

NORTH CAROLINA
CUMBERLAND COUNTY

IN THE GENERAL COURT OF JUSTICE
SUPERIOR COURT DIVISION
06 CVS 6091

MITCHELL, BREWER,
RICHARDSON, ADAMS, BURGE,
& BOUGHMAN, PLLC; GLENN B.
ADAMS, HAROLD L. BOUGHMAN, JR.,
AND VICKIE L. BURGE,
Plaintiffs,
v.
COY E. BREWER, JR., RONNIE A.
MITCHELL, WILLIAM O. RICHARDSON
AND CHARLES BRITTAIN,
Defendants.

PLAINTIFFS' RESPONSE TO
DEFENDANTS' SECOND MOTION
FOR SUMMARY JUDGMENT

Background

The Plaintiffs and Defendants in this case have had cross motions for summary judgment pending since January 9, 2008. Shortly after the Court of Appeals decided Crouse v. Mineo, 658 S.E.2d 33 (2008), Plaintiffs brought Crouse to this Court's attention through a Suggestion of Subsequently Decided Authority filed on June 2, 2008. Plaintiffs did so because they believe the case is dispositive of significant issues involved in the pending cross motions. However, that vehicle precluded Plaintiffs from presenting to this Court their view of Crouse and its impact on the pending motions. Plaintiffs also believed they were constrained from making a further motion for summary judgment by the Revised Consent Order Modifying Case Management Order entered by the Court on October 19, 2007. Given the delay in ruling on the pending motions, Plaintiffs on August 4, 2008, moved to supplement their complaint. They did so to reflect the Defendants' continued failure to discharge their fiduciary duties to the Firm and to the Plaintiffs. Now, however, Defendants have filed a new motion for summary judgment based entirely on Crouse. Plaintiffs respond to that motion herein.

In the briefing which proceeded this new motion, the parties have agreed that they practiced together under North Carolina's Limited Liability Company Act ("the Act"), and that they did so without a written operating agreement. The parties have agreed that they ceased practicing law with each other on or about July 1, 2005. The parties also appear to agree that the separation of their practices resulted in either a dissolution or a withdrawal, and that these are mutually exclusive outcomes under the Act.

Plaintiffs' position in this case is that no statutory "withdrawal" occurred, a result mandated by the explicit terms of the Act. Under the Act, the terms "withdrawal" and "dissolution" are not given their "plain meaning" but rather must be given their statutory meaning. When one applies the provisions of the Act, there was neither a statutory dissolution nor a statutory dissolution under the Act. Rather, the parties have ceased practicing with each other and are at an impasse. Under these conditions, the Act provides for a judicial dissolution.

Defendants, on the other hand, have urged this Court to adopt the concept of a "de facto" withdrawal, which they say is consistent with the "plain meaning" of the term "withdrawal." They say that under the "plain meaning" of "withdrawal", Plaintiffs are estopped to deny that a withdrawal has occurred.

On August 15, 2008, Defendants filed a second Motion for Summary Judgment. In their Motion, Defendants argue, based solely on the Court of Appeals' recent decision in Crouse, that: (1) The Firm has no standing to bring the action on its own behalf; (2) the individual Plaintiffs have no standing to bring this action as a derivative action; and (3) Defendants are not personally liable for any breach of their duties as managers of the Firm. Based on this interpretation of Crouse, Defendants believe they can take money from the Firm that rightfully belongs to the individual Plaintiffs (as is alleged in the Complaint), and neither the Firm nor the individual Plaintiffs can recover the misappropriated funds from the Defendants. Obviously this is unjust and unreasonable and, for the reasons set forth below, this Court must deny the Defendants' motion for summary judgment.

Argument

I. The Crouse Decision. Mr. Crouse and Mr. Mineo practiced law together in a North Carolina LLC known as Mineo and Crouse (“the Entity”). Crouse, at p.35. Mineo and Crouse did not have a written operating agreement. Id. at 36. Mr. Crouse filed claims for himself and the Entity alleging breach of fiduciary duty, an accounting, quantum meruit, and unfair trade practices under Chapter 75. Id. at 35. In substance, plaintiff alleged that defendant had misappropriated funds belonging to the plaintiff or to the Entity. Defendant filed a counterclaim for an accounting and also asserted a quantum meruit claim. Id. at 35. He later filed a motion to dismiss plaintiff’s claims because plaintiff lacked standing to prosecute the action on behalf of the Entity; plaintiff had no valid individual claims, the Entity had not authorized the action in its own name, and Chapter 75 was inapplicable. Id. at 35. In response, plaintiff moved the trial court to dissolve the Entity and appoint him as the trustee to wind up its affairs. Id. at 35-36. The trial court denied the plaintiff’s motion and granted the defendant’s motion to dismiss all of plaintiff’s claims. Id. at 35.

In pertinent part, the Court of Appeals made four key decisions of importance to the outcome of the motions for summary judgment now pending before this Court. In doing so, the Court of Appeals pointed out that a limited liability company is a “statutory form of business organization” which mandates that courts apply the statutory provisions of the Act to resolve disputes. Id. at p. 36. The Court of Appeals recognized that the Act contains numerous default provisions which courts must apply if the parties do not have a written operating agreement which contractually alters the provisions of the Act. Id. at 36. The Court of Appeals then applied the Act strictly.

First, the Court of Appeals considered whether the plaintiff had standing to file a claim derivatively on behalf of the Entity. The defendant argued that the plaintiff ceased to be a member of the Entity when he sought dissolution, and therefore could not maintain the action derivatively. Id. at 38. Looking strictly at the provisions of the Act, and relying on the

interpretation of similar provisions in other states, the Court of Appeals held that filing the petition for dissolution did not cause the plaintiff to cease to be a member. Id. at 39.

Second, the Court of Appeals considered whether the plaintiff had filed any claim derivatively on behalf of the Entity. The Court of Appeals acknowledged that the plaintiff did not intend to do so. Id. at 40. However, the Court found that the allegations of the complaint satisfied the two requirements supporting a derivative claim. That is, the plaintiff explained what efforts he had undertaken to cause the Entity to take action, and why the Entity had refused to do so. Id. at 40-41. Thus the Court of Appeals held that the allegations supported a derivative claim. Id. at 41.

Third, the Court of Appeals considered whether the plaintiff could maintain individual claims for quantum meruit and for Chapter 75 violations. The Court held that the plaintiff could maintain an individual claim for quantum meruit because that was a claim personal to him. Id. at 41-42. The Court held that the Chapter 75 claim arose out of the parties' relationship through the Entity and thus was not a proper individual claim. Id. at 42.

Finally, the Court of Appeals considered the motion to dissolve and to have the plaintiff appointed to wind up the affairs of the Entity pursuant to the provisions of the statute permitting dissolution under the Act. Id. at 42. The Court determined that although the trial court had the authority to appoint someone to "wind up" the Entity's affairs, that authority was discretionary and the Court declined to override the trial court's discretion. Id. at 42-43.

Crouse compels this Court to apply the Act in the absence of a written operating agreement changing its provisions. Crouse compels this Court to apply the Act literally. Crouse recognizes that under the Act when members of a limited liability company reach an impasse, the court may declare a judicial dissolution.

II. Crouse's Application to the Instant Case. Defendants misread Crouse. Contrary to the Defendants' position, Crouse clearly mandates summary judgment in favor of the Plaintiffs with respect to the dissolution/withdrawal issue.

A. This is a derivative action on behalf of the Firm and includes individual claims.

Claim One of the Supplemental Amended Complaint is a specific request by the Firm for an accounting from the Defendants. Claim One specifically states that “[p]ursuant to N.C.G.S. § 57C-8-01 [the statute that authorizes derivative member actions], the individual Plaintiffs on behalf of the Firm are entitled to an accounting from the Defendants. “ (Supplemental Amended Complaint at. ¶31). By contrast, in Claim Two, the individual Plaintiffs make a separate request for an accounting to them individually for the liquidating distributions to which the individual Plaintiffs were entitled and which were misappropriated by the Defendants. In the prayer for relief both the Firm and the individual Plaintiffs ask the Court for a judgment awarding them all amounts they are due as a result of the Defendants breach of their duties to the Plaintiffs.

Apparently recognizing that the Firm’s claims are filed as derivative claims, Defendants assert that Plaintiffs could not file the suit as a derivative action because they were not members of the Firm at the time the claims were filed because they had “withdrawn” from the Firm. Whether the individual Plaintiffs are still members of the Firm is the issue before the Court in the previously filed cross motions for summary judgment. In this regard, Crouse supports Plaintiffs’ position that they never “withdrew” as members of the Firm pursuant to the Act.

As in the present case, Crouse involves the break-up of a law firm and the proper disposition of contingent fees due the entity. Prior to filing his suit, Mr. Crouse filed Articles of Dissolution with the North Carolina Secretary of State on behalf of the firm. See Exhibit A.¹ By making this filing, Mr. Crouse made a clear and unequivocal statement to the world that he no longer wished to practice law with Mr. Mineo. See N.C.G.S. § 57C-6-04(b) (a “limited liability company shall continue in existence following its dissolution . . . but shall carry out only that business appropriate to wind up and liquidate its business and affairs.”) Mr. Mineo argued that by filing the articles of dissolution Mr. Crouse ceased to be a member of the firm. The Court

¹ The Court of Appeals incorrectly describes the filing with the Secretary of State dated July 29, 2003 as a “petition for dissolution.” As Exhibit A indicates, the filing was in fact Articles of Dissolution.

disagreed, holding that the filing of articles of dissolution by Mr. Crouse did not terminate his membership in the firm.

The Court of Appeals reached its decision based on a strict and literalistic application of the Act. The Court began by reviewing N.C.G.S. § 57C-3-02, the provision which enumerates the events which terminate a member's membership status in a North Carolina limited liability company. The Court focused on N.C.G.S. § 57C-3-02(3)(d), the only enumerated event that could have possibly applied under the facts in Crouse. Significantly, the Court did not consider events not described in N.C.G.S. § 57C-3-02(3), such as the making of an unequivocal statement to the world that Mr. Crouse no longer wished to practice law with Mr. Mineo, as an alternative basis for membership termination.

In applying N.C.G.S. § 57C-3-02(3)(d), the court looked to the definitional section of the Act and applied the term "person" as defined in the Act. Applying the canon of construction that "where the language of the statute is clear, the court must give the statute its plain meaning," the Court rejected Mr. Mineo's argument that Mr. Crouse was not a member of the firm at the time he filed his suit because the filing of articles of dissolution for the Entity was not among the events triggering membership cessation under N.C.G.S. § 57C-3-02(3).

As Defendants have stated, the facts in Crouse are eerily similar to the facts in the instance case. In both cases a PLLC member made an unequivocal statement to others that the member no longer wished to practice law with the other members. The other member(s) asserted that by making that statement, the member had "withdrawn" from the PLLC, not just literally but in the technical, legal sense under the Act. In analyzing this case, this Court, like the Court of Appeals in Crouse, should apply strictly the express language N.C.G.S. § 57C-3-02 and conclude that a member's statement that "I'm out of here" does not terminate his membership interest in the LLC under the Act.

B. The Individual Plaintiffs have standing to bring this action and Defendants are personally liable for breach of their duties as managers of the Firm.

In their brief, Defendants claim that the Plaintiffs “lack standing to bring their individual claims” and that Crouse “makes clear that such claims run to the PLLC and not the individual members.” (Defendants’ Brief in Support of Motion for Summary Judgment at p. 7). Defendants are correct in that generally speaking a manager is not liable to a member for breach of his duties as a manager. See G.S. § 57C-3-30(c) (Manager liability determined solely on the provisions of Chapter 57C and the laws of our state). An exception to this general rule, however, exists in those “situations amounting to a winding up or dissolution of the [entity].” Keener Lumber Co., Inc. v. Perry, 149 N.C. App. 19, 31, 560 S.E.2d 817, 825 (2002) (quoting Whitley v. Carolina Clinic, Inc., 118 N.C. App. 523, 528, 455 S.E.2d 896, 900 (1995)).²

In this case, the individual Plaintiffs have alleged that the Firm dissolved *de facto* in July, 2005 and that in the aftermath of that dissolution the Defendants have misappropriated for themselves the liquidating distributions that should have been paid to the individual Plaintiffs. As a result of this misappropriation of the individual Plaintiffs’ liquidating distributions, Plaintiffs are informed and believe that the Firm is insolvent and cannot honor its obligation under G.S. § 57C-6-05 to pay to the individual Plaintiffs their share of the Firm’s final liquidating distributions. Because Plaintiffs have alleged that Defendants failed to pay Plaintiffs the liquidating distributions to which they are entitled, the Plaintiffs are treated as creditors of the Company under G.S. §57C-4-08. As a result, Plaintiffs may avail themselves of all the remedies available to limited liability company creditors in general, including the right to pursue the Defendants individually in cases like those alleged here in which the Defendants, in the context of winding up the affairs of the Company, took monies that should have been paid to the Plaintiffs.

² Plaintiffs are not aware of any case applying the rule from Keener Lumber, a corporation, to limited liability companies, but Plaintiffs are not aware of any reason why this common law doctrine does not apply to other forms of business entities, including limited liability companies.

In this case, Defendants have moved for summary judgment. Defendants bear the burden of producing evidence of the necessary certitude that the Firm did not dissolve (either *de facto* or otherwise) in July, 2006 and that the Defendants have not abused their position as insiders by misappropriating the liquidating distributions owing to the individual Plaintiffs. Coldfelter v. Bates, 44 N.C. App. 107, 260 S.E.2d 672 (1979) (rev. denied 299 N.C. 329, 265 S.E.2d 394 (1980)). Because Defendants have not filed supporting affidavits or otherwise presented admissible evidence proving that the Firm did not dissolve in July, 2005 and that the Defendants did not misappropriate the liquidating distributions owned the individual Plaintiffs, Defendants have failed to meet their burden of proof and their motion for summary judgment must be denied. See G.S. § 1-1A, Rule 56(e).

Individual Plaintiffs have been requesting an accounting from the Defendants since early 2006 so that they can confirm whether the Defendants have breached their fiduciary duties to the individual plaintiffs, but the Defendants have refused same. Moreover, this Court's scheduling order of September 11, 2007, prohibits the Plaintiffs from conducting their own discovery on issues related to the amounts misappropriated by the Defendants until the resolution of the motions for summary judgment already pending before this Court. Under these circumstances, this Court should deny Defendants' second Motion for Summary Judgment. At a minimum, this Court should at least defer ruling on the summary judgment motion until such time as the limitations on discovery are lifted and the Plaintiffs have had the opportunity to develop the evidence necessary to respond to the Defendants' Motion for Summary Judgment.

III. Crouse's Impact on the Motion to Supplement. Defendants oppose the Plaintiffs' Motion to Supplement the Supplemental Amended Complaint (the "Supplement"). Defendants claim that the Supplement fails to allege a proper claim, relying on Crouse. But the Supplement is not intended to set forth a new or independent claim. Rather, as contemplated by Rule 15(d), it sets forth "transactions or occurrences of events which have happened since the date of the pleading sought to be supplemented." Plaintiffs believe the Supplement is appropriate in light of

this Court's denial of their motion for a preliminary injunction, the delay in ruling on summary judgment, the stay of further discovery, and the Defendants' continuing receipt of disputed proceeds for which the Defendants refuse to account. As explained herein, Crouse supports the Plaintiffs' original claims which are strengthened by the additional facts set forth in the Supplement.

Conclusion

Defendants' reliance on Crouse is misplaced. To the contrary, Crouse supports the Plaintiffs' position that they have not "withdrawn" as members of the Firm under the Act. Moreover, because there is an impasse, this Court should deny the Defendants' Motion for Summary Judgment, follow the Act, and declare a judicial dissolution.

Respectfully submitted this the 22nd day of September, 2008.

EVERETT, GASKINS, HANCOCK & STEVENS, LLP

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State of North Carolina
Department of the Secretary of State

ARTICLES OF DISSOLUTION OF
LIMITED LIABILITY COMPANY

Pursuant to §57C-6-06 of the General Statutes of North Carolina, the undersigned limited liability company hereby submits the following Articles of Dissolution for the purpose of dissolving the limited liability company.

1. The name of the limited liability company is: Mineo & Crouse, PLLC
2. The dates of filing of its Articles of Organization and all amendments thereto are as follows:

JUNE 6, 2001

3. The reason for filing the Articles of Dissolution is : (please check one of the following items)

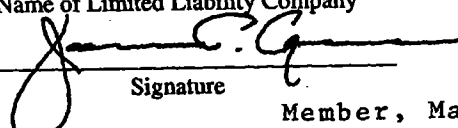
- The time specified in the articles of organization or the company's written operating agreement has occurred.
 The happening of an event specified in the company's articles of organization or their written operating agreement.
 The written consent of all members.
 The company no longer has any members.
 The entry of a decree of judicial dissolution under G.S. §57C-6-02.

4. The effective date (which shall be date certain) of the dissolution, as determined in accordance with N.C.G.S. §57C-6-01, is May 27, 2003.

5. Attach any other information determined by the managers filing these articles.

This the 29th day of July, 2003

Mineo & Crouse, PLLC
Name of Limited Liability Company


Signature

James T. Crouse, Partner and Registered Agent
Type or Print Name and Title

Member, Manager,

Notes:

1. Filing fee is \$30. This document must be filed with the Secretary of State.

CERTIFICATE OF SERVICE

I, E.D. Gaskins, Jr., do hereby certify that the foregoing has been duly served on all counsel of record, via email, and also electronically by submitting the document into the Court's electronic filing system to the following counsel of record who are registered to receive electronic service from the Court:

Charles F. Marshall
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Jim W. Phillips, Jr.
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This the 22nd day of September, 2008.

/s/ E.D. Gaskins, Jr.
E.D. Gaskins, Jr.