

FILED
COURT OF APPEALS

LEWIS & CLARK

NO. 35046-7-II

STATE

BY *yn*

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

HENRY DRAGT and JANE DRAGT, husband and wife,

Appellants,

v.

DRAGT/DETRAY L.L.C., a Washington limited liability company; and
E. PAUL DETRAY and PHYLLIS DETRAY and their marital
community,

Respondents.

BRIEF OF RESPONDENTS
E. PAUL DETRAY and PHYLLIS DETRAY

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I. RESPONDENTS' RESTATEMENT OF THE ISSUES

A. Issues pertaining to whether the Dragts had binding obligations to DeTray other than the invalid option provision in the LLC Agreement.

1. Did the trial court err in concluding that the Dragts were obligated to share the proceeds from the sale of their property with DeTray in the manner set forth in the LLC Agreement between the parties?

2. Are obligations to hold property for development and to share the proceeds from the sale of real property conceptually and legally distinct from an oral conveyance of an interest in real property?

3. Did the trial court err by finding that both Jane and Henry Dragt were bound by contractual obligations to hold their property for development and share the proceeds from the sale of their real property with DeTray?

4. Did the trial court's determination that the Dragts had agreed to hold their real property for development by DeTray depend on finding that the Dragts intended to convey an interest in the property to DeTray?

B. Issues related to the findings and conclusions that the parties modified the LLC Agreement.

5. Did the trial court err in finding that the parties agreed to modify the LLC Agreement on the basis of their subsequent behavior involving DeTray's payment of the Dragts' mortgage and DeTray's execution of a guarantee of the mortgage loan?

6. Is there clear and convincing evidence supporting a modification of the LLC Agreement when both the Dragts and DeTray executed loan documents providing benefits from DeTray to the Dragts related to the purpose of the LLC Agreement, but not required by the LLC Agreement?

7. Did the trial court err in finding that the modification of the LLC Agreement was supported by consideration?

8. Did the trial court err in finding that evidence of a course of conduct occurring after execution of the LLC Agreement can support a modification of the LLC Agreement?

9. Did the trial court err in concluding that the clause in the LLC Agreement barring oral amendments was unenforceable as a matter of law?

C. Other issues.

10. Did the trial court err in concluding that the Dragts breached the notice provision of the LLC Agreement by selling their real property, and permits and plans procured by DeTray, without notice to DeTray?

11. Did the trial court err in finding that the Dragts had an implied duty under the LLC Agreement to deal fairly with DeTray and act in good faith?

12. Did the trial court err in finding that the Dragts breached their duty of good faith and fair dealing by selling their real property, and permits and plans procured by DeTray, to a third party without prior

notice to DeTray, and by refusing to divide the proceeds from the sale with DeTray?

13. Did the trial court err in awarding and calculating damages against the Dragts in accordance with the terms of the LLC Agreement?

14. Did the trial court abuse its discretion in admitting a witness' report and testimony concerning the implementation of one of the terms of the LLC Agreement?

II. RESPONDENTS' STATEMENT OF THE CASE

A. Overview.

On July 8, 1996, Henry and Jane Dragt (the Dragts) and E. Paul DeTray ("DeTray") entered into a limited liability company agreement ("LLC Agreement"). The purpose of the LLC Agreement was to regulate the parties' collaboration on the development of a 220 acre parcel of property (the "Property") then owned by the Dragts and located within the City of Yelm in Thurston County. In Henry Dragt's words, the essence of the deal was that the Dragts were to "put up the land [and] . . . Paul [DeTray] was to put up the money and expertise" necessary to develop a high density residential subdivision. CP 220; RP (2/27/2006) 99 ln. 13-16, RP 128 ln. 11-14. The LLC Agreement also purported to give the LLC an option to acquire the Property, and included specific rules for the division of the profits from development.

Over the following eight years, DeTray made substantial efforts to advance the project, and the parties repeatedly re-affirmed their basic commitment to the joint development of the Property. Critically, the

parties also modified the precise terms of their mutual obligations. In particular, DeTray undertook to make the mortgage payments on the Property on behalf of the Dragts, and became a personal guarantor of the mortgage. Nothing in the express terms of the LLC Agreement required these commitments. In return, the Dragts implicitly agreed that they would compensate DeTray for his expenditures, either from the proceeds of development or from the sale of the property.

During the summer of 2004, the Dragts—while still receiving the benefits of DeTray’s development efforts, mortgage payments and personal guarantee—contracted to sell the Property, along with permits and plans pertaining to the Property, to Tahoma Terra, LLC. The Dragts gave DeTray no prior notice of their decision, and refused to compensate DeTray out of the proceeds of the sale as required by the agreement of the parties. This lawsuit ensued.

B. Proceedings Below.

The Dragts filed their Complaint for Declaratory Judgment seeking to void the option provision in the LLC Agreement on September 24, 2004. CP 24-68. DeTray counterclaimed for breach of fiduciary obligations, breach of contract and, in the alternative, for unjust enrichment. CP 401-408. The Dragts subsequently amended their complaint to allege claims for intentional misconduct and gross mismanagement on the part of DeTray. CP 74-79.

On May 5, 2005, the Dragts moved for summary judgment on the issues of the validity of the option provision and DeTray’s counterclaims.

The trial court granted the Dragts' motion in part, finding the option to be unenforceable. However, it denied the Dragts' request to dismiss DeTray's counterclaims. CP 312-323. The trial court reiterated this holding in response to a second motion for summary judgment brought by the Dragts. CP 453-454. In a third summary judgment proceeding, the trial court granted DeTray judgment on the Dragts' intentional misconduct claim, but reserved the gross mismanagement claim for trial. *See* Order on Motion for Partial Summary Judgment of Defendants E. Paul DeTray and Phyllis DeTray, dated February 10, 2006, attached as Appendix A to this Brief.¹

The bench trial on the Dragts' gross mismanagement claim and DeTray's counterclaims for breach of contract and unjust enrichment was held on February 27 and March 1 and 2, 2006. After the Dragts rested, the trial court granted DeTray's motion to dismiss the gross mismanagement claim pursuant to CR 41(b)(3). RP (3/1/2006) 130-132. Then, at the conclusion of the trial, the court summed up its position as follows:

When I started this case I had the initial impression that I had a poor—maybe not so poor, but a salt-of-the-earth dairy farmer who maybe had been unfairly dealt with by a sophisticated developer, but it turns out to be just the opposite, that I've got a clever dairy farmer who went to take advantage of the good graces and help of a developer who tried to maintain what would have been a good deal for the dairy farmer if he'd seen it through, and it's the

¹ Appellants did not designate the pleadings relating to Defendants' Motion for Partial Summary Judgment on Plaintiff's Claims for Gross Mismanagement and Intentional Misconduct in their original or amended Designation of Clerks' Papers. Pursuant to RAP 9.6(a), DeTray is submitting a Supplemental Designation of Clerks' Papers identifying these pleadings.

dairy farmer who plays fast and loose with the principles of good faith and candor, not the developer.

RP (3/2/2006) 45-46. The trial court proceeded to explain that it based this determination in part

on the demeanor of the testimony, not just the facts of the case, but the selective memory and inability to recall of Mr. Dragt and the candid answers given by Mr. DeTray. Mr. Dragt could recall things that helped him, but he somehow couldn't recall things that didn't help him."

RP (3/2/2006) 46.

In its remarks from the bench, the trial court indicated that DeTray was entitled to a recovery, and requested that the parties submit proposed findings of fact and conclusions of law covering both breach of contract and unjust enrichment. RP (3/2/2006) 44, 49. The trial court subsequently adopted findings of fact and conclusions of law holding the Dragts to be in breach of contract and in breach of their duties of good faith and fair dealing, and entered judgment against the Dragts in the total amount of \$2,244,382.17 (including \$176,608.29 in attorneys' fees). CP 890-892. This appeal followed. The Dragts have assigned error to the trial court's conclusions regarding breach of contract and breach of fiduciary duties, but make no objection to the dismissal of their gross mismanagement and intentional misconduct claims. Appellants' Brief, pp. 1-2.

C. Facts.

The Dragts are residents of Washington who owned and operated a dairy farm on the Property for approximately twenty years. In 1993, the Dragts sold their dairy herd and shut down the dairy, and began to explore

ways of using the Property to finance their retirement. As an interim measure, the Dragts leased the Property for cattle grazing. RP (2/27/06) 92 ln. 22 to 93 ln. 15.

In 1995, the Dragts approached Frank Kirkbride (“Kirkbride”) concerning the development of the Property. Kirkbride is the principal in a development management company called The Kirkbride Group, Inc. The Dragts entered into a “Pre Development Management Services Agreement” with Kirkbride dated November 11, 1995, whereby Kirkbride was engaged to determine the suitability of the Property for development. At the time, Kirkbride proposed several options to Henry Dragt, including the sale of the Property “as is,” which would have resulted in what the Dragts regarded as an unacceptably low sale price. RP (3/27/06) 96-97.

Kirkbride was acquainted with Paul DeTray (“DeTray”), and knew that DeTray had extensive experience with the development of residential projects. To help the Dragts achieve their goals for the Property, he recommended that they explore the feasibility of a joint venture with DeTray. In the course of their ensuing discussions with Henry Dragt, both DeTray and Kirkbride emphasized that there could be no guaranteed timeline for completion of development. DeTray and Kirkbride also explained to Dragt that he faced a choice of how much of the risks of delay and market fluctuation to bear. CP 197-198.

Following these discussions, DeTray had an attorney retained by his accountant draft the Limited Liability Company Agreement of Dragt/DeTray LLC (the “LLC Agreement”). Henry Dragt and Paul

DeTray executed the LLC Agreement on July 8, 1996, and Jane Dragt ratified her husband's agreement in a separate document that same day. Ex. 1, p. 26.

In the LLC Agreement, the Dragts granted the LLC an option to acquire the Property, but the relevant provision provides no legal description of the Property. All parties to the LLC Agreement nonetheless clearly understood and intended that the Property would be tied up for development by the LLC, and that the Dragts and DeTray had mutual obligations to the effect that the Dragts were to "put up the land [and] . . . Paul [DeTray] was to put up the money and expertise" necessary to develop a high density residential subdivision. CP 93, CP 220; RP (2/27/06) 99 ln. 13-16.

The LLC Agreement contains no deadline for completion of the development. Instead, the LLC Agreement provided for termination of the LLC in July 2046, or upon withdrawal of either member with mutual consent, and in other limited circumstances. Ex. 1, Article 2.5, Article 13. The LLC Agreement also describes the procedures for the notice of a potential sale and the first refusal rights of the remaining partners to purchase the selling partner's interest. Ex. 1, Article 12.2.

The LLC Agreement provides a mechanism for valuing the parties' contributions to the LLC and distributing ultimate profits. Ex. 1, Article 9.7. It also includes an attorneys fees and costs provision which allows the prevailing party in any litigation to recoup such fees and costs, an integration clause stating that it "constitutes the complete and final

agreement of the parties relating to the transactions contemplated by this Agreement,” and a provision stating that the Agreement may not be amended except by the unanimous written agreement of all of the members. Ex. 1, Articles 15.14, 15.3 and 15.13.

Approximately a year after the parties executed the LLC Agreement, Henry Dragt asked Paul DeTray to make the mortgage payments on the Property. CP 93 ln. 24-25; RP (2/27/06) 124 ln. 14 -24, RP 134 ln. 6-21; Ex. 9, Ex. 15.² Nothing in the LLC Agreement obligated DeTray to make such payments, but DeTray agreed to do so.³ DeTray continued making the payments, totaling \$241,873.60 in all, until October, 2004. Ex. 9, Ex. 15.

In February 2000, the bank holding the loan on the Property proposed a modification of the loan terms. At the request of Henry Dragt, DeTray cooperated in executing the loan modification. Ex. 19. Then, in July of 2003, DeTray executed a personal guarantee for a new loan to the Dragts from Venture Bank. DeTray executed the personal guaranty with the knowledge of, and at the request of, both Henry and Jane Dragt. Ex. 22-23.

² In their trial testimony, the parties did not recall precisely when the mortgage issue was first raised. However, Ex. 9 establishes that DeTray’s first payment was made on August 14, 1997.

³ In a prior pleading submitted to the trial court, the Dragts explicitly conceded this point. CP 83 ln. 5-6 (noting “the LLC had been paying the Dragts’ mortgage on the farm property, even though nothing in the LLC Agreement required it to do so”). See also CP 93 ln. 24-25.

DeTray's guaranty of the Venture Bank loan to the Dragts conferred a benefit on the Dragts, as the loan would not have issued without the guaranty. The benefit to the Dragts was bargained for, as the Dragts requested that DeTray sign the guarantee and gave supporting consideration. The consideration took the form of an implied understanding that Dragt would hold the Property for development by DeTray, and share any proceeds from the sale of the Property with DeTray.

From July 1996 through October 2004, DeTray made all investments and contributions as were reasonably necessary in order to proceed with the development. Among DeTray's expenditures was an outlay of \$234,435 to secure rights to connect to a new waste-water facility being constructed by the City of Yelm.⁴ Ex. 15, 52. DeTray also made expenditures on planning fees and engineering work. Ex. 15. DeTray's investments advanced the development and increased the value of the property. RP (2/27/06) 64, ln. 3-7. Those sums of money, including mortgage payments made, total \$593,462.66. Ex. 15.

One of the preconditions for the successful development of the Property was that Dragt/DeTray provide the city with perfected water rights sufficient to supply domestic water to the proposed development. Ex. 76. However, at some time prior to 2000, Henry Dragt had become

⁴ These connection rights are referred to as "ERUs", or "Equivalent Residential Units." The amount expended by DeTray on ERUs represents the sum of the \$124,371.62 in up-front costs, plus \$110,063.58 on interest. Ex. 15.

aware that at least one of the wells on the Property was not operational. Dragt did not communicate this information to DeTray or Kirkbride. DeTray and Kirkbride only discovered that there was a problem with one of the wells following an inspection by the City of Yelm in late 2000. Kirkbride then contacted Dragt and instructed him to immediately begin pumping water in order to reacquire his water rights. Kirkbride informed Dragt that he was concerned that the Property's water rights might have been lost, and explained to Dragt the delays this would cause in the further development of the Property. CP 200-201.

As time passed, both Dragt and DeTray became increasingly frustrated with the lack of progress in the development. On March 6, 2004 Dragt and DeTray held a Special Meeting of Members of the LLC. At that meeting Dragt expressed his frustration regarding the lack of progress. Dragt and DeTray agreed that they would wait several more months at which time Dragt and DeTray would then further discuss how and whether to proceed with the development. Ex. 2; RP (2/27/06) 112-113.

Unbeknownst to DeTray, Henry Dragt had previously—in November or December of 2003—been in contact with Janet Kessell of Summit Land Planning, and Doug Bloom, a local developer, regarding ways of possibly restoring the Property's water rights and developing the property. RP (3/1/2006) 6-8. Thereafter, in the early months of 2004, Dragt continued to meet with Kessell. By early 2004, Henry Dragt had decided to try to salvage the Property's water rights for his own personal

benefit, and not for the benefit of the LLC. He did not disclose this decision to DeTray. RP (2/27/06) 167 ln. 18 to 169 ln. 4.

Beginning at least in June 2004, Henry Dragt met with Janet Kessell, Doug Bloom, and attorney Curt Smelser who represented Steve Chamberlain, another local developer. Ex. 175, 170, 171. Attorney Curt Smelser provided Dragt with a legal opinion, dated June 29, 2004 to the effect that the Option contained in the LLC Agreement was void and unenforceable, and that under the other terms and conditions of the LLC Agreement the Dragts had no obligation whatsoever to hold the Property for the benefit of the LLC and could unilaterally sell the Property without obligation to the LLC or DeTray. Ex. 219.

In June and July 2004, Dragt entered into negotiations with Steve Chamberlain and Doug Bloom for the sale of the Property. Dragt did not advise DeTray of these negotiations. Instead, an understanding was developed between Dragt and his potential purchasers to keep these negotiations confidential and not disclose them to DeTray. RP (2/27/06) 181 ln. 17-23, RP (3/1/06) 14 ln. 6-16.

On August 30, 2004, the Dragts sold the Property for \$3,000,000.00 to Tahoma Terra, a limited liability company owned by Steve Chamberlain and Doug Bloom. Paragraph 1.5 of the Real Estate Purchase and Sale Agreement between the Dragts and Tahoma Terra defines the "Property" included in the sale as follows:

Approximately 220 acres of the real property legally described on Exhibit A, attached hereto and incorporated herein by this reference, together with all Certificates of Water Right (1581-A, G2-24778, and 4980) and any and all "Permits and Plans", which shall mean all (a) preliminary plat applications, deposits, governmental permits, approvals, licenses, easements, and certificates of occupancy, (b) surveys, architectural and engineering drawings and plans, consultant reports, appraisals, design work, soils tests and studies which related to the Real Property or any improvements thereon, and (electronic versions of any of the foregoing).

Ex. 176, p. 1 (emphasis added). Paragraph 12 of the

Purchase Agreement also provides:

WORK PRODUCT. Within five (5) days of the Mutual Acceptance Date of this Agreement by Buyer and Seller, Seller shall furnish to Buyer all Permits, Plans, and Surveys in Seller's possession. Said work product shall be a part of the purchase price and become the property of Buyer at Closing, free and clear of any encumbrances.

Ex. 176, pp. 6-7 (emphasis added). The "work product" transferred by the Dragts to Tahoma Terra as a part of the sale included a Critical Areas Study, a Conceptual Master Plan, and other documents prepared at DeTray's expense. CP 196.

The Dragts did not personally inform DeTray that they had sold the Property, permits, and plans to Tahoma Terra. RP (2/27/06) 181-182. Not until approximately October, 2004 did Steve Chamberlain and Doug Blood advise DeTray of Tahoma Terra's deal with the Dragts. RP (3/1/06) 14 ln. 21 to 15 ln. 8. On December 10, 2004, the Purchase and Sale Agreement between the Dragts and Tahoma Terra was amended in several respects, and the sale price increased to a total of \$3,300,000.00. Ex. 177A.

III. SUMMARY OF ARGUMENT

Throughout this litigation, the Dragts have taken the position that they don't owe Paul DeTray a single penny. CP 74-79, 476. Although they acknowledge their position to be "harsh," the Dragts assert that the invalidity of the option clause in the LLC Agreement requires that DeTray be left empty handed despite his eight years of effort at developing the property. RP (3/2/06) 18 ln. 3; Appellants' Brief, pp. 14-15.

The Dragts misunderstand the law and mischaracterize the relevant facts. In particular, they confuse the Dragts' contractual obligations to hold the Property for development and to share the proceeds from the sale of the Property with a conveyance of an interest in real property. Because neither of these obligations is equivalent to a property conveyance, they do not need to be documented in the manner required by the statute of frauds, nor do they suffer from the other defects alleged by the Dragts. The parties had valid, binding contractual obligations to each other, and the Dragts breached their obligations to DeTray's substantial detriment. The trial court did not err by so holding.

In addition, the trial court's finding that the parties modified the written LLC Agreement to include obligations to hold the Property for development by DeTray and to share the proceeds from the sale of the Property is supported by clear and convincing evidence.⁵ The evidence

⁵ However, as argued in detail below, in order to prevail on this appeal, DeTray need only show that the trial court's finding regarding the contract modification is supported by substantial evidence.

derives both from the parties' joint execution of documents relating to the Dragts' mortgage, and from DeTrays payments on the mortgage. The Dragts' attempts to find legal error in the trial court's conclusions of law pertaining to the modification also fail, because they rest on misunderstandings of the parol evidence rule, the implications of contract integration, and the legal requirements for creating valid new obligations

Close inspection of the other alleged errors of law and fact raised by the Dragts shows that the trial court's findings are supported by substantial evidence and that its conclusions of law comport with established Washington precedent. This Court should affirm the trial court, and award DeTray his attorneys' fees and costs on appeal.

Alternatively, if this Court should determine that there was no enforceable contract between the Dragts and DeTray, DeTray requests that the Court remand this matter to the trial court with directions to enter findings of fact and conclusions of law on DeTray's claim for unjust enrichment. In that event this Court should also remand the issue of fees for work below to the trial court, with the direction to award fees to the prevailing party.⁶

⁶ The Dragts must concede that DeTray is the prevailing party with regard to their gross negligence and intentional misconduct claims. In the event of a remand in which the trial court found the Dragts had been unjustly enriched, DeTray would clearly be the prevailing party below and entitled to fees under the LLC Agreement. *See, e.g., Labriola v. Pollard Group, Inc.*, 152 Wn.2d 828, 839, 100 P.3d 791 (2004) (noting that "[a]ttorneys fees and costs are awarded to the prevailing party even when the contract containing the attorneys fee provision is invalidated").

IV. ARGUMENT

A. Standard of Review.

1. Findings of Fact and Conclusions of Law.

This Court's review of the trial court's findings of fact and conclusions of law is a "two-step process." Landmark Dev., Inc. v. City of Roy, 138 Wn.2d 561, 573, 980 P.2d 1234 (1999). First, "the court must determine if the trial court's findings of fact were supported by substantial evidence in the record. If so, the court must then determine whether those findings of fact support the trial court's conclusions of law." Guarino v. Interactive Objects, Inc., 122 Wn. App. 95, 108, 86 P.3d 1175 (2004). Conclusions of law are reviewed de novo. Id.

"Substantial evidence" exists to for a factual holding "when there is a sufficient quantum of proof to support the trial court's findings." Id. In particular, "[c]onflicting evidence is substantial if that evidence reasonably substantiates the finding even though there are other reasonable interpretations." Id. However, if a trial court makes a factual finding that must be supported by "clear, cogent, and convincing evidence," the Court of Appeals will review to determine if the evidence presented at trial is sufficient to make the finding "highly probable." In re Sego, 82 Wn.2d 736, 739, 513 p.2d 831 (1971) (concerning the quantum of evidence necessary to sustain an order depriving a parent of custody of his or her children).⁷

⁷ As spelled out in Section IV Part C-1 below, DeTray does not believe there is any factual finding in this matter that must be supported by "clear, cogent, and convincing

2. Evidentiary Rulings

The Court of Appeals reviews a trial court's evidentiary rulings for abuse of discretion. *See, e.g., State v. Majors*, 82 Wn. App. 843, 848, 919 P.2d 1258 (1996). An abuse of discretion occurs only if there is a clear showing that the exercise of discretion was manifestly unreasonable, based on untenable grounds, or based on untenable reasons. *State ex rel. Carroll v. Junker*, 79 Wn.2d 12, 26, 482 P.2d 775 (1971). In a bench trial, the trial judge is assumed to give the evidence its proper weight. *State v. Melton*, 63 Wn. App. 63, 68, 817 P.2d 413 (1991), *review denied*, 118 Wn.2d 1016, 827 P.2d 1011 (1992).

B. The Dragts' contractual obligations to hold the Property for development by DeTray and to share the proceeds from any sale of the Property with DeTray are binding and enforceable.

The Dragts have consistently argued that DeTray's counterclaims for breach of contract and breach of fiduciary duty are completely dependent on the validity of the option provision in the LLC Agreement. Appellant's Brief, pp. 14-17; CP 80-91. Since the option provision is unenforceable, the Dragts insist that DeTray's counterclaims must fail. This position is mistaken, because the Dragts breached binding obligations to DeTray distinct from the option provision.

evidence." However, regardless of the relevant standard, there is ample evidence to support the trial court's findings and conclusions.

1. The Dragts' contractual obligations violate neither the statute of frauds nor the laws of community property.

In its Findings of Fact and Conclusions of Law, the trial court held that “Henry Dragt undertook to hold the Property for development by DeTray and to recompense DeTray for his capital contributions out of the proceeds from the sale of the Property.” CP 888 (CL 4) (emphasis added). The trial court thus found that the Dragts had two distinct contractual obligations to DeTray: 1) an obligation to hold the Property for development by DeTray, and 2) an obligation to compensate DeTray for his investments out of the proceeds of any sale of the Property. The Dragts’ protests to the contrary notwithstanding, neither of these obligations is identical to an option either as a matter of logic or as a matter of law.

An option is “a contract to enter into a future contract.” Hubble v. Ward, 40 Wn.2d 779, 785, 246 P.2d 468 (1952). In an option contract for land, the owner of the property (the optionor) sells to another party (the optionee) a time-limited right to purchase an identified parcel of real property at a specified price. The right transferred to the optionee is recognized as a property right, and an option to real property conveys an interest in that property to the optionee. McFerran v. Heroux, 44 Wn.2d 631, 638-39, 269 P.2d 815 (1954). Accordingly, an option contract for real property must comply with the real property statute of frauds, RCW 64.04.010.

Neither the Dragts’ obligation to hold their Property for development by DeTray nor their obligation to compensate DeTray for his

capital expenditures out of the proceeds of the sale of the Property is logically equivalent to an option. Neither entails an obligation to enter into a future contract (as opposed to an obligation to make future payments). Critically, neither obligation presumes that DeTray would acquire the Property, or had a right to acquire the Property. As a consequence, neither obligation can be deemed subject to the requirements of RCW 64.04.010 by virtue of their purported similarities to an option. The Dragts cite no legal authority that holds to the contrary.⁸

The same basic reasoning defeats the Dragts' argument that their obligations are unenforceable because they violate the rule that both spouses must consent to a conveyance of real property owned by the marital community. The Dragts' obligations to hold their Property for development by DeTray and to compensate DeTray for his expenditures out of the proceeds of any sale of the Property do not convey an interest in real property, and therefore do not violate RCW 26.16.030(3).

2. Neither of the Dragts' obligations is an unreasonable restraint on alienation.

The Dragts argue in the alternative that their obligation to hold the Property for development by DeTray constitutes an unreasonable restraint on alienation. Appellants' Brief, p. 21. It is important to note that this

⁸ The Opening Brief of Appellants ("Appellants' Brief") asserts that "[t]he obligation to hold one's property is a property interest," but the case they cite to support this proposition—McFerran v. Heroux, 44 Wn.2d 631, 269 P.2d 815 (1954)—only supports the parenthetical comment that "an option is recognized as a property right." Appellants' Brief, p. 20 (emphasis added). The case provides no support for the Dragts claim that an obligation to hold property—let alone an obligation to share proceeds from the sale of property—is the legal equivalent of an option.

objection targets only one of the two distinct contractual obligations found by the trial court: it pertains only to the Dragts' obligation to hold the Property. It has no bearing against the Dragts' obligation to compensate DeTray from the proceeds of any sale. *See, e.g.*, 18 Wash. Prac., Real Estate §17.7 (noting that "indirect restraints" such as due on sale clauses "generally do not violate the policy against restraints"). Even with regard to the Dragts' obligation to hold the Property for development by DeTray, the argument fails because it makes no effort to establish that any restraint imposed by the obligation is unreasonable, and ignores the underlying policy rationales for the rule against restraints on alienation.

Washington follows the reasonableness approach to restraints on alienation. "Unreasonable restraints on alienation of real property are . . . invalid; reasonable restraints on alienation . . . are valid if justified by the legitimate interests of the parties." McCausland v. Bankers Life Ins. Co., 110 Wn.2d 716, 722, 757 P.2d 941 (1988). In determining whether a restraint on alienation is reasonable, Washington courts "balance the utility of the purpose served by the restraint against the injurious consequences that are likely to flow from its enforcement." Alby v. Banc One Financial, 156 Wn.2d 367, 373, 128 P.3d 81 (2006). Moreover, "when evaluating the reasonableness of any agreement placing a restraint on alienation, courts should be reluctant to invoke common law principles . . . to invalidate a bargained for contract freely agreed to by the parties." Id. at 374.

The Dragts' obligation to hold the property for development by DeTray is not even a facial restraint on alienation, since the Dragts could have sold the property to anyone subject to DeTray's retention of an exclusive right to proceed with development. However, assuming for the sake of argument that the obligation could be seen as a restraint on alienation, it is clearly a reasonable one. The purpose served by the "restraint" in this instance is to facilitate the movement of the property from a low-valued agricultural use to a high density, high value development. Unlike the traditional restraint on alienation which attempts to maintain family control of land, there is no cognizable injurious consequence that could flow from enforcing the obligation at issue here. *Compare Richardson v. Danson*, 44 Wn.2d 760, 766, 270 P.2d 802 (1954) (noting that the law seeks to discourage such restraints as would "result in withdrawing . . . property from the ordinary channels of trade"). Even if there were a restraint on alienation imposed by the Dragts' obligation to hold the land for development by DeTray, it was bargained for and eminently reasonable.

3. The Dragts' obligations do not violate the rule against perpetuities.

The rule against perpetuities prohibits the creation of certain "future estates." *See, e.g., Betchard v. Iverson*, 35 Wn.2d 344, 348, 212 P.2d 783 (1949). Neither of the Dragts' obligation to hold the property for DeTray nor their obligation to compensate DeTray for his expenditures out of the proceeds of any sale creates a "future estate." Instead, they both

create obligations that “vested,” or became binding, at the time the obligations were assumed. The rule against perpetuities has no application to this case.

4. The Dragts’ obligations are not too indefinite to be enforced.

The Dragts’ obligations to hold the Property for development by DeTray, and to compensate DeTray for his expenditures out of the proceeds of any sale of the Property, are sufficiently clear to be enforced. In particular, there is no great difficulty in identifying behavior that constitutes a breach of each of these obligations. By selling the Property to another developer and thereby nullifying DeTray’s right to serve as the exclusive developer of the Property, the Dragts breached the obligation to hold the Property for DeTray. By attempting to keep all of the sales proceeds for themselves, the Dragts patently ignored the terms of the LLC Agreement spelling out how such proceeds are to be divided. Ex. 1, Article 9.7. The Dragts’ obligations are sufficiently clear to be enforced.

5. The Dragts’ agreement to hold the Property for development by DeTray does not “fail factually”.

Preoccupied with ridiculing the trial court for not discerning the alleged “paradox” in its ruling, the Dragts fail to notice the logical tensions in their own argument. *Cf.* Appellants’ Brief, p. 15. After having alleged that “[a]n agreement to hold property for development by another is simply an option by another name,” and having conceded that “neither the Dragts nor DeTray realized the option . . . was unenforceable until shortly before the property was sold,” they nonetheless assert that their

obligation to hold their property is “unsupported by the evidence.” Appellants’ Brief, p. 18, 16, and 23. It is difficult to see how these three statements can be maintained simultaneously.

The Dragts appear to have been led into this argumentative dead end by two factors: 1) their confusion (analyzed above) of an obligation to hold property for development with an option, and 2) their desire to depict the parties’ testimony concerning the “tying up” of the Property as supporting a total absence of obligations running from themselves to DeTray. Unfortunately for the Dragts, the evidence unambiguously shows they understood they had an obligation not to cut DeTray out of the process of developing the Property. CP 93 ln. 14-16; RP (2/27/06) 133 ln. 22 to 134 ln. 5. The lengthy excerpts from DeTray’s trial testimony cited by the Dragts at pages 24-25 of Appellants’ Brief establish only that DeTray knew the Dragts wanted to continue to derive income from their property while DeTray pursued the initial stages of development. RP (2/27/06) 54 ln. 14-18. DeTray’s knowledge on this point in no way undermines the fact that the Dragts had committed to hold the property for development by DeTray.

Ironically, the Dragts conclusion that “there is no evidence that [they] intended or agreed to give the LLC or DeTray any interest in their property other than the original option” is correct, but serves only to show their misunderstanding of the relevant issues. Appellants’ Brief, p. 25 (emphasis added). Apart from the failed option, the Dragts did not convey any interest in their Property to DeTray, but they did undertake the

conceptually and legally distinct obligations to hold their Property for development by DeTray and to compensate DeTray from the proceeds of any sale. Because they do not understand that these obligations are distinct from the option, the Dragts fail to make any cogent criticism of the legal and factual underpinnings of those obligations.

C. Clear and convincing evidence shows that the Dragts and DeTray modified their obligations after the execution of the LLC Agreement.

The trial court concluded that “[t]he parties to the LLC Agreement modified it after its execution by means of their subsequent oral agreements and course of conduct pertaining to DeTray’s ongoing mortgage payments for the Dragts and his personal guarantee for the new loan by Venture Bank.” CP 888 (CL 3). The Dragts now contend that the modification of a written contract must be proven by clear and convincing evidence, and that therefore the standard of review for this issue is whether the modification is “highly probable.” Appellants’ Brief, p. 26. The Dragts misstate the applicable standard of review, which is the “substantial evidence” standard. However, regardless of whether the exhibits and testimony are reviewed according to the “highly probable” or “substantial evidence” standards, they strongly support the trial court’s findings and conclusions on the contract modification issue.

1. The Dragts misstate the applicable standard of review.

Any fact which must be established by clear, cogent and convincing evidence is reviewed on appeal under a “highly probable” standard. See In re Sego, 82 Wn.2d at 739 (concerning facts necessary to

justify depriving father of custody of his children). However, the modification of a written contract is not such a fact. *See, e.g., Swanson v. Liquid Air Corp.*, 118 Wn.2d 512, 826 P.2d 664 (1992). In *Swanson*, the central issue was whether a “Memorandum of Working Conditions modified the [previously formed] employment relationship.” *Id.* at 519. The court concluded that the issue of contract modification was a question of fact, and that “the analysis is the same as that generally used to determine whether a contract has been formed: Would a reasonable person looking at the objective manifestations of the parties’ intent find that they had intended this obligation to be part of the contract?” *Id.* at 522 (emphasis added). By implication under *Swanson*, the burden of proof for establishing a contract modification is the same as that for establishing contract formation: by a preponderance of the evidence.⁹

2. Clear and convincing evidence supports the modification of the LLC Agreement.

As noted in *Swanson*, questions of contract modification—like questions of contract formation and interpretation—ultimately boil down to the intent of the parties. *See also Tanner Elec. Coop. v. Puget Sound Power & Light*, 128 Wn.2d 656, 674, 911 P.2d 1301 (1996) (noting that intent is the “touchstone” of contract interpretation). In Washington, the process of establishing the parties’ intent and interpreting any resulting

⁹ The cases the Dragts cite to assert the contrary are denigrated as “older cases” in the comment to Washington Pattern Instruction 301.07. *See* 6A *Wash. Prac.* Washington Pattern Jury Instructions—Civil WPI 301.07 (comment). WPI 301.07 itself makes no reference to any heightened burden of proof for establishing a contract modification.

contract is guided by the “context rule.” Berg v. Hudesman, 115 Wn.2d 657, 667, 801 P.2d 222 (1990).

Under the analytical framework of the context rule, “the intent of the parties may be discerned from the actual language of the agreement, the subject matter and objective of the contract, all the circumstances surrounding the making of the contract, the subsequent acts and conduct of the parties to the contract, and the reasonableness of respective interpretations advocated by the parties.” Flower v. T.R.A. Industries, Inc., 127 Wn. App. 13, 111 P.3d 1192 (2005). *See also* 6A Wash. Prac., Wash. Pattern Jury Instr. Civ. WPI 301.07 (noting that a contract modification can be established through “the words or conduct” of the parties) (italicized emphasis and brackets removed from original, underlined emphasis added); *and* Cardinal Development Co v. Stanley Const. Co., Inc., 497 S.E.2d 847, 851 (Va. 1998) (noting that a “course of dealing by contracting parties, considered in the light of all the circumstances, may evince mutual intent to modify the terms of [a] contract”).

Here, the words and conduct of the Dragts and DeTray following the execution of the LLC Agreement clearly modified their contract in the manner found by the trial court. The modifications are evidenced by the interactions of the parties concerning two critical events: DeTray’s payments of the Dragts’ mortgage, and his execution of a personal guarantee of the Dragts’ debt.

Approximately a year after the parties executed the LLC Agreement, Henry Dragt asked Paul DeTray to make the mortgage payments on the Property. CP 93 ln. 24-25; RP (2/27/06) 124 ln. 14 -24, 134 ln. 6-21; Ex. 9, Ex. 15. DeTray agreed, and continued making the payments, totaling \$241,873.60 in all, until October, 2004. Ex. 9, Ex. 15. As the Dragts have conceded, nothing in the LLC Agreement references or requires these payments. CP 83 ln. 5-6. The fact that Paul DeTray felt obliged to make them as part of his fiduciary responsibilities to the LLC speaks to his high standards of business ethics, but not to the question of whether the payments were in fact required under the LLC Agreement.

The Dragts have repeatedly argued that DeTray made these payments as a mere volunteer. CP 469-470; Appellants' Brief, p. 32-33. However, they offer no account of how DeTray knew how much to pay and where to pay it, nor do they attempt to reconcile DeTray's purported volunteer status with their knowing receipt of the benefit of DeTray's expenditures for almost seven years during which the Dragts were collaborating with DeTray on the commercial development of the Property. Moreover, Henry Dragt testified at trial that he understood he had a "commitment" to DeTray to reimburse him for the mortgage payments out of his share of profits. RP (2/27/06) 136 ln. 2-9. The evidence supports only one possible conclusion: that DeTray made the payments only in exchange for a new implicit promise from the Dragts that they would compensate him for the payments out of the proceeds of

any sale.¹⁰ *See, e.g., City of Everett v. Sumstad's Estate*, 95 Wn.2d 853, 855, 631 P.2d 366 (1981) (noting that courts “impute an intention corresponding to the reasonable meaning of a person’s words and acts” when determining if a contract has been formed).

The evidence concerning the loan guarantee is also consistent with the conclusion that the parties modified the LLC Agreement, and is inconsistent with any other interpretation. Nothing in the LLC Agreement calls for DeTray to become a personal guarantor of the Dragts’ debt. The loan guarantee documents, which bear the signatures of both DeTray and the Dragts, make it evident that the Dragts knew of and seconded the lender’s request that DeTray make a personal guarantee. *See* Ex. 22 (containing the Dragts covenant that they would “furnish executed guarantees of the loans in favor of lender, executed by the guarantors named below,” and naming DeTray and his wife); Ex. 23 (guarantees executed by DeTray and his wife). DeTray’s guarantee was dated July 18, 2003, approximately six years after the execution of the LLC Agreement. Ex. 23. DeTray would not have executed the guarantee if he were not convinced that the Dragts were committed to hold the property for his development and to compensate him for his ongoing expenditures and risks in the event of any sale. RP (2/27/06) 80 ln. 7-18.

Finally, there was clearly consideration flowing from DeTray to the Dragts to support the modification of the LLC Agreement. Not only

¹⁰ The Promissory Note on which DeTray began paying in 1997 was dated January 24, 1997—more than six months after the execution of the LLC Agreement. Ex. 18.

did DeTray's mortgage payments directly benefit the Dragts, so too did his personal guarantee. The fact that the Dragts could not themselves enforce the guarantee is irrelevant: the bank could enforce the guarantee, and this in turn provided a bargained-for benefit to the Dragts. *See, e.g., Labriola v. Pollard Group, Inc.*, 152 Wn.2d 828, 833, 100 P.3d 791 (2004) (noting "consideration is a bargained for exchange of promises"). The evidence clearly establishes all of the elements necessary to show that the parties modified the LLC Agreement.

3. DeTray's testimony concerning his understanding of the parties' obligations does not contradict the trial court's conclusion that the parties modified those obligations after executing the LLC Agreement.

The Dragts' principal challenge to the trial court's conclusion that Henry Dragt undertook new obligations "to hold the Property for development by DeTray and to recompense DeTray for his capital contributions out of the proceeds from the sale of the Property" consists of a lengthy recitation of Paul DeTray's trial testimony. *See* Appellants' Brief, pp. 24-25. The point of the recitation is to prove that DeTray "understood and believed *from the time he executed the LLC Agreement* that the Dragts were obligated to hold their property for development." Appellants' Brief, p. 27 (emphasis in original). According to the Dragts, it follows that the LLC Agreement could not have been modified. This challenge fails for two reasons.

First, the Dragts' argument makes no mention of the second part of the modification found by the trial court: Henry Dragt's obligation "to

recompense DeTray for his capital contributions out of the proceeds from the sale of the Property.” In a later section of their brief, the Dragts do point out that “the LLC Agreement provided all along that both members would be entitled to be reimbursed for their capital contributions,” but a duty flowing from the Dragts to DeTray personally is clearly different from a duty flowing from the LLC to DeTray. Appellants’ Brief, p. 31. The section of DeTray’s testimony relied on by the Dragts contains nothing at odds with the Dragts assuming a personal obligation to recompense DeTray after the LLC Agreement was executed.

Second, with regard to the modification to hold the property for development by DeTray, an option granted to the LLC is different (for the reasons explained above in Section B-1) from an obligation to hold the property for development by DeTray. The two obligations are not logically incompatible, and the second obligation (to hold the Property for DeTray) can be understood as a fall-back, alternative provision for the event that the LLC should choose not to acquire the Property by exercising the option. Contrary to the Dragts’ assertions, DeTray’s testimony is not inconsistent with the trial court’s findings.

4. The trial court did not err in concluding that the clause in the LLC Agreement prohibiting all but written amendments was unenforceable.

As a matter of law, the parties to a written contract retain their ability to modify it by subsequent mutual agreement. This is true even if the contract explicitly prohibits oral modifications, since “a contract may

be modified or abrogated by the parties thereto in any manner they choose, notwithstanding provisions therein prohibiting its modification or abrogation except in a particular manner.” Pacific Northwest Group A v. Pizza Blends, Inc., 90 Wn. App. 273, 278, 951 P.2d 826 (1998) (quoting Kelly Springfield Tire Co. v. Faulkner, 191 Wash. 549, 556, 71 P.2d 382 (1937)).

The Dragts acknowledge that Pizza Blends is good law, but contend that paragraph 15.3 of the LLC Agreement continues to bar subsequent unwritten modifications of the LLC Agreement because the parties never attempted to waive it. Appellants’ Brief, p. 35. The Dragts overlook the fact that a contractual provision such as paragraph 15.3 can be waived by conduct.

In Birkeland v. Corbett, 51 Wn.2d 554, 565, 320 P.2d 635 (1958), the State Supreme Court noted that a “waiver is the intentional and voluntary relinquishment of a known right, or such conduct as warrants an inference of the relinquishment of such right” (emphasis added). By soliciting DeTray’s mortgage payments and guarantee in transactions related to the Property, but not encompassed within the LLC Agreement, the Dragts clearly and unequivocally evinced an intent to waive the no-oral modification clause of the LLC Agreement. The trial court did not err in concluding that paragraph 15.3 was unenforceable.

In passing, the Dragts also accuse the trial court of “ignoring” the integration clause in paragraph 15.13 of the LLC Agreement. Appellants’ Brief, p. 36. The critical question in this case is whether the LLC Agreement was modified after its execution, not whether it was integrated at the time it was signed. By its own terms, paragraph 15.13 claims to supersede “all previous representations, contracts, agreements, and understandings of the parties,” and thus does not pertain to subsequent agreements and conduct. Ex. 1, Article 15.13 (emphasis added). *See also Emrich v. Connell*, 105 Wn.2d 551, 556, 716 P.2d 863 (1986) (noting that under the parol evidence rule, “prior or contemporaneous negotiations and agreements are said to merge into” an integrated writing) (emphasis added); *and Flower v. T.R.A. Industries, Inc.*, 127 Wn. App. 13, 29, 111 P.3d 1192 (2005) (noting that “[t]he parol evidence rule does not apply to subsequent agreements”). Because the issue before the trial court was modification, not integration, it did not err by “ignoring” the integration clause.¹¹

¹¹ Although the Dragts imply that the LLC Agreement was integrated, they have previously insisted that the agreement between the parties included terms—such as a three year maximum period for the property to be developed—that are not present in the LLC Agreement. CP 81 ln. 13-16; CP 93. Because of their previous arguments to the trial court, the Dragts are effectively estopped from arguing that the LLC Agreement was integrated.

5. The modification of the LLC Agreement does not lead to absurd results.

There is nothing “absurd” about the trial court’s conclusion that the parties modified the LLC Agreement to give the Dragts’ new obligations to hold the property for development by DeTray and to compensate DeTray out of the proceeds of any sale of the Property. As Washington courts have long recognized,

when a second contract deals with the same subject matter as did the first contract made by the same parties, but does not state whether or to what extent it is intended to operate in discharge or substitution, the two contracts must be interpreted together. In so far as they are inconsistent, the later one prevails; the remainder of the first contract . . . may be enforced.

Flower, 127 Wn. App. at 29 (citing to Lynch v. Higley, 8 Wn. App. 903, 911, 510 P.2d 663 (1973)).

Interpreting the LLC Agreement and its subsequent modification together in light of the facts shows the following: 1) until Henry Dragt consulted with attorney Curt Smelser, the parties believed the option provision in the LLC Agreement was valid, and therefore expected that their collaboration—and the development of the Property—would continue to be coordinated through the LLC; and 2) the parties nonetheless gave the Dragts “backup” obligations to hold the property for development by DeTray, and to compensate DeTray out of the proceeds of the sale of the Property, in exchange for the additional consideration DeTray provided in the form of the mortgage payments and the loan guarantee. These “backup” obligations would become binding if either the LLC decided to develop the Property without exercising the option (a

possibility clearly not foreclosed by the written LLC Agreement), or if the Dragts attempted to sell the Property to a new developer prior to the LLC completing its tasks (which is what occurred). The contingent or sequential character of the Dragts obligations flowing directly to DeTray, rather than to Dragt/DeTray LLC, render those obligations not only plausible, but essential to give effect to the clear intent of the parties to collaborate on the development of the Property.

D. The Dragts breached the notice provisions in the LLC Agreement.

Although the Dragts and DeTray modified the LLC Agreement by their actions after its execution, they did not negate it. As noted in Flower, if two contracts are made concerning the same subject matter, the latter contract controls if there are any inconsistencies, but “the remainder of the first contract . . . [in so far as it is] quite consistent with the second in substance and in purpose may be enforced.” Flower, 127 Wn. App. at 29 (internal quotations omitted). Because the additional obligations assumed by the Dragts and DeTray through modification of the LLC Agreement do not conflict in any way with the notice and distribution terms of the LLC Agreement, those terms remain in effect.

The trial court found that the Dragts breached the notice provision of the LLC Agreement by selling the Property to Tahoma Terra with no prior warning to DeTray. The Dragts assert that the trial court erred “because there is no provision in the LLC Agreement that required the

Dragts to notify DeTray before they sold their property.” Appellants’ Brief, p. 37. Here too, the Dragts are wrong.

Article 12.2 of the LLC Agreement states that any “Unit Holder desiring to transfer all or any portion of its Membership Interests or Economic Interests to a third party purchase . . . shall give written notice to the other Unit Holders and the Manager of its intention to so transfer such interest.” Ex. 1, Article 12.2(a). Article 1 of the LLC Agreement, in turn, defines “Membership Interest” to include “distributions of the Company’s assets . . .” Ex. 1, Article I.

When the Dragts sold their real Property to Tahoma Terra, they included in the sale “any and all Permits and Plans”, which were defined to include “all (a) preliminary plat applications, deposits, governmental permits, approvals, licenses, easements, and certificates of occupancy, (b) surveys, architectural and engineering drawings and plans, consultant reports, appraisals, design work, soils tests and studies which related to the Real Property or any improvements thereon.” Ex. 176. Thus, all of the plans and permits (including ERUs) procured by DeTray at no cost to the Dragts were included in the sale.

Equitable if not legal title to those permits and plans was vested in the LLC, not the Dragts. The concepts of equitable and legal title are directly applicable to this situation, since by statute members of an LLC owe one another duties as “trustees” with regard to LLC property:

Every member and manager must account to the limited liability company and hold as trustee for it any profit or benefit derived by him or her without the consent of a majority of the disinterested managers or members, or other persons participating in the management of the business or affairs of the limited liability company from (a) any transaction connected with the conduct or winding up of the limited liability company or (b) any use by him or her of its property, including, but not limited to, confidential or proprietary information of the limited liability company or other matters entrusted to him or her as a result of his or her status as manager or member.

RCW 25.15.155(2) (emphasis added). Equitably if not legally, the permits and plans were “assets” of the LLC, and any sale of those assets was subject to the notice provisions of Article 12.2.¹² The trial court did not err as a matter of law in finding that the Dragts breached the contractual notice provision by executing an agreement with Tahoma Terra to transfer LLC assets with no prior notice to DeTray.

The Dragts also claim that they gave DeTray notice of their decision to sell, but their assertion does not withstand even minimal scrutiny. There is absolutely no evidence in the record that the Dragts “told DeTray in March 2004 they were going to sell and told him in October 2004 they had signed a contract to sell.” Appellants’ Brief, p. 38 (making no citation to the record). Instead, the record shows that in March, 2004, the Dragts informed DeTray that they were frustrated with the pace of development, but agreed to wait three or four months before

¹² The Dragts should not be allowed to argue that the notice provision does not apply because the LLC assets involved in the sale to Tahoma Terra had never been “distributed.” Surely a provision that requires notice before the sale of LLC assets that have been distributed extends to cover the sale of LLC assets that are being sold by a member who has no individual claim to them.

pursuing other options. Ex. 2, RP (2/27/06) 113. Moreover, it was not the Dragts who informed DeTray that they were “going” to sell in October, 2004, but rather Steve Chamberlain and Doug Bloom—who informed DeTray that Dragt had sold the land. RP (3/1/06) 14 ln. 21-25; Ex. 176 (purchase and sale agreement dated August 30, 2004). The fact that the sale did not formally close until December, 2005 (approximately three months after the initiation of this lawsuit) is simply irrelevant to the issue of whether the Dragts complied with the provisions of Article 12.2, which require notice an offer to sell which the member intends to accept, not notice of an executed purchase and sale agreement. Ex. 1, Article 12.2. The Dragts presented DeTray with a *fait accompli*, not notice.

E. The Dragts breached their duty to act in good faith toward DeTray.

The trial court also found that the Dragts owed DeTray a duty to act in good faith, and that the Dragts breached this duty to the detriment of DeTray. In particular, the trial court’s fifth and sixth conclusions of law provide as follows:

As partners for the development of the Property, DeTray and the Dragts owed each other fiduciary duties of good faith and fair dealing in all respects. CP 888 (CL 5). The Dragts breached their duty of good faith to DeTray by selling the Property to Tahoma Terra without prior notice to DeTray, and by refusing to divide the proceeds from the sale as called for in the modified agreement of the parties. CP 888 (CL 6).

The Dragts assign error to these conclusions, on the twin grounds that a) “an implied duty of good faith cannot be used to add a term to the parties’

contract”, and b) because the parties were not partners, they had no fiduciary duties as a matter of law. Appellants’ Brief, pp. 39-40. The Dragts arguments misunderstand the applicable law, and fail to show any error by the trial court.

First, the trial court did not use the duty of good faith to add any term to the agreement between the Dragts and DeTray. As noted in the immediately preceding Section, the LLC Agreement contains a notice provision in Article 12. The Dragts did not make a good faith effort to adhere to the requirements of this provision, and thereby breached their duty of good faith.

Second, the fact that the Dragts and DeTray executed a written LLC Agreement is in no way dispositive on the question of whether they related to one another as partners. The Washington State Legislature located the statutes governing limited liability companies, Chapter 25.15 RCW, within Title 25 RCW which pertains to “partnerships. Moreover, under RCW 25.15.155(2), cited above, it is clear that the members of an LLC owe each other fiduciary duties. These fiduciary duties are sufficiently close to those owed by partners to one another that there is no error in finding the Dragts and DeTray to be partners.

Finally, the trial court was perfectly justified in rebuking Henry Dragt for concealing his dealings with Tahoma Terra from DeTray. RP (3/2/06) 44-48. Rather than provide DeTray advance notice of his desire to sell to Tahoma Terra, Henry Dragt sought legal protection from

Tahoma Terra for lawsuit he knew would result from his actions.¹³ Ex. 176, p. 11. Henry Dragt's acts and omissions clearly indicate deliberate concealment, and provide more than ample support for both the trial court's finding of bad faith and for its comments from the bench.

F. The trial court properly calculated damages.

To compensate DeTray for the Dragts breaches of contract, the trial court properly awarded him \$2,067,773.88 in damages. The trial court's determination of the damages amount is sound as a matter of law and is supported by substantial evidence. It should not be overturned on appeal. *See, e.g., Mason v. Mortgage America Inc.*, 114 Wn.2d 842, 850, 792 P.2d 142 (1990) (noting that "an appellate court will not disturb an award of damages made by the fact finder unless it is outside the range of substantial evidence in the record, or shocks the conscience, or appears to have been arrived at as the result of passion or prejudice").

1. The trial court used the proper measure of damages.

The Dragts' allege that the trial court used the improper measure of damages, and claim that "the only damages the LLC could have incurred was [sic] the loss of its 'option' rights." Appellants' Brief, p. 41. As explained in Section IV B-1 above, the Dragts' contractual obligations to

¹³ It is striking that Appellants claim to be unable to distinguish between DeTray's efforts to find a buyer for the Dragts' position and the Dragts' decision to sell the Property. Appellants' Brief, pp. 39-40, note 13. DeTray obviously could not sell the Dragts' position without the Dragts' advance consent. The Dragts, on the other hand, proceeded as if they could sell the Property with utter disregard for both their obligations under the modified agreement and for the notice provision of Article 12.2. DeTray's actions were perfectly consistent with his fiduciary duties toward the Dragts; the Dragts actions clearly breached their duties to DeTray.

hold the Property for development by DeTray and to compensate DeTray from the proceeds of any sale are not logically or legally equivalent to an option, and therefore the limitation on damages recoverable for breach of an option is irrelevant to DeTray's claims. *Cf. McFerran v. Heroux*, 44 Wn. 2d at 642-43.

DeTray was entitled to the benefit of the bargain he had struck with the Dragts, and thus to be made as well off as he would have been if the Dragts had performed their obligations. *See, e.g., Mason*, 114 Wn.2d at 840 (noting that “[c]ontract damages are ordinarily based on the injured party’s expectation interest and are intended to give that party the benefit of the bargain”). This is precisely what the trial court did in awarding DeTray his share of the proceeds of the sale to Tahoma Terra as set forth in Article 9.7 of the LLC Agreement.

The Dragts also argue that the trial court’s award of expectation damages was flawed because DeTray had only partially performed and was thus only entitled to restitution of his expenditures. Appellants’ Brief, p. 42, n. 14. Both the premise and the conclusion of this argument are independently incorrect. The premise is incorrect because DeTray had not merely “partially performed” his obligations under the agreement of the parties: he had done everything required to share in the proceeds of any sale of the property.¹⁴ Regardless of whether the Dragts’ premise is

¹⁴ The Dragts offer neither evidence nor argument to the contrary. Nothing in the LLC Agreement or the modified agreement of the parties requires any particular level of development of the Property. RP (2/27/06) 50 ln. 2-5.

incorrect, the purported conclusion does not follow because it is not true that “the correct measure of damages for part performance is restitution.” Appellants’ Brief, p. 42, n. 14.

The authority cited by the Dragts to support their conclusion in fact states that “[r]estitution is a proper remedy for a party who after partial performance has been prevented from further performance by a total breach of an indivisible contract.” Dravo Corp. v. L.W. Moses Co., 6 Wn. App. 74, 90, 492 P.2d 1058 (1972) (emphasis added). Both Dravo and the Restatement (Second) of Contracts make clear that it is the aggrieved party’s choice whether to seek damages measured by an expectancy or by restitution. *See* Dravo, 6 Wn. App. at 90 (noting that “restitution is an alternative remedy to damages for breach of contract”); *and* Restatement (Second) of Contracts (1981), § 373, Comment a (noting that “an injured party usually seeks . . . to enforce the other party’s broken promise [but] he may, as an alternative, seek, through protection of his restitution interest, to prevent the unjust enrichment of the other party”). In the instant case, DeTray is seeking damages for breach of contract, and is not limited to an award based on restitution.¹⁵

2. The trial court properly interpreted and applied Article 9.7 of the LLC Agreement.

The Dragts also assert that “whatever measure of damages is used,” paragraph 9.7 of the LLC Agreement does not govern the damages

¹⁵ As explained in Section IV Part I below, if DeTray’s claims based on breach of contract are rejected on the grounds that there was no valid contract between the parties, he is not foreclosed from advancing claims based on unjust enrichment.

calculation. Appellants' Brief, p. 42. However, Article 9.7 was clearly and unambiguously intended to govern the distribution of the proceeds of any sale of the Property by the LLC. Under the modified agreement of the parties, the Dragts were obligated to compensate DeTray in the event of a property sale even if they were the ones to sell the Property, rather than the LLC. Because the parties did not abrogate the rest of the LLC Agreement when they modified it, non-conflicting provisions in it remain binding. *See Flower*, 127 Wn. App. at 29. The division of the proceeds from the Dragts' sale to Tahoma Terra are governed by Article 9.7.

The trial court properly interpreted Article 9.7 in calculating damages. Contrary to the Dragts' assertion, Article 9.7 does not call for the Dragts to receive \$18,000 per acre in the event of any sale. Instead, Article 9.7 states that “[i]n return for his contribution of property Dragt shall be entitled to receive \$1,273.00 per acre when sold” (emphasis added). The only reference to \$18,000 per acre in Article 9.7 occurs in the following statement: “[w]hen real estate developments are owned or leased by the Company any allocation of funds based on land value shall be made based on an initial value of \$18,000 per acre.” This passage is inapplicable under the circumstances because no real estate development was “owned or leased by the company” and there is no need for any “allocation of funds based on land value.” Having unilaterally chosen to accept Tahoma Terra's offer for the property, the Dragts are in no position

to credibly complain that the contractually required division of the proceeds leaves them with less money than they would like.¹⁶

G. The trial court did not abuse its discretion in allowing the testimony of Frank Kirkbride.

The trial court did not abuse its discretion in admitting Kirkbride's testimony and Exhibit 221. *See State v. Majors*, 82 Wn. App. 843, 848, 919 P.2d 1258 (1996) (articulating the "abuse of discretion" standard as applied to evidentiary rulings). The Dragts wrongly claim that "Kirkbride . . . did not participate in drafting the LLC Agreement and therefore had no knowledge of contractual intent."¹⁷ Instead, as Kirkbride clearly testified, he "created [the] exhibits" to the LLC Agreement, exhibits which the Dragts have attempted to use to infer contractual intent. RP (3/1/2006) 135 ln. 17. *Cf.* Appellants' Brief, p. 10 (referring to the "pro formas"

¹⁶ In a footnote, the Dragts assert that "[t]he trial court interpreted paragraph 9.7 right the first time." Appellants' Brief, pp. 43-44, note 15. The Dragts are referring to the trial court's initial view that "Mr. Dragt should be given the value of his property, whatever that equity is," that "Mr. DeTray should be given the value of his contributions of \$593,462.66," and that "then the balance should be split fifty-fifty." RP (3/2/2006) at pp. 48-49. The Dragts overlook the fact that the trial court made no reference to Article 9.7 in this discussion. The Dragts also fail to mention that in describing the equitable value of the Property, the trial court was clearly referring to its value at the time it was first encumbered with a mortgage. RP (3/2/2006) 48 ln. 13-24. If this Court determines that the trial court's initial view of the just outcome is the proper resolution of the case, it should remand to the trial court with directions to establish the value of the Dragts' equity in the Property at the time it was encumbered with a mortgage on or about January 24, 1997.

¹⁷ The Dragts also incorrectly assert that Kirkbride "was called to rebut DeTray's own testimony regarding the parties' intent to value the Dragts' land at \$18,000 per acre." There is no such testimony from DeTray to rebut. Page 10 of Appellants' Brief purports to locate such testimony in the Report of Proceedings from February 27, 2006 at pages 66 through 67. Those pages simply contain DeTray's affirmation that "when real estate developments are owned or leased by the Company any allocation of funds based on land value shall be made based on an initial value of \$18,000 per acre." RP (2/27/06) at pp. 66-67 (emphasis added). Because no real estate developments were owned or leased by the company, this provision has no bearing on this case.

prepared by Kirkbride). As the originator of parts of the LLC Agreement, Kirkbride was properly allowed to testify about their meaning. RP (3/2/06) 142 ln. 20 to 143 ln. 3.

Even if Kirkbride's testimony and Exhibit 221 were improperly admitted, there is substantial evidence to support the trial courts Finding 45 and Conclusions 8 and 12. *Cf.* Appellants' Brief, p. 46. That Finding and those Conclusions all relate to the proper division of the proceeds from the Dragts' sale of the Property to Tahoma Terra. Because Article 9.7 is unambiguous, and clearly calls for the division awarded by the trial court, the plain language of the LLC Agreement itself adequately supports the trial court's determinations.

H. DeTray is entitled to his fees on appeal.

The LLC Agreement provides that the prevailing party in any dispute concerning its terms is entitled to its reasonable costs and attorneys fees. Ex. 178 at 25, ¶ 15.14. This contractual provision justifies an award of costs and fees to the prevailing party on appeal. *See, e.g., West Coast Stationery v. Kennewick*, 39 Wn. App. 466, 477, 694 P.2d. 1101 (1988). If this Court affirms the trial court, DeTray will be the prevailing party, and accordingly requests his fees and costs on appeal, in an amount to be determined later.

I. If this Court finds no enforceable contract existed between the Dragts and DeTray, it should remand to the trial court for entry of findings of fact and conclusions of law pertaining to unjust enrichment.

If this Court finds that there was no enforceable contract requiring the Dragts to hold their property for development and to split the proceeds from any sale with DeTray in accordance with the terms of the written LLC Agreement, it should remand this matter to the trial court with directions to enter findings of fact and conclusions of law regarding unjust enrichment.

DeTray anticipates that the Dragts will respond to this request by recycling their old argument that DeTray's pursuit of a contractual remedy bars his alternative request for a judgment based on unjust enrichment. CP 468. It is certainly true that a plaintiff cannot recover in unjust enrichment in the face of a valid contract. *See, e.g., McDonald v. Hayner*, 43 Wn. App. 81, 85-86, 715 P.2d 519 (1986). However, the trial court previously determined on summary judgment that the option contained in the written LLC Agreement is invalid. If this Court overturns the trial court's Findings and Conclusions and determines that the Dragts did not agree to hold their property for development by DeTray and share the proceeds from any sale, then there was no contract between the parties concerning the central issues in dispute. The fact that the written LLC Agreement may remain valid for some other hypothetical purpose is no bar to an unjust enrichment recovery based on the interactions of the

parties with regard to the Dragts' former dairy.¹⁸ If the contract modifications asserted by DeTray are invalid, the trial court should be instructed to enter findings and conclusion on DeTray's unjust enrichment claim.

V. CONCLUSION

Substantial evidence in the record court provides clear and convincing support for the trial court's determination that the Dragts and DeTray modified their contractual obligations through their words and conduct subsequent to the execution of the written LLC Agreement. The trial court correctly concluded as a matter of law that the modified contract was valid and legally enforceable, that the Dragts breached their new contractual duties (and their duty of good faith) by selling the Property to Tahoma Terra without notice to DeTray and without sharing the proceeds, and that DeTray was damaged in the amount of \$2,067,773.88. This Court should affirm the trial court, and grant DeTray his fees on appeal. In the alternative, if this Court finds that there was no valid contract between the parties concerning the development of the Property, it should

¹⁸ The linked cases of Bowman v. Hardgrove, 200 Wash. 78, 93 P.2d 303 (1939) and Hardgrove v. Bowman, 10 Wn.2d 136, 116 P.2d 336 (1941) clearly establish that a party seeking a recovery based on breach of contract is not barred from later recovering based on unjust enrichment if the asserted contract is found to be unenforceable. In Bowman v. Hardgrove, a lessor (Bowman) sought to evict a lessee (Hardgrove) on the grounds that a ten year lease was invalid because the lessor's wife had not signed it. The lessee defended the lease, but the court found it to be unenforceable. Bowman v. Hardgrove, 200 Wash. 78, 93 P.2d 303 (1939). In the "aftermath" case of Hardgrove v. Bowman, the lessee—who had previously maintained the validity of the lease—sought to recover in unjust enrichment for improvements he had made to the property. The court found for the lessee. Like the lessee Hardgrove, DeTray believes he has a valid contract with his opposing party. However, if the Court determines that there is no such valid contract, DeTray is entitled to recover in unjust enrichment, just as was the lessee in Hardgrove.

remand this matter to the trial court with directions to enter findings of fact and conclusions of law on DeTray's claim for unjust enrichment.

RESPECTFULLY SUBMITTED this 6th day of November, 2006.

R. ALAN SWANSON, PLLC

By: R. Alan Swanson, by
David J. Corbett, WSBA # 30895
R. Alan Swanson, WSBA # 1181 *per prior approval.*

EISENHOWER & CARLSON, PLLC

By: 
David J. Corbett, WSBA # 30895
Robert G. Casey, WSBA # 14183

Attorneys for Respondents
E. Paul DeTray and Phyllis DeTray

Certificate of Service

I certify that on the 6th day of November, 2006, I served the party listed below with a true and correct copy of the foregoing Brief of Respondents E. Paul DeTray and Phyllis DeTray in the above-entitled matter by depositing the same with ABC Legal Services for same-day delivery to:

Kevin A. Bay
Ryan, Swanson & Cleveland, PLLC
1201 Third Avenue, Suite 3400
Seattle, WA 98101-3034

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED at Tacoma, Washington, this 6th day of November, 2006.

Deidre M. Turnbull
Deidre M. Turnbull
Legal Assistant

FILED
CLERK OF DISTRICT COURT
TACOMA, WASHINGTON
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BY LR

APPENDIX A

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EXPEDITE
 Hearing was held:
Date: Friday, January 27, 2006
Time: 10:45 a.m.
Judge/Calendar: Hicks

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON
IN AND FOR THE COUNTY OF THURSTON

HENRY DRAGT and JANE DRAGT, husband
and wife,

Plaintiffs,

vs.

DRAGT/DETRAY L.L.C., a Washington limited
liability company; and E. PAUL DETRAY and
PHYLLIS DETRAY and their marital
community,

Defendants.

NO. 04-2-01956-4

**ORDER ON MOTION FOR PARTIAL
SUMMARY JUDGMENT OF
DEFENDANTS' E. PAUL DETRAY AND
PHYLLIS DETRAY**

THIS MATTER having come before the undersigned judge of the above-entitled Court for hearing on the Motion of Defendants E. Paul DeTray and Phyllis Detray, and their marital community, for Partial Summary Judgment of Dismissal of Plaintiffs' Claims for Gross Mismanagement and Intentional Misconduct, and the Court having read the records and files herein, including the following pleadings submitted by the Defendants:

1. Motion and Memorandum for Partial Summary Judgment on Plaintiffs' Claims for Gross Mismanagement and Intentional Misconduct.
2. Declaration of R. Alan Swanson in Support of Motion.
3. Reply Brief

And the Court having also reviewed the following pleadings previously filed by the Defendants:

ORDER ON MOTION FOR PARTIAL SUMMARY
JUDGMENT OF DEFENDANTS' E. PAUL DETRAY
AND PHYLLIS DETRAY - 1 -

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- 1 4. May 5, 2005 Declaration of Henry Dragt.
2 5. June 10, 2005 Declaration of Paul DeTray.
3 6. June 10, 2005 Declaration of Frank Kirkbride.

4 And the Court having also reviewed the following pleadings submitted by the Plaintiffs:

- 5 1. Opposition Brief to Defendants' Motion for Partial Summary Judgment.

6 And the matter having proceeded to hearing on January 27, 2006, and the Court having heard
7 arguments of Counsel, and being otherwise fully advised, NOW THEREFORE IT IS

8 ORDERED that the Defendants' Motion for Partial Summary Judgment of Dismissal of
9 Plaintiffs' Claim for Intentional Misconduct against Defendants E. Paul DeTray and Phyllis
10 DeTray, husband and wife, and their marital community is hereby granted, and said claim is
11 hereby dismissed with prejudice and without cost to either party; and it is further

12 ORDERED that the Defendants' Motion for Partial Summary Judgment of Dismissal of
13 Plaintiffs' Claim for Gross Mismanagement is hereby denied; however, it is further

14 ORDERED that any damages claimed by the Plaintiffs arising out of any alleged gross
15 negligence of the Defendants E. Paul DeTray and Phyllis DeTray be limited to any alleged
16 diminution in the value of the property which is said to have been now worth only 3 million
17 dollars instead of 4 million dollars, and that any claim of future speculative profits shall not be
18 considered.

19 DONE IN OPEN COURT this 10 day of Feb, 2006.

20 RICHARD D. HICKS

21 Honorable Richard Hicks

22 Presented By:

22 Approved as to Form and For Entry:

23 si
24 R. Alan Swanson, WSBA #1181
25 Attorney for Defendants

23 si
24 Kevin Bay, WSBA # 19821
25 Attorney for Plaintiff

26
ORDER ON MOTION FOR PARTIAL SUMMARY
JUDGMENT OF DEFENDANTS' E. PAUL DETRAY
AND PHYLLIS DETRAY - 2 -

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