

No. 74808-4

COURT OF APPEALS FOR THE STATE OF WASHINGTON,
DIVISION I

PHILIP HOLROYD, an individual; and on behalf of BRET'S
INDEPENDENT, LLC, a limited liability company,

Appellants,

v.

BRET HARTMAN, an individual,

Respondent.

FILED
Jun 27, 2016
Court of Appeals
Division I
State of Washington

APPELLANTS' OPENING BRIEF

David C. Tingstad, WSBA # 26152
Jonathan P. McQuade, WSBA # 37214
BERESFORD BOOTH PLLC
145 3rd Avenue South
Edmonds, WA 98020
Attorneys for Appellants

George Jay Jensen, WSBA # 31655
John Scott Hicks, WSBA # 13938
BALLARD LAW GROUP PLLC
5215 Ballard Ave NW Suite 6
Seattle, Washington 98107-4838
Attorneys for Appellants

Mona K. McPhee, WSBA # 30305
Desh International & Business Law
11400 SE 8th Street, Suite 260
Bellevue, WA 98004
Attorneys for Respondent

Marianne Kathryn Jones, WSBA # 21034
Attorney at Law
11819 NE 34th St.
Bellevue, WA 98005-1235
Attorneys for Respondent

TABLE OF CONTENTS

I. INTRODUCTION.....	1
II. ASSIGNMENTS OF ERROR.....	3
III. STATEMENT OF THE CASE	4
A. Formation of Bret’s Independent, LLC.	4
A. Hartman Mismanages Bret’s Independent LLC from 2008 through 2011.....	7
B. Hartman Does Not Wind Up the Business. Instead Hartman Transfers the Bret’s Independent Assets to His Own Company	10
C. Procedural Posture.	12
IV. ARGUMENT.....	14
A. The Court Reviews Summary Judgment Orders De Novo.....	14
B. The Trial Court Improperly Dismissed Bret’s Independent’s Derivative Claim.	15
1. Holroyd Had Standing to Bring the Derivative Suit.	15
2. The Derivative Suit is Not Time-Barred.....	16
C. The Trial Court Should Not Have Dismissed Holroyd’s Contract Claim as a Matter of Law.	19
D. Whether Hartman Breached His Fiduciary Duty is an Issue of Fact. 21	
1. Hartman Owes a Fiduciary Duty to both the LLC and to Holroyd. 21	
2. As Manager, Hartman Breached His Fiduciary Duty to Holroyd By Making Unauthorized Guaranteed Payments to Himself, Making Disproportionate Distributions, and Failing to Properly Wind Up the Company.	22
3. Hartman Breached His Fiduciary Duty By Transferring the LLC Assets to Bret’s Independent Without Consideration.	24

E. Bret's Independent and Holroyd are Entitled to Attorneys' Fees and Costs	26
V. CONCLUSION	26

TABLE OF AUTHORITIES

CASES

Afoa v. Port of Seattle, 160 Wn. App. 234, 238, 247 P.3d 482 (2011) --- 21

Atherton Condo. Apartment-Owners Ass'n Bd. of Directors v. Blume Dev. Co., 115 Wn.2d 506, 516, 799 P.2d 250 (1990)----- 15

Bishop of Victoria Corp. Sole v. Corporate Bus. Park, LLC, 138 Wn. App. 443, 456, 158 P.3d 1183 (2007) ----- 22

Burke v. Hill, 190 Wn. App. 897, 900, 361 P.3d 195 (2015) ----- 18

Chadwick Farms Owners Ass'n v. FHC LLC, 166 Wn.2d 178, 201, 207 P.3d 1251 (2009)----- 23

Dragt v. Dragt/DeTray, LLC, 139 Wn. App. 560, 575, 161 P.3d 473 (2007)----- 21, 22

Go2Net, Inc. v. C I Host, Inc., 115 Wn. App. 73, 85, 60 P.3d 1245 (2003) ----- 19

Horne v. Aune, 130 Wn. App. 183, 200, 121 P.3d 1227 (2005)----- 22

Johnson v. Spokane to Sandpoint, LLC, 176 Wn. App. 453, 457-58, 309 P.3d 528 (2013) ----- 15

Lang v. Hougan, 136 Wn. App. 708, 718, 150 P.3d 622 (2007)----- 24

Lokan & Assocs., Inc. v. American Beef Processing, LLC, 177 Wn. App. 490, 499, 311 P.3d 1285 (2013) ----- 19

Mahoney v. Shinpoch, 107 Wn.2d 679, 683, 732 P.2d 510 (1987) ----- 14

Peninsula Truck Lines, Inc. v. Tooker, 63 Wn.2d 724, 388 P.2d 958 (1964)----- 14

Powers v. W.B. Mobile Servs., Inc., 182 Wn. 2d 159, 164, 339 P.3d 173 (2014)----- 14

Sherron Assocs. Loan Fund V (Mars Hotel) LLC v. Saucier, 157 Wn. App. 357, 362, 237 P.3d 338 (2010) ----- 17, 24

<u>Walston v. Boeing Co.</u> , 181 Wn.2d 391, 395, 334 P.3d 519 (2014) -----	14
<u>Young v. Key Pharm., Inc.</u> , 112 Wn.2d 216, 225, 770 P.2d 182 (1989) -	14

STATUTES

I.R.C. §707(c) -----	8
RCW 23B.14.050 -----	18
RCW 23B.14.220 -----	18
RCW 25.15.150 -----	21
RCW 25.15.273 -----	17
RCW 25.15.293 -----	17
RCW 25.15.295 -----	11, 23
RCW 25.15.298 -----	17
RCW 25.15.300 -----	23
RCW 25.15.303 -----	16, 17, 18, 27
RCW 25.15.370 -----	16
RCW 25.15.401 -----	26
RCW 4.84.030 -----	26

OTHER AUTHORITIES

MAURICE, <u>Operational Overview of the Washington Limited Liability Company Act</u> , 30 Gonz. L. Rev. 183, 200 (1994/95)-----	22
---	----

RULES

CR 56-----	14
------------	----

I. INTRODUCTION

In this appeal, the Court will review the trial court's summary judgment dismissal of an LLC's derivative action filed against its manager/50% member, because the manager, while the LLC was insolvent, paid himself hundreds of thousands in guaranteed payments and then after dissolution, transferred the LLC assets to his personal corporation for no consideration. The Court will also review whether the claims of the other member, a member that had no knowledge of the manager's actions, should have proceeded to trial or were also properly dismissed by summary judgment.

Appellant Phillip Holroyd and Respondent Bret Hartman formed Bret's Independent, LLC, an automotive repair shop operating in North Seattle. Hartman and Holroyd were 50/50 members, and agreed to share management of the company. The parties executed an "operation agreement" that defined the parties' rights and responsibilities as both members and managers of Bret's Independent.

In 2008, after many years co-managing the LLC, Holroyd's mother had a heart attack and stroke, forcing Holroyd to cease the day-to-day management of the repair shop so he could care for his mother. Hartman continued managing Bret's Independent in Holroyd's absence.

Once Hartman took over management of Bret's Independent, the business started to fail. Hartman claims the down economy sunk the business, but Hartman likely caused the business decline.

From 2008 to 2011, Hartman paid himself \$263,288.00 in "guaranteed payments" above and beyond the distributions he paid to himself during these years. In contrast, Holroyd received no guaranteed payments and less in distributions than Hartman. The guaranteed payments and unequal distributions breach the terms of the Bret's Independent LLC operating agreement.

Hartman also failed to pay the LLC's creditors while continuing to pay these guaranteed payments above and beyond the LLC distributions. This included failing to pay Wells Fargo Bank, the original plaintiff/creditor in this action.

In November of 2011, Hartman caused Bret's Independent to cease operations. Hartman did not notify Holroyd, nor did he wind up the LLC affairs. Instead, and without Holroyd's knowledge or authority, Hartman transferred all of Bret's Independent's assets to a newly-formed corporation – Bret's Inc. – a corporation he owned wholly by Hartman and his son. The LLC received no consideration for its assets.

Upon learning of Hartman's actions, Holroyd filed a derivative action on behalf of the LLC and direct claims against Hartman for breach of contract and breach of fiduciary duty.

The trial court dismissed Bret's Independent's derivative action against Hartman on summary judgment. Further, and although the parties interpreted the parties' operating agreement differently, the trial court also dismissed Holroyd's contractual claims on summary judgment. Finally, the court dismissed Holroyd's direct claims against Hartman for breach of fiduciary duty and conversion of LLC assets.

The trial court erred by dismissing on summary judgment the LLC's derivative action, Holroyd's claim for breach of contract, Holroyd's claim for breach of loyalty, and Holroyd's conversion claims. There remain genuine issues of material fact that should be resolved by the fact-finder, not during a hearing on summary judgment. Hartman respectfully requests that this Court remand the matter to the trial court, so the fact-finder can resolve the genuine issues of material fact concerning Hartman's activities as manager of Bret's Independent, LLC.

II. ASSIGNMENTS OF ERROR

1. Whether the trial court erred by dismissing the LLC's derivative claim as a matter of law when it is undisputed that Hartman, as manager of the LLC, unilaterally decided to pay himself several hundred

thousand in guaranteed payments and distributions when the LLC was insolvent, and distributed the LLC's assets to his own corporation without consideration.

2. Whether the trial court erred by determining, as a matter of law, that Hartman did not breach the parties' operating agreement when Hartman paid himself guaranteed payments and unequal distributions in violation of the parties' operating agreement.

3. Whether the trial court erred by determining that Holroyd's claim for breach of fiduciary duty fails as a matter of law when Hartman paid himself several hundred thousand in guaranteed payments, made unequal distributions to the members, and converted the LLC assets by transferring the LLC assets to Hartman's own corporation for no consideration.

III. STATEMENT OF THE CASE

A. Formation of Bret's Independent, LLC.

On February 16, 1996, Bret Hartman and Phillip Holroyd formed Bret's Independent, LLC, a manager-managed limited liability company with the primary purpose of repairing and servicing Japanese vehicles. CP 572-73. From 1996 to 2011, Bret's Independent operated an auto-repair shop in the Lynwood area. CP 232.

From the date of formation, Hartman and Holroyd each held 50% of the LLC membership interests and were co-managers of the manager-managed LLC. CP 118; CP 120 – 121; CP 232. Hartman and Holroyd each held 50% of the membership interests of the company. CP 120 – 21. The parties dispute, however, whether Hartman and Holroyd were co-managers for the business’s entire operation. Hartman first claimed Holroyd “abandoned” his interest in the LLC. CP 84. In a subsequent motion, Holroyd claims it is “undisputed” that Holroyd was an equal owner and manager from the date of inception until the day operations ceased. CP 16 at ¶4; CP 1175 at ¶4¹; CP 1182.

Hartman and Holroyd also dispute when they executed an LLC operating agreement and the meaning and intent of that agreement. CP 120-21; CP 216.²

¹ Here, Hartman changes his story. In his initial motion for summary judgment, he claims “Holroyd abandoned his membership interest in Bret’s Independent.” CP 84. In Hartman’s second motion for summary judgment, Hartman claims that “[i]t is undisputed that Holroyd was still an equal owner and manager of the business during the entire period of 4+ years he claimed to have been taking care of his mother.” CP 1182 (emphasis added).

² Hartman first tendered an “Operation Agreement” during Holroyd’s deposition. As to that agreement, Holroyd claims that his signature was forged. CP 232. A 2nd Operation Agreement was tendered much later. It had a different signature, a different date, and had a notary block. Aside from that, the terms were identical to the first agreement.

Hartman testifies, and Holroyd agrees, that there is no other written agreement detailing Hartman's and Holroyd's duties as members and managers of Bret's Independent. CP 206.

An attorney did not draft the "operation agreement," unfortunately. Accordingly, many of the terms do not apply to a limited liability company. For example, the agreement states that the parties have formed a "Limited Partnership... subject to the provisions of the Washington State Limited Partnership Act." CP 120. Further, the agreement states that Hartman and Holroyd are the "General Partners" of the Bret's Independent limited liability company. CP 121.

Despite the lack of clarity, two provisions of this operating agreement are pertinent. First, the operating agreement provides that distributions would be made equally between Hartman and Holroyd:

The General Partner³ may make distributions annually or more frequently if there is excess cash on hand after providing for appropriate expenses and liabilities. Such interim distributions are allocated to each Partner according to the percentage of Partnership.(50/50%)

CP 120. Second, the operating agreement explicitly states that:

Financial agreements shall require the agreement and signatures of both Partners.

CP 121 (emphasis added).

³ Hartman and Holroyd are both defined as "General Partners." CP 121.

Although it is unclear whether Hartman and Holroyd considered themselves partners, members, or managers, or if they understood the legal difference between the three, there is no dispute that until 2008, Hartman and Holroyd both participated in management, draws, and distributions from the company.

A. Hartman Mismanages Bret's Independent LLC from 2008 through 2011.

In 2008, Holroyd's mother had a heart attack and stroke and needed full time care. CP 233. Holroyd claims he and Hartman agreed that Holroyd should act as her full-time caregiver. CP 217.⁴

Holroyd and Hartman disagree whether Hartman would manage Bret's Independent in Holroyd's absence. As stated above, Hartman initially claimed Holroyd "abandoned" the LLC. CP 84.⁵ Later, Hartman stated it was undisputed that Holroyd was still a co-manager. CP 1182.

In either event, no written agreements were executed regarding the ongoing management and financial responsibilities of the LLC after 2008. CP 217. There is also no dispute, and regardless of their actual legal

⁴ This seemed especially appropriate given that Bret's Independent still owed Irene Holroyd \$308,412.11 from a 2001 loan Ms. Holroyd made to the company. CP 232 at ¶5; CP 796.

⁵ Hartman uses this term "abandoned" throughout his pleading. A LLC member cannot "abandon" his or her membership interest. Rather, a member can disassociate from the LLC, as set forth in RCW 25.15.131. Hartman never claims there was an event of disassociation.

rights, Hartman managed all aspects of the business from 2008 until Bret's Independent ceased operations in November 2011. CP 233 – 34.

In early 2008, and right around the time Holroyd left to care for his mother, Bret's Independent started defaulting on its financial obligations to creditors. CP 207 at ¶5. According to Hartman, Bret's Independent's financial difficulties worsened from 2008 to 2011, such that in September 2011, Bret's Independent no longer had accounts receivables and "Bret's Independent was undisputedly upside down in its value at the time operation ceased." CP 207 at ¶6.

During this time when Bret's Independent couldn't meet its financial obligations, and "Bret's Independent was saddled with very significant debts to many creditors and the IRS" (CP 207), Hartman unilaterally decided to pay himself "guaranteed payments"⁶ each year ranging from \$42,000.00 to \$88,000.00 a year. CP 834 – 837. These guaranteed payments were not discussed with Holroyd, nor did Hartman and Holroyd ever agree to this financial arrangement.

In total, Hartman made \$263,288.00 in guaranteed payments to himself from 2008-2011. Holroyd received nothing.

⁶ If a limited liability company makes fixed payments for services or the use of capital to a member, and if those payments are not dependent upon the limited liability company's income, the payments are deemed "guaranteed payments." See I.R.C. §707(c).

<u>Year</u>	<u>Hartman</u>	<u>Holroyd</u>
2008	\$62,200.00	\$0.00
2009	\$70,579.00	\$0.00
2010	\$88,187.00	\$0.00
2011	\$42,322.00	\$0.00
Total:	\$263,288.00	\$0.00

CP 834-837.⁷ In 2011, when Hartman testified that “Bret’s Independent was undisputedly upside down in value,” Hartman unilaterally caused the LLC to distribute \$27,232.00 to Hartman (in addition to the \$42,322.00 guaranteed payment). Although an equal member, Holroyd received nothing. CP 867.

Hartman mismanaged the LLC in other ways. In 2008, the first year Hartman managed the LLC on his own, Hartman allowed the LLC’s registration to lapse. CP 217. Hartman justified this by testifying that Bret’s Independent lacked the \$63.00 to pay the Washington LLC registration fee. CP 380. In 2008, however, Hartman caused the LLC to pay him \$62,200.00 in guaranteed payments and an additional \$51,642.00 in distributions. CP 380. As a result of Hartman’s failure to pay a \$63.00

⁷ Each year, Hartman also caused the LLC to pay for his health insurance. CP 363.

fee, the State administratively dissolved the LLC on June 2, 2008. CP 647.

In 2008 and 2009, Bret's Independent also began defaulting on its equipment lease payments. (In 2009, Hartman paid himself \$70,579.00 in guaranteed payments.) CP 774. Hartman also claims that in 2011, the equipment lender, First Sound Bank, demanded full payment of the \$6,735.89 owing or it would foreclose on the LLC's equipment.

Similarly, in each year that Hartman managed the business, Bret's Independent defaulted on its L&I obligations as well as IRS payments owing on employment and withholding taxes. CP 774-75.

According to Hartman, Bret's Independent ceased operations in or around November 2011 due to the mounting debt. CP 207.

At no time in 2008 through 2011, did Hartman inform Holroyd that the State had administratively dissolved Bret's Independent or that there were significant creditor claims against the business. CP 217.

B. Hartman Does Not Wind Up the Business. Instead Hartman Transfers the Bret's Independent Assets to His Own Company

When Bret's Independent ceased operations, Hartman never notified Holroyd that Bret's Independent was closing its doors. CP 16. Further, there is no evidence that Hartman contacted any creditors or

otherwise wound up the activities pursuant to the terms of RCW 25.15.295.⁸ CP 84.

Instead, just before Bret's Independent ceased operations, Hartman formed Bret's Inc., a corporation owned wholly by Hartman and his son. CP 984 - 86. Bret's Inc. is an automotive repair company, offering the same services as Bret's Independent. Nearly all of the assets of Bret's Independent, including certain lifts, auto repair equipment, the website, goodwill and the Bret's Independent clients, were transferred to Hartman's new corporation. CP 579 - 580. Neither Bret's Independent nor Holroyd received any consideration for the transfer. Id.

Hartman did settle one LLC claim in December 2011. First Sound Bank had a secured interest in some of the LLC equipment. Hartman claims Bret's Inc. paid \$4,000.00 to First Sound Bank in exchange for a release of First Sound's security interest in certain Bret's Independent assets. CP 158. Those assets were then transferred free and clear to Bret's Inc. Id. There is a factual question as to the funding source of that

⁸ The former RCW 25.15.295(2) provides in part: "Upon dissolution of a limited liability company...the persons winding up the limited liability company's affairs may...close the limited liability company's business, dispose of and convey the limited liability company's business, dispose of and convey the limited liability company's property, discharge or make reasonable provision for the limited liability company's liabilities, and distribute to the members any remaining assets of the limited liability company."

payment. Like with all decisions concerning the LLC after 2008, Hartman did not consult Holroyd. CP 579 -80.

Hartman never attempted to settle the outstanding Wells Fargo lines of credit issued to Bret's Independent and guaranteed by Hartman and Holroyd, however. CP 551 – 58.⁹ Accordingly, Wells Fargo commenced this lawsuit. Id.

C. Procedural Posture.

On or around January 23, 2012, Wells Fargo filed suit against Bret's Independent, Hartman, and Holroyd for breach of contract related to delinquent business loans issued to Bret's Independent and guaranteed by Hartman and Holroyd. CP 551 – 58.

On November 28, 2012, Holroyd filed a cross-claim against Hartman for breach of fiduciary duty, breach of contract, violation of the Washington LLC Act, as well as a derivative action on behalf of Bret's Independent. CP 15 – 20.

On December 24, 2013, Hartman moved for summary judgment regarding Holroyd's cross-claims as well as the LLC's derivative claim. CP 71 – 93. Hartman claimed that the statute of limitations barred the LLC's derivative action because the State administratively dissolved the

⁹ Hartman makes no claim that he attempted to settle the Wells Fargo debt or that he otherwise attempted to transfer any LLC assets to Wells Fargo to settle all or a portion of the debt.

LLC. CP 79. Further, Hartman claimed that Holroyd could not bring an action on behalf of the LLC because he was not a “proper party in a derivative action.” CP 80.

On January 22, 2014, and with no findings entered, the trial court dismissed the LLC’s derivative action. CP 8-9. The trial court denied, however, Hartman’s motion for summary judgment on Holroyd’s claims for breach of contract, breach of fiduciary duty, and LLC violations under the statute. Judge Ellis determined that issues of fact remained. CP 8 - 9.¹⁰

Two years later, Hartman sought summary judgment on Holroyd’s cross-claims. On January 8, 2016, the trial court dismissed Holroyd’s cross claims by summary judgment. CP 12 – 14. Judge Appel entered no findings in his summary judgment order. *Id.* Holroyd moved for reconsideration but Judge Appel denied the motion. CP 10 – 11; CP 1320 - 28.

On February 26, 2016 Holroyd filed a Notice of Appeal seeking review of the dismissal of his cross-claims against Hartman as well as the derivative claims brought on behalf of Bret’s Independent. CP 1.

¹⁰ Wells Fargo’s claims were dismissed as time-barred. CP 5.

IV. ARGUMENT

A. The Court Reviews Summary Judgment Orders De Novo.

“The standard of review on appeal of a summary judgment order is de novo; that is, the appellate court conducts the same inquiry as the trial court.” Mahoney v. Shinpoch, 107 Wn.2d 679, 683, 732 P.2d 510 (1987).

Courts grant summary judgment if there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. CR 56. The court must consider facts and inferences in a light most favorable to the nonmoving parties. Powers v. W.B. Mobile Servs., Inc., 182 Wn. 2d 159, 164, 339 P.3d 173 (2014). Summary judgment is granted if, given the evidence, reasonable persons could reach only one conclusion. Walston v. Boeing Co., 181 Wn.2d 391, 395, 334 P.3d 519 (2014).

Before issues of law are considered, the moving party must first prove there is no issue of material fact. Young v. Key Pharm., Inc., 112 Wn.2d 216, 225, 770 P.2d 182 (1989); Peninsula Truck Lines, Inc. v. Tooker, 63 Wn.2d 724, 388 P.2d 958 (1964) (plaintiff, as party moving for summary judgment, had burden of showing that there was no genuine issue of facts, irrespective of where burden would rest at trial). “The moving party is held to a strict standard. Any doubts as to the existence of a genuine issue of material fact is resolved against the moving party.”

Atherton Condo. Apartment-Owners Ass'n Bd. of Directors v. Blume Dev. Co., 115 Wn.2d 506, 516, 799 P.2d 250 (1990). “Where different competing inferences may be drawn from the evidence, the issue must be resolved by the trier of fact.” Johnson v. Spokane to Sandpoint, LLC, 176 Wn. App. 453, 457-58, 309 P.3d 528 (2013).

Here, Hartman moved for summary judgment. Accordingly, this Court should review the facts and inferences in a light most favorable to Holroyd, the nonmoving party in this case.

B. The Trial Court Improperly Dismissed Bret’s Independent’s Derivative Claim.

It is unclear why the trial court dismissed Bret’s Independent’s derivative action. Hartman does not address the merits of the claim, instead arguing that Holroyd lacked authority to bring the suit, and in any event, the statute of limitations barred a derivative action. Both arguments contravene the express terms of the Washington Limited Liability Company Act and the case law concerning derivative actions.

1. Holroyd Had Standing to Bring the Derivative Suit.

“A member may bring an action in the superior courts in the right of a limited liability company to recover a judgment in its favor if managers or members with authority to do so have refused to bring the

action or if an effort to cause those managers or members to bring the action is not likely to succeed.” RCW 25.15.370.¹¹

Here, there is no dispute that Holroyd was both a member and manager of Bret’s Independent, LLC at the time of the alleged actions and at the time the suit was brought. As Bret’s Independent is a manager-managed limited liability company, however, Holroyd had two options to meet the second prong of the statute: (1) make a demand upon Hartman to bring a derivative suit; or (2) make a demand upon himself to bring the derivative suit. Although there is a factual dispute as to whether Hartman continued on as a manager, there can be no doubt that any demand on Hartman to bring suit against himself would be futile. Accordingly, Holroyd filed a derivative suit on Bret’s Independent’s behalf as authorized by the statute.

2. The Derivative Suit is Not Time-Barred.

Further, Hartman’s claim that the statute of limitations bars Bret’s Independent’s derivative suit also fails.

The administrative dissolution of an entity does not terminate the entity’s existence for all purposes. Under RCW 25.15.303, an

¹¹ A member may bring an action in the superior courts in the right of a limited liability company to recover a judgment in its favor if managers or members with authority to do so have refused to bring the action or if an effort to cause those managers or members to bring the action is not likely to succeed. See also, RCW 25.15.370 *repealed by* Laws 2015, ch. 188, §108, effective 1/1/16.

administratively dissolved limited liability company continues to exist and may carry on any business necessary and appropriate to wind up and liquidate its affairs. RCW 25.15.303¹²; see also, Sherron Assocs. Loan Fund V (Mars Hotel) LLC v. Saucier, 157 Wn. App. 357, 362, 237 P.3d 338 (2010) (“A dissolved, but not yet canceled, LLC could sue and be sued within the time limits of the statute.”)

RCW 25.15.303 allows a dissolved LLC, including an administratively dissolved LLC, to file a certificate of dissolution. See RCW 25.15.303 (“the dissolution of a limited liability company does not take away or impair any remedy available to or against that limited liability company, its managers, or its members for any right or claim existing, or any liability incurred at any time, whether prior to or after dissolution, unless the limited liability company has filed a certificate of dissolution.”) Accordingly, the three-year statute of limitations begins to run only after a certificate of dissolution is filed.

¹² “Except as provided in RCW 25.15.298, the dissolution of a limited liability company does not take away or impair any remedy available to or against that limited liability company, its managers, or its members for any right or claim existing, or any liability incurred at any time, whether prior to or after dissolution, unless the limited liability company has filed a certificate of dissolution under RCW 25.15.273, that has not been revoked under RCW 25.15.293, and an action or other proceeding thereon is not commenced within three years after the filing of the certificate of dissolution. Such an action or proceeding by or against the limited liability company may be prosecuted or defended by the limited liability company in its own name.”

Although the case involves a corporate entity, this Court's holding in Burke v. Hill is instructive. In Burke, the State administratively dissolved Innerspace, Inc. in 2008 for failing to file its annual report and pay its licensing fee. Burke v. Hill, 190 Wn. App. 897, 900, 361 P.3d 195 (2015). Innerspace, Inc. filed suit against Hill and another party in 2012. When Innerspace, Inc. did not reinstate the corporation in 2013, defendant Hill moved for summary judgment claiming "Innerspace's failure to apply for reinstatement of the corporation during RCW 23B.14.220's five-year reinstatement period rendered it irrevocably dissolved and without standing to maintain an action." Id. at 901. The trial court agreed, granting Hill's summary judgment motion. Id.

Division One overturned the trial court, holding that "[c]orporate dissolution does not prevent the commencement of a proceeding by or against a corporation in its corporate name. Nor does it abate or suspend a proceeding pending by or against the corporation on the effective date of dissolution." Id. (citing RCW 23B.14.050(2)(e) and (f)).

Bret's Independent did not file a certificate of dissolution. Accordingly, the certificate of formation has not been cancelled. Whether or not the LLC sought reinstatement while the lawsuit was ongoing is irrelevant per RCW 25.15.303 and this Court's holding in Burke.

As Hartman did not address the merits of Bret's Independent's derivative claim, but only focused on potential procedural bars, the derivative claim should not have been dismissed as a matter of law. First, Holroyd was a member and authorized to bring a derivative action. Second, Holroyd timely-filed Bret's Independent's derivative claim. Accordingly, the matter should be remanded to the trial court for determination on the merits.

C. The Trial Court Should Not Have Dismissed Holroyd's Contract Claim as a Matter of Law.

Summary judgment as to a contractual claim is only appropriate when “(1) the interpretation does not depend on the use of extrinsic evidence, or (2) only one reasonable inference can be drawn from the extrinsic evidence.” Lokan & Assocs., Inc. v. American Beef Processing, LLC, 177 Wn. App. 490, 499, 311 P.3d 1285 (2013) (citation omitted). In other words, “the parties' written contract, viewed in light of the parties' other objective manifestations, has only one reasonable meaning.” Go2Net, Inc. v. C I Host, Inc., 115 Wn. App. 73, 85, 60 P.3d 1245 (2003).

Here, the parties executed an “Operation [sic] Agreement for Bret's Independent, LLC” that required that distributions be made equally between Hartman and Holroyd:

The General Partner may make distributions annually or more frequently if there is excess cash on hand after

providing for appropriate expenses and liabilities. Such interim distributions are allocated to each Partner according to the percentage of Partnership. (50/50%)

CP 120. Second, the operating agreement explicitly states that:

Financial agreements shall require the agreement and signatures of both Partners.

CP 121 (emphasis added).

There is no dispute that from 2008 – 2011, Hartman failed to make equal distributions to the two members as required by the operating agreement. Instead, Hartman made unequal distributions to the members, as well as including paying himself \$263,288.00 in guaranteed payments during that time.

More importantly, Hartman did not abide by the contractual terms and seek permission or written agreement from Holroyd to make these guaranteed payments. Further, Hartman did not seek permission or written agreement from Holroyd to settle claims with creditors. Most importantly, Hartman never sought permission or written agreement to transfer the assets of Bret's Independent to Bret's Inc. for no consideration.

These actions constitute Hartman's breach of the Operation Agreement for Bret's Independent, LLC. At a minimum, there is an issue of material fact as to whether Hartman breached the express terms of the agreement.

D. Whether Hartman Breached His Fiduciary Duty is an Issue of Fact.

As a matter of law, Hartman owed a fiduciary duty to both the LLC and to Holroyd as a member of the LLC. The extent of Hartman's duty to Holroyd has not been defined. When the existence or extent of duty depends on proof of certain facts, summary judgment is inappropriate. Afoa v. Port of Seattle, 160 Wn. App. 234, 238, 247 P.3d 482 (2011). Here, the trial court erred by determining, as a matter of law, that Hartman did not breach his fiduciary duty owing to Holroyd.

1. Hartman Owes a Fiduciary Duty to both the LLC and to Holroyd.

Bret's Independent is a manager-managed limited liability company. In Washington, a manager-managed limited liability company grants one or more manager the right to manage the activities of the company and bind the company with regard to matters in the ordinary course of business. See RCW 25.15.150(2)(a). A manager holds office as manager unless the manager has been removed, resigned, or until a successor has been elected. RCW 25.15.150(2)(c).

"In a manager-managed limited liability company, only those members serving as managers owe fiduciary duties." Dragt v. Dragt/DeTray, LLC, 139 Wn. App. 560, 575, 161 P.3d 473 (2007). LLC

managers owe the LLC entity itself and its members fiduciary duties analogous to those owed in a partnership. Bishop of Victoria Corp. Sole v. Corporate Bus. Park, LLC, 138 Wn. App. 443, 456, 158 P.3d 1183 (2007) (citing MAURICE, Operational Overview of the Washington Limited Liability Company Act, 30 Gonz. L. Rev. 183, 200 (1994/95)). One of these duties is the duty of loyalty, which requires the fiduciary to avoid “secret profits, self-dealing, and conflicts of interest.” Horne v. Aune, 130 Wn. App. 183, 200, 121 P.3d 1227 (2005).

Here, Hartman does not deny he was a manager of Bret’s Independent, LLC. Prior to 2008, Hartman and Holroyd managed the LLC together. In 2008, and after Holroyd focused his time caring for his mother, Holroyd claims that he and Hartman agreed that Hartman would manage Bret’s Independent going forward. In either event, Hartman has been the acting manager of Bret’s Independent from 2008 through this lawsuit.

As the manager from 2008 - 2011, and as the court determined in Dragt and Bishop Victoria, Hartman owed fiduciary duties to both the LLC and to Holroyd, individually, in his capacity as a member of the LLC.

2. As Manager, Hartman Breached His Fiduciary Duty to Holroyd By Making Unauthorized Guaranteed Payments to

Himself, Making Disproportionate Distributions, and
Failing to Properly Wind Up the Company.

As manager of the company, and as stated above, Hartman had a fiduciary duty to the other member of the LLC – Holroyd. Whether Hartman breached his duty to Holroyd is an issue of fact that should be determined at trial.

Hartman first breached his fiduciary duty by unilaterally deciding to make \$263,288.00 in guaranteed payments to himself from 2008 – 2011, the years he managed the LLC without Holroyd’s assistance. These payments were not discussed with, authorized by, or agreed to by Holroyd. Rather, these payments reduced the profits of the company and minimized distributions available for Holroyd.

Further, by failing to wind up the company pursuant to the provisions of RCW 25.15.295, Hartman exposed Holroyd to liability under the former RCW 25.15.300(2):

Any person winding up a limited liability company’s affairs who has complied with this section is not personally liable to the claimants of the dissolved limited liability company by reason of such person’s actions in winding up the limited liability company.

The corollary is that the managers may be personally liable if they don’t wind up the entity properly. See Chadwick Farms Owners Ass’n v. FHC LLC, 166 Wn.2d 178, 201, 207 P.3d 1251 (2009).

Hartman made no attempt to wind up the affairs of Bret's Independent pursuant to the statute. Instead, Hartman transferred the company assets to a new entity owned solely by Hartman and his son. This denied Holroyd his right of ownership in the company assets. See Sherron Assocs. Loan Fund V (Mars Hotel) LLC v. Saucier, 157 Wn. App. 357, 363, 237 P.3d 338 (2010) ("In the absence of a governing statute, title to LLC-owned property passes to the owner of the canceled LLC subject to creditor claims.")

3. Hartman Breached His Fiduciary Duty By Transferring the LLC Assets to Bret's Independent Without Consideration.

Finally, Hartman does not deny that he transferred all of Bret's Independent assets, including the lifts and other auto repair equipment, website, clients, remaining cash, and goodwill, to his personal corporation for no consideration.

Conversion is the unjustified, willful interference with a chattel which deprives a person entitled to the property of possession. Lang v. Hougan, 136 Wn. App. 708, 718, 150 P.3d 622 (2007). "[I]f a director or officer converts corporate property, she has breached that duty to operate in good faith." Id.

The court's reasoning in Lang applies here. In that case, Lang and Hougan were equal owners of a property management corporation.

Hougan performed most of the day-to-day management activities of the corporation. Id. at 712. At some point, the relationship soured and a mutual split of the assets could not be reached. Without Lang's approval, Hougan contacted the company's clients and encouraged them to transfer their business to her new company. Id. at 713. Many clients agreed to do so. The trial court determined that because there was no non-compete, and because Lang had allowed his broker license to lapse, that there was no breach of fiduciary duty or conversion. Id. at 717.

Division Two disagreed, finding that "Hougan and Lang continued to have a fiduciary duty to each other and to LPM while the business was breaking apart." Id. at 718. Further, Division Two held that:

Courts have long recognized that a business's customer base, or "goodwill," is a commodity on which one may place a monetary value. To the extent that Hougan solicited LPM's clients without giving Lang fair compensation, we hold that she converted a corporate asset and hereby breached her fiduciary duty.

Id. at 719.

Here, Hartman simply took the LLC's lifts, tools, inventory, website, clients, and goodwill, without consulting Hartman. Due to Hartman's actions, factual issues remain as to whether a conversion occurred, as well as the amount and extent of Holroyd's damages, including a correct valuation of the assets Hartman improperly transferred

to Bret's Inc. Accordingly, it was error to grant summary judgment as to Holroyd's breach of fiduciary duty and conversion claims.

E. Bret's Independent and Holroyd are Entitled to Attorneys' Fees and Costs

In a derivative action, the court may award the plaintiff reasonable expenses in a derivative action. RCW 25.15.401. Similarly, should Holroyd succeed on his breach of contract, breach of fiduciary duty, and conversion claims once the matter is remanded, Holroyd will be entitled to his costs and disbursements. RCW 4.84.030.

Here, Holroyd has brought a derivative action on behalf of Bret's Independent, LLC. Should he prevail at trial, he is entitled to his fees and costs for that action. Similarly, Holroyd would be entitled to his own costs and disbursements he expended in his direct actions against Hartman.

V. CONCLUSION

Given the factual disputes and claims in this case, summary dismissal was improper. First, the trial court dismissed Bret's Independent's derivative suit without findings. It can only be presumed the trial court accepted the Hartman's argument that Holroyd did not have standing to bring the suit, or that the derivative action was time-barred. Neither is correct as Hartman states that is "undisputed" that Holroyd was

a 50/50 member and manager through dissolution of the LLC. Further, under RCW 25.15.303, an administratively dissolved limited liability company continues to exist and may carry on any business necessary and appropriate to wind up and liquidate its affairs, including bringing derivative suits. The statute of limitations does not begin to run until the LLC files a certificate of dissolution. No certificate of dissolution was filed. Accordingly, the derivative suit is timely.

Further, the undisputed facts show that Hartman transferred all of Bret's Independent's assets to his own corporation for no consideration. Hartman transferred Bret's Independent's personal property, inventory, website, goodwill, and clients to his corporation without notifying Holroyd and more importantly, without paying Bret's Independent or his 50% co-member.

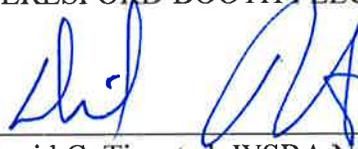
In addition to transferring these assets, and making unequal distributions favoring him, Hartman made over \$263,000.00 in "guaranteed payments" to himself while choosing not to pay creditor claims or make distributions to Holroyd. Hartman's actions making unequal distributions and guaranteed payments breached Hartman's fiduciary duty to Holroyd, and breached the LLC operating agreement.

Accordingly, this case should be remanded to the trial court to determine the nature and extent of Hartman's breach of contract, the

nature and extent of the conversion of Bret's Independent's assets, and why, through no cause of his own, Holroyd never received his share of the business distributions, property, and going concern value after Hartman's misappropriation of the company's assets.

DATED this 27th day of June, 2016.

BERESFORD BOOTH PLLC



David C. Tingstad, WSBA No. 26152
Jonathan P. McQuade, WSBA No. 37214
Attorneys for Appellants
145 Third Avenue So., Suite 200
Edmonds, WA 98020
Telephone 425-776-4100
davidt@beresfordlaw.com
jonathanm@beresfordlaw.com

PROOF OF SERVICE

Pursuant to the Rules of Appellate Procedure 18.5 and CR 5, I certify that on June 27, 2016, I filed this brief with the clerk of the court for the United States Court of Appeals Division I by the CM/ECF system. I also certify under the penalty of perjury that I served the foregoing document via regular mail, self-addressed postage prepaid and electronic mail on the interested persons as identified below:

George Jay Jensen
John Scott Hicks
BALLARD LAW GROUP PLLC
5215 Ballard Ave NW Suite 6
Seattle, WA 98107
Attorneys for Appellants
gjensen@ballardlawgroup.com
jhicks@ballardlawgroup.com

Mona K. McPhee
Desh International & Business Law
11400 SE 8th Street, Suite 260
Bellevue, WA 98004
Attorneys for Respondent
mmcphee@deshlaw.com

Marianne Kathryn Jones
11819 NE 34th St.
Bellevue, WA 98005
Attorneys for Respondent
mlaw@joneslawgroup.com

/s/David C. Tingstad 
David C. Tingstad, WSBA # 26152
Jonathan P. McQuade, WSBA # 37214
BERESFORD BOOTH PLLC
145 3rd Avenue South
Edmonds, WA 98020
Attorneys for Appellants