

**APPELLATE CASE NUMBER 68417-5-I  
WHATCOM COUNTY CAUSE NO. 11-2-00750-9**

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**IN THE COURT OF APPEALS, DIVISION I  
OF THE STATE OF WASHINGTON**

Choong H. Lee, DMD, PLLC, and CH LEE, PLLC,

Appellants,

v.

Thaheld/Lee-01, LLC, and Johann Thaheld,

Respondents.

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**BRIEF OF APPELLANT LEE DENTAL PRACTICE**

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## I. INTRODUCTION

Washington has for decades maintained a strong public policy against non-dentist corporations “owning, operating or maintaining” a dental practice. RCW 18.32.675(1); RCW 18.32.020(3). Washington courts give effect to this broad prohibition by routinely invalidating contractual arrangements where a non-dentist corporation assumes more than the most ministerial involvement in a dental practice.

Dr. Choong-hyun Lee and Lee Dental Practices filed this lawsuit to void a lengthy Service Agreement which has as its sole purpose to grant the non-dentist Thaheld an impermissible role in Lee Dental Practice over the Agreement’s 40-year term.

- The Service Agreement grants non-dentist Thaheld expansive control over Dr. Lee’s practice.
- The Service Agreement enmeshes the non-dentist Thaheld in Lee Dental Practices’ finances.
- The Service Agreement imposes onerous restrictions on Dr. Lee’s professional freedom.

Lee Dental Practices moved for summary judgment on the Services Agreement’s legality. The Whatcom County Superior Court (Judge Uhrig) denied Lee Dental Practices’ motion but

certified the ruling for interlocutory appeal, which was granted. Lee Dental Practices now requests that this Court reverse and remand with instructions to the trial court to enter summary judgment because the Services Agreement violates Washington law.

## **II. ASSIGNMENT OF ERROR**

The trial court erred by denying Lee Dental Practices' motion for summary judgment on January 27, 2012.

## **III. ISSUES PERTAINING TO ASSIGNMENT OF ERROR**

1. Does a 40-year contract between a dentist and a corporation that gives the corporation (1) fees tied to the practice's profits and to the salary of dentists; (2) the ability to force sale of the practice in the event the contract terminates with the corporation receiving half the proceeds, (3) the ability to negotiate contracts with third party payors, (4) an irrevocable power of attorney to collect accounts receivable and make withdrawals from the practice's accounts, (5) the ability to hire and fire all non-dentist staff, (6) dictates dentist compensation, (7) prohibits a dentist from quitting for 40 years, (8) imposes a 50-year non-compete on the dentist, (9) controls amendments to dentists' employment agreements, (10) controls whether the dental practice may admit new partners, (11) creates a "Policy Board" that gives the

corporation the ability to veto nearly any major operational decision, (12) prohibits the dental practice from drawing on its own bank accounts without the corporation's permission, and (13) requires the practice to operate only at locations acceptable to the corporation, facially contravene Washington's public policy against the corporate practice of dentistry, RCW 18.32.675(1)?

2. Where a dental services contract facially violates Washington's prohibition on the corporate practice of dentistry, does the fact that the corporation has not chosen to enforce some of the illegal contractual provisions salvage the agreement?

3. Under the parol evidence rule, may a party to a fully-integrated but facially illegal dental services contract introduce extrinsic evidence regarding the parties' conduct in an attempt to transform the agreement's illegal terms into legal ones?

4. Where the purpose of a thirty-seven page dental services contract is to grant a corporation illegal control over a dental practice, may a court give effect to savings clauses in order to reform the contract?

#### IV. STATEMENT OF THE CASE

##### A. Statement of Facts

###### 1. Origin of Services Agreement

Johann Thaheld, who is not a dentist, approached Dr. Choong-hyun Lee in 2010 and enticed him to execute a remarkable, thirty-seven page "Service Agreement" that purports to give Thaheld (1) a direct stake in the finances of Lee Dental Practices and (2) substantial control over the operation and management of Lee Dental Practices for a term of 40 years. CP 21-71 (hereinafter "Service Agreement").<sup>1</sup>

Dr. Lee, a licensed Washington dentist, has practiced dentistry in Whatcom County since 2004. CP 19. Dr. Lee and Thaheld signed the contract on behalf their respective companies on July 21, 2010. Service Agreement, p. 36. The parties' relationship quickly deteriorated over the following months, leading to this lawsuit.

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<sup>1</sup> Dr. Lee runs his practice through two professional companies, Choong H. Lee, DMD, PLLC and CH Lee, PLLC (collectively "Lee Dental Practices"). *Id.* Lee Dental Practices and Thaheld's corporation, Thaheld/Lee-01, LLC, are parties to the Service Agreement.

## 2. Thaheld's Involvement in Dental Practices' Finances.

The Agreement involves Thaheld in Lee Dental Practices' finances in the following ways:

- The Service Agreement purports to entitle Thaheld to a "Service Fee" equal to the salary of the highest paid dentist, with a minimum salary of \$120,000. Service Agreement, ¶ 7.3.1.
- Up to fifty percent of the practice's net profits are allocated to Thaheld as a monthly "Performance Fee." *Id.* at ¶¶ 7.3.2; 12.1.
- The Service Agreement requires Lee Dental Practice to sell all its clinics in the event that the Service Agreement terminates for any reason. *Id.* at ¶ 7.3.3.
- The Service Agreement gives Thaheld 50% of the proceeds of clinics Lee Dental Practices sells. *Id.* at ¶¶ 7.3.4-7.3.6.
- The Service Agreement states that Thaheld shall negotiate contracts with third party payors including prices, alternate delivery systems and "other purchasers of group dental care services." *Id.* at ¶ 4.9.
- The Service Agreement purports to grant Thaheld an irrevocable power of attorney for forty years to collect and receive all accounts receivable; to take possession and endorse in Lee Dental Practices name any notes and checks; to sign checks and make withdrawals and further states that Lee himself may only withdraw checks with Thaheld's permission and by providing Thaheld with reasonable advance notice. *Id.* at ¶ 4.12.1.

### 3. Thaheld's Control Over Dental Practices' Operations.

The Service Agreement purports to grant Thaheld expansive control over Lee Dental Practices' operations including issues that directly relate to the quality of dental care.

- The Service Agreement gives Thaheld the authority to monitor the dentists' compliance with procedures designed to insure "consistency, quality, appropriateness and necessity of dental care." Service Agreement, ¶ 4.6.
- The Service Agreement gives Thaheld unchecked power of "recruiting, hiring, managing and terminations" of all staff (including dental assistants) that are not practicing dentists as well as setting salaries and benefit levels. *Id.* at ¶4.8.
- The Service Agreement states that Thaheld may order dental supplies. *Id.* at ¶4.3.
- The Service Agreement dictates the form of future employment and consulting agreements for all dentists including setting dentist compensation by stating that no dentist may receive more than 23% of their collections. *Id.* at ¶5.2.
- The Service Agreement gives Thaheld a direct role in the accreditation process although Lee agrees to participate "if requested to do so" by Thaheld. *Id.* at ¶5.5.3.
- The Service Agreement requires that Lee Dental Practices obtain insurance showing Thaheld as an additional insured. *Id.* at ¶5.5.6.
- The Service Agreement purports to impose a fifty-year non-compete that prohibits Lee Dental Practices from sharing information about its own practice. *Id.* at ¶5.6.

#### 4. Limits on Dr. Lee's Activities.

The Service Agreement also places limitations on Lee Dental Practices and Dr. Lee's activities.

- Lee Dental Practices may only lease at locations that Thaheld approves, and Thaheld can require Lee Dental Practices to assign the lease to Thaheld. Service Agreement, ¶¶ 4.1.1; 4.1.2.
- Lee Dental Practices may not amend any employment or independent contractor agreement (including agreements with dentists) without Thaheld's permission. *Id.* at ¶5.1(a)(vi)(a).
- Lee Dental Practices may not acquire any clinic, merge or admit any partner without Thaheld's express permission. *Id.* at ¶5.1(a)(vi)(b).
- Lee Dental Practices must operate full time. *Id.* at ¶5.1(a)(ii).
- Dr. Lee is personally prohibited from at any time voluntarily terminat[ing] his employment." *Id.* at ¶5.1(b).
- Lee Dental Practices is required to transfer all rights and title to the practice's software and data to Thaheld. *Id.* at ¶4.2.1.

Finally, the Service Agreement creates a "Policy Board" composed of one representative of Thaheld and one of Lee Dental Practices. *Id.* at ¶3.1. The Board acts through a majority of its members, meaning that either member may veto a proposed action of the other by withholding consent. *Id.* The Board is vested with authority to:

- Approve or disapprove any capital equipment expenditure or expansion, *Id.* at ¶3.2.1, and also to set priority for major capital expenditures. *Id.* at ¶3.2.6.
- Approve or disapprove “all advertising and other marketing of the dental services.” *Id.* at ¶3.2.2.
- Approve or disapprove Lee Dental Practices’ “long-term strategic and short term operational goals, objectives and plans.” *Id.* at ¶3.2.5.
- Approve or disapprove support personnel plans, as well as any variations in dentist employment agreements. *Id.* at ¶3.2.7.
- Develop patient scheduling guidelines. *Id.* at ¶3.2.8.
- “[R]eview, approve and monitor” procedures for resolving patient claims. *Id.* at ¶3.2.10.
- Approve or disapprove Lee Dental Practices’ environmental and workplace health and safety guidelines. *Id.* at ¶3.2.11.
- Approve or disapprove the manner in which Lee Dental Practices “organiz[es] and deliver[s] emergency Dental Care.” *Id.* at ¶3.2.12(i).
- Approve or disapprove “guidelines for ensuring an appropriate response ... to dental and in-Clinic medical emergencies.” *Id.* at ¶3.2.12(ii).
- “[A]pprove or disapprove any merger or combination with or acquisition of any dental practice by” Lee Dental Practice. *Id.* at ¶3.2.14.

Additionally, Lee Dental Practices is required to develop a “philosophy of practice” and “set of practice guidelines” that is “reasonably acceptable to the Policy Board.” *Id.* at ¶5.5.3.

**B. Statement of Procedure**

Lee Dental Practices brought this action in Whatcom County Superior Court on March 18, 2011, CP 3-6, and subsequently sought a summary judgment ruling that the parties' Service Agreement is void as violating Washington's public policy against the corporate practice of dentistry. CP 7-18. Judge Ira Uhrig of the Whatcom County Superior Court denied Lee Dental Practices' motion, issuing a simple order to that effect on January 27, 2012. CP 96-97.

Lee Dental Practices sought interlocutory review of Judge Uhrig's ruling under RAP 2.3(b)(4), which this Court granted on October 11, 2012.

**V. ARGUMENT**

**A. Standard of Review**

A trial court's denial of summary judgment is subject to de novo review, with the appellate court engaging in the same inquiry as the trial court. Macias v. Saberhagen Holdings, Inc., 282 P.3d 1069, 1073 (Wash. 2012). Summary judgment is appropriate if there are no genuine issues of fact and the moving party is entitled to judgment as a matter of law. CR 56(c). "The legality of an

agreement is a question of law.” Fallahzadeh v. Ghorbanian, 119 Wn. App. 596, 601, 82 P.3d 684 (2004).

This issue is ripe for a legal determination. There are no disputed facts, and the relevant question is one of law. In the proceedings below, the parties agreed that Lee Dental Practices and Thaheld executed a Service Agreement. Thaheld also produced a declaration alleging a variety of other facts surrounding the execution of the Agreement and the parties’ subsequent conduct, which Lee Dental Practices did not dispute for the purposes of its motion.<sup>2</sup>

As a result, this Court need only apply the relevant statute to the undisputed facts and determine whether the level of control the Service Agreement gives Thaheld over Lee Dental Practices contravenes Washington’s prohibition on the corporate practice of dentistry.

**B. The Washington Legislature has Established a Broad Prohibition on the Unlicensed Corporate Practice of Dentistry.**

A non-dentist corporation may not practice of dentistry in Washington. RCW 18.32.675(1) provides:

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<sup>2</sup> While Lee Dental Practices accepts that Thaheld’s version of events controls for purposes of this appeal, Thaheld’s account is, as a matter of actual fact, false. Should this case go forward, Lee Dental Practices will strongly dispute Thaheld’s factual claims.

No corporation shall practice dentistry or shall solicit through itself, or its agent, officers, employees, directors or trustees, dental patronage for any dentists or dental surgeon employed by any corporation: PROVIDED [that the prohibition does not] apply to corporations or associations furnishing information or clerical services which can be furnished by persons not licensed to practice dentistry, to any person lawfully engaged in the practice of dentistry, when such dentist assumes full responsibility for such information and services.

The “practice of dentistry” is defined to include not only the actual delivery of dental services to the patient’s teeth and gums, but also the actions of anyone who “owns, maintains or operates an office for the practice of dentistry.” RCW 18.32.020(3) (emphasis added). Thus, the only exception is a narrow one for “clerical services.”

Washington case law confirms the broad intent and impact of RCW 18.32.675(1). In State v. Boren, 36 Wn.2d 522, 219 P.2d 566 (1950), a dentist bought a dental practice from two non-dentists. The dentist agreed to pay \$55,000 in \$750 monthly installments. Under the contract, the dentist drew a \$500 salary and one of the non-dentists worked for \$500 each month as office manager “buying the supplies and watching the charts and making out the accounts and payments, and general manager, and looking after the advertising.” *Id.* at 524. The non-dentist office manager also withdrew monthly bonus payments “in appreciation of the

increase in business.” *Id.* The court held that these activities ran afoul of the statutory prohibition on corporations owning, operating, or maintaining an office for the practice of dentistry. *Id.* at 532.

A recent decision by this Court held that a lease agreement between a dental practice and a non-dentist was illegal where a dental practice’s rental payments to the non-dentist consisted of 50 percent of the practice’s net profits. Fallahzadeh v. Ghorbanian, 119 Wn. App. 596, 82 P.3d 684 (2004). The non-dentist in that case also acted as the operating manager of the dental practice and handled the practice’s accounts. The non-dentist argued that the arrangement did not violate RCW 18.32.675 because the dentist “retained complete control of all business and professional activities for his practice.” *Id.* at 603. This Court was not persuaded:

Under Washington law, . . . [the non-dentist’s] non-involvement in the delivery of professional services is not determinative. In *State ex rel. Standard Optical Co. v. Superior Ct. for Chelan County*, 17 Wn.2d 323, 334, 135 P.2d 839 (1943), the fact that an optometrist retained complete professional control did not prevent the Washington Supreme Court from concluding that his employer was illegally maintaining and operating an optometry practice. Furthermore, this distinction is not particularly persuasive in light of the 50 percent net profit rent provision and the other terms of the lease. Regardless of whether [the non-dentist] was employed by the practice, he still retained a substantial beneficial

interest in the practice's profits. In this respect, the lease is no different than *Boren's* conditional sales contract, which also guaranteed to the sellers a steady income stream from the practice. Furthermore, [the non-dentist] reserved significant rights under the lease as a landlord. He had sole and exclusive discretion to approve any changes, modifications, or alterations. Thus, his absence from the practice's day-to-day operations did not affect his ability to control certain aspects of [the dentist's] practice, such as making physical improvements to the premises that might be necessary for patient care.

*Id.* at 603-04. The court held that the effect of the lease was to enable the non-dentist to obtain a financial interest in the dental practice in violation of Washington law. *Id.* at 605.

Also of note is a federal district court decision, Engst v. Orthalliance, Inc., No. C01-1469 (W.D. Wash. March 1, 2004) (unpublished, see CP 73-89)(See Appendix A attached). In Engst, the U.S. District Court for the Western District of Washington addressed contracts between an orthodontic practice management company ("Orthalliance") and a number of orthodontists. Under the contracts, Orthalliance would provide "practice management services, including payroll support, business systems and forms, information systems and accounting, inventory control, acquiring legal services, marketing and financial services, as well as

providing office facilities and equipment.” *Id.* at 2. Orthalliance’s fee was linked to the orthodontists’ gross revenue. *Id.* at 3.

Under the above facts, Chief District Judge Coughenour granted the orthodontists’ motion for summary judgment and invalidated the contract as illegal. Judge Coughenour held that it was “irrelevant” that Orthalliance “exercised no control over Orthodontists’ delivery of patient care services” because “Washington courts are quite clear that a non-licensed entity may be in contravention of the statute even if it had absolutely no involvement in the delivery of patient services.” *Id.* at 11; *see also OCA, Inc. v. Hassel*, 389 B.R. 469, 479 (E.D. La. 2008) (holding that management services contract between orthodontists and corporation was illegal under Washington law even where the corporation was not “involved in the provision of professional orthodontic services to patients and . . . the doctors retained authority over staffing level and compensation decisions.”).

In sum, Washington courts invalidate any contract where a non-dentist becomes involved in the maintenance or operation of a dental practice beyond the most ministerial administrative tasks, especially where the non-dentist corporation obtains a “substantial beneficial interest” in the practice’s profits.

**C. The Service Agreement Violates RCW 18.32.675(1)**

The Service Agreement at issue here is an extraordinary breach of Washington's public policy. The contract purports to grant Thaheld control over virtually all aspects of Dr. Lee's dental practice save for those that actually involve "hand-in-mouth" dentistry.

Under the Agreement, Thaheld obtains a "substantial beneficial interest" in the practice's finances. Fallahzadeh, 119 Wn. App. at 605. Thaheld's "performance" fee is tied directly to Lee Dental Practices' profits – up to fifty percent. Service Agreement, ¶7.3.1. Thaheld's "service" fee is tied directly to the salary of the highest paid dentist (with a \$120,000 minimum). *Id.* at ¶7.3.1. If the practice sells, Thaheld takes half the proceeds. *Id.* at ¶7.3.4-7.3.6.

The Agreement also gives Thaheld operational and managerial control that far exceeds "clerical services." For example, the Agreement gives Thaheld an irrevocable power of attorney to make withdrawals from Lee Dental Practices' bank accounts, and Lee Dental Practices may not draw from its own accounts without Thaheld's permission. *Id.* at ¶4.12.1. Thaheld controls "recruiting, hiring, management and terminations" of staff. *Id.* at ¶4.8. Thaheld is entitled to choose the location for Lee Dental Practices' clinics. *Id.* at ¶4.1.1. Thaheld controls any amendments

to Lee Dental Practices' employment agreements. *Id.* at ¶5.1(a)(vi)(a). Thaheld controls whether Lee Dental Practices may merge with another clinic, or admit new partners. *Id.* at ¶5.1(a)(vi)(b). Thaheld has the power to negotiate contracts with third party payors. *Id.* at ¶4.9.

Through the Service Agreement, Thaheld imposes restrictions on Lee Dental Practices that are inconsistent with the professional freedom RCW 18.32.675(1) protects. The Service Agreement caps dentist compensation at 23% of collections. Service Agreement, ¶5.2. Lee Dental Practices is required to operate "full time" regardless of whether it can do so consistent with responsible patient care. *Id.* at ¶5.1(a)(ii). Lee Dental Practices must develop a set of "practice guidelines" that are "reasonably acceptable" to Thaheld through his seat on a "Policy Board." *Id.* at ¶5.5.3. If the Agreement terminates for any reason, Lee Dental Practices is required to sell all of its clinics. *Id.* at ¶7.3.1. Perhaps most shockingly, the agreement effectively turns Dr. Lee into an indentured servant by prohibiting him from quitting his practice without Thaheld's permission during the Agreement's 40-year term. *Id.* at ¶¶5.1(b); 8.1.

Finally, Thaheld's position on the "Policy Board" gives him veto power in numerous operational areas. The Policy Board's power comes from its ability to approve or disapprove major actions and policies of Lee Dental Practices, including capital equipment expenditures, advertising, long term and short term goals, personnel plans, patient scheduling guidelines, procedures for resolving patient claims, workplace health and safety guidelines, as well as the organization and delivery of emergency Dental Care. *See generally id.* at ¶3.2 *et seq.* Thaheld and Lee Dental Practices are the only members of the Board. *Id.* at ¶3.1. Because the Board acts by majority vote, either party can effectively prevent the Board from acting by withholding its approval. The Board thus gives Thaheld the ability to prevent Lee Dental Practices from acting in any of the areas it governs.

In sum, the Service Agreement's entire function is to grant Thaheld a legally-impermissible role in Lee Dental Practices. It is far more onerous than the arrangements invalidated in Boren, Fallahzadeh and Engst. The trial court erred by denying Lee Dental Practices' motion for summary judgment as to the Agreement's illegality.

**D. Thaheld's Attempts to Salvage Facially Illegal Service Agreement Fail.**

Despite the Service Agreement's predominate illegal purpose, Thaheld argued to the trial court that the Agreement could nonetheless survive because Thaheld transformed it into a legal contract by not enforcing its terms and/or because of the Agreement's savings clauses. Thaheld essentially makes the ironic argument that the Court must enforce the Agreement because the Agreement's actual terms are entirely meaningless. Thaheld's arguments are severely flawed.

**1. Thaheld's Initial Failure to Enforce Does Not Make Contract Legal**

Before the trial court, Thaheld relied on a novel argument that even if the Service Agreement is facially illegal, "the actions of the parties varied from the terms of the Agreement and changed the effects of the same significantly." Thaheld argued that the parties' "true relationship" was consistent with Washington law.

Thaheld's argument fails for two reasons: first, because a facially illegal contract is void and unenforceable regardless of the parties' actions or intent, and second, because the parol evidence rule prevents a party from contradicting the terms of a written agreement using extrinsic evidence.

**a. Facially Illegal Agreements are Void.**

Thaheld's argument that the parties' actions transmuted the facially illegal agreement into a legal one is based on a fundamental misreading of Washington law regarding illegal contracts. Washington's rule is that illegal contracts are void *ab initio* as a matter of law. Hammack v. Hammack, 114 Wn. App. 805, 810, 60 P.3d 663, 666 (2003) ("A contract that 'seriously offends law or public policy' is 'void ab initio' or "null from the beginning."). An agreement found to be void *ab initio* never existed for legal purposes. "If an agreement is void, it is by definition not a contract. Rather than saying that a contract is void, it would be more exact to say that no contract has been created. . . . The result is that the contract is of no effect, is null, and is incapable of being enforced." 25 David. K. DeWolf & Keller W. Allen, *Wash. Prac., Contract Law And Practice* § 1.7, at 12 (2nd ed.2007).

Because the Services Agreement violates Washington law on its face, it is void. Rathke v. Yakima Valley Grape Growers Ass'n, 30 Wn.2d 486, 501, 192 P.2d 349 (1948) (holding that where an agreement "shows on its face that it is illegal ... the trial court was justified in dismissing the action on that ground."). There was no "contract" for the parties to modify through their actions.

Thaheld's argument that a court must look beyond a facially illegal agreement to the underlying circumstances misunderstands a line of Washington cases holding that "[t]he parol evidence rule does not exclude parol evidence to establish illegality." City of Redmond v. Kezner, 10 Wn. App. 332, 340, 517 P.2d 625 (1973); Auve v. Fagnant, 16 Wn.2d 669, 677, 134 P.2d 454 (1943); Engst, *supra*, at 7-8 (holding that if dental service management agreement was not in "actual direct" [i.e., facial] breach of RCW 18.32.675(1), Court was entitled to look beyond the four corners of the document to determine whether the parties were in "de facto" breach of the law).

These cases hold that a contract may be proven illegal by extrinsic evidence even if it is not illegal by its terms. In Auve, for example, the Washington Supreme Court held that a series of agreements that were not usurious on their face were properly held illegal where the agreements arose from an underlying transaction that was "tainted with usury." 16 Wn.2d at 679.

But while cases like Auve, Kezner, and Engst show that a facially legal contract may be proved illegal by reference to parol evidence, they do not stand for the proposition that the reverse is true. In fact, a facially illegal agreement cannot somehow become

legal because a party has not yet chosen to enforce the illegal provisions. Where a contract is facially illegal, it is “null from the beginning,” invalid and no action can be brought to enforce it. Hammack, 114 Wn. App. at 810; Rathke, 30 Wn.2d at 501. As far as courts are concerned, parties cannot “modify” a facially illegal “contract” because no contract existed in the first place.

In sum, the Service Agreement at issue is illegal on its face, void *ab initio*, and cannot be transformed into a legal agreement through the parties’ subsequent actions.

**b. Thaheld cannot create a material issue of fact by contradicting the terms of the Service Agreement.**

Even if it were somehow possible to “modify” an illegal agreement, Thaheld’s attempt to do so would be precluded by the parol evidence rule. Under the parol evidence rule, a contracting party is prohibited from using extrinsic evidence “to delete or contradict written terms that are inconsistent with the extrinsic evidence.” Schweitzer v. Schweitzer, 81 Wn. App. 589, 595, 915 P.2d 575 (1996) (trial court erred by using parol evidence to “subtract” a paragraph from a written agreement and give that paragraph no effect). While the Washington Supreme Court’s Berg

v. Hudesman decision broadened the scope of admissible extrinsic evidence,<sup>3</sup> the Court has subsequently clarified that under Berg:

[A]dmissible extrinsic evidence does not include:

- Evidence of a party's unilateral or subjective intent as to the meaning of a contract word or term;
- Evidence that would show an intention independent of the instrument; or
- **Evidence that would vary, contradict or modify the written word.**

Hollis v. Garwall, Inc., 137 Wn.2d 683, 695, 974 P.2d 836 (1999)  
(emphasis added).

The Service Agreement in this case is a fully-integrated agreement drafted by Thaheld. Service Agreement, ¶11.14. Thaheld's argument below boils down to an assertion that because he had not yet enforced certain of his contractual rights under the written Service Agreement, there is an "issue of fact" as to whether those terms fell out of the contract altogether. Indeed, Thaheld represented below that the parol evidence he relies on is intended to show that the "actual" contract between the parties was "materially different from the Agreement" as written.

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<sup>3</sup> 115 Wn.2d 657, 801 P.2d 222 (1990) (holding that extrinsic evidence is admissible to interpret even unambiguous agreements).

Thaheld's attempt to admit extrinsic evidence to directly contradict the parties' fully-integrated document and show that a completely different agreement "actually" existed is not permitted under the parol evidence rule or under Berg. Thaheld's may not rely on extrinsic evidence to argue that the substantial managerial and operational control the Service Agreement grants him does not exist.

**2. Thaheld Cannot Rely on the "Savings" Clauses to Reform the Pervasively Illegal Contract.**

The Service Agreement contains several clauses disavowing any illegal effect of the contract. The clauses state that, notwithstanding the Agreement's express terms, the parties do not intend that Thaheld engage in "Dental Care," defined in part as anything constituting the "practice of dentistry under the laws and regulations of the state in which such procedures ... are performed." Paragraph 2.5, 12.16; *see also, e.g.*, Paragraph 11.1. The Agreement further purports to require a court to "reform" the contract "to the extent necessary to make [any illegal] provision enforceable." Paragraph 11.6.

However, the Service Agreement's *raison d'être* is to give Thaheld a stake in Lee Dental Practices. Under Washington law

severance/reformation clauses cannot “save” a pervasively illegal contract.

As stated by the Washington Supreme Court, “where the illegality pervades the entire agreement, the courts will abstain from ... separation and refuse affirmative relief.” Rathke v. Yakima Valley Grape Growers Ass'n, 30 Wn.2d 486, 509, 192 P.2d 349 (1948). The doctrine has been aptly summarized by the Ninth Circuit:

It is a well-known principle in contract law that a clause cannot be severed from a contract when it is an integrated part of the contract. As one leading treatise has noted, “a contract should be treated as entire when by consideration of its terms, nature and purposes each and all of the parts appear to be interdependent and common to one another.” ...

As a leading treatise notes, severance is inappropriate when the entire clause represents an “integrated scheme to contravene public policy.”

Graham Oil Co. v. ARCO Products Co., 43 F.3d 1244, 1248 (9th Cir. 1994).

Illegal “services agreements” like the one at issue here are prime examples of contracts where severance is inappropriate because it is the relationship itself that is illegal, not a specific contractual clause. In Engst, *supra*, where the U.S. District Court for the Western District of Washington invalidated a dental service

management agreement similar to the one here, the court easily rejected a severability argument as follows:

Defendant argues that the Court should merely sever those parts of the agreements which are contrary to the law. However, the Court finds that it is the *entire relationship* between the parties which is in contravention of the law.

For these reasons, the Court finds that the agreements constituting the relationship between Defendant and Orthodontists ... are void and illegal as against public policy.

*Id.* at 15-16 (emphasis in original).

Washington's severability authority was similarly applied by another U.S. District Court in OCA, Inc. v. Hassel, 389 B.R. 469 (E.D. La. 2008) to an dental practice management agreement. In Hassel, a corporation ("OCA") entered into a "practice management" contract with Washington dental care providers (in that case, orthodontists). As here, the contract gave OCA a large stake in the practices' finances as well as substantial control over recruiting, marketing, hiring, payroll, billing, and the practices' bank accounts. *Id.* at 472. When the corporation filed for bankruptcy in the Eastern District of Louisiana, the legality of the contracts became an issue. On appeal from a ruling by the bankruptcy court

declaring the contracts illegal, the District Court applied Washington law and upheld the bankruptcy court's ruling, explaining that:

OCA's business relationships with the orthodontists were ones in which OCA controlled significant aspects of the orthodontic practices, shared in their profits, and played an active role in their operations. OCA was not a mere investor or involved in arms-length transactions with these orthodontic practices.

*Id.* at 478-79. The court further held that OCA's severability/savings clauses could not be given effect:

OCA's [severability] argument fails because the illegal elements of the [service agreements] are the *sine qua non* of the agreements. ... [T]here is no apparent way to excise the unlawful provisions and leave anything to govern a relationship between OCA and the doctors. As the Engst court observed in rejecting a similar argument in favor of severing illegal contractual provisions to the one that OCA makes here, "it is the entire relationship between the parties which is in contravention of the law." The same is true here, as the fundamental business arrangement between OCA and the doctors is illegal. The relationship between the doctors and OCA is predicated on OCA assuming and executing certain responsibilities that give it control over the practice's operations in exchange for a share of the profits. OCA offers no guidance on how to sever any of the unlawful provisions.

*Id.* at 480-81 (citation omitted); see also, e.g., Graham Oil, 43 F.3d at 1249 (refusing to sever three illegal provisions in an arbitration clause because the "various unlawful provisions are all a part of [the clause's] overall procedure"). This case mirrors those situations

where illegal portions of an agreement are not readily separable from legal ones.

The illegality of the Service Agreement is not a limited to a discrete illegal provision that can easily be excised. To the contrary, illegality “pervades the entire agreement.” Rathke, 30 Wn.2d at 509. Nearly every page contains a mechanism giving Thaheld control over Lee Dental Practices. It is an “integrated scheme to contravene public policy.” Graham Oil, 43 F.3d at 248.

Courts will only act to save a portion of a contract from illegality if it is remote from or collateral to the illegal transaction, or is supported by independent consideration. Sherwood & Roberts-Yakima, Inc. v. Cohan, 2 Wn. App. 703, 710, 469 P.2d 574, 578-79 (1970). There is no remote or collateral transaction to preserve here, only a single, integrated agreement granting Thaheld extensive control over Lee Dental practices.

The Agreement is flush with illegality and no reformation or severance is possible; it must be entirely invalidated.

## **VI. CONCLUSION**

For the above reasons, Appellant Lee Dental Practices requests that this Court reverse the trial court’s ruling denying Lee Dental Practices’ motion for summary judgment, and remand with

instructions that summary judgment be entered in favor of Lee  
Dental Practices.

DATED this 28th day of December, 2012.

ADELSTEIN, SHARPE & SERKA LLP

By: 

Jeffrey P. Fairchild, WSBA #18895  
Ivan M. Stoner, WSBA #43321  
Attorney for Choong H. Lee, DMD,  
PLLC and CH Lee, PLLC

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## **APPENDIX A**

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01-CV-01469-SUP

UNITED STATES DISTRICT COURT  
WESTERN DISTRICT OF WASHINGTON  
AT SEATTLE

E. DAVID ENGST, E.D. ENGST, P.S., DAVID  
L. CROUCH, DAVID L. CROUCH, M.S.D.,  
P.S., DONALD L. GRIM, and DONALD L.  
GRIM, D.D.S., M.S., P.S.,

Plaintiffs,

v.

ORTHALLIANCE, INC., a Delaware  
corporation,

Defendant.

CASE NO. C01-1469C

ORDER

I. INTRODUCTION

This matter has come before the Court on Plaintiffs' motion for summary judgment (Dkt. No. 47). The Court has determined that oral argument is not necessary. Having carefully considered the papers filed in support of and in opposition to Plaintiffs' motion, the Court hereby GRANTS the motion.

Plaintiffs also moved for permission to supplement their briefing for the summary judgment motion (Dkt. No. 86). For the reasons described below, the Court GRANTS the motion to supplement.

II. BACKGROUND

Plaintiffs are individual orthodontists (the "Orthodontists") and their associated professional

1 services corporations (the "Orthodontic Entities"). Between 1998 and 2000, Plaintiffs, or some subset  
2 thereof, executed a series of agreements with Defendant, an orthodontic practice management company.  
3 Defendant's business is to provide practice management services, including "payroll support, business  
4 systems and forms, information systems and accounting, inventory control, acquiring legal services,  
5 marketing and financial services," as well as providing office facilities and equipment. (Def.'s Resp. at  
6 4.)

7 There are four types of agreements at issue in the case at bar: 1) the purchase and sale  
8 agreements, 2) the consulting and business services agreements, 3) the employment agreements, and 4)  
9 personal guaranties.

10 The purchase and sale agreements were entered into by either an individual orthodontist or the  
11 orthodontist and his existing professional services corporation and Defendant Orthalliance. If the  
12 agreement was between only an individual orthodontist and Defendant, the agreement provided that the  
13 individual orthodontist would form a new professional corporation through which to conduct his  
14 orthodontic practice. Pursuant to the purchase and sale agreements, the Orthodontic Entities transferred  
15 most of their tangible assets, leasehold interests, personal goodwill and referral source contacts to  
16 Defendant. Under the agreements, patient records remained the property of the Orthodontic Entities.

17 The consulting and business services agreements were entered into by the Orthodontic Entities  
18 and Defendant. Under these agreements, Defendant was responsible for providing the Orthodontic  
19 Entities with office facilities and equipment, personnel and payroll, business systems, procedures and  
20 forms, purchasing and inventory control, accounting services and financial reporting, legal services,  
21 marketing assistance, planning for the opening of offices in new locations, billing and collection  
22 services, payment and disbursement of funds, and recordkeeping. (See Crouch Decl. Ex. B § 1.) Not  
23 only was Defendant responsible for *providing* office facilities and equipment, the agreement provided  
24 that Defendant would "consult with and advise the Orthodontic Entity on its equipment and office needs  
25 and the efficient configuration of its office space." (*Id.* § 1.2.) Likewise, Defendant's role went beyond

1 the provision of staff, extending into assisting the Orthodontic Entity with staff scheduling. In return for  
2 Defendant's services, the Orthodontic Entities paid Defendant a yearly fee of the greater of \$194,703 or  
3 17% of the Entity's Adjusted Gross Revenue. (*Id.* § 3.1.)

4 Under the consulting and business services agreements, all of the Orthodontic Entities' accounts  
5 receivables would go into an Orthalliance account with the Orthodontic Entity's name on it. Out of this  
6 account, Defendant would pay its consulting fee and all other expenses incurred by the Orthodontic  
7 Entity during the course of conducting its business. These expenses included taxes, rent, insurance,  
8 salaries, and other items. (*Id.* §§ 1.11-1.12.)

9 The third set of contracts, the employment agreements, were entered into by the individual  
10 orthodontists and their respective professional services corporations. Under the terms of these  
11 agreements, the Orthodontists agreed to be employed by the Orthodontic Entities for a period of five  
12 years, subject to renewal for successive one-year terms after that. The individual Orthodontists also  
13 agreed not to practice orthodontics at any other facility or for the benefit of any other patients.  
14 Defendant OrthAlliance was not a party to the employment agreements.

15 The last set of agreements were personal guaranties, executed by the Orthodontists and  
16 Defendant, in which the Orthodontists personally guaranteed payment of the amounts due to Defendant  
17 from the Orthodontic Entities for a term of five years.

18 Plaintiffs originally filed this action in King County Superior Court. It was removed to federal  
19 district court in September 2001. Plaintiffs complained of several things, including alleged breaches of  
20 contract by Defendant (who allegedly failed to provide services as required by the consulting and  
21 business services agreements) and allegedly illegal covenants not to compete. In the alternative,  
22 Plaintiffs also allege that the relationship between Orthodontists, the Orthodontic Entities and Defendant  
23 violates Washington's law against the corporate practice of dentistry, Wash. Rev. Code § 18.32.675.

24 Plaintiffs have now moved for summary judgment.  
25

1 III. ANALYSIS

2 A. *Supplementary briefing*

3 Plaintiffs' motion for summary judgment was originally filed on September 23, 2003 and noted  
4 for hearing on October 17, 2003. The noting date was subsequently changed to November 14, 2003.  
5 The final discovery deadline was September 29, 2003. However, on November 6, 2003, this Court  
6 issued an order granting Plaintiffs' motion to compel the production of Defendant's Contact Manager  
7 database and responses to five key interrogatories. Thus, in practice, discovery continued long after the  
8 briefing for the instant summary judgment motions was complete.

9 Plaintiffs moved for permission to file a supplementary brief both because of alleged new and  
10 relevant findings from their discovery and because on January 5, 2004, a Washington appellate court  
11 issued an opinion interpreting Wash. Rev. Code § 18.32.675, *Ghorbanian v. Fallahzadeh*, No. 50766-4-  
12 1 (Wash. Ct. App. Jan. 5, 2004). At the time Plaintiffs filed their motion for permission, it still appeared  
13 that the trial in this matter would commence on January 20, 2004. For this reason, Plaintiffs appended  
14 the substance of their supplementary brief to their motion for permission. Defendant's response to the  
15 motion for permission concentrated mainly on the substance of Plaintiffs' supplementary brief, but also  
16 sought to argue that Plaintiffs' new material "raises no new issues and should be dismissed." (Def.'s  
17 Rcsp. Supp. Pleadings at 8.)

18 While, as Defendant points out, Plaintiffs' supplemental briefs raise no new *issues*, the additional  
19 briefing contains material which is clearly relevant to the issues raised in the underlying motion for  
20 summary judgment, and which could not have been raised before. *Ghorbanian*, especially, is helpful as  
21 another data point in the sparse constellation of cases interpreting Washington's law against the  
22 corporate practice of dentistry. As for the additional pieces of evidence Plaintiffs seek to introduce, had  
23 Defendant's behavior not required this Court to issue an order to compel discovery long after the  
24 discovery deadline had passed, Plaintiffs could have introduced this evidence in their original brief. For  
25 these reasons, the Court finds that Plaintiffs' supplemental briefs are warranted and hereby GRANTS the

1 motion.

2 *B. Summary Judgment*

3 *1. Applicable law*

4 Rule 56 of the Federal Rules of Civil Procedure governs summary judgment motions, and  
5 provides in relevant part, that “[t]he judgment sought shall be rendered forthwith if the pleadings,  
6 depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show  
7 that there is no genuine issue of material fact and that the moving party is entitled to a judgment as a  
8 matter of law.” Fed. R. Civ. P. 56(c).

9 The Rules of Decision Act, 28 U.S.C. § 1652, provides that “[t]he laws of the several states,  
10 except where the Constitution or treaties of the United States or Acts of Congress otherwise require or  
11 provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases  
12 where they apply.” This action was removed by Defendant as a case in which this Court had jurisdiction  
13 because of complete diversity between the parties, as required under 28 U.S.C. § 1332. (*See* Def.’s  
14 Notice of Removal, Dkt. No. 1.) In diversity cases, which by their nature arise under state law, a federal  
15 district court must apply state substantive law. *Am. Triticale, Inc. v. Nyteo Servs., Inc.*, 664 F.2d 1136,  
16 1141 (9th Cir. 1981) (citing *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938)). Since this case is a  
17 diversity case, the Court shall therefore apply state substantive law. The parties agree that Washington  
18 state law should be applied to this matter.

19 The heart of the matter at hand is the legality of the contractual relationship between the  
20 Orthodontists, the Orthodontic Entities and Defendant. The legal effect of a contract is a question of law  
21 that may properly be determined on summary judgment. *Absher Constr. Co. v. Kent School Dist. No.*  
22 *415*, 890 P.2d 1071, 1073 (1995) (holding that “interpretation of an unambiguous contract is a question  
23 of law”). The validity of a contract, or lack thereof, whether due to illegality or its contrariness to public  
24 policy, is also a question of law that may be properly determined on summary judgment. *Motor*  
25 *Contract Co. v. Ven der Volgen*, 298 P. 705, 707 (1931).

26 ORDER – 5

1                   2.     *Washington's corporate practice of dentistry doctrine*

2     Section 18.32.675 of the Revised Code of Washington provides that

3     No corporation shall practice dentistry or shall solicit through itself, or its agent, officers,  
4     employees, directors or trustees, dental patronage for any dentists or dental surgeon  
5     employed by any corporation[.] . . . PROVIDED, That nothing contained in this chapter  
6     shall apply . . . to corporations or associations furnishing information or clerical services  
7     which can be furnished by persons not licensed to practice dentistry, to any person  
8     lawfully engaged in the practice of dentistry, when such dentist assumes full  
9     responsibility for such information and services. Any corporation violating the provisions  
10    of this section is guilty of a gross misdemeanor, and each day that this chapter is violated  
11    shall be considered a separate offense.

12    Wash. Rev. Code § 18.32.675 (2003).<sup>1</sup>

13     Section 18.32.020 further clarifies that “[a] person practices dentistry . . . who . . . owns,  
14    maintains, or operates an office for the practice of dentistry.” Wash. Rev. Code § 18.32.020 (2003).

15     There is ample Washington case law interpreting this statute. The principal part of these cases  
16    have involved either the employment of licensed professionals by corporations or business partnerships,  
17    *see, e.g., State ex rel. Standard Optical Co. v. Superior Court for Chelan County*, 135 P.2d 839, (Wash.  
18    1943), or mixed partnerships, in which some of the partners were licensed professionals and the others  
19    not, *see, e.g., Morelli v. Ehsan*, 756 P.2d 129 (1988). In *Standard Optical*, the Washington Supreme  
20    Court held that a corporation was to be prohibited from the practice of medicine through directly  
21    employing licensed professionals because

22                   [i]f such a course were sanctioned the logical result would be that corporations and  
23                   business partnerships might practice law, medicine, dentistry or any other profession by  
24                   the simple expedient of employing licensed agents. And if this were permitted  
25                   professional standards would be practically destroyed, and professions requiring special  
26                   training would be commercialized, to the public detriment. The ethics of any profession is  
                    based upon personal or individual responsibility. One who practices a profession is  
                    responsible directly to his patient or his client. Hence he cannot properly act in the  
                    practice of his vocation as an agent of a corporation or business partnership whose  
                    interests in the very nature of the case are commercial in character.

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27                   <sup>1</sup>This statute was amended in 2003 by the Act effective July 1, 2004, ch. 53, § 124, 2003 Wash.  
28    Laws 408-09 (reorganizing criminal statutes to simplify citation to offenses). The amendments effected  
29    by the Act were minor technical amendments only.

1 135 P.2d at 843 (citing *Ezell v. Ritholz*, 198 S.E. 419, 424 (S.C. 1938)).

2 At first glance, it appears that the arrangement in this case may not offend Washington's law  
3 against the corporate practice of medicine because the Orthodontic Entities were wholly owned by the  
4 Orthodontists, each of whom was a licensed dentistry professional, and because the Orthodontists were  
5 employed by the Orthodontic Entities. On its face, the case at bar does not appear to present a situation  
6 in which there is any impermissible entanglement between the Orthodontists and Defendant. However,  
7 the Court cannot ignore that the Orthodontists, the Orthodontic Entities and Defendant all co-exist in a  
8 certain *universe* of contractual agreements. Defendant itself has asserted that it, as a third-party  
9 beneficiary, may enforce the terms of the employment agreements between the Orthodontists and their  
10 respective Orthodontic Entities, particularly the covenant not to compete contained therein. This attempt  
11 to become involved in the employment agreements between the Orthodontists and their Orthodontic  
12 Entities belies Defendant's protestations that Orthodontists are not employed or controlled in any way by  
13 Defendant.  
14

15 *i. Court scrutiny of the purpose and effect of the parties' relationship*

16 Direct employment of a licensed professional is not the only way non-licensed entities have been  
17 found to fall afoul of Washington's law against the corporate practice of medicine. Indeed, the more  
18 recent cases in which courts have applied Washington's law against the corporate practice of medicine  
19 have all dealt with factual scenarios in which there is a more attenuated relationship between the non-  
20 licensed entity and the licensed professional. See, e.g., *State v. Boren*, 219 P.2d 566 (Wash. 1950);  
21 *Morelli v. Ehsan*, 756 P.2d 129 (Wash. 1988); *Ghorbanian v. Fallahzadeh*, No. 50766-4-1 (Wash. Ct.  
22 App. Jan. 5, 2004). Despite the lack of an *actual direct* employment relationship in these cases,  
23 however, the courts have not hesitated to find a *de facto* relationship which puts the non-licensed entity  
24 in contravention of the doctrine. These cases, while all dealing with very different factual scenarios,  
25

1 have all endorsed an approach whereby the court closely scrutinizes the *effect and purpose* of the  
2 contractual agreements between the parties, rather than limiting its scrutiny to the four corners of the  
3 *contracts themselves*.<sup>2</sup>

4 In *State v. Boren*, 219 P.2d 566 (Wash. 1950), the Supreme Court of Washington overruled a  
5 previous ruling in *State v. Brown*, 79 P. 635 (Wash. 1905) which had found that the portion of  
6 Washington's law against the corporate practice of dentistry as it was at that time, which prohibited an  
7 unlicensed entity from owning, maintaining, or operating an office for the practice of dentistry, violated  
8 Washington's constitution. The *Boren* court found fit to overrule *Brown*, simply finding that the state  
9 was fully within its power to find that a person or entity was engaging in the practice of dentistry who  
10 owned, maintained or operated an office for the practice of dentistry. 219 P.2d at 572.

11  
12 Barely twelve months later, the newly reinstated prohibition was tested in *Prichard v. Conway*,  
13 234 P.2d 872 (Wash. 1951). Justifying its own optimism, however, in *Campbell v. State*, 122 P.2d 458,  
14 462 (Wash. 1942) that "[i]t must be assumed that a law will be given a reasonable and not a strained  
15 construction" in dismissing fears similar to those in *Brown*, the supreme court refused to affirm the  
16 dismissal of a case about the conditional sale by the widow of a deceased dentist of her deceased  
17

---

18  
19 <sup>2</sup>Our sister court in the Northern District of Texas agreed with this fundamental premise of this  
20 approach when, in assessing a set of contracts substantially similar to the ones in the case at bar, also  
21 between Defendant and some orthodontic surgeons, it concluded that "[t]he Parties seek to accomplish  
22 in a trilateral contract that which they cannot in a bilateral contract, an express written employment  
23 contract." *Penny v. Orthalliance*, 255 F. Supp. 2d 579, 583 (N.D. Tex. 2003). The Court is not  
24 concerned here with the substance of the holding in that case, since the Texas statute in question is  
25 somewhat different than Washington's statute. Where the Texas statute states that a person is practicing  
26 dentistry if, among other things, he or she "owns, maintains, or operates an office or place of business in  
which the person employs or engages under any type of contract another person or persons to practice  
dentistry," Tex. Occ. Code Ann. § 251.003(a)(4) (Vernon Supp. 2003), while the Washington statute  
states simply that "[a] person practices dentistry, within the meaning of this chapter, who . . . owns,  
maintains or operates an office for the practice of dentistry," Wash. Rev. Code. § 18.32.020. The  
reasoning employed by the *Penny* court is thus inapposite in this case.

1 husband's practice to a licensed dentist. The terms of the agreement reached by the widow and the  
2 dentist provided that she would continue to have "the right to be the manager of [the office] and would  
3 have the right to superintend the business management of the office." *Prichard*, 234 P.2d at 874.  
4 Moreover, since Dr. Prichard did not have money for a down payment, the widow retained title to the  
5 fixtures and equipment and the lease was to be renewed in her name until Prichard's payments to her  
6 under the contract were complete, at which time all the property would become the property of Dr.  
7 Prichard.  
8

9 The *Prichard* court expressed its opinion that work performed by office managers, office  
10 secretaries and bookkeepers, though possibly essential to the profitability of a practice, did not constitute  
11 the practice of medicine or dentistry. 234 P.2d at 876. However, the court cautioned that

12 the fact that the same details are supervised by one who, instead of being an employee, is  
13 selling the practice under a conditional sales contract, *does not of necessity constitute*  
14 *such ownership, maintenance or operation of an office for the practice of medicine or*  
15 *dentistry as is contemplated by [the statute], although it could well be a factor requiring a*  
*closer scrutiny of the entire transaction to determine whether it is actually what it*  
*purports to be or, instead, is a scheme or subterfuge to violate the law."*

16 *Id.* (emphasis added). This cautionary statement effectively limits the holding in *Prichard* to the specific  
17 facts before it, while requiring future courts faced with similar facts to inquire into the "real" import or  
18 effect of similar agreements. In this passage, the *Prichard* court recognizes that some agreements may,  
19 on their face, appear to be one thing while really being another, and suggests that close scrutiny may be  
20 required to determine what the underlying transaction really is.

21 In January 2004, a Washington state appellate court reaffirmed this state's commitment to this  
22 approach – namely that of looking beyond the surface of an agreement to divine its intent – and found  
23 that the illegal practice of dentistry can assume many forms. *Ghorbanian v. Fallahzadeh*, No. 50766-4-1  
24 (Wash. Ct. App. Jan. 5, 2004), available at <http://www.courts.wa.gov/opinions/index.cfm?fa=opinions>.  
25

1 opindisp&docid=507664MAJ. *Ghorbanian* is significant in several ways. First, it lends more credence  
2 to the particular type of judicial scrutiny the Court believes appropriate in this case. Second, it is the  
3 first reported case since *Morelli v. Ehsan*, 756 P.2d 129 (Wash. 1988) to have addressed and applied  
4 Washington's law against the corporate practice of medicine. This long period of apparent desuetude,  
5 about fifteen years, had led some observers to wonder if the doctrine was still live. See, e.g., Lisa R.  
6 Hayward, Note and Comment, *Revising Washington's Corporate Practice of Medicine Doctrine*, 71  
7 Wash. L. Rev. 403, 405 (1996). However, *Ghorbanian* indicates that the doctrine, for better or for  
8 worse, is still alive and kicking. Moreover, *Ghorbanian* illustrates Washington courts' continued  
9 willingness to find that the law prohibits more than direct employment contracts or direct involvement in  
10 patient care.

12 *Ghorbanian* involved a lease agreement between two tenants-in-common, Ghorbanian, D.D.S.,  
13 P.S., a dental practice, and Fallahzadeh, an individual. *Ghorbanian*, No. 50766-4-1 at \*2. In exchange  
14 for rent in the amount of 50% of the practice's net profits, Ghorbanian was permitted use of the building.  
15 In addition to the landlord-tenant relationship, Fallahzadeh was also employed as the practice's office  
16 manager. Fallahzadeh made several personal loans to the dental practice, as well as signed a \$200,000  
17 personal guarantee for the promissory note Ghorbanian gave in payment for the dental practice.

18 As the office manager, Fallahzadeh had check-writing authority and handled the practice's  
19 accounts. On September 8, 2001, Ghorbanian became concerned that Fallahzadeh might have been  
20 embezzling from the practice, fired Fallahzadeh and reported him to the Renton police. Later that  
21 month, Fallahzadeh's attorney sent a letter to Ghorbanian demanding payment of allegedly overdue rent.  
22 Ghorbanian subsequently claimed that their agreement was illegal.

24 The state appellate court found that the combined effect of the rental agreement and the  
25 discretionary power retained by Fallahzadeh over the practice's funds and physical assets was that

1 Fallahzadeh was illegally owning, operating, or maintaining an office for the practice of dentistry in  
2 contravention of Washington law.

3                   ii.     *Non-involvement in delivery of patient services*

4             Washington courts interpreting the statute have been quite clear in holding that the non-licensed  
5 party's "noninvolvement in the delivery of professional services is not determinative." *Ghorbanian*, No.  
6 50766-4-1 at 4 (citing *Standard Optical*, 135 P.2d 839, 844 (stating that "[w]hile it may be assumed that  
7 the optometrist in his practice exercised his professional judgment conscientiously in each individual  
8 case, *this has no bearing upon the questions here presented*") (emphasis added)). *See also, Morelli*, 756  
9 P.2d at 131 (favorably quoting from *Standard Optical* to support its holding that general partner who did  
10 not exercise any control over the actual provision of medical services was still illegally engaged in the  
11 provision of medical services). Therefore, the fact that a non-licensed party may not have any  
12 involvement whatsoever in the delivery of patient services is wholly irrelevant to the analysis to be  
13 undertaken by the courts.

14                   2.     *Application of the law to the case at bar*

15             The question the Court must answer here is whether Defendant, through its web of contractual  
16 relationships with Orthodontists and the Orthodontic Entities, effectively owned, maintained, or operated  
17 an office for the practice of dentistry, or otherwise practiced dentistry in violation of the law.  
18

19             As a preliminary matter, the Court notes that Defendant's arguments that it exercised no control  
20 over Orthodontists' delivery of patient care services are irrelevant. As discussed *supra*, Washington  
21 courts are quite clear that a non-licensed entity may be in contravention of the statute even if it had  
22 absolutely no involvement in the delivery of patient services.  
23

24             Defendant seeks to compare the situation at bar favorably to the fact scenario in *Prichard*,

1 arguing that the functions it was obliged to provide, if indeed it was *obliged* to provide any of them,<sup>3</sup>  
2 were no more than the functions performed by the office manager, office secretary and bookkeeper  
3 approved by the *Prichard* court. Defendant further argues that just as in *Prichard*, the case at bar  
4 involves what is essentially a conditional sales agreement.

5         The Court must reject Defendant's argument on both counts. First, the list of services Defendant  
6 was responsible for providing far exceeded the normal duties of an office manager, office secretary or a  
7 bookkeeper, or even of all three combined. According to the consulting and business services  
8 agreements between Defendant and the Orthodontic Entities, Defendant was responsible for providing  
9 office facilities and equipment, personnel and payroll, business systems, procedures and forms,  
10 purchasing and inventory control, accounting services and financial reporting, legal services, marketing  
11 assistance, planning for the opening of offices in new locations, billing and collection services, payment  
12 and disbursement of funds, and recordkeeping. (See Crouch Decl. Ex. B § 1.) Not only was Defendant  
13 responsible for *providing* office facilities and equipment, the agreement provided that Defendant would  
14 "consult with and advise the Orthodontic Entity on its equipment and office needs and the efficient  
15 configuration of its office space." (*Id.* § 1.2.) By the very terms of the agreements, Defendant played an  
16 advisory role that would be considered far beyond the proper role of an office manager.  
17

18         Second, the facts in this case, though they do describe a sale of sorts, are quite different from  
19 those in *Prichard*. The sale in *Prichard* was from a non-dentist to a dentist. The seller retained the title  
20 to the property and took a share of profits. In the case before the Court today, the sale is from the dentist  
21 to the non-dentist. Here, it is the *buyer* who has title to the property and takes a share of profits. For  
22

23 \_\_\_\_\_  
24         <sup>3</sup>Defendant contends that under the agreement, it offered a "menu" of services, implying that the  
25 Orthodontists were free to choose, or not choose, to take advantage of various services. (Def.'s Resp. at  
26 4.)

1 these reasons, the Court finds that the facts of this case are so different that *Prichard* cannot be  
2 formulaically applied. Moreover, as the Court pointed out in its discussion of *Prichard*, the *Prichard*  
3 court itself foreclosed a formulaic approach even to extremely similar facts. 234 P.2d at 876. Therefore,  
4 the case at bar requires a full analysis, and cannot be disposed of through a mere analogizing to  
5 *Prichard*.

6 Defendant also seeks to compare this case favorably to *Ghorbanian*, claiming that the *depth* of  
7 Defendant's involvement in the management of Orthodontists' practices may not have been on a level  
8 with Fallahzadeh's. However, the *scope* or *range* of Defendant's involvement far exceeds  
9 Fallahzadeh's. Furthermore, Defendant argues that Plaintiffs were free to reject any or all of  
10 Defendant's services at their discretion. While this is a factually accurate representation of the  
11 consulting and business agreements, it is also a fact that these services were offered as consideration for  
12 the payment of the greater of 17% of "adjusted gross revenue" or \$194,703. In this context, Defendant's  
13 argument is analogous to the general assertion that anytime an individual pays money for an item or  
14 service, that individual is not required to accept or receive that item or service. This is, strictly speaking,  
15 true. However, payment of money for an item or service can be taken as a clear intent to accept or  
16 receive that service. Likewise, Plaintiffs' payment of money to Defendant can be and is taken by the  
17 Court as a clear manifestation of intent to accept the services offered by Defendant. In any case, if the  
18 Court were to take Defendant at its word, the effect on Defendant's case would be even more damaging.  
19 Effectively, Defendant would be extracting money from the Orthodontic Entities in exchange for *nothing*  
20 whatsoever, and yet still be in what amounts to a virtual employer relationship (because of its third-party  
21 enforcement efforts) with the individual Orthodontists.

22 Here, Defendant only entered into two direct contractual relationships with Orthodontists, the  
23 purchase and sale agreements and the personal guaranties in which each Orthodontist agreed to be

1 personally liable for the amounts due to Defendant from the Orthodontic Entities under the consulting  
2 and business services agreements. Defendant also seeks to enforce, as a third-party beneficiary, the  
3 covenants not to compete entered into between Orthodontists and the Orthodontic Entities as part of the  
4 employment agreements. The Court finds that the effect of the latter two relationships together is both  
5 to put Defendant in the position of a virtual employer of Orthodontists *and* to enable Defendant to retain  
6 a beneficial interest in the profits from the practice of dentistry. The Court recognizes that the share of  
7 profits Defendant is entitled to under the consulting and business agreements is potentially far less than  
8 the large percentages (around half) considered by the *Prichard*, *Morelli* and *Ghorbanian* courts.  
9 However, the consulting and business agreements also named a set minimum amount, \$194,703. The  
10 personal guaranties entered into between Orthodontists and Defendant clearly anticipated that this fixed  
11 amount might well exceed the entire amount of "adjusted gross revenue" realized by the Orthodontic  
12 Entities in any given year. Therefore, the low 17% share represents only a percentage floor and is not  
13 determinative.  
14

15 For these reasons, the Court finds that Defendant was, through its interconnected contractual  
16 relationships to Orthodontists and the Orthodontic Entities, practicing dentistry in violation of  
17 Washington's law against the corporate practice of dentistry. Section 18.32.675 of the Revised Code of  
18 Washington provides that the corporate practice of dentistry is a gross misdemeanor. Since the  
19 relationship between Defendant and Orthodontists are constituted of several smaller contracts between  
20 assorted parties, each of the contracts constituting the overall relationship between Defendant and  
21 Orthodontists are illegal, including the contracts between Orthodontists and Orthodontic Entities.  
22

### 23 3. *Effect of illegality on the contracts*

24 In Washington, the general rule is that agreements which are illegal and contrary to public policy  
25 will not be enforced. *Red Devil Fireworks Co. v. Siddle*, 648 P.2d 468, 471 (Wash. Ct. App. 1960)

1 (citing *Hederman v. George*, 212 P.2d 841 (Wash. 1949)). Instead, the parties will be left where the  
2 court finds them. *Hederman v. George*, 212 P.2d 841 (Wash. 1949); *Reed v. Johnson*, 67 P. 381 (Wash.  
3 1901). An exception to this rule may exist where the parties are not *in pari delicto*, *Sherwood &*  
4 *Roberts-Yakima, Inc. v. Leach*, 409 P.2d 160 (1965), but there is no indication that the parties in this  
5 case did not act knowingly. Importantly, in Washington, good faith intentions do not excuse either party  
6 from knowing the law. *Morelli*, 756 P.2d at 132; *Ghorbanian*, No. 50766-4-1 at \*5.

7  
8 The Court found *supra* that the relationship between Defendant and Orthodontists, constituted by  
9 the agreements, was illegal. Washington courts have already spilled a great amount of ink on the public  
10 policy reasons underlying the law prohibiting the corporate practice of medicine. *See, e.g., Boren*, 219  
11 P.2d at 568-72. It is not necessary for the Court here to examine the public policy goals of the doctrine,  
12 but merely to point out that Washington precedent establishes that violation of the doctrine is *per se*  
13 contrary to public policy. *See, e.g., id.; Morelli*, 132-33. Therefore, the Court finds that the relationship  
14 between Defendant and Orthodontists is also necessarily against public policy.

15 In the case at bar, the agreements executed between the parties make specific reference to  
16 *Morelli*, the leading case at the time the agreements were signed. (*See, e.g., Crouch Decl. Ex. A at §*  
17 *3.04*). All parties, regardless of which party proposed the inclusion of *Morelli*, were clearly aware that  
18 their relationship was limited by Washington's law against the corporate practice of dentistry. There is  
19 no evidence to suggest that one party had set out to hoodwink another party to the agreement. Evidence  
20 of the pre-contractual communications between the parties indicate that all parties were on notice about  
21 the potential impact of Washington law. Regardless of whether the parties believed that these clauses  
22 protected their agreement, since the nature of the intent is irrelevant in Washington, the Court finds that  
23 the parties acted knowingly and were thus *in pari delicto*.

24  
25 Defendant argues that the Court should merely sever those parts of the agreements which are

1 contrary to the law. However, the Court finds that it is the *entire relationship* between the parties which  
2 is in contravention of the law.

3 For these reasons, the Court finds that the agreements constituting the relationship between  
4 Defendant and Orthodontists (including the agreements between Orthodontists and the Orthodontic  
5 Entities) are void as illegal and against public policy. The Court also finds that the parties acted  
6 knowingly and thus were *in pari delicto*. Therefore, the parties are to be left where they are.

7  
8 IV. CONCLUSION

9 In accordance with the foregoing analysis, the Court hereby GRANTS Plaintiffs' motions to file  
10 a supplementary pleading and for summary judgment. Plaintiffs' claims for breach of contract, fraud  
11 and misrepresentation, and violation of the Consumer Protection Act are hereby DISMISSED.  
12 Defendant's counterclaims against Plaintiffs for specific performance, breach of contract, detrimental  
13 reliance, tortious interference, unjust enrichment, and breach of guaranty are hereby DISMISSED.  
14 Defendant is to retain ownership of the assets it obtained through the purchase and sale agreements.  
15 Orthodontists are to retain the payments they received from Defendant under the purchase and sale  
16 agreements. No party has any obligation to another party under the consulting and business services  
17 agreements.  
18  
19

20 SO ORDERED this 1<sup>st</sup> day of March, 2004.

21  
22  
23   
24 CHIEF UNITED STATES DISTRICT JUDGE  
25  
26



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Mr. Hugh Klinedinst  
Belcher Swanson Law Firm PLLC  
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(XX) Personally Delivered

Delia A White  
DELIA A. WHITE

SUBSCRIBED AND SWORN to before me this 28th day of December 2012.



Marissa McCauley  
NOTARY PUBLIC, in and for the State of  
Washington; Residing in: Bham  
Printed Name: MARISSA MCCAULEY  
My commission expires: 2-12-16

S:\Lee, Choong\EMPLOYMENT\Adv. Johann Th... CERT-DELIVERY 12-28-12