

FILED

JAN 24 2013

COURT OF APPEALS
DIVISION III
STATE OF WASHINGTON
By _____

NO. 307921

COURT OF APPEALS, DIVISION III
OF THE STATE OF WASHINGTON

KATHLEEN G. KILCULLEN,

Respondent,

v.

CALBOM & SCHWAB, P.S.C.,

Appellant.

BRIEF OF RESPONDENT

STEVEN C. LACY
Attorney for Respondent
Lacy Kane, P.S.
300 Eastmont Avenue
East Wenatchee, WA 98802
(509) 884-9541
WSBA NO. 10814

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I. INTRODUCTION

Appellant Calbom & Schwab, P.S.C., has sought review by this Court for the Revised Order Re: Plaintiff's Motion for Partial Summary Judgment. Calbom & Schwab argues that the trial court erred in rendering its decision directing Calbom & Schwab to pay back the loan by Respondent, Kathleen G. Kilcullen, within four (4) months from entry of the Order.

The trial court did not err. Washington law allows a court to impose a reasonable term for the performance of a contract. The trial court was also within its equitable powers to terminate the benefit enjoyed by Calbom & Schwab at the expense of Kilcullen. The trial court should be affirmed.

II. ISSUES PRESENTED BY CALBOM & SCHWAB'S ASSIGNMENTS OF ERROR

Kathleen Kilcullen was a shareholder of the law firm, Calbom & Schwab. The shareholders agreed to loan their profit distributions back to Calbom & Schwab so that it would have adequate funds for operating expenses. The arrangement benefitted the firm as a tax saving strategy and avoided expensive borrowing from a lending institution. Shareholders realized a benefit by the maximization of profit for the firm. The loans did

not provide a specific time for repayment. Instead, the arrangement was that the loans would be repaid upon the achievement of financial benchmarks, of which, Calbom & Schwab had the ability to manipulate.

Kathleen Kilcullen was terminated by Calbom & Schwab in January, 2010.¹ Did the trial court err in imposing a reasonable time for Calbom & Schwab to repay Kilcullen with its Revised Order Re: Plaintiff's Motion for Partial Summary Judgment?

Did the trial court err when it determined that Calbom & Schwab's ability to manipulate its accounts to avoid reaching financial benchmarks made its promise to repay the loan illusory?

After determining that Calbom & Schwab's promise was illusory, thereby invalidating the contract for failure of consideration, did the trial court properly apply equity in finding that Calbom & Schwab was unjustly enriched and ordering repayment of the loan within four (4) months?

1
Calbom & Schwab emphasizes that the termination was "*for cause*." Of course, Kilcullen disputes that characterization and her lawsuit includes a claim for breach of the employment contract as there existed no just cause for her termination. Issues of her termination are irrelevant for this appeal.

III. STATEMENT OF THE CASE

A. Statement of Facts

Kathleen Kilcullen became a shareholder of Calbom & Schwab in 1992. (CP 22). During her time with Calbom & Schwab, Ms. Kilcullen was instrumental in developing and growing the firm's Social Security practice, the largest such practice in Central and North Central Washington. (Id.).

In 2009, the other shareholders of Calbom & Schwab, G. Joe ("Joe") Schwab, Jeff Schwab and David L. Lybbert, began appropriating the resources of Calbom & Schwab for the benefit of Schwab & Schwab, P.C., another entity that those three shareholders had formed. The resources appropriated included personnel, equipment, supplies, servers, funds, financial statements, work product, and client information. Kilcullen expressed her opposition to the misappropriation of those resources. (CP 23).

Despite her repeated requests, Kilcullen was never given any information reflecting the hours, time, and money spent on Schwab & Schwab. The other three shareholders of Calbom & Schwab claimed that employees were keeping track of their time spent towards Schwab & Schwab so that such wages would be paid by Schwab & Schwab. Kilcullen confirmed that this was not true when signing pay checks. An employee

received a full paycheck from Calbom & Schwab despite performing a substantial amount of work for Schwab & Schwab during the pay period. (Id.).

During 2009, the other shareholders held meetings without notice or invitation to Kilcullen. Substantive decisions were made during the meetings without the participation or knowledge of Kilcullen. Joe Schwab claimed that the decisions benefitted both companies. He told Kilcullen that he had forgotten to tell her about the meetings. Kilcullen was not only cut-off from the decision-making for Calbom & Schwab, but she was ignored at staff meetings, as well. (Id.).

In early December, 2009, Kilcullen received a request to sign papers requiring Calbom & Schwab's guarantee of a loan of \$100,000 to Schwab & Schwab. Kilcullen refused to sign the papers. (CP 24). In an email sent on December 29, 2009, Joe Schwab stated that if the loan could not be processed and guaranteed by Calbom & Schwab, Calbom & Schwab would be dissolved. (Id.). Kilcullen heard nothing more about the loan issue. (Id.).

By a letter dated January 27, 2010, Kilcullen was given notice by Joe Schwab that she was terminated. (Id.). Kilcullen was informed that she was divested of her shares in Calbom & Schwab in late April, 2010. (Id.).

It was standard practice for the shareholders of Calbom & Schwab to loan the corporation money from their yearly profits for operating expenses to start up the following year. This relieved the corporation from borrowing funds for that purpose. (Id.). The arrangement also helped Calbom & Schwab avoid federal income tax. (CP 38). Interest on the loans is set at a variable rate consisting of the prime rate plus two percent (2%). Since December 16, 2008, the prime rate has been 3.25 %. The funds loaned back to Calbom & Schwab have been incurring interest at 5.25%. (CP 24).

Repayment of the loans was conditioned on the requirement that, at the end of any given month, Calbom & Schwab would have at least \$300,000 in its accounts comprising the following: (1) a minimum of \$200,000 available as reserve for the payment of expenses and salaries; and (2) \$100,000 available to distribute to the shareholders in accordance with percentage of ownership. (CP 25).

At the end of 2009, the year end statement for Calbom & Schwab reflected that \$89,650.83 was owed to Kilcullen because of the operating expense loans. (Id.). Kilcullen received payments for interest when she was employed. (Id.). Since her termination, she has not received any interest payments. (Id.).

B. Procedural History

Kilcullen filed the action below on September 10, 2010, alleging breach of contract and an action for monies owed. (CP 2-5). Kilcullen seeks repayment of funds loaned by her to Calbom & Schwab. (CP 3-4).

The trial court rendered its decision below after Kilcullen filed her Motion for Partial Summary Judgment Regarding Operating Loan. (CP 12-21). The trial court determined that there was a question of fact whether a \$20,000 “shareholder’s distribution” was a payment towards the loan. (CP 93). It determined that the remaining amount of the principal, \$69,560.83, along with interest at 5.25% since the date of the loan, was due and owing. The trial court directed that Calbom & Schwab pay Kilcullen the monies owed within four (4) months of the date of the Order. (*Id.*).

By Order filed September 26, 2012, this Court has recognized that Calbom & Schwab may appeal the trial court’s Order as a matter of right.

IV. ARGUMENT

A. Review of Order on Summary Judgment

A decision granting summary judgment is reviewed de novo. *Braaten v. Saberhagen Holdings*, 165 Wn.2d 373, 383, 198 P.3d 493 (2008). The appellate court engages in the same inquiry as the trial court. *Hontz v. State*,

105 Wn.2d 302, 311, 714 P.2d 1176 (1986).

Summary judgment shall be granted "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." CR 56(c). "A material fact is one upon which the outcome of the litigation depends." *Clements v. Travelers Indem. Co.*, 121 Wn.2d 243, 249, 850 P.2d 1287 (1993). The court is to consider the facts and all reasonable inferences in the light most favorable to the non-moving party. *Wilson v. Steinbach*, 98 Wn.2d 434, 437, 656 P.2d 1030 (1982). If from all the evidence, reasonable persons could reach only one conclusion, summary judgment should be granted. *Clements*, 121 Wn.2d at 249; *Wilson*, 98 Wn.2d at 437.

B. Loan to be Re-Paid within a Reasonable Time

Ms. Kilcullen's loan to Calbom & Schwab created a contract. "A contract "may arise by inference or implication from circumstances which, according to the ordinary course of dealing and the common understanding of men, show a mutual intention on the part of the parties to contract with each other." *Bell v. Hegewald*, 95 Wn.2d 686, 690, 628 P.2d 1305 (1981). Profit shares paid to Ms. Kilcullen were loaned back to Calbom & Schwab

to cover the next year's operating expenses. This benefitted Calbom & Schwab by avoiding the costs and expenses associated with obtaining a loan or line of credit from a financial institution. It was also a savings to Calbom & Schwab because the arrangement allowed Calbom & Schwab to avoid paying corporate taxes. (CP 29). As a shareholder of Calbom & Schwab, Ms. Kilcullen recognized any benefit to Calbom & Schwab meant more profits for the shareholders. (CP 25).

The terms of the contract can be determined by the course of the parties' actions. The interpretation of a contract should be made by "viewing the contract as a whole, 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." *Berg v. Hudesman*, 115 Wn.2d 657, 667, 801 P.2d 222 (1990)(quoting *Stender v. Twin City Foods, Inc.*, 82 Wn.2d 250, 254, 510 P.2d 221 (1973)).

The loan back to the company did not include explicit terms concerning the duration of the loan or when Kilcullen could expect payment. The Washington Supreme Court has long ago considered the absence of such terms and its rules of interpretation have withstood the test of time. In order

for a contract to be enforceable, a contract must be reasonably certain as to its terms and duration. *Foelkner v. Perkins*, 197 Wash. 462, 466, 85 P.2d 1095 (1938). "The fact that an agreement does not fix a definite time when money should be returned, advanced, or repaid would not make the contract fatally defective for uncertainty or indefiniteness. The general rule is that, where a thing is to be done, and no time is fixed, it will be presumed that a reasonable time was intended." *Merchants' Bank of Canada v. Sims*, 122 Wash. 106, 112, 209 P. 1113 (1922); *see also Foelkner*, 197 Wash. at 467 (when no time is provided for performance, the court will presume that a reasonable time was intended); *see also Cromwell v. Gruber*, 7 Wn. App. 363, 366, 499 P.2d 1285 (1972) (where contract silent as to duration, court may imply a reasonable time).

Calbom & Schwab misrepresents the record and states that the trial court imposed a period of four (4) months as the time for performance. (Brief of Appellant, pg 17). Kilcullen has been waiting many years for Calbom & Schwab's performance. At the end of 2009, Kilcullen was owed \$89,650.83. (CP 25). By the time that the trial court issued its Order, thirty-nine (39) months had passed since Kilcullen's last loan to Calbom & Schwab. (CP 33; CP 92-94). The record shows Kilcullen loaning her money back to Calbom

& Schwab since 2002. (CP 32; CP 43). With the Order, Calbom & Schwab was given an additional four (4) months to perform.

Clearly, the trial court determined that a reasonable time for performance had passed. Such a determination is not open to dispute. Over four years has passed since Kilcullen loaned any money. It has been over three years since Calbom & Schwab fired her. The debt had its origins over ten years ago. Instead of determining that the notes were due at the date of the Order or earlier, the trial court allowed an extra four (4) months for Calbom & Schwab to make arrangements for payment before it would be in default. The trial court implied a reasonable period for the performance of the contract.

C. Kilcullen's Loss of the Benefit of the Bargain Constitutes Breach

A valid contract must be supported by consideration. *King v. Riveland*, 125 Wn.2d 500, 505, 886 P.2d 160 (1994). "Consideration is 'any act, forbearance, creation, modification or destruction of a legal relationship, or return promise given in exchange.'" *Labriola v. Pollard Group, Inc.*, 152 Wn.2d 828, 833, 100 P.3d 791 (2004)(quoting *King*, 125 Wn.2d at 505). Consideration is described as a "bargained-for exchange of promises." 152 Wn.2d at 833.

Part of the consideration for Kilcullen was her continued employment as an attorney and a shareholder at Calbom & Schwab. Shareholders would realize a benefit from the loan arrangement which reduced costs and avoided tax liabilities for the corporation. (CP 25; CP 29). This arrangement became a benefit of the bargain as shareholders received additional profits because of the savings. Once Kilcullen was terminated from her employment and her shares were taken away, Kilcullen was deprived of this benefit. The deprivation of a benefit of the bargain is a factor to consider for the material breach of a contract. *Bailee Communications, Ltd. v. Trend Business Systems*, 53 Wn. App. 77, 83, 765 P.2d 339 (1988).

This Court can sustain a trial court's judgment upon any theory established by the pleadings and supported by the evidence, even if the theory was not considered by the trial court. *LaMon v. Butler*, 112 Wn.2d 193, 200-01, 770 P.2d 1027 (1989). The trial court's decision can be supported by a determination that Calbom & Schwab materially breached the contract by taking away Kilcullen's benefit of the bargain--her continued employment and shareholder status.

D. Court's Decision Afforded a Remedy Through Equity

1. An Illusory Promise

The trial court's decision can also be affirmed through the exercise of equity. The unwritten agreement concerning the loaning of shareholder profit shares back to Calbom & Schwab provided that the shareholder would be paid back once there existed a \$200,000 reserve for the payment of salaries and expenses and \$100,000 available for distribution to the shareholder attorneys. (CP 25). If the court was to enforce the contract without any time requirements for performance, an inequitable outcome results. It has been over three years since Ms. Kilcullen was terminated from her employment. By the date of the trial court's Order, thirty-nine (39) months had passed since Kilcullen last loaned money back to Calbom & Schwab. (CP 33; CP 92-94). At least ten years has past since Kilcullen began to loan her profit shares back to Calbom & Schwab. (CP 32; CP 43).

Calbom & Schwab is in control of its accounting practices and operations. It has the ability to control the amount of its profits. It is conceivable that Calbom & Schwab will never satisfy the benchmark of \$200,000 of reserve. Significant is Joe Schwab's statement that in 2010 the corporation retained its profits and paid taxes of \$86,457.00. (CP 28). Mr.

Schwab does not explain how Calbom & Schwab utilized those profits. It is obvious that Calbom & Schwab chose not to pay its lending shareholders.

Under the arrangement, Calbom & Schwab is granted discretion to determine whether the reserve account is maintained at the threshold amount. Its promise to pay the shareholders attorneys and Kilcullen was illusory. *See King County v. Taxpayers of King County*, 133 Wn.2d 584, 599-600, 949 P.2d 1260 (1997) (illusory promise is a promise which makes performance optional for the promisor); *see also Spooner v. Reserve Life Ins. Co.*, 47 Wn.2d 454, 458, 287 P.2d 735 (1955) (promise may be illusory if it is so indefinite it cannot be enforced, terms of the promise make its performance optional, or performance is entirely discretionary on the part of the promisor). If a promise is illusory, there is no consideration and, therefore, no enforceable contract. *Omni Group, Inc. v. Seattle-First Nat. Bank*, 32 Wn. App. 22, 24-25, 645 P.2d 727, *rev. denied*, 97 Wn.2d 1036 (1982).

2. Equitable Remedy Available

No consideration was provided by Calbom & Schwab's illusory promise to pay back the shareholders once its reserves reached benchmarks. Without consideration, there was no enforceable contract. The trial court had the authority to award relief to Kilcullen under the doctrine of unjust

enrichment. *See Young v. Young*, 164 Wn.2d 477, 484, 191 P.3d 1258 (2008) (unjust enrichment is the method of recovery for the value of the benefit retained absent a contract because fairness and justice require it). The circumstances are, indeed, unjust considering that Calbom & Schwab utilizes Kilcullen's money at no benefit to her because it deprived her of her continued employment and shareholder status. Meanwhile, it enjoyed the fruits of her labor. (CP 77).

Unjust enrichment involves implying a contract in law due to issues of fairness. *See Young*, 164 Wn.2d at 484 (citing *Bill v. Gatavara*, 34 Wn.2d 645, 650, 209 P.2d 457 (1949) ("the terms 'restitution' and 'unjust enrichment' are the modern designations of the older doctrine of 'quasi contracts.'")). The elements for unjust enrichment are: (1) The defendant receives a benefit from the plaintiff; (2) the defendant appreciates or has knowledge of the benefit received at the plaintiff's expense; and (3) the circumstances are such that it would be inequitable and unjust for the defendant to retain the benefit without payment. 164 Wn.2d at 484-85.

Young v. Young involved the improvement of real property by tenants. The Washington Supreme Court observed that recovery under the doctrine of unjust enrichment for the improvement to real property may be measured

by the amount of the benefit conferred upon the defendant or, alternatively, by the extent the property has been increased in value. 164 Wn.2d at 487. In a matter not involving real property, the Idaho Court of Appeals has held that recovery under unjust enrichment is based on the amount of benefit which would be unjust for the defendant to retain. *Erickson v. Flynn*, 138 Idaho 430, 434, 64 P.3d 959, 963 (2002); *see also Cerkonek v. Dibble*, 42 Wn.2d 451, 459, 256 P.2d 488 (1953)(measure of recovery for unjust enrichment is the "amount of which it is against conscience for the defendant to keep" (*quoting* Keener on Quasi Contracts 183)).

Calbom & Schwab has been unjustly enriched by receiving and retaining Kilcullen's money after her employment was terminated and her shares were taken away. It is unjust for Calbom & Schwab to continue to enjoy this arrangement while Kilcullen does not realize a corresponding benefit. The trial court's Order can be sustained through the doctrine of unjust enrichment.

V. CONCLUSION

The trial court did not err in implying a reasonable term for the contract. The trial court's decision can be affirmed through the theory that Calbom & Schwab deprived Kilcullen her benefit of the bargain when it terminated her employment and took her shares. The trial court can also be

affirmed because Calbom & Schwab should no longer enjoy Kilcullen's funds with no corresponding benefit to her. Notions of Equity dictate that Calbom & Schwab should pay Kilcullen her money.

Respectfully Submitted this 22nd day of January, 2013.

LACY KANE, P.S.

By Stewart R. Smith
STEWART R. SMITH, WSBA No. 22746
Attorneys for Respondent