

FILED
COURT OF APPEALS DIV I
STATE OF WASHINGTON

2011 AUG -1 AM 10: 59

No. 66752-1

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

NAME INTELLIGENCE, INC., a Washington corporation; and JAY
WESTERDAL, an individual

Appellants,

vs.

GUSTAVO NELSON ARZOLA, an individual, MICHAEL KLATT, an
individual, and SUSAN PROSSER, an individual,

Respondents.

APPEAL FROM THE SUPERIOR COURT
FOR KING COUNTY
THE HONORABLE CAROL A. SCHAPIRA

BRIEF OF APPELLANTS

SMITH GOODFRIEND, P.S.

HOLMQUIST & GARDINER, PLLC

By: Howard M. Goodfriend
WSBA No. 14355

By: Hamilton H. Gardiner
WSBA No. 37827

1109 First Avenue, Suite 500
Seattle, WA 98101
(206) 624-0974

1000 2nd Avenue, Suite 1770
Seattle, WA 98104
(206) 438-9116

Attorneys for Appellants

TABLE OF CONTENTS

I. INTRODUCTION 1

II. ASSIGNMENTS OF ERROR..... 2

III. ISSUES RELATED TO ASSIGNMENTS OF ERROR 3

IV. STATEMENT OF THE CASE 3

 A. Name Intelligence Granted Its Employees The Right To Corporate Stock Before It Was Purchased By A California Corporation In 2008..... 3

 B. Respondents Agreed To Surrender Their Stock Rights And Received The First Of Three Payments From Name Intelligence..... 5

 C. Name Intelligence Postponed Payment Of The Second And Third Payments To Respondents After A Dispute With Its Purchaser Delayed The Purchaser’s Second Payment To Name Intelligence And Its Shareholders. 7

 D. Two Superior Court Judges Denied Summary Judgment, Rejecting The Argument That the Payments Due Respondents For Cancellation Of Their Stock Rights Were “Wages” Under RCW ch. 49.52..... 8

 E. The Trial Court Held That The Cancellation Agreement Payments Were “Wages” As A Matter Of Law And Entered Judgment Against Name Intelligence And Westerdal For Punitive Damages And Attorney Fees..... 10

V.	ARGUMENT	12
A.	Standard of Review: The Trial Court’s Summary Determination That Payments Under The Stock Right Cancellation Agreement Constitute “Wages” Under RCW 49.52.050 Is Reviewed De Novo As An Error Of Law.	12
B.	Payments Owed Former Employees In Consideration Of An Agreement To Cancel Their Stock Rights Are Not “Wages” Under RCW Ch. 49.52 Because They Are Not Payments For Labor Or Services.....	13
1.	The Wage Withholding Statute Applies To Fixed Amounts Owed Employees As Compensation For Their Services.....	13
2.	Stock Rights Are Not “Wages” Governed By RCW 49.52.050 Because The Total Number Of Shares Granted Respondents Was Discretionary.....	15
3.	The Stock Right Payments Are Not “Wages” Because The Payments Were Based On The Value Of Name Intelligence And Not On The Value Of The Respondents’ Services.	17
4.	The Cancellation Agreement Paid Respondents For Their Proprietary Interest In The Corporation, And Not For Their Services Or Labor.	18
C.	The Trial Court Erred In Awarding Attorney Fees And Litigation Expenses Under RCW 49.48.030 And RCW 49.52.070.	21
VI.	CONCLUSION.....	22

TABLE OF AUTHORITIES

FEDERAL CASES

<i>Coulombe v. Total Renal Care Holdings, Inc.</i> , 2007 WL 1367601 (W.D. Wash. 2007), <i>aff'd</i> , 298 Fed.Appx. 617 (9th Cir. 2008).....	16, 17
<i>Falkowski v. Imation Corp.</i> , 309 F.3d 1123, <i>amended by</i> , 320 F.3d 905 (9 th Cir. 2003)	19
<i>International Business Machines v. Bajorek</i> , 191 F.3d 1033 (9 th Cir. 1999)	16, 18, 19
<i>May v. Honeywell Int'l, Inc.</i> , 331 Fed.Appx. 531 (9 th Cir. 2009)	18

STATE CASES

<i>Bates v. City of Richland</i> , 112 Wn. App. 919, 51 P.3d 816 (2002)	14, 18
<i>Byrne v. Courtesy Ford, Inc.</i> , 108 Wn. App. 683, 32 P.3d 307 (2001), <i>rev. denied</i> , 146 Wn.2d 1019 (2002)	15, 16
<i>Catalyst Health Solutions v. Magill</i> , 414 Md. 457, 995 A.2d 960 (2010)	19
<i>Dautel v. Heritage Home Center, Inc.</i> , 89 Wn. App. 148, 948 P.2d 397 (1997), <i>rev. denied</i> , 135 Wn.2d 1003 (1998)	18
<i>Dice v. City of Montesano</i> , 131 Wn. App. 675, 128 P.3d 1253, <i>rev. denied</i> , 158 Wn.2d 1017 (2006)	18
<i>Ellerman v. Centerpoint Prepress, Inc.</i> , 143 Wn.2d 514, 22 P.3d 795 (2001)	14

<i>Guiry v. Goldman, Sachs & Co.</i> , 31 A.D.3d 70, 814 N.Y.S.2d 617 (2006)	17
<i>Hmelyar v. Phoenix Controls</i> , 339 Ill. App. 700, 791 N.E.2d 695 (2003).....	19
<i>Hume v. American Disposal Co.</i> , 124 Wn.2d 656, 880 P.2d 988 (1994), <i>cert. denied</i> , 513 U.S. 1112 (1995).....	22
<i>MacDonald v. Wockner</i> , 44 Wn.2d 261, 267 P.2d 97 (1954)	12
<i>Mackey v. American Fashion Institute Corp.</i> , 60 Wn. App. 426, 804 P.2d 642 (1991).....	13
<i>Marriage of Langham and Kolde</i> , 153 Wn.2d 553, 106 P.3d 212 (2005)	18
<i>Morgan v. Kingen</i> , 141 Wn. App. 143, 169 P.3d 487 (2007), <i>aff'd</i> , 166 Wn.2d 526, 169 P.3d 487 (2009)	13, 14, 19
<i>Paolini v. Albertson's Inc.</i> , 143 Id. 547, 149 P.3d 822 (2006), <i>answer to certified question conformed to</i> , 482 F.3d 1149 (9 th Cir. 2007)	19
<i>Powell v. Republic Creosoting Co.</i> , 172 Wash. 155, 19 P.2d 919 (1933)	16
<i>Schilling v. Radio Holdings, Inc.</i> , 136 Wn.2d 152 , 961 P.2d 371 (1998)	14
<i>Simon v. Riblet Tramway Co.</i> ,8 Wn. App. 289, 505 P.2d 1291, <i>cert. denied</i> , 414 U.S. 975(1973).....	16

STATUTES

RCW 4.84.010.....	2, 22
RCW 49.46.010.....	14, 22
RCW ch. 49.48.....	8
RCW 49.48.030.....	11, 21-22
RCW ch. 49.52.....	8, 13
RCW 49.52.050.....	1, 3, 12-13, 15-16, 21-22
RCW 49.52.070.....	1, 3, 8, 10-12, 21-22

OTHER AUTHORITIES

<i>The American Heritage Dictionary of the English Language 2007 (3rd ed. 1992).....</i>	14
--	----

I. INTRODUCTION

Washington's wage withholding statute imposes double damages only on an employer or its principal who willfully deprives an "employee of any part of his or her wages." RCW 49.52.050(2), .070. Here, after a corporation granted its employees the right to shares of its stock, it was purchased by another entity. The corporation agreed to pay the employees for all their rights to the corporation's stock based on the amount the purchaser promised to pay over time for all the corporation's assets. After the purchaser failed to make its second payment, the corporation delayed its second payment to the former employees, who then filed suit for breach of contract and wrongful wage withholding. Summarily reversing the summary judgment rulings of two previous superior court judges, the trial court held that the payments were a "byproduct" of the employment relationship, and awarded punitive damages and fees under the wage withholding statute. Because the payments were owed to the former employees for their property rights in the corporation, and not for their services, the corporation and its CEO ask this court to reverse the judgments entered against them.

II. ASSIGNMENTS OF ERROR

1. The trial court erred in entering the following Findings of Fact and Conclusions of Law (App. A):

FF 2.15, CP 481: The Court found that stock options are not wages but that the cash payments under the SRC Agreements were “wages” as that term is defined in RCW 49.48 et seq. and RCW 49.52 et seq because it is compensation arising out of the employment relationship.

FF 5.2, CP 484: Therefore, plaintiffs are entitled to an additional award of the amount of wages unlawfully withheld by defendants for the May 2009 payment.

FF 5.3, CP 484: Plaintiffs are entitled to an award of \$7,381.82.

2. The trial court erred in entering its Findings of Fact and Conclusions of Law Re: Plaintiff’s Motion for Attorney fees and Costs, and in particular in concluding that fees could be awarded “based on the wrongful withholding of wages” (FF 1.1, 1.2, 1.14, CL 2.1, 2.2, 2.3, 2.4, 2.5, CP 488, 490-93), and in awarding “litigation costs” or “expenses” that are not compensable under RCW 4.84.010. (FF 1.19, CL 2.7 and CL 2.8, CP 492-93) (App. B)

3. The trial court erred in entering its Judgment. (CP 525) (App. C)

III. ISSUES RELATED TO ASSIGNMENTS OF ERROR

Respondents were granted the right to acquire shares of stock while employed by appellant corporation before the corporation was purchased by another entity, when respondents agreed to surrender their stock rights in return for cash payments by the corporation. The cash payments were calculated based on the amount the purchaser had agreed to pay for all the corporation's assets.

Are the payments contractually owed by the corporation to its former employees for their stock rights "wages" within the meaning of the wrongful withholding of wages statute, RCW 49.52.050 and .070?

IV. STATEMENT OF THE CASE

A. **Name Intelligence Granted Its Employees The Right To Corporate Stock Before It Was Purchased By A California Corporation In 2008.**

Appellant Name Intelligence, Inc. is a Washington corporation formed in 2003. (CP 348) Appellant Jay Westerdal was a co-founder of Name Intelligence and served as its CEO and President. (CP 348)

The respondents, Gustavo Nelson Arzola, Michael Klatt, and Susan Prosser, were employees of Name Intelligence beginning in

2006. (CP 293, 308, 318) At the time of hiring, each received the right to future grants of Name Intelligence stock during their term of employment as part of a performance-based reward system. (CP 100, 126, 293, 308, 318, 349; Ex. 1)¹ Employees were allotted a fixed number of shares upon hiring, and then for every year in which they received an above average, or average, performance rating. (CP 100, 126, 293, 308, 318, 349; Ex.1) The number of shares varied based upon Name Intelligence's evaluation of the employee's performance. (CP 100, 126; Ex. 1) Under respondents' employment agreements, the shares vested after five years of service. However, "all shares that are allocated will be immediately granted" upon the sale of Name Intelligence to a third party. (CP 100, 126; Ex. 1)

In April 2008, Name Intelligence was sold to a California company, Thought Convergence, Inc. (FF 2.4, CP 479) The purchase was memorialized in a Securities Exchange Agreement (Ex. 101; CP 355-82), that required a \$6 million payment to Name

¹ The trial court and the parties below repeatedly referred to the employees' stock rights as "options." The term is a misnomer, however, as an option gives its owner the right to purchase at a particular price, and the respondents did not have to pay to exercise their right to acquire their shares.

Intelligence on May 2, 2008, a second \$5 million payment on May 2, 2009, and a third and final payment of \$5 million on May 2, 2010. (FF 2.13, CP 480)

Because the sale included all assets of the company, Name Intelligence sought to buy all outstanding stock rights in the corporation. (CP 349; FF 2.10, CP 480) In early April 2008, Westerdal proposed to the respondents that they cancel their stock rights in exchange for cash payments, and estimated the amounts of those payments based on the purchase price in the Exchange Agreement with Thought Convergence. (CP 349, 383; *see also* 1/27 RP 29-30) Westerdal told respondents that the cash to be paid "is subject to closing costs so numbers will vary 1 or 2 percent." (CP 349-50, 383)

B. Respondents Agreed To Surrender Their Stock Rights And Received The First Of Three Payments From Name Intelligence.

Respondents agreed to sell their stock rights back to the company in return for three cash payments made over two years, timed to coincide with the payments required by the Exchange Agreement. Each of the respondents memorialized their agreement to cancel their stock options with Name Intelligence,

signing a Stock Right Cancellation Agreement also dated May 2, 2008. (CP 295-99, 310-14, 320-24, 349; Exs. 2-4) The respondents expressly agreed to surrender all stock rights and “all the shares of Common Stock due thereunder.” (CP 296, 311, 321; Exs. 2-4 § 2(b)) While the Cancellation Agreements contained sums certain, each of the three respondents confirmed that the amounts payable would be subject to adjustment, and “shall be subject to the same terms, conditions and adjustments of the Post-Closing Payments in the Exchange Agreement.” (FF 2.12, CP 501; CP 296, 311, 321; Exs. 2-4 § 2(a))

The respondents' employment with Name Intelligence terminated, and each became an employee of Thought Convergence on the Exchange Agreement's effective date, May 2, 2008. (1/27 RP 82, 133) Name Intelligence paid each of the respondents their first payments due under the Cancellation Agreements on May 2, 2008. (CP 350) Arzola received \$57,311, Klatt received \$91,699, and Prosser received \$ 25,000. (CP 293, 308, 318) Mistakenly believing that withholding was required by law, Name Intelligence withheld FICA and Medicare tax on the 2008 payment. (1/31 RP 288-89; FF 2.15, CP 481)

C. Name Intelligence Postponed Payment Of The Second And Third Payments To Respondents After A Dispute With Its Purchaser Delayed The Purchaser's Second Payment To Name Intelligence And Its Shareholders.

A dispute arose between Thought Convergence and Name Intelligence regarding the Exchange Agreement before the second payment was due on May 2, 2009. (CP 350) After mediation failed, Thought Convergence filed an action against Name Intelligence, Westerdal, and other shareholders in federal district court in California on May 1, 2009. (CP 350; FF 3.1, CP 481) Thought Convergence sought rescission of the Exchange Agreement, or alternatively, reductions in the amounts due Name Intelligence in the second and third post-closing payments. (CP 350) Thought Convergence made partial payments to Name Intelligence for the second post-closing payment on May 8 and May 26, 2009. (CP 350-51) In a meeting in June 2009, Westerdal, whose employment had been terminated by Thought Convergence, told the respondents and other Name Intelligence shareholders that the uncertainties and attendant legal expenses resulting from the Thought Convergence lawsuit would delay distributions to them. (CP 351; 1/31 RP 226-28)

Name Intelligence did not pay 100% of the amounts stated in the Cancellation Agreements because the litigation could reduce the amount it would receive. (FF 3.2, CP 481; 1/27 RP 51) Respondents refused Westerdal's offer of a principal distribution (excluding interest), and brought this action for breach of the Cancellation Agreement and unjust enrichment against Name Intelligence in August 2009. (CP 1-7, 352) They named Jay Westerdal individually as a defendant in a claim for "refusal to provide the plaintiffs their compensation" under RCW 49.52.070. (CP 6)

D. Two Superior Court Judges Denied Summary Judgment, Rejecting The Argument That the Payments Due Respondents For Cancellation Of Their Stock Rights Were "Wages" Under RCW ch. 49.52.

On December 17, 2009, King County Superior Court Judge Paris Kallas granted partial summary judgment, holding that Name Intelligence breached the Cancellation Agreement as to the second payment due in May, 2009. (CP 235-37) Judge Kallas refused to find as a matter of law that the sums owed were wages under RCW ch. 49.52 and RCW ch. 49.48. (CP 236; 12/17 RP 33-34) Judge Kallas certified a judgment of \$175,573 under CR 54(b) in favor of the three respondents. (CP 242) That judgment was satisfied in

full in March 2010, when Thought Convergence and Name Intelligence settled their dispute by agreeing to a post-closing adjustment under the Exchange Agreement that reduced the third and final payment by \$125,000, 2.5% of the amount originally due, to \$4,875,000. (CP 353-55, FF 4.2, 4.3; CP 482-83)

Name Intelligence had incurred half a million dollars in fees defending the Thought Convergence action. (1/27 RP 93) In addition to a 2.5% reduction to reflect the amount of Thought Convergence's final payment, Name Intelligence reduced its payments under the Cancellation Agreement by \$14,046.00 to reflect a pro-rata percentage of Name Intelligence's legal expenses in the Thought Convergence litigation based on the shares of stock held by each of the former employees. (CP 353; FF 4.4, CP 483) Name Intelligence tendered a check that included these reductions to respondents on May 7, 2010, two days after Thought Convergence made its final payment under the Exchange Agreement. (FF 4.4, CP 483) The respondents rejected the tender because it contained the language "Final Payment and Full Settlement." (CP 265, 288; FF 4.5, CP 483) On May 24, 2010, after one of the four original plaintiffs settled, Name Intelligence

tendered a “good faith partial payment,” reducing final payment by \$11,007. Respondents accepted this tender. (FF 4.5, 4.6, CP 483)

Judge Jean Rietschel entered a partial summary judgment holding as a matter of law that Name Intelligence owed an additional \$11,007 from the third and final payment. (CP 412-14) Like Judge Kallas, Judge Rietschel refused to hold that these contractual amounts due under the Cancellation Agreement constituted wages under RCW 49.52.070. (CP 413)

E. The Trial Court Held That The Cancellation Agreement Payments Were “Wages” As A Matter Of Law And Entered Judgment Against Name Intelligence And Westerdal For Punitive Damages And Attorney Fees.

The case was brokered for trial to Judge Carol Schapira (“the trial court”). Although Judges Kallas and Rietschel had denied summary judgment and respondents never moved for reconsideration of either of those decisions, the trial court held as a matter of law that the payments due under the Cancellation Agreement were “a byproduct of employment” and thus wages for purposes of the wage withholding statute. (1/26 (AM) RP 29) The trial court then found following trial that the May 2009 payment was not the subject of a bona fide dispute and that Name Intelligence willfully withheld that payment because the respondents were not

as a matter of law responsible for any portion of legal fees incurred by Name Intelligence or Westerdal under a “reasonable reading of the agreements.” (FF 3.6, CP 482) The trial court held that there was a bona fide dispute as to only 2.5% of the final payment due under the Cancellation Agreement – the prorated portion of the sums withheld from Name Intelligence by Thought Convergence under the Exchange Agreement. (FF 4.7, CP 484)

The trial court held both Name Intelligence and Westerdal liable under RCW 49.52.070 for exemplary damages of \$145,007 for the May 2009 payment and \$7,281.82 for the May 2010 payment. (FF 5.2, 5.3, CP 484) In addition, it awarded prejudgment interest for the contractual amounts due from the date they were owed totaling \$15,773.78 (CP 485-86), attorney fees of \$97,860, and all litigation expenses (not just statutory costs) totaling \$4,349.54, under RCW 49.48.030 and RCW 49.52.070 (CP 493). The trial court’s total judgment was \$283,479.14 against Name Intelligence and \$256,698.36 against Westerdal. (CP 426)

Name Intelligence and Westerdal timely appealed. (CP 494-95) They challenge only the trial court’s award of exemplary damages, attorney fees and litigation expenses.

V. ARGUMENT

A. **Standard of Review: The Trial Court's Summary Determination That Payments Under The Stock Right Cancellation Agreement Constitute "Wages" Under RCW 49.52.050 Is Reviewed De Novo As An Error Of Law.**

Washington's wage withholding statute prohibits an employer from willfully depriving an employee of "wages:"

Any employer or officer, vice principal or agent of any employer, whether said employer be in private business or an elected public official, who

. . .

(2) Willfully and with intent to deprive the employee of any part of his or her wages, shall pay any employee a lower wage than the wage such employer is obligated to pay such employee by any statute, ordinance, or contract;

RCW 49.52.050. The statute imposes liability on any employer, as well as "any officer, vice principal or agent of any employer" violating any of the provisions of RCW 49.52.050(2) "for twice the amount of the wages unlawfully rebated or withheld by way of exemplary damages, together with costs of suit and a reasonable sum for attorney's fees." RCW 49.52.070. Application of the wage withholding statute to payments made under a particular contract is a question of law. **MacDonald v. Wockner**, 44 Wn.2d 261, 269, 267 P.2d 97 (1954) ("legal question whether the contract . . . would

fall within the terms of the so-called 'Anti-Kickback' statute, RCW 49.52.050");² *Morgan v. Kingen*, 141 Wn. App. 143, 160-61, ¶ 47, 169 P.3d 487 (2007) (definition of "wages" under RCW 49.52.050 is a question of law), *aff'd*, 166 Wn.2d 526, 169 P.3d 487 (2009). See *Mackey v. American Fashion Institute Corp.*, 60 Wn. App. 426, 429, 804 P.2d 642 (1991) ("The question of whether a statute applies to a factual situation is a question of law and fully reviewable on appeal.").

B. Payments Owed Former Employees In Consideration Of An Agreement To Cancel Their Stock Rights Are Not "Wages" Under RCW Ch. 49.52 Because They Are Not Payments For Labor Or Services.

1. The Wage Withholding Statute Applies To Fixed Amounts Owed Employees As Compensation For Their Services.

Washington's wage withholding statute prohibits an employer from willfully depriving an "employee of any part of his or her wages." RCW 49.52.050(2). The payments owed under the Cancellation Agreement were not "wages" under the statute because they were not fixed amounts owed in consideration of labor and services, but payments made to former employees for

² The law is commonly called the "Anti-Kickback" statute because its first section makes it illegal for an employer to "collect or receive from any employee a rebate of any part of wages." RCW 49.52.050(1).

their ownership interest in Name Intelligence. The trial court therefore erred in awarding double damages for wrongful withholding of wages.

The wage withholding law was enacted in 1939 to “protect the wages of an employee” and to ensure “that the employee shall realize the full amount of wages which by statute, ordinance or contract he is entitled to recover from his employer.” *Ellerman v. Centerpoint Prepress, Inc.*, 143 Wn.2d 514, 520, 22 P.3d 795, 798 (2001); quoting *Schilling v. Radio Holdings, Inc.*, 136 Wn.2d 152, 159, 961 P.2d 371 (1998) (emphasis in original). Because the Legislature did not define the term “wages,” courts give the term its plain and ordinary meaning: “Payment for labor or services to a worker, especially remuneration on an hourly, daily, or weekly basis or by the piece.” *Morgan v. Kingen*, 141 Wn. App. at 161, quoting *The American Heritage Dictionary of the English Language* 2007 (3rd ed. 1992). See also *Bates v. City of Richland*, 112 Wn. App. 919, 939-40, 51 P.3d 816 (2002) (applying definition of “wage” under Minimum Wage Act, RCW 49.46.010(2), as “compensation due an employee by reason of employment.”).

The stock rights issued to respondents were not “wages” under RCW 49.52.050. First, like a bonus, the ultimate number of shares was subject to the discretion of Name Intelligence. Second, even if the number of shares to which each respondent was entitled was fixed, the value of those shares was not based on the value of the former employees’ services but on the value of the corporation. Third, and most significantly, under their Stock Right Cancellation Agreements, the former employees were owed money for their proprietary interest in the corporation, not for wages paid for their services.

2. Stock Rights Are Not “Wages” Governed By RCW 49.52.050 Because The Total Number Of Shares Granted Respondents Was Discretionary.

Not every emolument of employment is “wages.” For instance, a television won at a lottery was “not wages” under RCW 49.52.050 because “at most, the television . . . could only be a ‘bonus’” in *Byrne v. Courtesy Ford, Inc.*, 108 Wn. App. 683, 689, 32 P.3d 307 (2001), *rev. denied*, 146 Wn.2d 1019 (2002). Relying on decisions holding that “a bonus, unless given consistently and repeatedly, is a mere gratuity, and not compensation,” Division Two held that a discretionary bonus cannot be deemed “wages” under

RCW 49.52.050 in **Byrne**, 108 Wn. App. at 690-91, citing **Simon v. Riblet Tramway Co.**, 8 Wn. App. 289, 292, 505 P.2d 1291, cert. denied, 414 U.S. 975 (1973); **Powell v. Republic Creosoting Co.**, 172 Wash. 155, 156, 19 P.2d 919 (1933). Here, payments due former employees for their interest in their company are not “wages” under RCW 49.52.050 even if they are, as expressed by the trial court, a “byproduct of employment.” (1/26 RP 29)

Relying in part on the distinction between earned compensation and discretionary remuneration, the federal district court has held that a grant of stock options is not wages for purposes of RCW 49.52.050 where “the award of stock options fell within [the employer’s] discretion” in **Coulombe v. Total Renal Care Holdings, Inc.**, 2007 WL 1367601 (W.D. Wash. 2007), *aff’d*, 298 Fed.Appx. 617 (9th Cir. 2008). In that case, Judge Robart also held that the stock options were not wages because their value depends not on an employee’s labor but on the “vagaries of stock valuations.” 2007 WL 1367601 at *6, quoting **International Business Machines v. Bajorek**, 191 F.3d 1033, 1039 (9th Cir. 1999). Here, as in **Coulombe**, the number of shares granted the former employees was discretionary, as it was based on the

employer's assessment of their performance. (CP 100, 126, 293, 318; Ex. 1)

3. The Stock Right Payments Are Not “Wages” Because The Payments Were Based On The Value Of Name Intelligence And Not On The Value Of The Respondents’ Services.

Even if they had been given “consistently and repeatedly,” though, and regardless of whether they were a “byproduct of employment,” once granted the stock rights were not “wages” owed as consideration for the respondents’ services because the value of those stock rights depended not on the value of those services or on any respondent’s personal productivity, but on the value of the corporation. “Stated otherwise, the equity-based compensation at issue here lacks the ‘direct relationship between an employee’s own performance and the compensation to which that employee is entitled’ contemplated by” the wage withholding statute. ***Guiry v. Goldman, Sachs & Co.***, 31 A.D.3d 70, 73, 814 N.Y.S.2d 617, 619 (2006) (rights under stock ownership plan did not constitute “wages” under New York wage withholding law) (citation omitted). Similarly here, the respondents’ stock rights had no quantifiable value until the value of Name Intelligence was established by the Exchange Agreement.

Thus, [“e]ven where stock options may be awarded pursuant to plans giving rise to expectations of stock awards . . . they ordinarily do not give rise to an expectation calculable as a sum of money.” *Bajorek*, 191 F.3d at 1039. The right to stock is therefore unlike pension benefits and contractually-earned severance pay, which are considered wages, because like hourly pay, these benefits are quantifiable remuneration for the employee’s services. See *Bates v. City of Richland*, 112 Wn. App. 919, 939-40, 51 P.3d 816 (2002) (pension benefits); *Dice v. City of Montesano*, 131 Wn. App. 675, 689, ¶ 28, 128 P.3d 1253, *rev. denied*, 158 Wn.2d 1017 (2006) (severance). See also *May v. Honeywell Int’l, Inc.*, , 331 Fed.Appx. 531 (9th Cir. 2009) (vested short term disability benefits); *Dautel v. Heritage Home Center, Inc.*, 89 Wn. App. 148, 152 n.1, 948 P.2d 397 (1997) (commissions), *rev. denied*, 135 Wn.2d 1003 (1998).

4. The Cancellation Agreement Paid Respondents For Their Proprietary Interest In The Corporation, And Not For Their Services Or Labor.

The stock rights gave respondents a proprietary interest in a corporation, akin to the rights granted under vested stock options. See *Marriage of Langham and Kolde*, 153 Wn.2d 553, 564, 106

P.3d 212, 218 (2005) (“there can be little doubt that stock options are property.”). As the Ninth Circuit held in interpreting the California anti-kickback statute, stock options are not wages but are instead the “contractual right to buy stock.” **Bajorek**, 191 F.3d at 1039. See also **Falkowski v. Imation Corp.**, 309 F.3d 1123, 1132, *amended by*, 320 F.3d 905 (9th Cir. 2003) (“options are not wages.”).³

Here, each of the respondents was issued the right to acquire corporate shares in Name Intelligence. (CP 295-99, 310-14, 320-24, 349; Exs. 2-4) The trial court correctly held that the stock rights themselves were not “wages.” (FF 2.15, 481) If the stock rights themselves “are not wages,” (FF 2.15, CP 481), Name Intelligence's agreement to buy those rights back from the respondents could not meet a definition of “wages” as “payment for labor or services.” **Morgan v. Kingen**, 141 Wn. App. at 161.

³ Employee stock options also were held not to be “wages” under state wage withholding statutes in **Paolini v. Albertson's Inc.**, 143 Id. 547, 149 P.3d 822, 825 (2006) (“wages” does not encompass stock options and other nonmonetary compensation), *answer to certified question conformed to*, 482 F.3d 1149 (9th Cir. 2007); **Catalyst Health Solutions v. Magill**, 414 Md. 457, 995 A.2d 960, 969-72 (2010) (options not “wages” or “compensation that is due to an employee for employment” under Maryland Wage Act). See also **Hmelyar v. Phoenix Controls**, 339 Ill. App. 700, 791 N.E.2d 695, 701 (2003) (unvested and unexercised stock options not “wages” under Illinois Unemployment Act).

The respondents' employment with Name Intelligence terminated on May 2, 2008, when their company was purchased by Thought Convergence. (1/27 RP 82, 133) The respondents made no claim that they were owed salary or any other monetary benefits due in consideration of their services. Under the Cancellation Agreement, they agreed to surrender all stock rights and "all the shares of Common Stock due thereunder." (CP 296, 311, 321) Like the principal shareholders of Name Intelligence, respondents were owed payments in consideration of their proprietary interest in the corporation, and not as employees performing labor or services.

Employees may be granted an equity interest in their employer as an incentive toward productivity. That interest can take many forms – limited partnership or limited liability shares, general partnership interests, or as here, the right to acquire company stock. Once that interest is granted, however, it is like any other equity interest in the employing entity. The fact that the respondents' equity interest in Name Intelligence can be traced as a "byproduct" of employment does not transform it into "wages" under a law intended to protect employees from unscrupulous

employers who withhold part of the compensation due them for their labor.

The payments due respondents under the Stock Right Cancellation Agreements were not wages for purposes of the wage withholding statute. The trial court erred in awarding double damages under RCW 49.52.070.

C. The Trial Court Erred In Awarding Attorney Fees And Litigation Expenses Under RCW 49.48.030 And RCW 49.52.070.

This court should also reverse the award of attorney fees and litigation expenses because respondents had no contractual or statutory right to attorney fees. The Cancellation Agreement did not contain an attorney fee clause. (CP 295-99, 310-14, 320-24, 349; Exs. 2-4) Because the wage withholding statute is inapplicable, respondents had no right to fees under RCW 49.52.070, which authorizes the recovery of attorney fees against an employer who has violated RCW 49.52.050(2).

The trial court's reliance on RCW 49.48.030, which provides for an award of fees "in any action in which any person is successful in recovering judgment for wages or salary owed to him," was also error. Even under the MWA's definition of "wages,"

RCW 49.46.010, the payments due respondents under the Cancellation Agreement were not due as “compensation by reasons of employment” but were recovered in return for their ownership rights in Name Intelligence.

In any event, the respondents were not entitled to all their litigation expenses as prevailing parties below. The trial court erred in refusing to limit respondents to statutory costs under RCW 4.84.010. See *Hume v. American Disposal Co.*, 124 Wn.2d 656, 674, 880 P.2d 988 (1994) (“Costs have historically been very narrowly defined, and RCW 4.84.010 limits cost recovery to a narrow range of expenses such as filing fees, witness fees, and service of process expenses.”), *cert. denied*, 513 U.S. 1112 (1995).

VI. CONCLUSION

Contract payments owed to former employees in consideration of their ownership interest in a corporation were not “wages” merely because they were a “byproduct” of employment. This court should reverse and vacate the judgment for exemplary damages under RCW 49.52.050 and for attorney fees and litigation expenses under RCW 49.52.070 and RCW 49.48.030.

Dated this 29th day of July, 2011.

SMITH GOODFRIEND, P.S.

HOLMQUIST & GARDINER, PLLC

By: 

By: 

Howard M. Goodfriend
WSBA No. 14355

Hamilton H. Gardiner
WSBA No. 37827

Attorneys for Appellants

DECLARATION OF SERVICE

The undersigned declares under penalty of perjury, under the laws of the State of Washington, that the following is true and correct:

That on July 29, 2011, I arranged for service of the foregoing Brief of Appellants, to the court and to the parties to this action as follows:

Office of Clerk Court of Appeals - Division I One Union Square 600 University Street Seattle, WA 98101	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input checked="" type="checkbox"/> U.S. Mail <input type="checkbox"/> Overnight Mail
Hamilton H. Gardiner Holmquist & Gardiner, PLLC 1000 2nd Avenue, Suite 1770 Seattle, WA 98104	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input checked="" type="checkbox"/> U.S. Mail <input type="checkbox"/> E-Mail
Joseph A. Grube Ricci Grube Aita & Breneman 1200 Fifth Avenue, Suite 625 Seattle, WA 98101	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input checked="" type="checkbox"/> U.S. Mail <input type="checkbox"/> E-Mail

DATED at Seattle, Washington this 29th day of July, 2011.



Tara D. Friesen