Burks*.

The Rehes also imply that they were somehow entitled to transfer the 38th Avenue Lot to their "Real Estate Privacy Trust" because they had made an unrecorded "shareholder loan" or a "capital contribution" in order for Unique to acquire the property in the first place. *Response* at 8, 28. First, the trial court never made a finding that the Rehes were entitled to transfer the 38th Avenue Lot, and in fact found that "[t]here were no documents reflecting any shareholder loans to Unique, and no such loans were reflected on the Rehe tax returns." FOF 18 and 32.[6] The Rehes assign no error to these Findings.

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[5] The Rehes offer no argument or case law to explain why their post-litigation stripping of the 38th Avenue Lot does not similarly justify piercing the corporate veil.

[6] The Rehes also argued throughout the jury portion of the trial that the transfers of both the 38th Avenue and 89th Street properties were in repayment of "shareholder loans" pursuant to Jury Instruction 24 at CP 1282, but the jury rejected this defense, along with the Rehes' self-serving claims of a shareholder loan.

Second, even if the Rehes were the original source of the capital used by Unique to purchase the 38th Avenue Lot, the Rehes were not entitled to later strip the asset back out of corporation to the detriment of the corporate creditors. RCW 23B.06.400(2); RP 3/21/12 at 6-10. The Rehes failed to introduce any expert testimony or legal authority to suggest that they were allowed to distribute assets to themselves for no consideration under such circumstances. In fact, a shareholder's attempt to deal himself corporate assets during the pendency of a lawsuit is exactly the kind of "extraordinary circumstance" that the doctrine of corporate disregard is intended to rectify. *Morgan*, 93 Wn.2d at 584-89.

The Rehes' main complaint appears to be asking why NWC didn't pursue an UFTA claim against the Rehes' Nevada shell company, Winnemucca Ventures. *Response* at 30. The reason is clear: Bill Rehe repeatedly hid and lied about the transfer, refused to provide discovery or interrogatory responses about the transfer (even after the Court ordered him to do so), and obscured ownership of the property by deeding it to a Nevada shell LLC that had no publicly disclosed members. CP 735, 772-773; Ex. 269; Ex. 270; RP 3/15/12 at 123-125; see also *Appellant's Brief* at 7-8, 24.[7] Bill Rehe did everything he could to obscure the fact that he stripped the corporation of the 38th Avenue Lot, and he almost

succeeded.[8] Mr. Rehe cannot use his own deceit as a reason to preclude a form of relief expressly afforded by controlling case law. If the Rehes had wanted NWC to bring an action under the UFTA, they should not have gone to such lengths to hide the facts surrounding that transfer.[9]

In short, Washington law allows NWC to seek a remedy for the "gutting" of corporate assets either through an action on corporate disregard or through an action under the Uniform Fraudulent Transfer Act. The trial court committed clear legal error when it held that the gutting of the 38th Avenue Lot would not be considered as part of the corporate disregard claim and was not properly before it. The Court of Appeals should reverse the trial court's determination regarding the corporate

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[7] The Rehes do not even attempt to rebut these facts.

[8] NWC had received permission in May, 2011 to add Sahara Enterprises, transferee of the 89th St. Property, for a projected December, 2011 trial date. CP 1357-1359. However, NWC did not learn that the 38th Avenue lot had been similarly transferred to a different out-of-state Rehe-owned shell company until late summer, 2012. CP 335. Petitioning the Court for leave to amend and then serving that entity would have necessitated a further delay in the trial date, which had already been continued 7 times and for over 36 months. NWC had already asserted a claim for corporate disregard against the Rehes. It was entitled to have this new and critical evidence considered as part of that claim.

[9] In their *Response*, at page 2, Note 1, the Rehes note that NWC filed a separate UFTA lawsuit after the trial court decision to recover the 38th Avenue Lot. The Rehes suggest that this means that NWC agrees with the trial court ruling. Consistent with *Morgan*, that lawsuit was filed to preserve the UFTA claim as an alternative or additional remedy in the event the trial court decision on corporate disregard is upheld and/or a future judgment against the Rehes does not end up affording full relief to NWC. In addition, reversal of the trial court's erroneous decision on the corporate disregard claim is necessary in order to vacate the associated fee award to the Rehes.

disregard, and remand with instructions to consider the evidence of corporate gutting presented by NWC.[10]

b. The trial court erred in finding that the Rehes' blatant diversion of corporate funds was not the "intentional use of corporate form to a stockholder's benefit and a creditor's detriment."

The evidence of corporate "gutting" ignored by the trial court can "***independently support disregard*** of the corporate entity" *Morgan*, 93 Wn.2d at 585 (emphasis added), and justifies reversal in this case. However, the trial court also erred by misapplying the legal standard for finding "intentional use of the corporate form to violate or evade a duty."

To prove "intentional use of the corporate form to violate or evade a duty," a plaintiff need not prove direct evidence of intent, but need only prove "some form of manipulation of the corporation to the stockholder's benefit and creditor's detriment." *Meisel*, 97 Wn.2d at 410 (quoting *Truckweld*). Evidence of such manipulation includes, *inter alia*:

> Commingling of funds and other assets, failure to segregate funds of the separate entities, and the ***unauthorized diversion of corporate funds or assets to other than corporate uses***; the treatment by an individual of the assets of the corporation ***as his own***;

[10] In the alternative, the unrebutted evidence of the transfer combined with the trial court's other uncontested findings of fact (see FOF 29, 31 and 32) is so stark that this Court can render a determination on the issue of corporate disregard itself, and avoid the necessity of a retrial on this issue.

Thomas V. Harris, *Washington's Doctrine of Corporate Disregard*, 56 Wash.L.Rev. 253, 260 n.38 (1981) (emphasis added) (*cited by Meisel*, 97 Wn.2d at 410).

NWC provided ample evidence of the Rehes' manipulation of the corporation to their own benefit, and to NWC's detriment. As even the trial court found, Mr. Rehe cashed corporate checks made out to "CASH", paid personal expenses with corporate checks, paid ***personal credit card expenses*** with corporate checks, lived in a corporate-owned house for years without paying rent, "treated his corporate and personal assets as one and the same," and commingled his assets and liabilities with those of Unique. FOF 29, 31 and 32. The Rehes do not challenge these findings, and they are verities on appeal.

The trial court erred, however, in finding that this corporate manipulation was "not designed to defraud, manipulate or misrepresent the corporate status" and was "not done fraudulently or with the intent to defraud." COL 5, CP 1026. As discussed above, the trial court improperly applied the "intent" standard in *Meisel* when it ignored its own findings of corporate manipulation and attempted to determine intent separately. The trial court's failure to even properly cite the standards in *Meisel* ("fraud, misrepresentation, ***or some form of manipulation of the corporation to the stockholder's benefit and creditor's detriment.***"

Meisel, 97 Wn.2d at 410), combined with the trial court's undue emphasis on an "intent to defraud" (COL 5; CP 1026), confirms that the trial court was confused regarding the requisite intent standard. The trial court improperly ignored the fact that direct proof of intent is almost never possible.[11]

In addition to the trial court's legal error, the trial court's finding that the Rehes' corporate abuses were not designed to violate or evade a duty is not supported by substantial evidence. In fact, the only evidence supporting that finding is Mr. Rehe's self-serving testimony of his own subjective intent. In contrast, NWC provided extensive evidence of Mr. Rehe's "manipulation of the corporation to the stockholder's benefit and creditor's detriment." *Meisel*, 97 Wn.2d at 410. The trial court specifically found that these abuses occurred, FOF 29 and 32, yet ignored the legal consequence of those specific findings. There is no substantial evidence in support of the trial court's further finding that Mr. Rehe lacked the intent to violate or evade a duty.

The Rehes claim that "Bill Rehe's accounting practices were not designed to intentionally evade a duty to a creditor." *Response* at 23.

[11] "A fraudulent intent is seldom confessed or blazoned upon a banner. In most cases it can only be proved by circumstantial evidence." *Allen v. Kane*, 79 Wash. 248, 255-56, 140 P. 534 (1914). As the *Allen* Court went on to explain, "there is no circumstance more persuasive and more often recognized by the courts as convincing than the fact that

First, the issue was not "accounting practices" but the actual diversion of assets from the Corporation to Rehes. The evidence plainly established that the Rehes diverted, over time, more than $80,000 in cash (Ex. 273; RP 3/15/12 at 230-243), cash receipts the corporation should have received from rent worth nearly $100,000 over a four year period (Ex. 273; RP 3/15/12 at 244-248), and over $600,000 in real property assets into their own pockets (Exs. 89, 92, 121) while their company was illiquid and floundering.[12] *See* Note 15, *infra*. Mischaracterizing this as nothing more than an "accounting practice" is legally incorrect and factually unsupportable given the trial court's unequivocal findings of corporate abuse. FOF 29, 31 and 32.

Second, the Rehes' argument misstates the "intent" requirement. NWC must show that the "use of the corporate form" was ***intentional***, not that it was specifically intended to violate a duty. For example, if the Rehes ***unintentionally*** paid some personal expenses with corporate funds (as a result of reaching for the wrong check book, for example), such unintentional acts would not ground an action for corporate disregard. However, where the shareholders intentionally and repeatedly pay

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a debtor, on the eve of a suit against him, transfers all of his property to another, thus placing it beyond the reach of execution." *Id.*

[12] In their *Response*, the Rehes also do not deny that their use of corporate cash to pay for personal expenses occurred while Unique was posting losses on its tax returns.

personal expenses with corporate funds, use corporate assets for personal benefit, and are subsequently unable to pay their corporate debts, the intentional use of the corporate form is present regardless of whether the shareholders had any "evil intent." Unique used its cash to pay for its shareholder's personal expenses and did not require the shareholders to pay for use of corporate assets, while simultaneously failing to pay its corporate creditors. How can this conduct be anything but "the intentional use of the corporate form to violate or evade a duty?" These are the very factors cited by *Meisel* to determine violation of a duty.

In further support of the ultimately irrelevant point of whether Bill Rehe had evil intentions,[13] the Rehes argue that Mr. Rehe misunderstood the nature of an S-Corporation, and thought that it was a "flow-through" entity that he could treat as he liked.[14] *Response* at 6 and 24. Even if Mr. Rehe did "misunderstand", it doesn't change the outcome here. Whether or not an S-Corporation is a "flow-through" entity (whatever that means),

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[13] In an effort to confuse this court as well, the Rehes claim that the inability of NWC's expert witness Paul Pederson to testify as to the Rehes' "intent" is somehow fatal to the claim. *Response* at 27. But the Rehes fail to explain how an expert witness would have any knowledge of their specific intentions years earlier. Mr. Pederson plainly testified that what the Rehes were doing was improper. RP 3/15/12 at 230-231; 3/22/12 at 6-7, 13-14.

[14] Also relevant to Mr. Rehe's intent is the fact that, as the jury found, he acted with actual intent to hinder, delay, or defraud his creditors in December, 2008 and again in July, 2009. CP 408. His transfer of the 38th Avenue Lot on January 20, 2009 can only be viewed in light of those unappealed elements of the jury verdict, which the trial court agreed with in FOF 20-21.

Mr. Rehe is still not allowed to strip cash out of an unprofitable company whose liabilities exceed its liquid assets. RCW 23B.06.400(b).[15] And having an S-Corporation does not mean Mr. Rehe can write off personal expenses as business expenses. These actions were intentional, they interfered with Unique's ability to pay its creditors, and they justify corporate disregard regardless of whether Mr. Rehe specifically intended to violate any particular duty.

If Bill Rehe – a lawyer with an M.B.A – wants to avail himself of the liability protections of his corporation, he must obey the rules. He may not funnel corporate cash into his own pockets while incurring substantial corporate debt, and then tell his corporate creditors that the money is all gone. If he chooses to do so, he is personally liable under Washington's law regarding corporate disregard. Even if Mr. Rehe wrongly believed that he was allowed to manipulate his corporation in this fashion, his mistaken belief is no defense. Ignorantia legis neminem excusat. *See State v. Reed*, 84. Wn. App. 379, 384, 928 P.2d 469 (2000).

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[15] RCW 23B.06.400 prohibits shareholder distributions when the corporation would otherwise be unable to "pay its liabilities as they become due in the usual course of business." Throughout 2006 and 2007, Unique repeatedly failed to pay its liabilities as they came due, all the while Mr. Rehe was diverting corporate cash assets to pay for his personal expenses. See Exs. 33, 43, and 102; See also RP 3/14/12 at 20. By Mr. Rehe's own admission, there was no time after October, 2007 when Unique had sufficient liquid reserves in its bank accounts to pay its outstanding debt to Unique. RP 3/26/12 at 3-16; see also Ex. 275 and 277.

The Rehes cite to *Truckweld Equip. Co. v. Olson*, 26 Wn. App. 638, 618 P.2d 1017 (1980) and several other cases in an attempt to support the trial court's determination. *Response* at 24-26; 28-29. However, these cases are not applicable. *Truckweld* involved a corporate creditor (plaintiff Truckweld) that extended credit to a financially-struggling corporation. The shareholder, Olson, ***did not*** divert corporate funds into his own pockets or strip assets from the corporation when it began to fail. In fact, while Truckweld pointed to the lack of corporate minutes and other documents, Truckweld's primary complaint was that Olson failed to commit additional capital to sustain the corporation. The appellate court held that such a claim could not sustain an action for corporate disregard because there was no evidence of the "manipulation of the corporation to the stockholder's benefit and creditor's detriment." *Id.* at 645.

This case is not *Truckweld.* Whereas the stockholder in *Truckweld* committed no corporate abuses, Mr. Rehe diverted hundreds of thousands of dollars worth of corporate assets to his personal use, and stripped the corporation of its remaining assets after the lawsuit had been filed. *Truckweld* is not authority for the proposition that a shareholder may regularly divert funds and assets to his own personal use at the expense of the corporation, and thereby render it unable to satisfy judgments to

creditors. Indeed, the Rehes have cited no authority for the proposition that, under such circumstances, the corporate veil should be respected.

Finally, the Rehes claim, erroneously, that the trial court's decision on corporate disregard is an exercise of "discretion." *Response* at 28. The Rehes presumably mean that this Court needn't look too closely at the trial court's decision. The Rehes are wrong: this isn't a matter of discretion, but of substantial evidence and applying the proper legal standards to the facts.[16] As discussed above, the proper legal standard for proof of "intentional use of the corporate form to violate or evade a duty" is evidence of "fraud, misrepresentation ***or some form of manipulation of the corporation to the stockholder's benefit and creditor's detriment***." *Meisel*, 97 Wn.2d at 410 (emphasis added). The trial court properly found manipulation of the corporation, at FOF 29, 31 and 32, but then erred by failing to impose the appropriate legal consequence of such manipulation. Mr. Rehe intentionally diverted substantial corporate assets to his own benefit and to NWC's detriment. There was overwhelming evidence of intent, and there is no substantial evidence to support the trial court's erroneous conclusion that Mr. Rehe did not intend to violate or evade a

[16] As addressed above at page 3, *supra*, the proper standard of review is not "abuse of discretion." The proper standard is set out in *Rogerson Hiller Corp.*, 96 Wn. App. at 924: questions of fact are reviewed for substantial evidence, and legal questions are reviewed *de novo*.

duty. The trial court erred in failing to properly apply the standards in *Meisel* to the facts of this case. The Court of Appeals should apply the proper legal consequence to the trial court's factual findings of corporate manipulation.

2. The trial court erred in finding that the Rehes' corporate gutting and substantial diversion of funds did not result in an unjustified loss to NWC.

As addressed in NWC's opening brief, corporate disregard also requires a showing that the corporate abuse caused "unjustified loss" to the creditor. Under Washington law, an "unjustified loss" occurs when the shareholder's conduct has an "***effect on the plaintiff's ability to collect a judgment from the defendant corporation***." *Morgan*, 93 Wn.2d at 589 (emphasis added); *see also Eagle Pac. Ins. Co. v. Christensen Motor Yacht Corp.*, 85 Wn. App. 695, 708, 934 P.2d 715, 722 (1997), *aff'd*, 135 Wn.2d 894, 959 P.2d 1052 (1998). The trial court failed to employ or even reference this standard when it erroneously concluded that the Rehes' abuses did not cause unjustified loss. COL 10; CP 1026.

NWC's judgment against Unique was $512,000. CP 1030. With the successful return of the 89th Street Property, Unique now owns a single asset with an assessed value of $327,000. CP 92. Under the best of circumstances, foreclosure of that Property would still leave a deficiency judgment of over $180,000. NWC argued that the Rehes' gutting of the

38th Avenue Lot deprived Unique of a $200,000 asset that would otherwise have been available to satisfy NWC's judgment, and that the Rehes' diversion of assets deprived Unique of an additional $180,000 in liquid assets that also would have been available to help satisfy NWC's judgment. Exs. 121 and 273; RP 3/26/12 at 48-50. In other words, NWC presented clear proof that the Rehes' gutting of the corporation and regular diversion of funds had a substantial effect on NWC's ability to recover the full amount of its judgment.

The Rehes claim that NWC has a "causation problem" but doesn't explain what this "problem" is. *Response* at 30. Nor do the Rehes address the simple arithmetic outlined above. Instead, the Rehes spend several pages discussing proximate cause, and the distinction between "cause in fact" and "legal causation." *Response* at 31-32. Then, the Rehes simply drop the distinction without applying it to this case, or addressing the argument raised in NWC's *Opening Brief* at 36-38.

This focus on "proximate cause" is a distraction and it ignores the controlling case law. The cases on corporate disregard do not discuss proximate cause as a separate requirement. The cases do, however, employ a clear and straight-forward standard of causation: did the shareholder's conduct have an "effect" on the creditor's ability to collect on its judgment. *Morgan*, 93 Wn.2d at 589; *Eagle Pac. Ins. Co.*, 85 Wn.

App. at 708. The answer here is obvious, and the trial court's conclusion to the contrary on causation is not supported by any evidence.

Even if one applies the traditional "proximate cause" test to the theory of corporate disregard, it is clearly already incorporated into the elements establishing corporate disregard. "Cause-in-fact" is present where the shareholder's acts have had an "effect" on a creditor's ability to recover on a judgment. *Morgan*, 93 Wn.2d at 589. "Legal causation" is established by the fact that the doctrine of corporate disregard applies only when the shareholder has manipulated of the corporation to his personal benefit, and to the detriment of the creditor. *Meisel*, 97 Wn.2d at 410. Both elements are clearly present in the case law and in this case.

While admitting that Mr. Rehe's unreported distributions were technically improper and likely violated tax laws as well, the Rehes argue that all the improper distributions "could have" been performed lawfully and therefore caused no "unjustified loss." *Response* at 27-28. However, the Rehes never introduced any evidence to support this proposition. Notably lacking was any expert testimony to demonstrate that a corporation in Unique's financial condition, i.e., inadequate liquid assets, could, during any of the relevant periods, distribute cash or other assets to its shareholders ahead of its creditors. No expert would testify to such a practice, because it is in direct violation of Washington law.

The Rehes wrongly claim that NWC's own expert, Paul Pederson, testified that Unique "could have" distributed the diverted assets to the Rehes as income or distributions. *Response* at 7. The Rehes mischaracterize Mr. Pederson's testimony, and neglect to acknowledge that the Rehes' proposed finding to this effect was rejected by the trial court. CP 449-450 at ¶ 36. NWC encourages the Court to review the testimony cited by the Rehes in support of this proposition. RP 3/22/12 at 10-12. Mr. Pederson stated that proper reporting of the distributions would correct things "[f]rom an accounting standpoint," but would not render them proper. *Id.* And he testified that such reporting would merely "reconcile" the corporate balance sheets.[17] *Id.* But Mr. Pederson also explained that he was testifying as to general accounting principles, not Washington corporate law. RP 3/21/12 at 12. Mr. Pederson never testified that distributions to shareholders would have been legally permissible while the corporation was incurring debt, reporting annual losses, and failing to pay its bills as they came due.

The Rehes also argue that, because Bill Rehe's "accounting practices" predated Unique's contract with NWC, NWC could not be

[17] A company may be able to commit fraud and still have accounting records that appear accurate and consistent. Conversely, a company can operate legitimately, but have messy books. What Mr. Pederson and NWC have complained about is not poor documentation, but actual assets leaving the corporation and flowing into the Rehes' pockets for no consideration, while the corporation was not paying its bills.

harmed thereby. *Response* at 24 and 29. First, the testimony that the Rehes cite to refers only to the practices of maintaining a "box" for project receipts. *Response* at 6; RP 3/26/12 p. 22. More importantly, as discussed above, the Rehes' actual diversion of corporate assets to their personal benefit is not an "accounting practice." NWC's complaint is not that Unique kept "messy books," but that it diverted hundreds of thousands of dollars' worth of assets into the pockets of its shareholders, at the same time that it was ignoring its mounting debts and contingent liabilities. *See* Note 15, *supra*. More to the point, assuming arguendo that the Rehes had been diverting funds for years, this does not make it permissible and does not change the fact that it had an adverse effect on NWC's ability to recover its judgment.[18]

The Rehes also argue that their gutting of the 38th Avenue property did not render Unique insolvent.[19] *Response* at 35. However,

[18] The Rehes also misquote Mr. Pederson as claiming that the diversion of corporate funds had ceased in 2006. Again, this is incorrect: as Mr. Pederson testified at multiple points, and as all his summary exhibits revealed, the diversion of corporate cash occurred throughout the life of the contract, from March 2006 through late 2007. RP 3/22/12 at 20-21; Ex. 121, 272, 273, and 275. The trial court recognized this when it found "the substantial majority of such questionable expenses occurred before 2008." FOF 30. The Rehes' personal use of the corporate real estate continued until 2009. This proves that the diversion of corporate funds and assets continued throughout the time when Unique was becoming indebted to NWC. Given the Rehes' practice of regularly using corporate assets to pay for personal expenses, it is no surprise that Unique was eventually unable to pay NWC.

[19] In support of this proposition, the Rehes point to testimony of Paul Pederson. It should be noted that where Mr. Pederson testified to Unique's insolvency, he was employing the definition of insolvency contained in the Uniform Fraudulent Transfer Act

insolvency is not the relevant standard in determining whether the Rehes' misconduct caused an unjustified loss. Again, the standard in Washington is whether the misconduct had ***an effect on the creditors' ability to collect on a judgment***. This standard is far less stringent than "insolvency" and protects a corporate creditor even if, at the time of the gutting, the creditor's claim is not capable of exact determination.[20] Moreover, although the Rehes proposed a finding to the effect that the transfer of the 38th Avenue Lot did not render Unique insolvent, the trial court correctly rejected that finding. CP 447-448 at ¶ 25.

The Rehes also argue that NWC should have insisted on greater security, and that NWC is asking this Court for a personal guarantee that it failed to secure under its contract. *Response* at 32-33. The Rehes point to *Truckweld*, *supra*, for support, but again, this case isn't *Truckweld*. In *Truckweld*, the creditor ***knew*** the debtor company was in financial trouble but extended credit anyway. Subsequently the debtor company went under due to "a combination of unfortunate timing and persistent working capital problems." *Truckweld*, 26 Wn. App. at 645. In contrast, here the

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at RCW 19.40.011, as reflected in Jury Instruction # 25 at CP 1283. Accordingly, Mr. Pederson testified as to Unique's then-existing liquidated debt to NWC in January, 2009, and the sufficiency of the assets at that time. RP 3/15/12 at 195-197. Mr. Pederson expressly did not testify as to Unique's contingent and unliquidated obligation to pay attorney fees. *Id.*

debtor company, Unique, is unable to pay NWC's judgment because Bill Rehe siphoned funds into his own pocket and gutted the corporation of its major assets. NWC was ***unaware*** of Mr. Rehe's wrongful diversion of corporate funds, and the Rehes failed to introduce evidence of anything NWC could have done that would have revealed the misconduct prior to entering into the contract. Review of balance sheets or profit and loss statements for prior years would not have revealed the abuse that occurred during the contract performance. Indeed, it took years of hard fought discovery to put the pieces together.

In *Truckweld*, "[i]t was Truckweld's failure to utilize these safeguards which contributed to its loss, not any misconduct or abuse of the corporate form by Olson." *Truckweld*, 26 Wn. App. at 646. Here, in contrast, it was Mr. Rehe's abuse of the corporate form that left Unique an asset-less shell. The *Truckweld* court held, "We know of no rule of law requiring a corporate stockholder to commit additional private funds to an already faltering corporation." *Id.* But the counterpart to this is equally true: the law does not allow a corporate stockholder to ***divert the funds and assets*** of a corporation and thereby cause it to fail.

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[20] Stated another way, a shareholder cannot unilaterally cap or reduce the amount of a creditor's claim by stripping out some, but not all, of the assets from the corporate debtor.

Further, the Rehes cite to the "economic loss rule" to suggest that a trial court should not in effect give NWC a remedy that it did not negotiate. *Response* at 33. The Rehes ignore the progression of the economic loss rule into the Independent Duty Doctrine.[21] *Eastwood v. Horse Harbor Found., Inc.*, 170 Wn.2d 380, 394, 241 P.3d 1256 (2010). Under the Independent Duty Doctrine, a plaintiff can recover in tort for the breach of a duty that arose independently of the contract. *Id.* Corporate shareholders have a duty not to manipulate a corporation to a shareholder's benefit and a creditor's detriment. The source of this duty is the common law,[22] and RCW 23B.06.400. Even under the Independent Duty Doctrine analysis, the Rehes' breach of this independent duty entitles NWC to a remedy.

The Rehes' argument is, essentially, that unless corporate asset-stripping is specifically prohibited by a contract, it is permitted. They offer no authority for this frivolous proposition, and it flies in the face of common sense, state law, and generations of precedent. The Rehes were

[21] "An injury is remediable in tort if it traces back to the breach of a tort duty arising independently of the terms of the contract. Because the term "economic loss rule" inadequately captures this principle, we adopt the more apt term "independent duty doctrine." *Eastwood*, 170 Wn.2d at 402.

[22] *See* Discussion, *supra*, at page 4 and NWC's *Opening Brief* at pages 16 and 29-30.

not entitled to gut their corporation of assets while it was incurring significant liability.

3. This Court should remand with instructions that the trial court enter judgment in favor of NWC on its claim of corporate disregard.

As discussed above, NWC was required to prove that Bill Rehe manipulated the corporation to his benefit and to the detriment of NWC, and that this manipulation had an effect on NWC's ability to collect on a judgment. The first element is shown independently by (1) Bill Rehe's gutting of Unique by transferring the 38th Avenue Lot seven months after NWC filed suit, and (2) Bill Rehe's repeated diversion of hundreds of thousands of dollars worth of Unique's cash assets, as reflected in FOF 29, 31 and 32. The second element is shown by the simple fact that NWC's judgment against Unique is larger than Unique's sole existing asset. When the Court applies the proper legal standards to these facts with its *de novo* review, the outcome is clear: this Court should remand with instructions for the trial court to enter judgment against the Rehes, and in favor of NWC, on the issue of corporate disregard.

B. The trial court erred in awarding fees to the Rehes that were incurred by other defendants in their failed attempts to defeat NWC's successful claims.

This trial consisted of four causes of action and four defendants: a breach of contract claim against Unique Construction, an UFTA claim

against Sahara Enterprises, an UFTA claim against the William K and Marion L LLLP, and a claim of corporate disregard against the marital community of William and Suzanne Rehe. Trial was spread over three weeks, and between the Judge and the jury, a total of 26 hours of witness testimony was presented. Less than three hours of that time, and only 7 of 153 exhibits (CP 1287-1303) were devoted solely to the issue of corporate disregard. This is the only issue upon which any of the Defendants "won."

Despite the fact that 89% of the trial testimony (CP 427-442) and 146 of the 153 trial exhibits (CP 1287-1303) were devoted to issues upon which the Rehes did not prevail, the trial court awarded the Rehes the vast majority of fees spent on the entire trial, on behalf of ***all the Defendants***. Why did the trial court do this? Supposedly because it determined that the Defendants' attorney Mr. Burns "would have been here had he only been representing the Rehes" and "would had to have been at virtually everything and throughout the trial." RP 7/27/12 at 52-53.

This is not an appropriate basis for an award of fees. Mr. Burns represented all the Defendants, but the Rehes are only entitled to fees related to ***the issues upon which they prevailed***. And since the Rehes failed to segregate their fees accordingly, they are not entitled to any fees. The trial court's award of fees to the Rehes should be reversed.

1. The Trial Court erred in not requiring the Rehes to segregate their fees from the fees of the unsuccessful defendants.

In awarding fees, a trial court ***must segregate*** the time spent on unsuccessful claims from the time spent on successful ones. *Mayer v. City of Seattle*, 102 Wn. App. 66, 79–80, 10 P.3d 408 (2000). "The party claiming an award of attorney fees has the burden of segregating its lawyer's time." *Boguch v. Landover Corp.*, 153 Wn. App. 595, 619, 224 P.3d 795 (2009) (*citing Loeffelholz v. Citizens for Leaders with Ethics & Accountability Now*, 119 Wn. App. 665, 690, 82 P.3d 1199 (2004)). By awarding the Rehes fees for time their attorney spent on the unsuccessful defense of the Contract and UFTA claims for other defendants, the trial court violated these basic principles of Washington law.

The Rehes make refer to the "intertwined" nature of the claims in this litigation. *Response* at 38-39. They are apparently attempting to invoke the doctrine of "irrevocably intertwined" causes of action. However, they cite no case law to establish how, or if, the doctrine can apply to the Rehes and the other defendants in this case.

Under Washington law, time need not be segregated where a plaintiff's successful claim is "inextricably intertwined" with an unsuccessful claim. *Mayer v. Sto Indus., Inc.*, 156 Wn. 2d 677, 693, 132 P.3d 115 (2006). However, claims are only "inextricably intertwined"

where "[t]he unsuccessful claims were premised upon the same facts and issues underlying the successful claims .... and were merely alternate avenues of obtaining the damages that Plaintiffs were awarded." *Broyles v. Thurston County*, 147 Wn. App. 409, 447-48, 195 P.3d 985, 1005 (2008).

Contrary to the Rehes' unsupported assertion, the claims and counterclaims in this lawsuit were not inextricably intertwined. This can be readily determined from the following undisputable fact: had it so chosen, Northwest Cascade could have prosecuted the contract action against Unique Construction first, and later pursued the two UFTA claims and the veil-piercing claim, either in a separate action, or through a supplemental proceeding under RCW 6.32.270. CR 18(b); see also CR 69. Where separate causes of action could have been tried separately, they are not "inextricably intertwined":

> it is at least conceivable that both the foreclosure and misrepresentation actions could have proceeded independently with each party obtaining a judgment against the other. If so, the actions were not inextricably intertwined.

Mehlenbacher v. DeMont, 103 Wn. App. 240, 247, 11 P.3d 871 (2000). Accordingly, the breach of contract claims and UFTA claims were not "inextricably intertwined" with the veil-piercing claim.[23]

[23] Indeed, the corporate disregard claim was tried separately to the bench at the request of the Rehes (CP 395), and is readily separable on the Minutes of Proceedings. RP 428-442.

In short, and as reflected in the testimony in this action, there were three distinct sets of facts and issues in this case: (1) the facts related to the performance of the contract; (2) the facts related to Mr. Rehe's fraudulent transfers of both corporate and personal property; and (3) the facts related to Mr. Rehe's abuse of the corporate form. Only this last set of facts relates to NWC's unsuccessful veil-piercing claim. Where "plaintiffs bring different claims based upon different facts and legal theories," the claims are not inextricably intertwined. *Brand v. Dep't of Labor & Indus. of State of Wash.*, 139 Wn. 2d 659, 673, 989 P.2d 1111 (1999); see also *Travis v. Wash. Horse Breeders Ass'n, Inc.*, 111 Wn.2d 396, 411, 759 P.2d 418 (1988). The claims of corporate disregard were not "inextricably intertwined" with the breach of contract and UFTA claims.[24]

The Rehes claim that not even NWC could segregate its fees. *Response* at 39.[25] The Rehes cite to the trial court's decision on fees, which stated

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[24] As NWC has previously argued, there is one limited exception to this fact: the evidence and issues surrounding the Rehes' fraudulent transfer of stock funds to the William K and Marion L LLLP largely dovetailed with the issues surrounding the fraudulent transfer of the 89th Street Property, because both UFTA actions related to a common time frame and overlapping liabilities between the Rehes personally and Unique. However, this fact is irrelevant to the issues before this Court on appeal.

[25] The Rehes mischaracterize and take out of context the statements of NWC's counsel. *Response* at 38, 39 and 42. NWC's counsel simply acknowledged that there were a few isolated events that might warrant minor adjustments to the 11% allocation model proposed.

> Both counsel have indicated to this Court that it is difficult for them to segregate out what fees were incurred and which claims, and I have no reason but to accept the statements of both counsel, and if they can't segregate the fees, I can't imagine how any other Court would expect this court to segregate the fees.

RP 7/27/12 p. 52, CP 998. The Rehes, and the trial court, are wrong: NWC did segregate its fees, using a proportional, percentage-based methodology approved by case law. *See, e.g., Crest Inc. v. Costco Wholesale Corp.*, 128 Wn. App. 760, 767, 115 P.3d 349, 352 (2005); *Clausen v. Icicle Seafoods, Inc.*, 272 P.3d 827, 833-34 (2012). NWC allocated its fees based on the proportion of time spent at trial on the various issues. CP 931. NWC showed that 89% of the testimony time at trial related to the issues upon which NWC prevailed. *Id.* The trial court largely adopted this approach with respect to NWC's fees. CP 997.

NWC's proportional-based segregation model is perfectly appropriate for circumstances in which segregation is difficult.

> Appellate courts ... have permitted the use of a percentage reduction in segregating fees and costs when, as here, the specifics of the case make segregating actual hours difficult.

Clausen, 272 P.3d at 833-34. Mere "difficulty" in segregating hours does not translate into "inextricably intertwined" claims, though it may justify a proportional method of segregation.

The Rehes have no basis for invoking of the "inextricably intertwined" doctrine. Looking closely at what the Rehes have argued, both here and before the lower court, their real argument is that the Rehes had to defend everything: the breach of contract action against Unique, as well as the UFTA claims against Sahara and the action on corporate disregard against them personally. *Response* at 44; RP 7/27/12 at 33-34; CP 461. The Rehes offer no justification for this argument: surely, they could have conceded Unique's contractual liability on the debt to NWC. But regardless, this theory is flawed because even if the Rehes "had to" defend the contract and UFTA actions, ***they still lost on those causes of actions*** and they are ***not entitled to fees*** under the contract for issues upon which they did not prevail. The trial court's and the Rehes' approach would defeat the point of prevailing party fee clauses and routinely convert trial court losers into winners of fee awards.

The Rehes also try to justify the trial court's decision by citing the number of parties, and the amount of time the various claims had been pending. The Rehes argue that NWC lost, or voluntarily non-suited, on four of six defendants, and on three of five claims. First of all, the Rehes fail to point to any case law in support of this head count method of segregation. Second, the Rehes' calculations are not accurate: the Rehes count the marital community of William and Suzanne Rehe as two

separate parties, and also ignore NWC's jury verdict against the William K and Marion L LLLP. Third, the number of defendants NWC sued has no bearing on how much time Mr. Burns spent defending ***the Rehes***. Fourth, they fail to explain how the mere duration that a claim was pending has any relationship with the amount of fees incurred. The only proper factor for consideration is the amount of time Mr. Burns devoted to the issue of corporate disregard on which the ***Rehes*** prevailed. This was a single defense to a single separately tried claim, out of four claims against four separate defendants. Even if this head count method were a proper basis for an award of fees, it does not justify an award of nearly all the Defendants' cumulative defense fees, including fees incurred on losing causes.

The Rehes also attempt to invoke the "broad discretion" of the trial court as grounds for the fee award. *Response* at 40. Unlike other discretionary rulings, however, case law has significantly circumscribed the discretion of the trial court in awarding fees.

> [T]he court ***must*** separate the time spent on those theories essential to [the cause of action for which attorneys' fees are properly awarded] and the time spent on legal theories relating to the other causes of action.... This must include, on the record, a segregation of the time allowed for the [separate] legal theories....

Hume v. Am. Disposal Co., 124 Wn.2d 656, 673, 880 P.2d 988 (1994) (alterations in original; emphasis added) (citing *Travis*, 111 Wn.2d at 411). The trial court clearly did not do so here.

The Rehes argue that the trial court's written order sets forth a defensible basis for the fee award, but when the trial court wrote its written order on fees, it was under the ***mistaken impression*** that the fees requested by the Rehes had ***already been segregated***:

> THE COURT: Okay. So did I misunderstand, Mr. Burns, that $128,000 and change was what the defendants incurred in attorney's fees in defending against piercing the corporate veil, or is that the total amount as Mr. Murphy suggests in his briefing?
>
> MR. BURNS: It's the total amount.
>
> THE COURT: It's the total amount. So I did misunderstand.

RP 7/27/12 p. 32. Thus, there is no written segregation, on the record, supporting the Rehe fee award.[26] Even if this Court were to reference the trial court's ***oral ruling***, there is no segregation on the record. The oral ruling found as follows:

> I would agree with Mr. Burns that he would had to have

[26] The Rehes refer to the "extensive Declaration of Martin Burns", stating that he had attempted to "color code" the time spent on different issues. *Response* at 16. There is no indication, however, that Mr. Burns segregated out the 89% of trial time devoted to the contract and UFTA claims (CP 472-475), the multiple dismissals of the Rehes' counterclaim (CP 489-90; 494), or the numerous hours devoted to jury instructions (CP 472-475). None of that time had anything do with the corporate disregard claim. In fact, the Rehes never attempted to segregate their fees by issue or apply any plausible theory of segregation because it would have resulted in a much smaller award.

> been at virtually everything and throughout the trial. I remember most of our time spent on jury instructions, however, dealt with the UFTA claim ..., not the issue of veil piercing that the Rehes prevailed on. So that time he might have still been present but, really, that wasn't -- all that time that we spent on those jury instructions and the verdict form, I think related, really, to the UFTA. I think everybody pretty much agreed on everything other than that. Given that the reality, however, that Mr. Burns was in fact representing all of the defendants, but keeping in mind that he would have been here had he only been representing the Rehes, I don't think $128,000 is the right number. I do think it should be significantly less. On the other hand, I don't think $14,000 is the right number either. That certainly isn't the number that Mr. Murphy incurred in pursuing that claim, even under his theory of 11 percent. Given that Mr. Burns would have been here throughout, in any event, I believe that an appropriate figure is -- one second, I just had it in my head. $85,000 is what I'm awarding to the Rehes against the plaintiff on piercing the corporate veil.

RP 7/27/12 p. 52-53. "The trial court ***must*** create an adequate record for review of fee award decisions, which means in part that the record must show a tenable basis for the award." *Loeffelholz*, 119 Wn. App. at 690 (emphasis added). The record reflects no separation of time, no effort made by the trial court to determine how much of Mr. Burns' time was devoted to the breach of contract or UFTA claims, and no explanation as to where the $85,000 figure came from. As the trial court stated, "I just had it in my head." RP 7/27/12 p. 53. This does not create an adequate record for review of the fee award to the Rehes.

The last refuge of the Rehes – and this is apparent throughout their *Response* – is the notion that somehow the Rehes' fees are "reasonable" relative to the amount of fees expended by and awarded to NWC. There is no case law or legal justification cited by the Rehes to suggest that an award of fees can be justified based upon some holistic, comparative analysis of one defendant's fees versus a plaintiff's fees, particularly when they relate to different claims and parties.[27] Instead, a prevailing party is entitled to fees actually expended on issues upon which ***that party*** prevailed. What NWC expended on other claims directed to other defendants is wholly irrelevant. Here, it is undisputed that a significant portion of the fees awarded to the Rehes was for time actually spent unsuccessfully defending the UFTA and Contract claims that comprised 89% of the trial time and the vast majority of exhibits. The fact that NWC spent more, over all, than the Rehes on attorney fees in the entire case does not change this fact, or justify an award of fees for time spent on losing issues.[28]

This "holistic" approach to the fee awards here is even more problematic because these fee awards cannot be offset. NWC's fee award

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[27] Indeed, by blurring together all the defendants as one entity being defended the Rehes' argument is patently inconsistent with its defense of the corporate disregard claim.

[28] For a detailed explanation for why NWC's fees were as high as they were, see NWC's Response to the Respondents' Cross-Appeal at Section III below.

is against Unique, not the Rehes, and NWC must pay the Rehes' fee award regardless of whether Unique can pay NWC's fee award. The trial court's fee award, combined with its erroneous decision on corporate disregard, means that NWC will be unable to recover its fees from Unique, while nevertheless being required to pay the Rehes. All the while, the Rehes are still sitting on the 38th Avenue Lot that once belonged to Unique, as well as the hundreds of thousands of dollars in personal liquid assets that the Rehes were able to shelter while Unique was incurring the debt to NWC that it never paid.

2. The trial court erred by using an untenable basis for the award of fees to the Rehes.

One clearly stated basis for the trial court's award of fees to the Rehes was its belief "that Mr. Burns was in fact representing all of the defendants, but keeping in mind that he would have been here had he only been representing the Rehes." RP 7/27/12 p. 52-53. There is no case law in Washington that suggests this is a proper basis for a fee award in this or any circumstance. Rather, a trial court is ***required*** to segregate out time spent by a party's lawyer on ***unsuccessful legal theories or defenses***. *Mayer*, 102 Wn. App. at 79–80. Regardless of the fact that Mr. Burns "would have been" present for the trial even if he had only represented the Rehes, he ***was in fact present*** as a legal, and paid, representative of

unsuccessful defendants Unique and Sahara Enterprises – and he mounted an ***unsuccessful defense*** of the contract and UFTA claims on their behalves. There is no support for the proposition that the Rehes may recover fees for the time that Mr. Burns spent on the unsuccessful defense of Unique and Sahara, and the Rehes point to no legal authority.

3. The award of fees to the Rehes was manifestly unreasonable.

Beyond the untenable justification for the trial court's fee award to the Rehes, the award also stands as manifestly unreasonable. The Rehes, while calling NWC's 11% figure somewhat "random," don't actually disagree with the fact that the bench portion of the trial comprised approximately 11% of the total trial time, nor did they present their own breakdown of trial time. The figure comes directly from the official record of the trial.[29] The Rehes prevailed only on a single defense to a single claim that comprised 11% of the trial testimony. In spite of this fact, the trial court awarded the Rehes nearly all of the fees that Mr. Burns had incurred on behalf of all defendants and all claims throughout the course of his representation of the Defendants.

[29] The total time for the veil-piercing "bench portion" of the trial testimony was less than three hours, out of nearly 26 hours of total trial testimony. CP 427-442; see also CP 594-595. By comparison, more than 16 hours of testimony was spent on the breach of contract issues, and almost 7 hours of testimony was spent on UFTA claims. *Id.*

In *Loeffelholz*, the Court of Appeals held that the trial court's award of 50% of the defense fees manifestly unreasonable. As that court explained,

> The record does not show that the claims were so interrelated as to excuse segregation. Nor will the record support a finding that $50,000 was reasonably incurred to establish a single defense (immunity) to a single claim (the IA defamation claim). This case embodied many claims and issues, and an award of nearly half the total fees incurred represents too high a proportion to be reasonable.

119 Wn. App. at 690. Similarly, it is manifestly unreasonable for the trial court to award the Rehes with more than two-thirds of the Defendants' total attorney fees when they prevailed only on a single issue that took up only 11% of the trial testimony. The trial court's fee award should be reversed.

C. This Court should award fees on appeal.

NWC is entitled to an award of fees on appeal, pursuant to the contract between the parties.

III. RESPONSE TO CROSS-APPEAL

A. The trial court did not abuse its discretion in awarding NWC approximately 71% of its fees for successfully litigating the breach of contract and UFTA claims.

The Rehes complain that the trial court's award of $270,000 in attorney fees to NWC was an abuse of discretion.

The amount of an award of attorney fees is discretionary, but will be overturned when there has been an abuse of discretion. *Mayer*, 102 Wn. App. at 79. An award of fees is an abuse of discretion when it is "manifestly unreasonable or based upon untenable grounds, or if no reasonable person would take the position adopted by the trial court." *Id.* (*citing Allard v. First Interstate Bank of Wash., N.A.*, 112 Wn.2d 145, 148–49, 768 P.2d 998 (1989)).

The Rehes argue only that the total amount of fees awarded to NWC was "excessive." There is little actual argument contained in the cross-appeal to justify the Rehes' position. However, NWC's Motion for Fees and Sanctions reveals that NWC was subjected to multiple abusive litigation tactics by the Rehes throughout this litigation. The Rehes cannot complain that NWC spent attorney fees in response to these tactics. The trial court was well within its discretion to award NWC fees for this work.

In the absence of any substantive challenge to NWC's fees, NWC will not repeat the full extent of the Rehes' litigation abuses that drove the litigation costs in this case, but refers this Court to its *Motion for Prejudgment Interest, Costs, Attorney Fees, and Sanctions*, at CP 578-593. There, NWC describes in detail the various ways in which Bill Rehe materially increased the cost of this litigation. These include:

- Unique asserted a $2 million dollar counterclaim that required NWC to bring a successful Motion for Partial Summary Judgment. CP 62-68, CP 1-2.
- The Defendants delayed by months in providing responses to NWC's Discovery Requests. CP 611.
- Mr. Rehe fraudulently transferred assets away from Unique with actual intent to hinder, delay, or defraud creditors, forcing NWC to hunt those assets down. CP 408.
- Mr. Rehe lied at his deposition, claiming to have owned the 89th Street Property in his personal capacity, when the day before he had caused that property to be transferred from Unique to the Black Point Real Estate Privacy Trust. CP 734-735.
- Mr. Rehe lied at his deposition, claiming that the 38th Avenue Lot has been "transferred to another company to pay bills." *Id.*
- The Defendants forced NWC to move to compel responses to discovery requests that they refused to answer. NWC's Motion to Compel, 9/9/2010 (to be supplemented).
- Even after receiving a court order (Ex. 269), Mr. Rehe still failed to comply, refusing to provide any information about

the circumstances of various property transfers, and failing to disclose the existence of various financial accounts. Ex. 270; CP 768-783.

- Mr. Rehe subsequently transferred both the 38 Avenue and 89th Street properties a second time, this time to Nevada LLCs with undisclosed members and further hiding his ties to the properties. RP 3/15/12 at 107-123.
- Mr. Rehe produced fraudulent tax forms for his company, Temporal Funding LLC. The forms, covering 4 years and signed by Mr. Rehe, appeared to show that Unique Construction owned 40% of Temporal. When NWC finally acquired originals from the IRS, it discovered that none of the forms had been filed with the IRS until *after* they had been produced to NWC. Most importantly, the documents showing Unique's supposed 40% ownership interest were never filed with the IRS. *Compare* CP 786-829 to Trial Ex. 84.
- At a later deposition, Bill Rehe repudiated unsigned discovery responses that he had personally filed. CP 850. Counsel for NWC asked Mr. Rehe's counsel to provide signed copies of the discovery responses, but despite

repeated requests (*Id.*, CP 616-617; CP 618-619), Mr. Burns never responded to NWC. NWC's counsel was forced to bring yet another motion to compel and motion for sanctions in an attempt to force Mr. Rehe to acknowledge the discovery responses. NWC's Motion for Sanctions, 10/28/2011 (to be supplemented).

- Several weeks after the deadline for discovery had lapsed, the Rehes provided voluminous additional documents that had been repeatedly requested but never produced. CP 58 at ¶¶ 10-11; CP 113-220. NWC was forced to move to strike this material. CP 46-48.
- Defendant Sahara Enterprises failed to answer the Second Amended Complaint, forcing NWC to bring yet another Motion for Default. NWC's Motion for Default, 10/28/2011 (to be supplemented).
- In addition, Sahara's Answer, served three weeks before trial, sought to resurrect the $2 million counter-claims that had earlier been dismissed. CP 23-33. NWC was forced, , to again move to dismiss the counter-claims. CP 34-55.
- Finally, as the trial court was well aware, the defendants fought over every issue, no matter how clear the evidence

contract. The Rehes sought to reopen every extra work order that had been approved and paid during the project, and NWC was forced to prepare and present its case accordingly. The Rehes even sought to resurrect their twice-dismissed counter-claims yet again, this time in the form of an alleged "offset" at trial. CP 379-380; RP 3/15/12 at 129-144; RP 3/20/12 at 51-68.

If NWC's fees were high, it is only because the Rehes forced NWC to work that much harder to recover on its claims. When a party refuses to comply with discovery requests and court orders, fraudulently transfers multiple assets not once but twice, and lies under oath, it necessarily makes litigation more expensive for the other side. In the end, the Defendants failed to convince the Jury of any of their claims or defenses, but it was not for want of trying, albeit trying in numerous inappropriate ways.

The Rehes focus on NWC's fees in the month of November, 2011, claiming they were quite high. However, trial in this case was originally scheduled to begin the last week in November. In that month alone, NWC was forced (1) to prepare for a three week trial; (2) to draft a Motion to Strike Unique's improperly-reasserted $2 million counter-claim; (3) to draft motions in limine regarding a host of irrelevant issues that had been

raised by the Rehes; (4) to draft proposed jury instructions, including the crafting of UFTA instructions that lacked a form instruction; (5) to draft the trial brief; (6) to review, and object to, the Rehes' late-produced documents; (7) to prepare the joint statement of evidence; (8) to subpoena witnesses; (9) to prepare all evidence binders and other supporting documents; (10) to meet with witnesses; and (11) to be present at the Tacoma Courthouse while the case trailed other cases set for trial with higher priorities. CP 706-713. Trial preparation for this case in the month of November was a full-time job for two attorneys and a paralegal.

Finally, the Rehes complain that the amount in controversy was insignificant compared to the amount awarded in fees. First, this is not true. NWC was awarded $216,000, including the amount owed and accumulated interest under the contract. CP 1028. NWC was awarded only slightly more than this amount – $270,000 – in attorney fees. CP 1029. The amount of fees awarded is not unduly disproportionate to the amount of the recovery.

Moreover, "[t]he size of the attorney fees in relation to the amount of the award is not in itself decisive" but is merely one factor for the Court's consideration. *Travis*, 111 Wn.2d at 409-10. In *Travis*, the

Appellate Court approved a fee award that was "much larger than the damage award" (though the Court reversed in part on other grounds). *Id.*[30]

In short, the Rehes have failed to sustain their burden to show that the fee award to NWC was an abuse of discretion. NWC presented the Court with a proportional model for the segregation of its time that was consistent with case law and based on the testimony time spent at trial on the various claims. NWC also presented detailed billing records of the work performed on this case. The Court was well within its discretion in adopting NWC's proportional model, as modified, to calculate the award to NWC.' The Rehes' cross-appeal should be denied.

IV. CONCLUSION

The trial court failed to employ the proper legal standards in ruling on the claim of corporate disregard. It intentionally and unequivocally disregarded the fact that the Rehes gutted Unique of the 38th Avenue Lot after the suit was commenced, apparently in the mistaken belief that an UFTA claim alone was the sole remedy for that act. Further, the trial court improperly applied the relevant "intent" standard, and for this reason its finding that the Rehes' regular diversion of corporate assets was not

[30] A corollary to this argument is the Rehes' argument that NWC's contract claim was "relatively straight forward", implying that it should have been inexpensive to litigate. *Response* at 45. This conclusion is contradicted by the hard data regarding trial duration and numbers of exhibits, as well as the litany of abuses by the Rehes. *See* discussion, *supra* at pages 44-47.

"intended" to evade a duty is not based on substantial evidence. Finally, the trial court failed to employ the proper standard under Washington law that equates the element of an "unjustified loss" with an "effect on a creditor's ability to recover a judgment." Compounding its error, the trial court then awarded the Rehes fees spent on the other defendants' unsuccessful defense of the separate, and separable, breach of contract and UFTA claims. For these reasons, the trial court's judgment on the corporate disregard claim and related fee award should be reversed, and this Court should remand with instructions to enter judgment on behalf of NWC, and against the Rehes, on the issue of corporate disregard, and for an award of legal fees for that claim.

In contrast, the trial court's award of fees to NWC, based upon NWC's detailed records and its proportional segregation model based on time spent on various issues at trial, was not an abuse of discretion and should be upheld.

RESPECTFULLY SUBMITTED this 3rd day of April, 2013.

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CERTIFICATE OF SERVICE

I hereby certify that I caused to be served on April 3, 2013 a true and correct copy of the foregoing document to the counsel of record listed below, via the method indicated:

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