

Case No. 74808-4

COURT OF APPEALS, DIVISION ONE,
OF THE STATE OF WASHINGTON

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

Appellant,

v.

BRET HARTMAN

Respondent

RESPONDENT'S RESPONSIVE BRIEF

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I. INTRODUCTION

Even if Bret's Independent, LLC made the guaranteed payments to Hartman as characterized by Holroyd, summary judgment was properly granted and the trial court did not err in dismissing the case because each of Holroyd's claims contain fatal flaws that Holroyd cannot overcome.

II. RESPONSE TO ASSIGNMENTS OF ERROR

The trial court properly granted summary judgment dismissing Holroyd's derivative action because (i) Holroyd explicitly agreed to the dismissal in his pleadings before the trial court and, (ii) under RCW 25.15.370 (2012) Holroyd did not have standing to bring the claim.

The trial court properly dismissed Holroyd's claim for breach of contract because there is no enforceable contract as to the terms alleged by Holroyd and Holroyd's own testimony alleges that his signature is forged.

The trial court properly dismissed Holroyd's claim for breach of fiduciary duty because Holroyd was not owed a fiduciary duty at the time of the alleged violations on which he bases his claim.

The trial court properly dismissed both Holroyd's claims for breach of contract and breach of fiduciary duty because there is no evidence that Holroyd suffered damages and without this element Holroyd's claims fail.

III. STATEMENT OF THE CASE

A. The Formation of Bret's Independent, LLC

In January 1996, Holroyd and Hartman began Bret's Independent, LLC, an automotive repair/service business. (CP 1152) A Certificate of Formation was filed with the Washington Secretary of State on February 15, 1996. (CP 1152) Holroyd stated under penalty of perjury that there is no written operating agreement for the LLC. (CP 1070)

B. Holroyd's Departure

Holroyd left Bret's Independent operations and management (CP 647-649) However, prior to that, in early 2007, Bret's Independent began experiencing significant financial difficulties and was unable to meet many financial obligations with withdrawals/debits from the checking account of Bret's Independent which often exceeded deposits/credits to the account and had outstanding IRS liens and debts. (CP 586-588; CP 1161) Hartman found evidence of Holroyd's drug use on the premises of Bret's Independent sometime in 2007. (CP 589) His drug use is confirmed by a declaration submitted by his wife, Lisa Holroyd in their dissolution proceedings. (CP 651) Sometime between 2010 and 2011, Holroyd moved to the state of California. (CP 648-649)

C. Assets/Liabilities of the LLC

Bret's Independent, LLC did not own any real property. Hartman managed the entire operations with his knowledge and personal services for its customers. (CP 594)

Bret's Independent also did not own the fixtures, partitions and other leasehold improvements nor did it own most of the non-fixture equipment located at the leased premises. (CP 586-587) Bret's Independent was the Lessee of an equipment lease with Puget Sound Leasing/First Sound Bank. (CP 686-693) The Equipment Lease was secured by an interest in the equipment located at the Bret's Independent premises. (CP 691) Hartman and Holroyd personally guaranteed the Equipment Lease. (CP 692) Under the Equipment Lease, in the event of default, First Sound Bank had the right, without court order, to repossess and remove the equipment. (CP 690) First Sound Bank sought foreclosure of the equipment; Hartman ceased his participation and operation of the business known as Bret's Independent. On or about December 2011, prior to removal of the Equipment from the premises, Hartman on behalf of Bret's Inc., a new Washington corporation, purchased the equipment from First Sound Bank. (CP 695)

D. Dissolution and Cease of Business of the LLC

It is undisputed the Secretary of State of Washington administratively dissolved the LLC on June 2, 2008 and such dissolution

was not the action of Hartman. (CP 712) The payment of the renewal for 2008 would have been due in February before Holroyd moved to California. Since he was the signer of the 2007 annual report in the prior year, he was also within his rights and obligations as co-manager to renew the entity in 2008. He did not do so in 2008, 2009, 2010 and 2011. Neither did Hartman renew the LLC license during those years.

IV. ARGUMENT

A. Standard of Review

The standard on review of a trial court's entry of summary judgment is de novo review. The Court of Appeals performs the same inquiry as the trial court in order to "ascertain whether the trial court correctly granted a motion for summary judgment. In reviewing a summary judgment motion, [the Court] can only look to the evidence in the record before the trial court at the time the motion was made." *Hines v. Data Line Sys., Inc.*, 114 Wn.2d 127, 148, 787 P.2d 8, 19 (1990).

Summary judgment should be granted if the evidence, viewed in the light most favorable to the non-moving party, shows there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. *Id.* When the moving party demonstrates that there is no dispute as to any issue of material fact, then the burden shifts to the nonmoving party. If the nonmoving party fails to demonstrate the existence

of an essential element of a claim, an element on which that party would have the burden at trial, then summary judgment should be granted. *Thomas v. Bremer*, 88 Wn. App. 728, 735, 946 P.2d 800 (1997). “[A] complete failure of proof concerning an essential element of the nonmoving party’s case necessarily renders all other facts immaterial.” *Id.* (internal citations omitted).

B. Holroyd Agreed to Summary Judgment Dismissing the Derivative Action.

On January 22, 2014, the trial court considered Hartman’s initial Motion for Summary Judgment Dismissal of Holroyd’s Cross Claims including the derivative action that Holroyd ostensibly brought on behalf of the LLC. The trial court granted the motion as to the derivative action and it is this 2014 order that Appellant appeals. (CP 848-851; Appt’s Br. at 12-13; 15-19.) The record on review of the trial court’s 2014 order entering summary judgment dismissing the derivative action supports dismissal of the derivative action with prejudice. (CP 1342-1346; CP 1143; CP 848-851; *see also* CP 1147-1290.)

In Philip Holroyd’s Response to Hartman’s Motion for Summary Judgment Dismissal of Philip Holroyd’s Cross Claims, *Holroyd agreed to dismissal of the derivative action.* (CP 1143) Holroyd intentionally did so

in order to avoid the risks of continuing with the claims and reviving potential creditor claims. (Id.)

As reinstatement ... relates back to the date of dissolution, it would also revivify creditor claims.... As such, Mr. Holroyd agrees to dismissal of the derivative claim.

(Id.) Thus, the concession was one of tactical, strategic choice. And, it was a choice made in the course of a motion for summary judgment in which claims are determined finally (i.e., with prejudice) rather in the context of a motion for voluntary dismissal pursuant to Civil Rule 41 (i.e., without prejudice). (*See id.*) Regardless of the accuracy of Holroyd's assessment of the risks viewed in hindsight, Holroyd cannot now argue that the summary judgment to which he agreed that resulted in the dismissal of the derivative action with prejudice should be overturned.

Given that Holroyd agreed to entry of summary judgment that effected the dismissal of the derivative action, Hartman is entitled to attorney fees for responding to Holroyd's appeal. RAP 18.1 and RAP 18.9. An appeal is frivolous if there is no debatable issue upon which reasonable minds might differ, and it is so totally devoid of merit that there is no possibility of reversal. *See Streater v. White*, 26 Wn. App. 430, 435, 613 P.2d 187, *rev. denied*, 94 Wn.2d 1014 (1980); *Millers Casualty Ins. Co. v. Briggs*, 100 Wn.2d 9, 665 P.2d 887 (1983). The appeal of the derivative action is frivolous because Holroyd conceded, for strategic reasons, to entry

of the summary judgment dismissal with prejudice in his pleadings that were before the trial court in 2014 and he now seeks reversal of his own concession. (CP 1143) The appeal of this issue is therefore devoid of merit.

Even if such claims could be reinstated, the trial court did not err in dismissing the claims because the derivative action brought by Holroyd necessarily fails when Holroyd failed to properly plead the derivative action on behalf of the LLC. RCW 25.15.380 (2012) mandates that “the complaint shall set forth with particularity,” the efforts, if any, of the party to secure initiation of the action by a manager or member or the reason for not making such effort. Holroyd’s complaint does not meet this requirement. (CP 1342-1346) Moreover, Holroyd did not address this deficiency in the responsive pleading that he submitted to the trial court. (CP 1133-1146) Thus, the record as to the derivative action in this case supports dismissal of the derivative action with prejudice. Therefore, Holroyd’s derivative action claim was properly dismissed and this Court should affirm the trial court’s order.

C. There is No Enforceable Written or Oral Contract Terms Supporting Holroyd’s Claim for Breach of Contract.

1. There is No Contract Between the Parties.

Summary judgment under CR 56(c) is appropriate where, viewing all admissible facts and reasonable inferences most favorably to the

nonmoving party, the court finds no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. *Briggs. V. Nova Servs.*, 166 Wn.2d 794, 801, 213 P.3d 910 (2009); *Qwest Corp. v. City of Bellevue*, 161 Wn.2d 353, 358, 166 P.3d 667 (2007) (citing *Hubbard v. Spokane County*, 146 Wn.2d 699, 707, 50 P.3d 602 (2002)). A genuine issue of material fact exists where “reasonable minds could differ on the facts controlling the outcome of the litigation.” *Ranger Ins. Co. v. Pierce County*, 164 Wn.2d 545, 552, 192 P.3d 886 (2008).

The evidence that was before the trial court and that constitutes the record before this Court, viewed in the light most favorable to Holroyd, is that there was no written Operating Agreement. (CP 234-239) (Holroyd acknowledges in his own declaration testimony that “there was no operating agreement of for the Business” and never suggests otherwise in the record). Holroyd attested in his 2014 declaration that,

We did not enter into a written operating agreement for the Business. The “operation Agreement” set forth at Exhibit 2 of Hartman’s [2014] Motion for Summary Judgment is a forgery. The signature alleged to be mine is not mine and the address given for me is an address I did not acquire or live at until 1999, 3 years after the purported date of signature of the “Operation Agreement.

(CP 641)¹ (Holroyd’s 2014 Declaration was also before the trial court in the

¹ In his opening appellate brief, Holroyd cites CP 120-121 which references the Operating Agreement he claims was forged. (CP 641.)

2015 summary judgment record as Exhibit 6 to Hartman's motion) (CP 640-645.) As the record shows, for the purposes of the 2015 Motion for Summary Judgment, Hartman acknowledges the lack of written operating agreement as an undisputed fact. (CP 134.)

While this Court reviews the grant of summary judgment *de novo*, the nonmoving party cannot create a question on which reasonable minds could differ by contradicting his own evidence in the record and altering his position about whether there was a written operating agreement. The record shows that Holroyd testified in a declaration that "We did not enter into a written operating agreement for the Business." Hartman, for the purposes of the motion, agreed. Holroyd now claims the parties did have a written operating agreement. In essence, Holroyd seeks to retract his sworn statement.² Such an act does not create a genuine issue of material fact. Therefore, there is no agreed written contract against which this Court can consider Holroyd's claim that Hartman breached a contract.

Without a written contract with the terms on which Holroyd relies as the bases for his assignments of error for this Court's review, then Hartman could not have breached those terms and Holroyd's claim

² It appears that many of Holroyd's citations to the Clerk's Papers are inaccurate and, therefore, challenging for Respondent to discuss in his argument. *See* RAP 10.3(a)(6) (the brief should contain "The argument in support of the issues presented for review, together with citations to legal authority and references to relevant parts of the record.")

necessarily fails. In addition, Holroyd does not here re-assert his claim of oral contract presented to the trial court.³ Therefore, summary judgment as to Holroyd's breach of contract claim should be affirmed.

2. Hartman did not Breach the Terms of the Written Operating Agreement.

Holroyd asserts in his opening brief to this Court, for the first time in this case, that an enforceable written agreement between the parties exists. Even if this Court now views the record in the light most favorable to Holroyd and determines that the written "Operating Agreement" governs the party's relationship, the terms of the "Operating Agreement" do not require equal distributions. Rather, the Operating Agreement only requires that distributions be allocated to each partner according to their percentage ownership. (CP 120 ("...may make distributions annually or more frequently if there is excess cash on hand after providing for appropriate expenses and liabilities. Such interim distributions are allocated to each Partner according to the percentage of Partnership. (50/50%)".))

³ In response to the 2015 motion for summary judgment, Holroyd asserted that an oral contract existed whereby he would take care of his mother while Hartman managed the business. (CP 218) Oral agreements for a limited liability company must satisfy the requirements of Statute of Frauds and are not permitted by RCW 25.15.005(5) (2014) which defines an operating agreement to only refer to a written agreement. *Noble v. A&R Envtl. Servs., LLC*, 140 Wn. App. 29, 164 P3d 519 (2007). There are no terms of an oral contract in the record of this case, and a claim based on oral contract would fail as time-barred. RCW 4.16.080.

Holroyd appears to incorrectly assume that distributions made “according to the percentage of Partnership. (50/50%),” means that the total distribution amount each partner *receives* each year should be equal amounts. This is an inaccurate statement of tax laws and accounting principles. As reflected in the Schedules K-1 submitted to the record by Holroyd, from 2008 through 2011 both Hartman and Holroyd were attributed 50% each of profit, loss, and capital (Section J) and equal amounts of “ordinary income” (Line 1 of Part III). Line 1 reflects the partner’s share of the ordinary income (loss) from trade or the business activities of the partnership. (IRS Form 1065 (Instructions for Schedule K-1).) Notably, Line 19 of Part III, titled Distributions, reflects the subcategory of Section L that is titled “Withdrawals & distributions.” Review of that entire Section L demonstrates that these amounts were withdrawals or “draws” rather than distributions of profits. (CP 294-297; CP 325-328) Yet Holroyd agreed to allow Hartman to take draws when he decided not to. (CP 1071 and 1134.)

If Holroyd disputed the amounts on the Schedules K-1 or if Holroyd intended to claim damages for failure to make distributions according each member’s percentage of partnership, then he should have submitted evidence in support of these claims from the accountant who drafted the Schedules K-1. That evidence, however, is not in the record.

There is no admissible evidence in the record that there was any failure to make distributions to Holroyd within the terms of the written agreement. Instead, distributions were attributed annually according to the agreement, and that is “according to the percentage of Partnership. (50/50%).”⁴ (See CP 294-297; CP 325-328.) There is no evidence in the record contradicting that these distributions were not attributed “according to the percentage of Partnership. (50/50%).” Holroyd’s incorrect assumption, on which he bases his claims, does not create an issue of fact or law that would require reversal of the trial court’s dismissal on summary judgment. Furthermore, Hartman did not breach the terms of the written contract and summary judgment dismissing the claim for breach of contract is warranted.

D. Holroyd Failed to Produce Evidence of Damages and his Individual Claims Cannot Survive.

An action cannot be sustained when a party fails to produce any evidence supporting an essential element that is to be proven by that party at trial. See *Thomas*, 88 Wn. App. at 735. Both of Holroyd’s individual claims to which he assigns error on appeal, his claims for breach of contract and breach of fiduciary duty, were properly dismissed on summary

⁴ See also, e.g. RCW 25.05.150 (partnership ownership and distributions) and RCW 25.15.200 and 25.15.205 (2012) (limited liability member ownership and distributions).

judgment because Holroyd produced no evidence supporting the common essential element of proof of damages. (CP 216-576.)

A breach of contract is actionable only when the plaintiff can prove that a contract exists, the contract imposes a duty, that duty is breached, and the breach proximately causes damages to the one owed the duty. *Nw. Indep. Forest Mfrs. v. Dep't of Labor & Indus.*, 78 Wn. App. 707, 712, 899 P.2d 6, 9 (1995). The essential elements to establish liability for breach of fiduciary duty are duty, breach, causation, and damages. 29 David K. DeWolf, *Washington Practice, Washington Elements of an Action: Breach of Fiduciary Duties*, § 12:1, at 347–48 (2012); *see also* 6 Washington Practice: Wa. Pattern Jury Instructions: Civil 107.10 (6th ed. Supp. 2013).

As a matter of law, Holroyd cannot prove damages as to either claim. First, as set forth above, Holroyd was attributed distributions pursuant to the statutory and, if applicable, contractual requirements. (*See supra* pp. 10-13.) Furthermore, withdrawals (or draws) from an LLC or partnership do not take away from the entity's profit. 26 U.S.C. §704(b). Therefore, according to the undisputed Schedules K-1, Holroyd has not suffered due to "unequal" draws as he claims.

Second, while Hartman received guaranteed payments between 2008 to 2011 and Holroyd did not, these circumstances arose due to the mandates of the Internal Revenue Code. "Guaranteed payments" are

payments made to a partner for services performed by the partner on behalf of the company and made without regard to the income of the partnership.⁵ 26 U.S.C. §707(c). Guaranteed payments are the functional equivalent of a salary. These payments factor into the performance of the entity and are treated as an expense and pass along certain tax burdens to the individual rather than the business. (Id.) This accounting is mandated because the IRS assumes that an owner who works in an entity is being paid. (Id.) It is not disputed that Hartman performed services for the partnership between 2008 and 2011. And, there is no evidence in the record establishing why Hartman should not have been provided Guaranteed Payments for those services or disputing the amount that Hartman should have been compensated for his services. (See CP 241-576.) Therefore, Holroyd had not suffered damages as a result of Holroyd receiving guaranteed payments.

Third, Holroyd has no evidence of damages arising from the alleged transfer of assets or claim of conversion. Although direct recovery to shareholders may be allowed under exceptional circumstances, resulting in a “forced distribution of corporate assets to shareholders,” a judgment in

⁵ Self-employed health insurance premium payments are part of guaranteed payments. “Premiums for health insurance paid by a partnership on behalf of a partner, for services as a partner, are treated as guaranteed payments. The partnership can deduct the payments as a business expense, and the partner must include them in gross income.” (IRS Pub. 541 at https://www.irs.gov/publications/p541/ar02.html#en_US_201601_publink1000104261 (last visited Jul. 23, 2016).)

favor of the individual stockholders is improper where third party rights of higher priority are involved. *La Hue v. Keystone Inv. Co.*, 6 Wn. App. 765, 496 P.2d 343, 1972 (1972). The assets Holroyd alleges were improperly transferred were either assets that the business had leased or assets that were in foreclosure that Hartman then purchased. (CP 695.)

The evidence in the record shows that the equipment primarily used for the business's operations was leased from Puget Sound Leasing. (CP 686-693.) Section 11 of the equipment lease provides that "[t]he Equipment is, and shall remain, the property of the Lessor (Puget Sound Leasing) and Lessee (Bret's Independent, LLC) shall have no right, title or interest therein or thereto except as expressly set forth in this Lease." (Id.) Section 20 of the lease provides that the Lessor may repossess the equipment at any time without notice to the lessee to repossess the equipment. (Id.)

The remaining equipment for the operations of the business were fixtures located on the leased premises, and were rendered the Landlord's property under the terms of the Lease signed by both Holroyd and Hartman in 2006. Section 8.1 states, "All fixtures ... and other leasehold improvements, either now located on or hereafter placed on the Premises, are part of this Lease and shall be considered a part of the Premises. Said term shall include all items of personal property that are or become attached to the Premises." Section 4 reads, "Lessee shall not remove the

Equipment from the Premises.” (CP 657) The Lease expired on May 9, 2011. (CP 655.) Upon termination of the Lease, Section 21 dictates that the Lessee surrender the premises, which according to Section. 8.1 includes surrender of all fixtures. (CP 659-660.) The LLC’s lease of the premises expired in May 2011 and the equipment that was located on the premises became the legal property of the landlord. (See CP 655-677.) Then, in September 2011 the landlord lost its control and possession of the premises to a receiver appointed by a bankruptcy court and the landlord listed the property for sale. (CP 681-684.)

Moreover, general and conclusory statements of damages are insufficient to overcome the burden of a nonmoving party in a summary judgment proceeding, *Baldwin v. Silver*, 147 Wn. App. 531 (2008), and, the party opposing a motion for summary judgment “may not rely on speculation, argumentative assertions that unresolved factual issues remain, or in having its affidavits considered at face value...the nonmoving party must set forth specific facts that sufficiently rebut the moving party’s contentions and disclose that a genuine issue as to a material fact exists.” *Seven Gables Corp. v. MGM/UA Entm’t Co.*, 106 Wn.2d 1, 13, 721 P.2d 1 (1986).

In the record before the trial court on summary judgment, Holroyd failed to produce specific facts or evidence of damages resulting from his

causes of action against Hartman that would be sufficient to create a material question of fact. (CP 241-576.) In fact, the Schedules K-1 reflect that Holroyd's capital account⁶ of the business was negative when he departed from the business in 2008. Hartman submitted ample specific evidence which Holroyd did not and could not refute to withstand a summary judgment motion that both of their capital accounts were also negative in 2011 regardless of whether there were any assets which belong to Bret's Independent at the time business ceased in October 2011. (CP 294-297; CP 325-328.)

Furthermore, at the time the trial court heard the 2015 motion for summary judgment, there were no viable creditor claims for which Holroyd could suffer damages. Holroyd has not submitted evidence of any other specific damages other than conclusory statements. Therefore, without any specific evidence of damages, Holroyd's claims were properly dismissed on summary judgment and this Court should affirm.

⁶ Each partner's equity in the partnership is reflected in a capital account. It is important to distinguish between tax capital accounts, IRC section 704(b) book capital accounts, and book capital accounts which are based on generally accepted accounting principles (GAAP). Generally, book capital accounts reflect the FMV of assets at the time of contribution and distribution. The book capital accounts thus accurately show the partners' economic interests in the partnership and track their "business deal".

E. Holroyd Lacks Standing to Claim Breach of Fiduciary Duty.

The doctrine of standing prevents “a plaintiff from asserting another’s legal rights.” *Trinity Universal Ins. Co. of Kan. v. Ohio Cas. Ins. Co.*, 176 Wn. App. 185, 199, 312 P.3d 976 (2013), *rev. denied*, 179 Wn.2d 1010 (2014). The damages that Holroyd seek in his claim for breach of fiduciary duty arise out of allegations that Hartman’s actions harmed the worth of the LLC’s assets and, in his view, resulted in Holroyd receiving less than his share (whether due to guaranteed payments, creditor claims in the winding up process, or conversion of the LLC’s assets). The injury Holroyd complains of is misappropriation of the business’s funds and assets. Even if Hartman may owe fiduciary duties to Holroyd as a partner or LLC member, Holroyd, as an individual, is not the proper party to bring the claims he asserts in cross-complaint and in his assignments of error.⁷

Limited partnership statutes and corporate shareholder case law agree that direct and derivative suits ought to be distinguished. RCW 25.10.701(2); *see also* RCW 25.10.706-721; *Sabey v. Howard Johnson & Co.*, 101 Wn. App. 575, 584-85, 5 P.3d 730 (2000) (discussing when

⁷ Hartman acknowledges that the parties have thus far been unclear on the form of entity given that the LLC was dissolved in 2008. They have proceeded in court as if the LLC continued. However, after June 2, 2008, there was no formal legal entity conducting the business of Bret’s Independent, LLC, and it is more appropriate to state that the on-going business occurred so that either Hartman was conducting the business as a sole proprietor or, viewed in a light more favorable to Holroyd, the parties were engaged in a partnership. Ultimately, the legal effect of the issues before this case generally reach the same result whether an LLC or a partnership.

corporate shareholders may make direct, rather than derivative claims). The former Washington Limited Liability Company Act likewise distinguished between such suits. RCW 25.15.370-.385 (2012). The reasons for distinguishing between direct and derivative suits and the right to bring claims directly or derivatively include benefits that can only be achieved through a derivative suit, namely: a derivative suit (a) ensures that when a business entity suffers injury, the entity is made whole and all the equity owners share in this result, and (b) prevents equity holders from recovering in a manner upsetting the creditor priority scheme when the business entity has become insolvent. *See Moore v. Los Lugos Gold Mines*, 172 Wn. 570, 598, 21 P.2d 253 (1933); *LaHue v. Keyston Inv. Co.*, 6 Wn. App. 765, 780-81, 496 P.2d 343 (1972).

These principles of standing govern when a partner, member, or owner can bring claims against another individual partner, member, or owner. They require that the injury complained of be one “that is not solely the result of an injury suffered or threatened to be suffered by the limited partnership,” i.e., the entity. RCW 25.10.701(2) (limited partnership test for when direct suit may be brought); *Sabey*, 101 Wn. App. at 584-85 (outlining the test for corporate shareholders).

Moreover, RCW 25.15.235(2) (2012), which addresses Limitations on Distributions, provides that “(a) member who receives a distribution in

violation of subsection (1) of this section, and who knew at the time of the distribution that the distribution violated subsection (1) of this section, shall be *liable to a limited liability company* for the amount of the distribution.” (Emphasis added.) RCW 25.15.295(2) (2012), which addresses the duties of winding up states that it is the “limited liability company,” that engages in the activities of winding up.

Holroyd claims that Hartman breached his fiduciary duty and caused injury as a manager of the LLC. Holroyd specifically states in his cross-complaint that Hartman failed “to preserve said assets, and/or taking other steps to convert the assets of Bret’s Independent, LLC to his new company, Bret’s Inc.” (CP 1344.) In his appeal, Holroyd complains of injury arising from, according to Holroyd, the making of guaranteed “payments [that] that reduced the profits of the company and minimized distributions available for Holroyd,” (Appt’s Br. at p. 23), “failing to wind up the company pursuant to the provisions of RCW 25.15.300(2),”⁸ (id.), and by “transferr[ing] the company assets...denied Holroyd of his right of ownership in the company assets,” (id. at p. 24). All of these injuries are to the entity, and Holroyd’s claims of injury are derivative to the entity’s

⁸ Even if the failure to wind up properly “exposed Holroyd to liability,” that risk had evaporated by the time of the 2015 motion for summary judgment and Holroyd has failed to produce evidence of injury and damages.

injury. Therefore, Holroyd has not alleged the type of personal injury sufficient to confer standing for a direct suit and he is not the party entitled to the “‘fruits of the action’; the LLC is.” *Nw. Indep. Forest Mfrs.*, 78 Wn. App. at 716 (quoting 3A Lewis H. Orland & Karl B. Tegland, *Washington Practice; Rules Practice*, at 420 (4th ed. 1992)).

Holroyd’s derivative action was properly dismissed with prejudice with Holroyd’s agreement on January 22, 2014. Holroyd does not have standing individually to bring his remaining claims which are derivative claims. Therefore, this Court should affirm the grant of summary judgment as to Holroyd’s claims for breach of fiduciary duty.

F. Holroyd has not Alleged Any Facts Which Could Establish a Breach of Fiduciary Duty by Hartman.

Even if Holroyd has standing to bring his claim for breach of fiduciary duty, each of the bases for his claim fail as a matter of law and for lack of evidence.

As a matter of law, Hartman did not breach any fiduciary duty by authorizing guaranteed payments to himself. There was no contract term prohibiting this action. (*See supra*, pp. 8-13.) As a manager and the only owner working for and providing services to the LLC from the time Hartman left in 2008 through 2011, RCW 25.15.150(2)(a) (2012), which vests managers with decision-making powers, permits this decision.

The facts of this case as presented by Holroyd are similar to the facts presented in *Bishop of Victoria Corp. Sole v. Corporate Bus. Park, LLC*, 138 Wn. App. 443, 158 P.3d 1183 (2007). In *Bishop*, Joseph Finley and the Bishop of Victoria Corporation (“BV”) formed a limited liability company for the purpose of purchasing a significant piece of real property with the intent to sell the property for a substantial profit. *Bishop*, 138 Wn. App. at 447. Under the terms of the LLC’s operating agreement, Finley and BV were both managers. *Id.*, at 448. The LLC purchased real property and obtained a mortgage on the property. When the property did not immediately sell, the LLC refinanced, executing a promissory note secured by the property. For a time, the LLC was able to make payments, but eventually reserves ran out and only one member, BV, started making monthly payments to the mortgage holder on behalf of the LLC. BV later determined that it was financially detrimental to continue to be solely responsible to pay for the mortgage payments while the property could not be sold as the parties expected. BV stopped making any further payments for the mortgage. BV’s failure to make further payments caused the interest rate on the loan to rise and a default ensued. The lender sued the LLC, Finley and BV for foreclosure and money judgment in the amount of the loan plus interests. BV thereafter raised money through a separate entity (Fisgard) to purchase the judgment from the lender without the consent and participation

of Finley. *Id.*, 138 Wn. App. 443.

Finley in turn brought an action against BV for breach of contract and breach of fiduciary duty by missing the mortgage payments and causing “the business to fail”, by raising money through another entity to offer a creditor of the LLC which lead to the release of BV only (not Finley) from its obligation to the judgment, and finding a buyer for the purchase of foreclosed asset which used to belong to the LLC. Finley also brought a separate suit to prevent the sale of the foreclosed asset by BV’s affiliated entity which was denied at the trial court level. *Id.*

“A partner does not violate a duty or obligation... merely because of the partner’s conduct furthers the partner’s own interest.” *Bishop*, 138 Wn. App. at 458 (quoting RCW 25.05.165(5)). It is also not a breach of fiduciary duty to fail to disclose facts that are neither significant nor material. *Id.*, at 459. The *Bishop* Court explained that even when one member fails to inform another of its actions to take protective action when a business is failing, (i.e., raise funds through another newly formed entity in order to negotiate with the lender to purchase a judgment from the creditor in detriment of the failing LLC and other owner), there is no breach of fiduciary duty for such failure when the information is not material. “A material nondisclosed fact in the context of a general partner’s fiduciary duty is one that ‘might be expected to have induced action or forbearance

by the other partners.”” *Id.*, at 459 (quoting *Diamond Parking, Inc. v. Frontier Bld. Ltd. P’ship*, 72 Wn. App. 314, 320, 864 P.2d 954 (1993)). The *Bishop* Court notes that a failure to disclose is insufficient by itself to avoid summary judgment when the disclosure would not have been material, or the failure to disclose is not sufficiently adverse to the complaining party’s interests.

Holroyd claims breach of fiduciary duty because Hartman made unauthorized guaranteed payments, made disproportionate distributions and failed to properly wind up the company for breach. (Appt’s Br. at pp. 22-23.) Holroyd’s claims are based on the premise that Hartman had a duty to contribute his efforts and assets indefinitely into the failing business, and that Hartman may not purchase the assets or have business dealings with parties (such as the Landlord and the Equipment Lessor) to minimize Hartman’s own loss and reduce the personal liabilities from his personal guarantees incurred as a part of the LLC owned with Holroyd.

As a matter of law, there was no breach of fiduciary duty arising from a failure to disclose to Holroyd that guaranteed payments were made to Hartman. And the evidence in the record suggests that Holroyd agreed to Hartman performing services for the company for which the guaranteed

payments were incurred.⁹ In his declaration Holroyd states, "This approach continued when the Business experienced a downturn in revenues after the economic downturn in 2007. In an attempt to shore it up financially, at the end of 2007 I stopped taking financial draws to free up cash for the needs of the Business. Rather than the money being used to pay me, it was used to pay suppliers and to continue to allow Mr. Hartman to receive draws. I also discussed with Mr. Hartman the need to cut back and that it might make sense to bring in a manager. However, we finally agreed that he would continue to run the day-to-day operations." (CP 1071.) In their summary judgment response, Holroyd argued, "With the economic downturn in 2007, the Business suffered a decrease in revenues. Mr. Holroyd agreed to forego draws from the Business, as of the end of 2007, in order to allow those funds to go towards the other cash needs of the Business, including the draws being taken by Mr. Hartman." (CP 1134.) Holroyd cannot now complain of Hartman running the business and the guaranteed payments that arise as a result of day-to-day operations and the draws being taken by Mr. Hartman when in the declaration and briefing he admits he agreed to both.

Therefore, as held by the *Bishop* Court, any information not disclosed by Hartman to Holroyd regarding Hartman's efforts to reduce his

⁹ Holroyd argues but did not assign error to the trial court's dismissal of any separate claim of conversion.

own personal liability is not “material” and such non-disclosure could not constitute a breach of fiduciary duty. The trial court properly dismissed the claim for breach of fiduciary duty and this Court should affirm.

Moreover, Holroyd makes minimal citation to the record in support of his appeal of the trial court’s entry of summary judgment dismissing his breach of fiduciary claim. In support of his related assignments of error, Holroyd makes minimal reference to potentially relevant portions of the record in his statement of facts and none in his argument section.¹⁰ (Appt’s Br. at pp. 7-12, 21-26.) On review, it is not the appellate court’s function “to comb the record with a view toward constructing arguments for counsel.” *In re Estate of Lint*, 135 Wn.2d 518, 532, 957 P.2d 755 (1998) (RAP 10.3 is not simply a nicety but an obligation for the parties to demonstrate why the evidence does or does not support their position).

G. Hartman Requests Costs and Attorney Fees on Appeal and for his Defense of Holroyd’s Cross Claims.

Hartman requests an award of attorneys’ fees and costs associated with the defense of the cross claims by Holroyd against him. RAP 18.1; RCW 4.84.010.

Hartman also requests an award of attorney fees on appeal for the derivative action because Holroyd’s appeal of that issue is frivolous when

¹⁰ See footnote 2, *supra*.

Holroyd made a strategic decision to agree to dismissal of the derivative action on summary judgment. RAP 18.9; *see Resp's Br., supra*, pp. 5-8.

Holroyd should not be awarded attorney fees because his request is based on the derivative action to which he agreed be dismissed. (*See CP 1143.*)

V. CONCLUSION

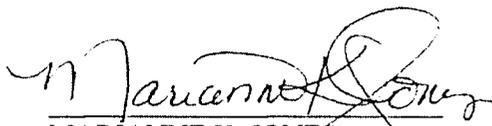
Holroyd's claims for derivative action and those claims brought personally against Hartman for breach of fiduciary duty and breach of contract were properly dismissed on summary judgment. Hartman requests that this Court affirm the trial court's orders dismissing all claims.

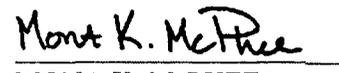
RESPECTFULLY SUBMITTED this 27th day of July, 2016.

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