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COURT OF APPEALS
DIVISION TWO

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION TWO

CINDY LEVI, an individual, and KINGDOM INVESTORS, LLC, Plaintiffs/Appellees, v. SHENANDOAH "SHENA" KORN and DR. DAVID KORN, husband and wife, Defendants/Appellants.	2 CA-CV 2009-0087 DEPARTMENT B MEMORANDUM DECISION Not for Publication Rule 28, Rules of Civil Appellate Procedure

APPEAL FROM THE SUPERIOR COURT OF PINAL COUNTY

Cause No. CV200702162

Honorable Robert Carter Olson, Judge

AFFIRMED

Sheridan Larson, PLLC
By Michael J. Sheridan
Mesa
Attorneys for Plaintiffs/Appellees

Sherman & Howard, LLC
By Thomas M. Quigley
Phoenix
Attorneys for Defendants/Appellants

E C K E R S T R O M, Judge.

¶1 Appellants Shenandoah Korn and her husband, Dr. David Korn, appeal from a judgment entered after a bench trial in favor of appellee Cindy Levi, that dissolved the company they had operated together, Kingdom Investors, LLC. The Korns contend the trial court erred in ordering an accounting and adjustment of Kingdom's capital accounts in connection with the dissolution of the company. They also challenge the court's allocation of attorney fees and its grant of relief on Levi's claims for unjust enrichment and breach of the implied covenant of good faith and fair dealing. We affirm for the reasons set forth below.

Factual and Procedural Background

¶2 "When reviewing issues decided following a bench trial, we view the facts in the light most favorable to upholding the court's ruling." *Bennett v. Baxter Group, Inc.*, 223 Ariz. 414, ¶ 2, 224 P.3d 230, 233 (App. 2010). In 2006, Shenandoah Korn (hereinafter "Korn") was a realtor selling a multiple-unit residential property. She and Levi formed Kingdom Investors, a limited liability company (LLC), in May of that year. Under the terms of their operating agreement, Korn and Levi were to share equally in profits and losses of the company and were to contribute "cash, business, [and] expertise" to it. Levi subsequently purchased the multiple-unit property. As her initial contribution of capital to the company, Korn invested her $12,000 commission check from the sale of the property. Levi transferred the property to the company, and it was apparently the company's only asset.

¶3 In order to purchase the property, Levi took out two mortgages and a home equity loan. Given the unfavorable terms of the mortgages, however, the business

operated at a loss while the amount of debt increased. Levi repeatedly attempted to contact Korn in early 2007 to address these financial problems, either by refinancing, buying out Korn's interest, or selling the property. Korn largely refused to respond to Levi's correspondence and telephone calls. The two eventually discussed their problems around May 2007. Korn insisted that they hold the property for another three years. Although Levi maintained that the losses were unsustainable, Korn stated they did not concern her because the loans were in Levi's name and Levi was individually liable for them.

¶4 Indeed, pursuant to § 2.2 of the operating agreement, the company's members were not required to make additional capital contributions except for additional purchases and acquisitions. Moreover, § 9.5 of the agreement provided that only the assets of the company could be used to return a member's capital contribution. In the event those assets were insufficient after discharging the company's debts and liabilities, no member had recourse against the other to recover the cash or other property she had invested. Thus, as the trial court noted, under the terms of the operating agreement Korn was entitled to a portion of any gain but bore no risk beyond the loss of her initial capital contribution.

¶5 After Levi retained counsel and made additional attempts to resolve the situation, she filed a complaint against Korn in October 2007.[1] The complaint alleged claims of fraud, negligent misrepresentation, breach of fiduciary duty, breach of the covenant of good faith and fair dealing, unjust enrichment, and dissolution. Several of

[1]Levi later amended her complaint to add Kingdom Investors as a plaintiff.

these counts were based upon Levi's discoveries that Korn had previously been convicted of robbery, possessed only a provisional real estate license, and had formerly owned a piece of property that had been subject to foreclosure. Levi testified at the bench trial that, had she known this information earlier, she would not have entered into a business relationship with Korn.

¶6 The trial court ultimately found in favor of the Korns on the claims of fraud, negligent misrepresentation, and breach of fiduciary duty. It found in favor of Levi on her remaining claims, however, and specified that the judgment entered was independently supported by each of these claims. As to Levi's claim of breach of the covenant of good faith and fair dealing, the court found Korn had "breached her duty of good faith and fair dealing by her actions while establishing and operating her business relationship with [Levi]." The court noted Levi "became financially captive, putatively bore all risks, and was effectively controlled by . . . Korn," causing harm to Levi that was reflected in and measured by the parties' respective capital accounts in Kingdom Investors.

¶7 As to the dissolution count, the trial court found Levi and Korn were deadlocked in managing the company, causing it to suffer irreparable injury. The court also found it was not reasonably practical to carry on the business in conformity with the operating agreement. Based upon the testimony of both Levi and Korn, the court found the parties did not intend § 9.5 to cause one member to bear all the risk, notwithstanding the terms of the agreement. Rather, "both parties admitted, confessed and acknowledged

on the witness stand that each was entitled to half of the profits and obligated for half of the losses."

¶8 Accordingly, the trial court ordered a final accounting and an involuntary dissolution of the company and granted "a money judgment against the party with the final, lower member capital account balance, in an amount equal to half of the difference between the two member capital accounts." As part of this accounting, the court credited Levi's account for the attorney fees and legal costs she had incurred, finding them to be business expenses directly attributable to Korn's conduct.[2]

¶9 The trial court entered judgment pursuant to Rule 54(b), Ariz. R. Civ. P. It retained jurisdiction to supervise the dissolution of the company and sign a formal money judgment when the final amount was determined. This appeal followed.

Dissolution

¶10 The Korns claim the trial court "erred when it issued a money judgment for the purpose of equalizing the parties' capital accounts despite the express terms of the Operating Agreement prohibiting such a claim between the members of the LLC." We reject this argument for two reasons.

¶11 First, the operating agreement was not fully admitted into evidence. As a sanction for failing to disclose materials and appear at a pretrial conference, the trial court precluded the Korns from presenting any evidence at trial. On Levi's motion, the court admitted only § 2.2 of the operating agreement, which specified that members could be

[2]The trial court also determined Levi's transfer of the property to the company had been induced by Korn and constituted unjust enrichment. However, we need not address this alternative ground for the judgment given the disposition of this appeal.

called upon to contribute additional capital only for acquisitions. Although Levi had stipulated to the admission of the entire operating agreement before sanctions were imposed, she later withdrew the stipulation. Thus, the Korns' reliance on terms of the operating agreement that were not admitted into evidence is misplaced. *Cf. In re Marriage of Kells*, 182 Ariz. 480, 482, 484, 897 P.2d 1336, 1338, 1370 (App. 1995) (holding document on file with court but not formally admitted into evidence lacks evidentiary value absent stipulation or local rule to contrary).

¶12 Second, the trial court found the terms of the operating agreement did not reflect the parties' intent that they share risks and bear losses equally. The court based this finding on the parties' own testimony. The Korns contend the court misconstrued this testimony. They claim the parties merely recited the terms of the agreement at trial, and the court failed to recognize the distinction between an agreement to share losses and an agreement to contribute equal capital. We are unable to evaluate this claim, however, given the incomplete record before us. The Korns have included in the record on appeal a transcript from the first day of the two-day trial, when Levi testified. But they have not included a transcript from the second day, which contains Korn's own testimony. In the absence of this transcript, we presume it supports the court's findings. *See Baker v. Baker*, 183 Ariz. 70, 73, 900 P.2d 764, 767 (App. 1995).

¶13 The partial record before us is consistent with the trial court's findings. Levi testified at the first day of trial that Korn had said the operating agreement was "merely a form and . . . was something that she didn't really agree with." Levi's further testimony, some of which referred to correspondence admitted at trial, provided a basis

for the court to conclude the parties had intended and agreed to be financially responsible for half the company's losses. We therefore find no basis in the record to disturb the judgment on the dissolution claim.

¶14 Although it may seem extraordinary to uphold a judgment that requires a capital contribution from an LLC member and that conflicts with the terms of an operating agreement, this result stems from the unique procedural history and posture of this case. On appeal, the Korns have not challenged the propriety of the trial court's piecemeal admission of the operating agreement as a sanction for their pretrial conduct. Instead, they suggest this ruling was merely a "procedural curiosity" to be disregarded by this court. Moreover, they have denied this court the ability to review the trial court's findings by failing to provide a complete record of the proceedings below.

¶15 The Korns contend these steps were unnecessary because the operating agreement was indispensable evidence for Levi's case. They note, specifically, that under A.R.S. § 29-702(A), a promise by an LLC member to make a capital contribution to the company must be in writing and signed by the member in order to be enforceable. Although we agree with this general point of law, the Korns overlook that the application of this statute, like the analogous parol evidence rule, may be waived. *Cf. Cedic Dev. Corp. v. Sibole*, 25 Ariz. App. 185, 187-88, 541 P.2d 1169, 1171-72 (1975) (holding parol evidence rule waived by failure to raise specific objection and affirming judgment supported by parol evidence). As our supreme court observed in *Cooper v. Holder*, 24 Ariz. 415, 420, 210 P.2d 690, 692 (1922), *quoting Brady v. Nally*, 45 N.E. 547, 549 (N.Y. 1896):

> "[Parties] may waive the rules established by the courts to govern the admission of evidence, the same as they may waive the rule established by the Legislature . . . that certain contracts must be in writing; and a waiver may be inferred from the failure of the party, for whose benefit the rule was made, to . . . in some way . . . i[n]sist upon compliance with the law."

An opposing party's admission under oath that an agreement exists thus eliminates the need for a written instrument that would otherwise be required by statute. *Cf. Owens v. M.E. Schepp Ltd. P'ship*, 218 Ariz. 222, ¶ 29, 182 P.3d 664, 671 (2008) (acknowledging waiver rule with respect to statute of frauds).

¶16 Here, viewing the partial record in the light most favorable to upholding the judgment, *see Bennett v. Baxter Group, Inc.*, 223 Ariz. 414, ¶ 2, 224 P.3d 230, 233 (App. 2010), we presume Korn testified that the terms of the operating agreement did not reflect her intent regarding how the business would operate and that she had agreed to be "obligated for half of the losses," as the trial court expressly found. Assuming this was the substance of Korn's testimony—that she essentially admitted Levi was entitled to recover half the company's losses—we can find nothing improper in the monetary judgment.

¶17 The Korns also contend the trial court had "no statutory or contractual authority" to order an accounting. We note from the court's judgment that the Korns did not oppose the company's dissolution at the conclusion of trial, and there is nothing in the record to suggest the Korns made an objection to an accounting below. In any event, a trial court has the power to wind up and dissolve a limited liability company pursuant to A.R.S. § 29-785. Section 29-782(B), A.R.S., provides a non-exhaustive list of actions

that may be undertaken upon dissolution, including "making provisions for discharging [the company's] liabilities" and "[d]oing all other acts required to liquidate its business and affairs." Ordering an accounting falls within this statutory power or, at least, is not contrary to any statute or contractual provision the Korns have identified on appeal. We therefore find no error in the judgment.

Covenant of Good Faith and Fair Dealing

¶18 The Korns next argue the trial court erred in granting judgment in favor of Levi based on an implied covenant of good faith and fair dealing. "The law implies a covenant of good faith and fair dealing in every contract." *Rawlings v. Apodaca*, 151 Ariz. 149, 153, 726 P.2d 565, 569 (1986). Each party to a contract therefore has a duty not "to impair the right of the other [party] to receive the benefits which flow from the[] agreement or contractual relationship." *Id.* In determining what benefits were expected to flow from the relationship, "'the relevant inquiry always will focus on the contract itself, to determine what the parties did agree to.'" *Id.* at 154, 726 P.2d at 570, *quoting Wagenseller v. Scottsdale Mem'l Hosp.*, 147 Ariz. 370, 385, 710 P.2d 1025, 1040 (1985).

¶19 Our courts have noted that the good faith doctrine creates an apparent tension in the law:

> The general rule is that an implied covenant of good faith and fair dealing cannot directly contradict an express contract term. However, "[i]nstances inevitably arise where one party exercises discretion retained or unforeclosed under a contract in such a way as to deny the other a reasonably expected benefit of the bargain."

Bike Fashion Corp. v. Kramer, 202 Ariz. 420, ¶ 14, 46 P.3d 431, 434-35 (App. 2002) (citations omitted), *quoting Wells Fargo Bank v. Ariz. Laborers, Teamsters & Cement Masons Local No. 395 Pension Trust Fund*, 201 Ariz. 474, ¶ 66, 38 P.3d 12, 30 (2002) (alteration in *Wells Fargo Bank*). Thus, because the implied covenant requires that a party's actions be faithful to the agreed common purpose and consistent with the other party's justified expectations, a party may not exercise a retained contractual power in bad faith. *Wells Fargo Bank*, 201 Ariz. 474, ¶ 66, 38 P.3d at 30.

¶20 Whether the implied covenant of good faith and fair dealing has been breached is a question of fact. *Maleki v. Desert Palms Prof'l Props., L.L.C.*, 222 Ariz. 327, ¶ 28, 214 P.3d 415, 421 (App. 2009). Following a bench trial, we apply a deferential standard of review to a trial court's factual findings. *See Federoff v. Pioneer Title & Trust Co. of Ariz.*, 166 Ariz. 383, 388, 803 P.2d 104, 109 (1990). Our inquiry is limited to "whether the trial court had before it evidence that might reasonably support its action when viewed in the light most favorable to sustaining the findings." *Id.* Because it is a trial court's role to make factual determinations, "we will sustain the[] findings unless they are clearly erroneous or unsupported by any credible evidence." *Id.*; *accord Maleki*, 222 Ariz. 327, ¶ 28, 214 P.3d at 421.

¶21 Here, Korn's conduct appeared to be consistent with the written terms of the parties' operating agreement. However, given her evasiveness when asked to address the mounting debt, her refusal to sell the property or her interest in the company, and her statements that she "d[id]n't care" about the business's losses because Levi was primarily responsible for them, the trial court could have found that Korn denied Levi the benefits

that she reasonably expected to flow from their business relationship. *See Rawlings*, 151 Ariz. at 153-54, 726 P.2d at 569-70. Choosing to hold the company's property for an extended period of time with the hope that it might then regain value could be a reasonable business decision under some circumstances, as the Korns note on appeal. *See Wells Fargo Bank*, 201 Ariz. 474, ¶ 66, 38 P.3d at 30 (recognizing need for parties to exercise discretion under contract without judicial second-guessing). But the evidence here supported a finding, which we infer the court made, that the decision had been motivated by Korn's bad faith and the minimal capital she had at stake. We therefore find no basis to disturb the trial court's finding that Korn breached the implied covenant of good faith and fair dealing. Nor do we find the damages awarded to be improper simply because the calculation of that amount was based on the parties' capital accounts in their shared company. *See Maleki*, 222 Ariz. 327, n.3, 214 P.3d at 422 n.3 (noting breach of implied covenant may support damage award).

Attorney Fees

¶22 The Korns contend the trial court erred in awarding Levi attorney fees because she did not properly request such an award in her amended complaint, as required by Rule 54(g)(1), Ariz. R. Civ. P. We note, however, that Levi did in fact request attorney fees in her amended complaint in connection with all the counts on which she prevailed.

¶23 "[T]he general law in Arizona [is] that a party must timely present [her] legal theories to the trial court so as to give the trial court an opportunity to rule properly." *Payne v. Payne*, 12 Ariz. App. 434, 435, 471 P.2d 319, 320 (1970). A party

therefore waives on appeal any argument not presented properly in the lower court. *Schoenfelder v. Ariz. Bank*, 165 Ariz. 79, 88, 796 P.2d 881, 890 (1990). Moreover, an appellant must provide citations to the record in an opening brief demonstrating that an issue raised on appeal has been presented and ruled upon below. *Gibson v. Boyle*, 139 Ariz. 512, 521, 679 P.2d 535, 544 (App. 1983); *Gangadean v. Byrne*, 16 Ariz. App. 112, 114, 491 P.2d 501, 503 (1971); *see* Ariz. R. Civ. App. P. 13(a)(6) (requiring citation to record for each issue raised). The failure to comply with the latter requirement may similarly result in the waiver of an issue on appeal. *Spillios v. Green*, 137 Ariz. 443, 447, 671 P.2d 421, 425 (App. 1983). Because the Korns have not maintained that they objected below to the fee award on the ground that Levi had not sufficiently requested attorney fees in the pleadings, we need not address this argument further.

¶24 The Korns also challenge the award on the ground the trial court lacked authority to grant fees in a judicial dissolution action brought pursuant to § 29-781, and the court "specifically refused to award attorneys' fees on the breach of good faith and fair dealing claim." Regarding the latter point, we disagree with the Korns' characterization of the record. In the judgment, the court found the Korns' request for costs and attorney fees had been "rendered moot" by the court's instruction that they be included as business expenses and credited to Levi's capital account. Yet the court also indicated that the monetary judgment entered was independently supported by its ruling on the claim for breach of the covenant of good faith and fair dealing, and the court included attorney fees in its calculation of the judgment. Thus, the court did in fact award attorney fees on the claim of breach of the covenant of good faith and fair dealing.

¶25 Levi maintains on appeal that the fee award was correctly based on A.R.S. § 12-341.01(A), which allows recovery of attorney fees by the prevailing party in a matter "arising out of a contract." The Korns do not dispute that this statute provides a legal basis for awarding attorney fees on a claim for breach of the covenant of good faith and fair dealing. *See* Ariz. R. Civ. App. P. 13(a)(6) (appellant must include argument and citation to authority for each issue raised); *Ritchie v. Krasner*, 221 Ariz. 288, ¶ 62, 211 P.3d 1272, 1289 (App. 2009) (failure to properly develop argument results in waiver). An appellate court may affirm a superior court's judgment on any basis supported by the record. *Ariz. Water Co. v. Ariz. Dep't of Water Res.*, 208 Ariz. 147, n.10, 91 P.3d 990, 995 n.10 (2004). Accordingly, in the absence of a showing that the trial court erred in awarding attorney fees under this statute based on Korn's breach of the covenant of good faith and fair dealing, we will not disturb the judgment.

Conclusion

¶26 On the record before us, we do not find the trial court committed reversible error in ordering an accounting or in computing the judgment in connection with the dissolution claim. We similarly find no basis to disturb the trial court's award of attorney fees or its finding that Korn breached the covenant of good faith and fair dealing. And because the judgment was independently supported by these two claims, we need not address the court's ruling on Levi's claim for unjust enrichment.

¶27 Affirmed.

/s/ Peter J. Eckerstrom
PETER J. ECKERSTROM, Judge

CONCURRING:

/s/ Garye L. Vásquez
GARYE L. VÁSQUEZ, Presiding Judge

/s/ Virginia C. Kelly
VIRGINIA C. KELLY, Judge