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IN THE SUPREME COURT OF IOWA
No. 19-1790

TRACY BARKALOW, TSB HOLDINGS, L.L.C., and BIG TEN PROPERTY MANAGEMENT, LLC,
Plaintiffs/Appellees/Cross-Appellants,
vs.
BRYAN CLARK, JEFFREY CLARK,
Defendants/Appellants/Cross-Appellees,
and JOSEPH CLARK,
Defendant/Cross-Appellee.

BRYAN CLARK AND JEFFREY CLARK,
Counterclaim Plaintiffs/Appellants/Cross-Appellees,
v.
TRACY BARKALOW
Counterclaim Defendant/Appellee/Cross-Appellant.

Appeal from the Iowa District Court in and for Johnson County
Case No. LACV079040
The Honorable Paul D. Miller

Plaintiff-Appellee / Cross-Appellant Tracy Barkalow's Combined Final Brief

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III. THE DISTRICT COURT ERRED BY NOT ORDERING DISSOLUTION BASED ON DEFENDANTS' OPPRESSION.

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ROUTING STATEMENT

This case should be transferred to the Iowa Court of Appeals pursuant to Iowa R. App. P. 6.1101(3)(a) and (b) because it does not present a fundamental and urgent issue of broad public importance requiring prompt determination by the Iowa Supreme Court.

STATEMENT OF THE CASE

This appeal centers on Iowa Code § 489.701's judicial dissolution sections, with four primary issues on appeal. The first is whether the district court properly ordered dissolution based on its conclusion that it was not reasonably practicable to carry on Outside Properties, LLC's (the "LLC's" or the "Company's") activities in conformity with the certificate of organization and the operating agreement. The second is whether the district court had the authority and grounds to provide for equitable relief in addition to dissolution as part of its order dissolving the LLC. The third is whether, alternatively to dissolving based on the "not reasonably practicable" standard, the district court should have dissolved and provided additional equitable relief based on the majority members acting in a manner that was oppressive to a minority member. The fourth is whether alternatively to dissolving the Company and providing the additional equitable relief, the district court should have awarded Plaintiff-Appellant Tracy Barkalow ("Barkalow") damages for the Appellants' and Joseph Clark's breaches of fiduciary duty.

In 2009, Barkalow, Appellants Jeffrey Clark and Bryan Clark ("Appellants"), and Defendant Joseph Clark – the three Clarks are referred to herein as the "Clarks" – formed the Company. (Appendix Volume I ("App. I") at 391). Pursuant to the Certificate of Organization, Barkalow and the Clarks each remitted $41,000 capital contributions. (*Id.*). The Certificate of Organization specifically states that "no additional capital contributions will be required." (*Id.*). Barkalow understood that provision to mean that after the members made their initial capital contributions, none of the members would have to put more money into the Company. (Trial Tr. Vol. 1 60:19-61:10). He had that understanding because, at the time the LLC was formed, only one property purchase was contemplated, with the down payment financed by the members' initial capital contribution. (Trial Tr. Vol. 1 at 58:4-59:11). Nothing in Company's Operating Agreement allows for (i) unilaterally capital contributions; or (ii) a member making demand of another to make an equal capital contribution or face dilution of his ownership interest. (App. I at 321).

Subsequent to its formation, the Company has acquired seven rental properties in Iowa City, all through debt and seller financing. (App. I at 263; Appendix Volume II ("App. II") at 219). So, Barkalow's expectation to not have to put in additional capital did not change as the Company acquired additional properties, because the Company did not use capital contributions to acquire these properties. (Trial

Tr. Vol. 1 at 61:8-:18; App. II at 219).

Barkalow's relationship with Appellants deteriorated and became acrimonious in 2013. (App. I at 297). In late 2013, Jeffrey Clark requested information from Company accountant Jason Wagner on how to dilute Barkalow's interest in the Company. (App. II at 199). Wagner determined that if all Clark family debt (with the exception of $95,000 owed to Jeffrey Clark) was transferred "to equity as capital contributions," each of the Clark brothers' ownership interest in the Company would increase to 32.5% and Barkalow's interest would decrease to .83%. (App. II at 197; Trial Tr. Vol. 3 at 25:10-28:12). The dilution analysis done by Wagner at Jeffrey Clark's request is exactly what played out when the Appellants were finally presented an opportunity to dilute Barkalow in 2015.

In December 2015, the Company's balloon payment of roughly $1,000,000 owed to Ellis Shultz came due. (Trial Tr. Vol. 1 at 101:14-:17). When the Shultz loan came due in December 2015, the Clarks took advantage of the situation to proceed with diluting Barkalow's interest in the Company from twenty-five percent to one-tenth of one percent. (App. I at 436). Despite debt financing being available to fund the Shultz payoff, the Clarks decided to unilaterally contribute capital to pay off the Shultz debt. (App. I at 400, 401-03; Trial Tr. Vol. 3 at 200:13-:25). There was never any voting proposal or vote to authorize

this capital call. (*Id.*). The Defendants just unilaterally contributed the funds, and thereby increased their ownership and diluted Barkalow's ownership in the Company. (App. I at 437). The evidence shows that dilution of Barkalow's interest was at the forefront of the Clarks' minds when they unilaterally contributed the funds to pay off the Shultz debt in December 2015. (App. I at 400, App. II at 113, 193; Trial Tr. Vol. 3 at 35:8-36:15).

In 2016, Appellants further diluted Barkalow's interest – and diluted Joseph Clark's interest – by making contributions to the Company to pay off loans owed by the Company to the Clarks and entities owned by the Clarks and their family members. (App. I at 406, App. II at 207, 208, 220-22, 223-27). They made these contributions despite the Company servicing the Clark family loans, the loans not being past due or in default, and the Company having a schedule pursuant to which it would repay the loans with interest over a 10-year period. (App. I at 401-03, 404-05, App. II at 91-112, 185-86). The Company simply had no legitimate business reason to prepay the Clark family loans, and the contributions were made for purposes of oppressing Barkalow, diluting his interest, and frustrating his reasonable expectations as a member of the Company. (App. I at 406-09, App. II at 207, 208, 220-22, 223-27).

As the district court found, in addition to this conduct by Appellants, the Company is otherwise dysfunctional at the governance level and is only able to

operate pursuant to an Interim Management Agreement, which was entered into to avoid the appointment of a receiver or issuance of injunctive relief pending this lawsuit. (App. I at 297-98).

Barkalow and his entities TSB Holdings, L.L.C. and Big Ten Property Management, LLC brought this action, with Barkalow seeking dissolution of the LLC based on member oppression and company dysfunction, as well as for recovery of damages against Defendants. Following a five-day bench trial and post-trial briefing, the district court issued its Ruling on August 8, 2019. The court denied Barkalow's and the other plaintiffs' claims for relief except one – the court held that it was not reasonably practicable for the Company to carry on in conformity with the certificate of organization and the operating agreement and therefore ordered that the Company be dissolved and that the 2015 and 2016 contributions be reclassified as loans and the members each be restored to their original 25% interest in the Company.

STATEMENT OF FACTS

I. The Formation of the Company and Acquisitions of Properties through Debt Financing.

On or about October 2, 2009, Barkalow, Appellants and Joseph Clark formed the entity Outside Properties, L.LC. ("Outside Properties" or the "Company") by filing a Certificate of Organization with the Iowa Secretary of State. (App. I at 391). Pursuant to the Certificate of Organization, Barkalow and the Clarks each remitted

$41,000 capital contributions. (*Id.*). Barkalow's capital contribution was funded by a loan made by the Defendants through the Company. (App. I at 263). Barkalow later repaid this loan. (*Id.* at 280).

The Certificate of Organization specifically states that "no additional capital contributions will be required." (App. I at 391). Barkalow testified that he took this provision to mean that after the members made their initial capital contributions, none of the members would have to put more money into the Company. (Trial Tr. Vol. 1 60:19-61:10). He had that understanding because, at the time the LLC was formed, only one property purchase was contemplated, with the down payment financed by the members' initial capital contribution and the balance of the purchase price paid through monthly payments, and a small balloon payment that was due in 2019. (Trial Tr. Vol. 1 at 58:4-59:11).

Outside Properties was formed at Barkalow's request. (Trial Tr. Vol. 1 at 45:20-46:1, 51:2-54:13). Barkalow and Bryan Clark and Jeffrey Clark verbally agreed that Outside Properties would be an investment vehicle pursuant to which Defendants would make their initial capital contribution for purposes of Barkalow, through Outside Properties, acquiring a parcel of property, and then use seller and debt financing to acquire additional properties in the Iowa City area. (*Id.* 51:2-54:13). Barkalow and Bryan Clark and Jeffrey Clark verbally agreed that Barkalow would then be able to buy out Bryan Clark and Jeffrey Clark within 5 years. (*Id.*).

The Company's Operating Agreement states that member meeting quorums and voting rights (if demanded) shall be determined by the capital contribution of each member. (App. I at 325, §§ 2.5 & 2.7.1). However, nothing in the Operating Agreement allows for (i) unilaterally capital contributions; or (ii) a member making demand of another to make an equal capital contribution or face dilution of his ownership interest.

When the Company was formed, Joseph Holland, attorney for the Clarks who would become the Company's attorney, wrote to Jeffrey Clark with copy to Barkalow raising concerns with the inability to make adjustments to ownership interests for additional capital contributions or withdrawals. (App. I at 441) ("There is no provision for adjustment of Capital Accounts on a periodic basis for additional capital contributions or withdrawals"). Holland recommended that these governance documents be "revised and finalized prior to any significant business activities," but the Company never addressed the issues raised in his letter. (*Id.* at 443).

In 2010, the members of Outside Properties executed a First Amendment to the Operating Agreement (the "Amendment"), which divided the membership of the company into two classes. (*Id.* at 329). The Amendment designates the original four members – Barkalow and the Defendants – as Class A members, with "[a]ll membership interest currently held by the undersigned are Class A member units

which are voting units in the Company." (*Id.*). The Amendment states that Class B units are non-voting member units, and the Class A members were allowed to convert their Class A units to Class B units and transfer such units to "third parties who shall become non-voting members of the Company." (*Id.*). The Amendment refers to a "separate Member Interest Purchase Agreement," but such an agreement never was executed. (*Id.*).

Up through the time of the Amendment, Barkalow and the Defendants each held a 25% interest in Outside Properties. (App. II at 244-53). Subsequent to the Amendment, the Defendants each separately converted 14% of their Class A membership units to Class B units and transferred such units to their respective children in varying percentages. (*Id.* at 276-309). The 2014 federal tax returns for the Company state Barkalow had a 25% ownership interest in Outside Properties, and the Defendants each had an 11% ownership interest. (*Id.* at 560-93).

Subsequent to its formation, the Company has acquired seven rental properties in Iowa City. (App. I at 263; App. II at 219). As stated above, the first property located at 817 Melrose Avenue was purchased through the members' initial contributions and seller financing. (Trial Tr. Vol. 1 at 58:4-59:11). As 817 Melrose was the only property the members contemplated purchasing when the Company was formed, Barkalow's expectation was that none of the members would have to put more money into the Company beyond the initial contributions. (*Id.*).

Outside Properties then, in July and August 2010, purchased 331 S. Lucas Street and 6 Triangle Place through mortgage loans from U.S. Bank, N.A. (*Id.* at 63:3-:8, 65:3-:14; App. II at 219). The Company then acquired three properties – 3 Triangle Place, 5 Triangle Place, and 805 Melrose Avenue – from Elis Schultz in September 2010 for $1.2 million. The Company made a 10% down payment through a loan to the Company from entities owned by the Clarks and their family members (the "Clark Family Entities"), with the balance of the purchase price owed due in 2015. (Trial Tr. Vol. 1 at 67:10-:22; App. II at 12-13 (current liabilities reflecting amounts owed to Clark family entities); Trial Tr. Vol. 3 at 28:14-30:4; App. I at 397). Finally, in June 2012, the Company acquired the property at 419 South Governor Street through use of a loan from Clark Family Entities. (Trial Tr. Vol. 1 at 67:23-68:22; App. II at 65-71).

So, Barkalow's expectation to not have to put in additional capital did not change as the Company acquired additional properties, because the Company acquired these properties through debt financing and/or seller financing. (*Id.* at 61:8-:18; App. II at 219). Aside from the down payment on the Company's first property purchase, the entirety of the Company's operations was funded through debt and seller financing. (Trial Tr. Vol 1 at 58:7-:1, 63:3-:8; 65:3-69:3; App. II at 219).

In 2011, without Barkalow's notice or consent, and without the loan owing to U.S. Bank being due or in default, Bryan Clark prepaid the Company's loan owing to U.S. Bank in an amount over $1,000,000, through a loan to the Company from Appellants and Joseph Clark and Clark Family Entities. (Trial Tr. Vol.1 at 78:8-79:10, 80:14-81:24; App. II at 12-13, 14-15). The Clark Family Entities' loans to the Company were booked as debt of the Company. (*Id.*).

II. Barkalow's Deteriorating Relationship with Appellants and Appellants' Desire to Dilute Barkalow.

Barkalow's relationship with Appellants deteriorated and became acrimonious in 2013. (App. I at 297). Barkalow obtained independent financing for personal debt guaranteed by Appellants in mid-2013, and was released from his obligations under the Security Agreements with Appellants and Joseph Clark, (*Id.* at 331-39, 340-46, 347-354), but there were ongoing disputes between the parties in 2013 regarding how each party was treated as it related to these agreements. (*See id.* at 360-63, 454-56, 457-59, 460, 461). Barkalow was also frustrated with the zoning issues that had arisen related to the 902-906 N. Dodge property he had purchased from the Clarks. (*Id.* at 364-66). It was in 2013 that Jeffrey and Bryan Clark confirmed to Barkalow that they would not honor the verbal agreement they had with Barkalow allowing him to buy out their interests in the Company. (*See* Trial Tr. Vol. 1 86:2-:10; App. I at 367-68). All of these issues contributed to the souring of the relationship between Appellants

and Barkalow.

Following this deterioration of the relationship between Appellants and Barkalow, Jeffrey Clark in November 2013, with copy to Bryan, e-mailed Wagner, stating that "Barkalow has not placed any down payments into Outside Properties since it was started and had promised to many times." (App. II at 199). Jeffrey then asked the following questions: "If we were to adjust his existing ownership in the LLC based on his equity in Outside Properties, what percent of ownership would he have? What amount would he have to come up with to be an equal (25%) partner? How would we go about adjusting him ownership?" (*Id.*). On that e-mail from Jeffrey Clark to Wagner, Wagner wrote a note stating that Barkalow would have to come up with $298,000 to still be a 25% owner if all of the Clark entity debt was moved to equity in the Company. (*Id.*; Trial Tr. Vol. 3 at 24:8-25:9).

In response to Jeffrey Clark's e-mail, Wagner developed two spreadsheets to analyze the effect on Barkalow's ownership interest if various Clark family debt was transferred to equity of the Company. (App. II at 197; Trial Tr. Vol. 3 at 25:10-28:12). He determined that if all Clark family debt (with the exception of $95,000 owed to Jeffrey Clark) was transferred "to equity as capital contributions," each of the Defendants' ownership interest in the Company would increase to 32.5% and Barkalow's interest would decrease to .83%. (App.

II at 197). Wagner testified that these spreadsheets represent his analyses, done at Jeffrey Clark's request in 2013, of how Barkalow's ownership interest would be diluted if the Clark family loans were converted to capital contributions. (Trial Tr. Vol. 3 at 25:10-28:12).

Jeffrey Clark disputed Wagner's testimony, and testified that he did not know why Wagner developed the analyses evidenced in Exhibit 106. Jeffrey Clark's e-mail refers to Barkalow not placing any "down payments" into Outside Properties, and Jeffrey confirmed at trial that the "down payments" he was referring to were the down payments to purchase properties that were financed from Clark family loans. (App. II at 195; Trial Tr. Vol. 3 at 183:14-189:11). Despite confirming that he was referring to the Clark family loans that funded the down payments, and despite Wagner's testimony that he understood Jeffrey to be asking about the effect on Barkalow's interest if such loans were converted to capital, Jeffrey Clark testified that all he was asking for from Wagner was how much Barkalow owed on the loan he took for the initial $41,000 capital contribution. (*Id.*). Jeffrey Clark's explanation strains credulity, especially given that (i) Wagner, the Clark family's own accountant, testified that he understood that Jeffrey Clark was asking him to determine how Barkalow would be diluted if the Clark family loans were treated as capital contributions; and (ii) when the Defendants proceeded with the dilution event in 2015, it resulted in

almost exactly the same change in ownership percentages as determined by Wagner in 2013. (*Compare* App. II at 197 *with* App. I at 436).

III. The 2015 Contributions.

In December 2015, the balloon payment of roughly $1,000,000 owed by the Company to Ellis Shultz came due. (Trial Tr. Vol. 1 at 101:14-:17). When the Shultz loan came due in December 2015, the Clarks took advantage of the situation to proceed with diluting Barkalow's interest in the Company from twenty-five percent to one-tenth of one percent. (App. I at 436). While the Clarks claim that a member capital call was the only way in which to obtain funds to pay off the Shultz debt, the evidence and testimony submitted by Barkalow shows that the Company had other sources of funds available to it to pay the Shultz debt. Both Bryan Clark and Jeffrey Clark initially offered to fund, at least in the short term, the payment with funds from a personal line of credit (they both testified that these same lines of credit were how they ended up funding their capital contribution in 2015). (App. I at 394, 429-31; Trial Tr. Vol. 1 at 102:15-103:22; Trial Tr. Vol. 3 at 197:13-198:25, 206:6-:11; Trial Tr. Vol. 5 at 15:20-16:4). Barkalow and attorney Robert Downer both testified that a loan could easily be obtained from Hills Bank prior to the Shultzs initiating a foreclosure action. (App. I at 480; Trial Tr. Vol. 1 at 112:24-114:15; Trial Tr. Vol. 1 at 143:10-:19, 158:9-160:2). Funding was also available from U.S. Bank, but Jeffrey Clark

testified that he was against utilizing a U.S. Bank secured loan to pay off the Shultz debt in December 2015 because the unsecured, undocumented Clark family loans would have been placed in a subordinate position to the U.S. Bank loan. (Trial Tr. Vol. 3 at 201:21-203:20).

So, despite debt financing being available to fund the Shultz payoff, the Defendants decided to unilaterally contribute capital to pay off the Shultz debt. There was never any voting proposal or vote to authorize this capital call. (App. I at 400 ("There was not any approved member vote . . ."); *id.* at 401-03 (neither the December 7 or December 17 meeting voting proposals list having a vote to contribute the capital); Trial Tr. Vol. 3 at 200:13-:25). The Defendants just unilaterally contributed the funds, and thereby increased their ownership and diluted Barkalow's ownership in the Company. (App. I at 436).

The Defendants claim that they were not considering the effect on ownership interest when they made the contributions in 2015. That is simply false. As an initial matter, Wagner took notes subsequent to the Shultz debt coming due in which he wrote "Want to be treated as a loan, <u>no</u>. Want to treat as a capital call. Want to dilute as <u>capital call</u>. Does this dilute." (App. II at 193-94). While he could not recall who wanted to take these actions, Wagner did testify that party to be diluted would be whoever would not make the capital contribution, which, of course, turned out to be Barkalow. (Trial Tr. Vol. 3 at

35:8-36:15). Additionally, on the same day that the Defendants contributed the funds (December 9, 2015) (App. II at 114), Jeffrey Clark e-mailed the other Class A Members of the Company stating: "all members, except for Tracy Barkalow, have contributed capital which will be reflected on the books. Meaning that Joe Clark, Jeff Clark and Bryan Clark will show upward adjusted capital contributions on the books based on the total payoff amount. The total payoff amount was $1,005,290.26." (App. I at 400). Dilution of Barkalow's interest was at the forefront of the Defendants' minds when they unilaterally contributed the funds to pay off the Shultz debt in December 2015.

IV. The 2016 Contributions.

While the 2015 capital contributions were done to oppress Barkalow and dilute his interest, at least Appellants could point to the Shultz payoff as an excuse for making the capital contributions. Appellants have no such reasonable excuse for diluting Barkalow's and Joseph Clark's interest in 2016 when they contributed capital to pay off the loans owed by the Company to Appellants and the Clark Family Entities. As explained below, while Jeffrey and Bryan Clark claim that the Clark family loans were past due, in default, and in jeopardy of not being repaid because of Barkalow's refusal to honor their terms, as of January 2016, the Company was servicing the Clark family loans, the loans were not past due or in default, and

the Company had a schedule pursuant to which it would repay the loans with interest over a 10-year period.

Wagner, accountant for both the Company and the Clark family, created amortization schedules for the Clark family loans, and the loans were on a ten-year payment plan. (App. II at 161-84, 185-86; Trial Tr. Vol. 3 at 29:14-33:5). While the Company ceased servicing the loans after June 2014, (App. II at 161-84), at the December 17, 2015 member meeting, the Class A members voted on whether to "immediately pay back 'all Clark entity loans' interest and required back payments . . . ." (Vol. I at 402). The Clarks voted yes, and Barkalow voted no, so the proposal passed. (*Id.*). Based on this resolution passing, the Company paid the Clark family loans for unpaid interest and back payments on December 19, 2015. (App. II at 101, 104, 105, 108, 110-12; Trial Tr. Vol. 3 at 76:7-77:17). At the Company's January 15, 2016 member meeting, the Class A members voted on whether to "continue to pay all 'Clark entity loans' interest and required payments from the Outside Properties LLC checking account. . . ." (App. I at 404). The Clarks voted yes, and Barkalow voted no, so the proposal passed. (*Id.*). Based on this resolution passing, the Company made the scheduled interest payment on these loans on January 30, 2016. (App. II at 101, 104, 105, 108, 110-12). Despite Bryan Clark's testimony to the contrary, as of January 2016, the Clark family loans were not past due or in default, and had a schedule pursuant

to which the Company would repay them with interest over a 10-year period. (Trial Tr. Vol. 3 at 29:14-33:5, 76:7-77:17).

The district court found that "the Clark entities had made demands for repayment of the loans, which had no set due date." (App. I at 280). But there is no evidence corroborating that the Clark entities had made demands to Outside Properties for repayment of their loans, and certainly no evidence supporting the basis for such demands, given that the Company was repaying such loans pursuant to a 10-year amortization schedule. Bryan Clark texted to Joseph Clark that that the 2016 capital contribution "had something to do with the interfamily loans trying to consolidate them and turn them into loans by the three of us." (App. II at 78). Bryan Clark also wrote to Wagner that "[w]e voted to change the inter-family loan to capital contributions from Jeff Bryan and Joe." (App. II at 204). So, again, the Clark entity loans were not due, past-due, or in default. Appellants just opted to convert family debt to their own capital to increase their interest in the Company and dilute Barkalow's. In addition to wanting to further dilute Barkalow's interest in the Company, Jeffrey and Bryan Clark also put the interests of the Clark family and the Clark family entities before the interests of the Company and its other members, Barkalow in particular. The Company simply had no legitimate business reason to prepay the Clark family loans.

The evidence submitted at trial – and largely overlooked by the district court – proved that the actual reason for paying off these loans was to further dilute Barkalow out of the Company. The Company's meeting minutes created by the Defendants' then-attorney for the February 19, 2016 LLC member meeting shows demand by the Defendants that Barkalow contribute capital in amount equal to the amount being contributed by Appellants, or face further dilution of his equity interest in the LLC. (App. I at 406-09). The meeting minutes from February 19, 2016 confirmed Appellants' position that Barkalow's unwillingness to provide additional capital diluted his interest – "This capital contribution by the Clarks diluted Tracy's position in the Company, both in terms of profit interest and in terms of voting interest." (*Id.* at 406). These same meeting minutes reflect various offers of resolution regarding the capital contribution and voting rights issues being discussed but ultimately rejected by the various members. (*Id.* at 406-09). Upon Barkalow rejecting Appellants' final offer, Appellants stated the following:

> Tracy's rejection of those offers left them with few alternatives, and that if he wasn't willing to put capital into the company and was more interested in preserving his right to sue . . . , it wasn't fair or prudent for the Clarks to continue lending money to the Company . . . **while allowing Tracy to be an equal participant in the potential for future appreciation**. . . . [T]he Clark brothers had no option other than to request additional voluntary capital contributions from the members in order to finance payoff of the loans that had been made from the various Clark entities. (This option was previously considered [at] the January 15, 2016 meeting, but was tabled at that meeting at Joe's request, because he wanted to allow space to consider whether there might be

> another viable option that **wouldn't further dilute Mr. Barkalow**. . . .)."

(*Id.* at 407 (emphasis added)). Appellants thereafter made a purported capital contribution in the total amount of $949,998, further diluting Barkalow's interest in the Company.

Appellants funded at least part of this 2016 contribution from a loan from Iowa-Illinois Square LLC, one of the same Clark family entities that was paid off by the Company with funds from the 2016 contribution. (App. II at 229; App. II at 61; Trial Tr. Vol. 3 at 38:11-:39:9; Trial Tr. Vol. 4 at 120:6-121:19). Joseph Clark did not participate in the 2016 contribution because borrowing money from one of the same sources of the original debt did not make sense to him. (Trial Tr. Vol. 4 at 120:6-121:19). And he is correct, if the goal was to pay off Clark family debt, then borrowing from a Clark family entity to do so does not make sense. Jeffrey and Bryan Clark's actions only make sense if their real goal was to find the necessary funds to be able to further dilute Barkalow.

While Appellants claim that the purpose of the 2016 contribution was not to dilute Barkalow, but to pay off the Clark family loans (which, as evidenced above, did not need to be paid off), the e-mails between the Clarks' attorney, Paul Morf, and Wagner clearly show that the primary objective in making the 2016 contribution was to further dilute Barkalow. On March 24, 2016, Morf wrote to Wagner, "as accountant for Outside Properties LLC," and attorney

Joseph Holland, "as counsel for Outside Properties LLC," requesting to see copies of the ownership ledger and the books the Company once the books reflect the 2015 and 2016 contributions. (App. II at 220). He stated that the "effect of these voluntary, non-mandatory capital contributions will be to **greatly dilute the ownership of Mr. Barkalow**, who opted not to participate, although he was given every opportunity to do so." (*Id.* at 221 (emphasis added)). Wagner responded, stating "[j]ust to be clear, the intention with the $1,000,000 capital contribution in December 2015 is to change not only the Capital %s in Outside Prop, **but also the Profit and Loss %s. The effect of this will be to dramatically increase the three boys Profit, Loss, and Capital %s to nearly 33% each.**" (*Id.* at 220-21 (emphasis in original)). Wagner sent another e-mail to Morf in June 2016 regarding the 2016 contributions, stating "[a]ssuming the interfamily debt is moved over as the previous email stated and papered properly. Tracy would be dropped down to approx.. .533% ownership with a Capital account just below $10,000." (*Id.* at 225). Once the books were updated, Barkalow's interest was in fact diluted to just over 0.5%. (*Id.* at 207-08).

V. The Company's Dysfunction.

The ongoing disputes between the Class A members regarding the governance, management and operations of the Company were laid out

thoroughly in the trial record. The district court found that the following ongoing disputes existed:

- Disputes as to how to interpret the Company's Operating Agreement.
- Disputes as to who is the Company's general manager.
- Disputes over ownership interests and voting interests in the company.
- Disputes on whether to treat financial events as distributions or expenses.
- Disputes regarding how to treat cash infusions.
- Disputes regarding refinancing the Company's debt.
- Disputes regarding keeping the Company's books.
- Dispute regarding the payment of property management fees.
- Disputes over who was to provide Wagner the information do to the accounting for the Company.
- Disputes as to who the tax matters partner should be and who should sign tax returns.
- Disputes as to who the Company's accountant should be.
- Disputes as to who should have possession of the Company checkbook and sign the Company's checks.

- Disputes over scheduling of member meetings.

(App. I at 297-98, citing to App. I at 369-71, 372-86, 410, 411-15, 432-35, 444-47, App. II at 142-53, 154-60; *see also* App. I at 416-17, 418-24, 425-26, 437-38, 439-40; *see also* Trial Tr. Vol. 3 at 79:15-82:12; Trial Tr. Vol. 4 at 40:22-44:23). The district court also relied on the testimony from Company accountant Wagner that the disputes between the Class A Members make it difficult, if not impossible, to properly take care of the Company's finances and accounting. (App. I at 298; *see also* Trial Tr. Vol. 3 at 82:8-:12).

The district court made the following findings and conclusions regarding the Interim Management Agreement: "The Company is also operating now under an 'Interim Management Agreement', so obviously all issues concerning ordinary governance procedures and operating the Company in the future have not been resolved and will continue to be future disputes if not dissolved. The Interim Management Agreement was entered into only to avoid the necessity of appointing a receiver or possibly issue a temporary injunction during the pendency of the lawsuit." (App. I at 298).

The district court then pointed out a few of the issues that Joe testified that he had with Jeff and Bryan: (i) that Bryan borrowed funds from Clark family entities to pay off the US Bank loan in 2011, which was not due or in default, without notice to Joe or formal company action to approve the US Bank loan

payoff; (ii) that he was not aware or notified of Bryan's and Jeff's 2016 capital contributions until months after they were made; and (iii) that he had difficulty obtaining information from Jeff and Bryan concerning their additional capital contributions. (*Id.*). Joseph Clark testified that, unless the district court ordered the dissolution of the Company or some other equitable relief, these same parties would have been back in Court arguing over the governance, management and control of the Company. (Trial Tr. Vol. 3 at 152:10-153:6).

ARGUMENT

I. THE DISTRICT COURT CORRECTLY ORDERED THE DISSOLUTION OF OUTSIDE PROPERTIES, LLC.

A. Standard for Review.

This Court reviews *de novo* the district court's ruling on judicial dissolution of a limited liability company pursuant to Iowa Code § 489.701. *Baur v. Baur Farms, Inc.*, 832 N.W.2d 663, 668 (Iowa 2013).

B. Argument.

1. Iowa Code § 489.701(1)(d)(2) and the Court's Order.

Court-ordered dissolution of an LLC is appropriate if it is not reasonably practicable to carry on the Company's activities in conformity with the certificate of organization and the operating agreement. Iowa Code § 489.701(1)(d)(2).

The district court properly held that the Company is not operating in conformity with its governance documents, nor is it reasonably practicable for it to do so. The ongoing disputes between the Class A members regarding the governance, management and operations of the Company were laid out thoroughly in the trial record and are listed above. The disputes include, but are not limited to, disputes as to how to interpret the Company's Operating Agreement; disputes over ownership interests and voting interests in the company; disputes on whether to treat financial events as distributions or expenses; disputes regarding how to treat cash infusions; disputes as to who should have possession of the Company checkbook and sign the Company's checks; and disputes over scheduling of member meetings. (Statement of Facts § V, *supra*). The district court also relied on the testimony from Company accountant Wagner that the disputes between the Class A Members make it difficult, if not impossible, to properly take care of the Company's finances and accounting. (*Id.*). The court held that it "cannot repair the lack of trust in the relationship between Jeff, Bryan and Tracy." (App. I at 298).

The district went on to hold that "[i]t is simply not reasonably practicable to carry on the Company's activities in conformity with the certificate of organization and operating agreement in light of the intensity, longevity and number of disputes and issues existing between Tracy, Bryan and Jeff which are

fueled by their continuing long-time acrimonious, bitter, and toxic relationship." (*Id.*). The district court concluded that "[t]he relationship between the members is not repairable and certainly the duty of good faith that each must bring to the Company will be nonexistent in the future." (*Id.*).

Jeffrey and Bryan argued below that the "**interim** Management Agreement" is evidence that the continued operation of the Company is practicable. (App. I at 203 (emphasis added)). But, as the district court found, the Management Agreement is "interim," meaning that it is temporary and "was entered into only to avoid the necessity of appointing a receiver or possibly issue a temporary injunction during the pendency of the lawsuit." (App. I at 298). The district court concluded that "I cannot ignore what I consider to be total dysfunction at the governance level." (*Id.*).

The Company is functioning not in conformity with its governance documents, but pursuant to an interim agreement entered into during the pendency of this lawsuit. As testified to by Joseph Clark, unless the district court ordered the dissolution of the Company or some other equitable relief, these same parties would have been back in Court arguing over the governance, management and control of the Company. (Trial Tr. Vol. 4 at 152:10-153:6). Based on the evidence submitted at trial, the district court properly held that it

was not reasonably practicable for the Company to carry on in conformity with the certificate of organization and the operating agreement.

2. The Standard for Dissolution Based on Reasonable Impracticability to Carry On Its Activities was Met in this Case.

Without citation to any Iowa appellate authority, Jeffrey and Bryan argue that courts impose a nearly impossible bar to judicially dissolve a company based on "impracticability to carry on." While certainly dissolution is a drastic remedy, and one in which a court must exercise with "caution," *Baur v. Baur Farms, Inc.*, 832 N.W.2d 663, 678 (Iowa 2013), neither Section 489.701 nor any Iowa caselaw imposes a higher evidentiary standard or burden that must be met for the court to order dissolution based on impracticability.

"'[T]here is no prevailing interpretation' of the term 'not reasonably practicable' in relation to the dissolution of limited liability companies." *In re Hefel*, 2011 WL 4356215, *3 (N.D. Iowa Bankr., Sept. 19, 2011) quoting *Kirksey v. Grohmann*, 754 N.W.2d 825, 828 (S.D. 2008). But the very cases to which Appellants cite support the district court's decision to dissolve based on "total dysfunction at the governance level," and that the Company is not operating pursuant to its governance documents, but an interim Management Agreement. *See, e.g.*, *In re Arrow Inv. Adv., LLC*, 2009 WL 1101682, *2 (Del. Ch., April 23, 2009) (cited to by Appellants at 43) ("dissolution is reserved for

situations in which the LLC's management has become so dysfunctional **or** its business purpose so thwarted that it is no longer practicable to operate the business") (emphasis added); *Dunbar Grp., LLC v. Tignor*, 593 S.E.2d 216, 219 (Va. 2004) (cited to by Appellants at 42, 44) ("Only when a circuit court concludes that present circumstances show that it is not reasonably practicable to carry on the company's business in accord with its articles of organization and any operating agreement, may the court order a dissolution of the company."). But for the interim Management Agreement, the "management of the entity is unable or unwilling to reasonable permit or promote the stated purpose of the entity to be realized or achieved." *In re 1545 Ocean Ave., LLC*, 893 N.Y.S.2d 590, 598 (N.Y. App. Div. 2d Dept. 2010) (cited to be Appellants at 44-45).

Appellants cite to an Iowa Business Specialty Court decision which analyzed whether a judicial dissolution was warranted, under the "reasonably practicable" standard, based on plaintiffs' allegations of the members being deadlocked in choosing a new manager. *Busse v. Busse*, Iowa District Court for Linn Cty. Case No. LACV083022, at 66 (May 22, 2017). The court held that the LLC "continued to operate as intended," so dissolution would be improper. But the court concluded as much because, given that the LLC was manager-managed and not member-managed, the disputes between the members did not largely affect the operations of the LLC. *Id.* at 65-66. The Company here is not manager-

managed, but managed by the members whose relationship is "not repairable and certainly the duty of good faith that each must bring to the Company will be nonexistent in the future." (App. I at 298). The ruling in *Busse* is only relevant to the extent it shows that member dysfunction, while perhaps of less concern in a manager-managed company, is of great concern in a member-managed company such as Outside Properties.

Jeffrey and Bryan attempt to trivialize the Company's dysfunction, arguing "[t]hat Mr. Barkalow does not get along with the Clark brothers is not a valid basis for dissolving this viable company . . . ." (Appellant Proof Brief at 42). They argue that the Company is profitable, so the district court should have just ignored the utter dysfunction at the governance level. But simply because an otherwise dysfunctional company not operating pursuant to its governance documents is profitable does not mean that it should continue to operate. *See, e.g.*, *Vila v. BVWeb Ties LLC*, 2010 WL 3866098, *6-*8 (Del. Ch., Oct. 1, 2010) (rejecting the argument that it is "reasonably practicable to continue" the LLC's existence because it was "earning a modest profit"); *Phillips v. Howe*, 2011 WL 4404034, *26 (Del. Ch., Sept. 22, 2011) ("The fact that [the LLC] has continued to operate marginally . . . is irrelevant to deadlock, because [the LLC] never operated *in conformity with the parties' agreement*.") (italics in original).

In *Kirksey v. Grohmann*, 754 N.W.2d 825 (S.D. 2008), the South Dakota Supreme Court found that there was "no dispute that the ranching and livestock operation, as a business, can continue despite the [member] sisters' dissension. However, the question is whether it is reasonably practicable for the company to continue *in accordance with* the operating agreement." *Id.* at 830. The court answered that question in the negative – that "[l]eaving two sisters, half the owners, with all the power in the operation of the company cannot be a reasonable and practicable operation of a business." *Id.* at 831.

Appellants argue that the district court, in ruling that Appellants' and Joe's 2015 contributions were valid and diluted Barkalow's and, with Appellants' 2016 contributions, Joseph Clark's interests and voting rights in the Company, effectively resolved the dysfunction by effectively making Appellants controlling members and breaking any continued deadlock. The district court addressed this very issue in its Ruling:

> Jeff and Bryan argue that many of the listed disputes have now been decided by the Court and that the LLC can continue to operate in a profitable manner. Although the Court has determined many of the disputes, it cannot repair the lack of trust in the relationship between Jeff, Bryan and Tracy. I note that the members bring their attorneys to company meetings. Jeff and Bryan have alleged that Tracy converted company funds to his own account. Conversion is the legal term used for theft. The Company is also operating now under an "Interim Management Agreement", so obviously all issues concerning ordinary governance procedures and operating the Company in the future have not been resolved and will continue to be future disputes if not dissolved. The Interim Management

> Agreement was entered into only to avoid the necessity of appointing a receiver or possibly issue a temporary injunction during the pendency of this lawsuit. I cannot ignore what I consider to be total dysfunction at the governance level.

(App. I at 298).

The district court recognized that its holding on the contributions would have given Appellants control of the Company, yet it still properly held that it was not reasonably practicable for the Company to continue given the members' dysfunctional relationship and distrust. Joseph Clark testified that he wanted the court to return the members to 25% interest and then divide up the Company's properties. He testified: "I don't believe that we can go on the way that we're going and not be back here in a couple of years with another situation." (Day 4 Trial Tr. at 152:10-153:6). The district court clearly relied on Joseph Clark's testimony that, regardless of controlling interest, dysfunction would prevail and that the court would face further member litigation if the company was not dissolved. So, the court made the most equitable decision it could – to dissolve the Company.

The district court's rationale is similar to that of the South Dakota Supreme Court's in the *Kirksey* case. In that case, the four related members "neither trust nor cooperate with each other," they "cannot communicate regarding the LLC except through legal counsel," and two members "hold all the power, with the other two having no power to influence the company's direction." *Kirksey*, 754 N.W.2d at 830. *Id.* Based on those findings, the court ordered dissolution because it was not

"reasonably practicably to carry on the LLC's business in conformity with its articles of organization and operating agreement." *Id.* The same rationale applies in this case, and the district court did not err in ordering the Company to be wound up and dissolved.

II. THE DISTRICT COURT PROPERLY ORDERED THAT THE PURPORTED CAPITAL CONTRIBUTIONS BE RECHARACTERIZED AS DEBT.

A. Standard for Review.

This Court reviews *de novo* the district court's ruling. *Baur*, 832 N.W.2d at 668.

B. Argument.

Barkalow sought and obtained a judicial order pursuant to Iowa Code § 489.701 that does the following: (i) recasts the 2015 and 2016 "contributions" as loans; (ii) declares that each of the four members be restored to their original 25% equity interest in the Company; and (iv) dissolves the Company. Appellants argue that the district court exceeded its statutory and equitable authority by recasting the 2015 and 2016 contributions as loans and setting the ownership interest back to 25% per member.

1. The Operating Agreement Does Not Control in the Judicial Dissolution Setting.

Appellants argue that the Company's operating agreement controls and that the district court exceeded its equitable and statutory authority by, as part of

its order for dissolution, recharacterized the Clarks' contributions as loans. Appellants argue that "[e]ven though the district court was acting in equity jurisdiction in dissolving Outside Properties, it was nonetheless constrained by Outside Properties' operating agreement and governing documents." (Appellant Proof Brief at 54). But the district court, ruling on judicial dissolution, is explicitly not constrained by the Company's governance documents. Iowa Code § 489.110 states that a company's operating agreement governs the company's activities and the relations among its members, except that an "operating agreement shall not "[v]ary the power of a court to decree dissolution in the circumstances specified in section 489.701, subsection 1, paragraphs 'd' and 'e'." *Id.* § 489.110(3)(g).

Appellants rely on *Felt v. Felt*, 928 N.W.2d 882, 2019 WL 2372321, * 7 (Iowa Ct. App., June 5, 2019), for the proposition that the district court could not have recharacterized the contributions as loans because the Company's governance documents allowed for such contributions, and the court exceeded its authority by ordering reclassification in contravention of the governance documents. The *Felt* case analyzed whether, under the terms of a limited liability company's operating agreement, there were any members added within ninety days following the death of the last member of the company. If no new members were properly added, the company would statutorily dissolve at the end of the

ninety-day period. The district court ruled that new members were added, but the court of appeals reversed, holding that "none of the unit holders of Felt Farms LLC complied with the contractual requirements for membership by signing a joinder agreement prior to the expiration of the ninety-day statutory period. Therefore, the LLC dissolved . . . ."

But the *Felt* case was not one for application for judicial dissolution under Section 489.701(1)(d) or (e), and therefore is inapposite. As stated above, while an operating agreement usually controls governance issues, an operating agreement does not control the court sitting in equity upon an application for dissolution. The court can shape whatever equitable relief it believes is most appropriate under the circumstances of the particular case. In this case, the district court properly held that recharacterizing the contributions as loans as part of the dissolution was the best way to work out the equities between the members.

In support of their argument that the court did not have authority to recharacterize the contributions to loans, Appellants rely on the Court of Appeals' decision in *Maschmeier v. Southside Press, Ltd.*, which the Supreme Court declined to follow in *Baer*. 435 N.W.2d 377 (Iowa Ct. App. 1988). In *Maschmeier*, the court found that its equitable authority allowed it to order the majority stockholders to purchase the stock of the oppressed minority

stockholders. Appellants latch onto the fact that the court then ordered that "the method of payment should be in a manner consistent with the bylaws." *Id.* at 383. But Appellants fail to mention that the court affirmed the district court's order of the buyout despite there being buyout provisions in the bylaws, and that court ordered the buyout only once the stockholders were unable to agree on how to exercise the provisions of the bylaws. *Id.* at 382-83. There, as here, the court exercised its equitable authority in a dissolution action and ordered a buyout – and the value of said buyout – when there was corporate dysfunction requiring such action.

2. Iowa Code § 489.701(2) Does Not Preclude a Court from Providing Equitable Relief in Addition to Dissolving a Company Based on it not being Reasonably Practicable to Carry on the Company's Activities.

Iowa Code § 489.701(2) states that a "court may order a remedy other than dissolution" in a proceeding for dissolution based on member oppression under 701(1)(e). Appellants argue that this subsection means that courts are only allowed to grant relief other than dissolution in oppression cases, and not in cases based on impracticability of carrying on the company's activities in conformance with the governance documents. Appellants' argument fails for several reasons. First, nothing in the statute, the comments following Section 701 of the Uniform Limited Liability Company Act, (https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx

?DocumentFileKey=e4ceb7e3-92e4-7d79-c8f9-912e670bef23&forceDialog=0 at 151-55), or any caselaw supports Appellants' argument that Section 489.701(2) prevents a court from granting ancillary equitable relief as part of its decision to dissolve a LLC based on member dysfunction. Simply because the statute allows for allows for relief BESIDES dissolution in the one instance does not mean that the statute does not allow for relief IN ADDITION TO dissolution in the other. *Krull v. Thermogas Co.*, 522 N.W.2d 607, 612 (Iowa 1994) ("In searching for legislative intent, we are bound by what the legislature said, not by what it should or might have said. So we cannot under the guise of statutory interpretation enlarge or otherwise change terms of a statute.").

Second, Iowa courts and other courts routinely hold that the district court's equitable powers are expansive, and further hold that, where the statute does not provide an exclusive remedy or otherwise forbid the court from exercising its equitable jurisdiction, the court has the power to craft an equitable remedy given the certain facts of each case. "The court, sitting in equity, has considerable flexibility in resolving the dispute" concerning company liquidation. *Baur*, 832 N.W.2d at 677 and Iowa Code sections and cases cited therein. "[T]he invocation of equity jurisdiction permits the necessary reach and flexibility in working out the equities among these parties." *Moser v. Thorp Sales Corp.*, 256 N.W.2d 900, 907 (Iowa 1977); *see also Holi-Rest, Inc. v. Treloar*, 217 N.W.2d 517, 526-27 (Iowa

1974) ("That this court has the power in equity to fashion such relief is beyond dispute. . . . If based on sound principles, and beneficent results follow their enforcement, affording necessary relief to the one party without imposing illegal burdens on the other, new remedies and unprecedented orders are not unwelcome aids to the chancellor to meet the constantly varying demands of equitable relief."); *Holden v. Construction Mach. Co.*, 202 N.W.2d 348, 363-64 (Iowa 1972) ("Wherever a situation exists which is contrary to the principles of equity and which can be redressed within the scope of judicial action, a court of equity will devise a remedy to meet the situation, though no similar relief has been given before."); *Bankers Surety Co. v. Linder*, 137 N.W. 496, 499 (Iowa 1912) ("[T]he power of a court of equity is not limited to settling the rights of the parties upon what has been done in the past, but it reaches forth and declares their duties and rights for the future.")..

The district court deciding a judicial dissolution action sits in equity, and 489.701 does not provide exclusive remedies or otherwise explicitly limits the scope of the court's equitable jurisdiction. *See, e.g.*, 27A Am. Jur. 2d Equity § 214. Therefore, "all inherent equitable powers of the district court are available for the proper and complete exercise of the court's equitable jurisdiction . . . ." *Id.*; *see also id.* § 216 ("Once the legislature has created a statutory equitable remedy, unless a court's inherent equitable powers are explicitly restricted by the

statute, the court retains the power to exercise jurisdiction, to do equity, and to mold each decree to the necessities of the particular case.").

Iowa's business corporation dissolution statute only specifically calls for dissolution as a remedy, Iowa Code § 490.1430, yet Iowa courts are allowed to "fashion other equitable relief" aside from dissolution. *Sauer v. Moffitt*, 363 N.W.2d 269, 275 (Iowa 1984) (holding that while the statute only explicitly allows for dissolution, the district court is allowed to "fashion other equitable relief," including partial liquidation and redemption of the plaintiffs' shares). Iowa courts have "long recognized a court's equitable power in a shareholder proceeding seeking judicial dissolution . . . to instead order majority shareholders to purchase the shares of the minority . . . ." *Heidecker Farms, Inc. v. Heidecker*, 791 N.W.2d 429, *11 (Iowa Ct. App., Oct. 6. 2010). As acknowledged by Appellants in their Final Pretrial Statement, Iowa courts examining dissolutions of LLCs look to Iowa decisions regarding corporate dissolutions. (App. I at 91, citing *Morse v. Rosendahl*, 2016 WL 3273725, *5-6 (Iowa Ct. App., June 15, 2016) and *Rothgeb v. Axis Grp. Holdings, LLC*, 2013 WL 6278639, * 4 n.2 (S.D. Iowa, Feb. 25, 2013)). Given that Iowa courts may provide equitable remedies beyond dissolution of a corporation – despite the statute only allowing for dissolution – the district court did not err by providing additional equitable relief (recategorizing the contributions as debt) as part of its order for dissolution.

Similarly, the New York limited liability company judicial dissolution statute, NY Limit. Liab. Co. § 702, is nearly identical to Iowa Code § 489.701(1)(d)(2). It reads: "On application by or for a member, the supreme court in the judicial district in which the office of the limited liability company is located may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement." *Id.* While this statute, like Section 489.701(1)(d)(2), only provides for dissolution, New York courts specifically state that Section 702's "statutory remedy of dissolution is equitable and the court may fashion a remedy suitable to the circumstances." *Flax v. Shirian*, 3 N.Y.S.3d 284, *9 (N.Y. Supreme Court 2014); *see also Mizrahi v. Cohen*, 104 A.D.3d 917, 920 (N.Y. S. Ct., App. Div., 2013) (holding that while "[t]he Limited Liability Company Law does not expressly authorize a buyout in a dissolution proceeding . . . in certain circumstances, a buyout may be an appropriate equitable remedy upon the dissolution of an LLC." (internal citations omitted)); *In re Superior Vending, LLC*, 71 A.D.3d 1153, 1154 (N.Y. S. Ct., App. Div., 2010) (ruling that, "[a]lthough the Limited Liability Company does not expressly authorize a buyout in a dissolution proceeding," a buyout was a proper equitable remedy).

Federal courts hold that "[w]here Congress allows resort to equity for the enforcement of a statute, all the inherent equitable powers of the district court are

available for the proper and complete exercise of the court's equitable jurisdiction, unless the statute explicitly, or 'by a necessary and inescapable inference,' limits the scope of that jurisdiction." *F.T.C. v. Security Rare Coin & Bullion Corp.*, 931 F.2d 1312, 1314 (8th Cir. 1991) (quoting *Porter v. Warner Holding Co.,* 328 U.S. 395, 397–98, 66 S.Ct. 1086, 1088–89, 90 L.Ed. 1332 (1946)).

Nothing in Section 489.701 limits the scope of the court's jurisdiction to provide the appropriate equitable relief. The statutory remedy is equitable, and the district court, sitting in equity, has the ability to fashion the appropriate relief given the circumstances. No court has ruled that Section 701 of the Revised Uniform Limited Liability Company Act limits the available equitable relief to dissolution in "not reasonably practicable" cases. That the statute states that relief other than dissolution may be granted in cases of oppression should not be interpreted to bar a district court from granting additional equitable relief as part of its order for dissolution in "not reasonably practicable" cases.

3. The Court Had Adequate Grounds to Order the Additional Equitable Relief.

Not only did the district court have the authority to grant the relief it did, it also has reasonable bases for doing so. The district court clearly looked to the testimony and requests for relief submitted by Joseph Clark. The district court found Joseph Clark to be a credible witness and cited to his unsuccessful attempts to "act as a peacemaker between Tracy and [Joe's] brothers" in its analysis of whether it

was "reasonably practicable" for the Company to continue to operate. (App. I at 297-98). Joseph Clark testified that "I don't believe that we can go on the way that we're going and not be back here in a couple of years with another situation." (Day 4 Trial Tr. 152:10-153:6). He asked the court to provide the relief which the court ended up granting – recategorize the 2015 and 2016 contributions as loans, (App. I at 229, 232), and order the dissolution of the Company based on it not being "reasonably practicable" to carry on the Company's activities based on the member dysfunction. (*Id.* at 223-24, 236). He requested that the contributions be recategorized as loans despite taking part in the 2015 contribution. Joseph Clark requested the same relief as Barkalow, and the district court concluded that such relief was the most equitable relief to provide under the circumstances.

Appellants claim that Barkalow will receive a windfall based on the district court returning the members to their original – and correct – 25% ownership interest. Appellants argue that Barkalow "stands to receive a return of approximately ten times his initial investment ($422,937) even though in the district court's words, 'he had not contributed one dollar toward this growing business . . . .'" (Appellant Proof Brief at 64, quoting from App. I at 280). There are a few issues with Appellants' argument and the court's statement. First, prior to the December 2015 contribution, none of the members had contributed anything more than their initial $41,000 capital contributions. The Company had funded its operations through debt financing, with

none of the members making any further contributions. Second, if the members are returned to their initial ownership interest, **all** the members – and not just Barkalow – will receive a return of approximately ten times their initial investment. Additionally, the Clarks will receive their recategorized loans with an annual rate of return of 3.85%, which breaks out to roughly $31,144.77 per year each for Bryan and Jeffrey, and $12,857.31 per year for Joe.

Third, if this Court reverses the district court's recategorization of the contributions to loans and Barkalow is left with a membership interest of 1.94% or below, then that would produce a windfall to Jeffrey and Bryan. To explain, if the stipulated valuation figures submitted at trial hold up upon liquidation, (App. II at 219), then, under Appellants' proposal, Barkalow's initial $41,000 contribution made in 2009 would result in Barkalow receiving $79,037 upon liquidation. Assuming for sake of argument that liquidation takes place in 2020, Barkalow would net $38,037 eleven years after his $41,000 investment, so an 8.4% average annual return. Conversely, under Appellants' argument, they each would receive $1,636,552 upon liquidation. Assuming they receive the same $79,037 for their initial $41,000 contribution in 2009 that Barkalow received for his, that would leave a return of $1,557,515 for their $808,955 "contributions" made in December 2015 and Jun 2016. Again, assuming for sake of argument that liquidation takes place in

2020, Appellants would net $748,560 some five years after the December 2015 contribution, so roughly a 18.5% average annual return.

Therefore, based on all of the above, the district court did not err in recategorizing the contributions as loans as part of its order for dissolution of the Company.

III. THE DISTRICT COURT ERRED BY NOT ORDERING DISSOLUTION BASED ON DEFENDANTS' OPPRESSION.

A. Preservation of Error.

Barkalow preserved error on this issue by presenting evidence regarding Appellants' oppressive conduct at trial, and by further briefing the legal issues in plaintiffs' Post-Trial Brief, Post-Trial Reply Brief, and Rule 1.904(2) Motion to Reconsider, Enlarge or Amend. (App. I 111-13, 130-39, 245-49, 301-10). The district court addressed the issue by denying dissolution based on oppression in its Ruling, (App. I at 278-81), and by denying plaintiffs' Rule 1.904(2) Motion. (App. I 311-15).

B. Standard for Review.

This Court reviews *de novo* the district court's ruling. *Baur*, 832 N.W.2d at 668.

C. Argument.

The district court erred by not ordering the dissolution the Company pursuant to Iowa Code § 489.701(1)(d)-(e). Court-ordered dissolution of an LLC is

appropriate if the members in control of the company have acted in a manner that is oppressive and directly harmful to the applicant (Barkalow). Iowa Code § 489.701(1)(e)(2). Barkalow sought relief pursuant to Iowa Code § 489.701 based on the Defendants' oppressive conduct that directly harmed him, namely the purposeful dilution of his ownership interest in the Company in 2015 and again in 2016.

Majority members act oppressively when their actions frustrate the reasonable expectations of the minority members. *Baur*, 832 N.W.2d at 674. "The determination of whether the conduct of controlling directors and majority shareholders is oppressive . . . and supports a minority shareholder's action for dissolution of a corporation must focus on whether the reasonable expectations of the minority shareholder have been frustrated under the circumstances. We need not catalogue here all the categories of conduct and circumstances that will constitute oppression frustrating the reasonable expectations of minority shareholders' interests." *Id.* Whether a dilution event constitutes oppression and a frustration of a member's reasonable expectations is a question that depends on the circumstances of each case. *Compare Matter of Twin Bay Vil., Inc. v. Kasian*, 153 A.D.3d 998, 1003 (N.Y. App. Div. 3d Dept. 2017) ("[W]e discern no basis to disturb Supreme Court's determination that petitioners' reasonable expectations were substantially defeated by respondents' oppressive actions in 2001, 2004 and 2009 inasmuch as

those actions intentionally diluted and ultimately sought to extinguish petitioners' ownership interest in the corporation.") *with Estate of Lawrence v. Quail Aero Serv. (In re Dissolution of Quail Aero Serv.)*, 300 A.D. 2d 800, 806 (N.Y. App. Div. 3d Dept. 2002) ("[D]ilution of the value of the minority shareholder's stock will not amount to oppressive conduct when the minority shareholder is given an opportunity to supply capital and thereby maintain its percentage interest in the corporation.").

1. The District Court Erred by Holding that Barkalow's Reasonable Expectations Were Not Frustrated by Appellants.

Appellants frustrated the reasonable expectations of Barkalow to not be required to contribute additional capital and not have his ownership interest diluted. They did so by requiring Barkalow to contribute capital in 2015 and 2016 or face dilution of his ownership interest, and thereafter by unilaterally contributing capital without a legitimate business basis for doing so and for the sole (or predominant) purpose of diluting Barkalow's interest.

To explain, the Certificate of Organization states that "no additional capital contributions will be required." (App. I 391-94). Barkalow testified that he took this provision to mean that after the members made their initial capital contributions, none of the members would have to put more money into the Company. (Trial Tr. Vol. 1 at 60:19-61:10). He had that understanding because, at the time the LLC was formed, only one property purchase was contemplated.

(*Id.*). Barkalow's expectation to not have to put in additional capital did not change as the Company acquired additional properties, because the Company acquired these properties through debt financing and/or seller financing. (Statement of Facts § I, *supra*). Aside from the down payment on the Company's first property purchase, the entirety of the Company's operations was funded through debt and seller financing. (*Id.*). Given that, it was reasonable for Barkalow to expect that he would not be required to contribute additional capital.

While the Company's Operating Agreement states that member meeting quorums and voting rights (if demanded) shall be determined by the capital contribution of each member, (App. I at 325, §§ 2.5 & 2.7.1), nothing in the Operating Agreement allows for (i) unilaterally capital contributions; or (ii) a member making demand of another to make an equal capital contribution or face dilution of his ownership interest. The governance documents do not allow for the contribution events described herein, especially given that the actions taken were for the wrongful purpose of diluting Barkalow.

The Defendants frustrated the reasonable expectations of Barkalow to not be required to contribute additional capital and not have his ownership interest diluted. They did so by requiring Barkalow to contribute capital in 2015 and 2016 or face dilution of his ownership interest, and thereafter by unilaterally

contributing capital without a legitimate business basis for doing so and for the sole (or predominant) purpose of diluting Barkalow's interest.

2. The 2015 and 2016 Contributions Were Required, in Violation of the Company's Governance Documents.

The district court disagreed with Barkalow and ruled that Appellants' actions were not oppressive and that dissolution was not warranted on oppression grounds. The district court held that the capital contributions were "neither 'unilaterally' made nor required of Tracy." (App. I at 281). The court held that the contributions were not unilateral because "Tracy was given the opportunity to contribute equally in both capital calls," and they were not required because "he did not in fact make any additional contributions." (*Id.*). "Having been given the opportunity to make an equal contribution to protect his proportionate interest in Outside Properties, and choosing not to participate in either capital call, Tracy lack the ability to prevent the other members from doing so." (*Id.* ("The undisputed facts that Tracy was offered an opportunity to participate in both capital calls and declines precludes Tracy's claim of oppressive conduct as a matter of law.").

The district court accepted Jeffrey Clark's and Bryan Clark's primary argument that Barkalow was not "required" to contribute capital – he had the option to do so, but if he did not, his ownership interest would be diluted to below 1% of the Company. Their argument and the district court's acceptance

of it fundamentally misunderstands what "required" means. "Require", in this context, is defined as "to impose a compulsion or command on; compel." Merriam-Webster Dictionary. The Defendants compelled Barkalow to make these contributions or face repercussions – the dilution of his ownership in the Company. There was nothing voluntary about these contributions. And even Joseph Clark, who participated in the 2015 contribution only to then have Jeffrey and Bryan dilute him when he refused to participate in the 2016 contribution, acknowledges that these contributions were required, and therefore in violation of the Company's Certificate of Organization. In his post-trial brief, Joseph Clark states:

> Implicit in this provision [of the Certificate of Organization] that the Company cannot require a member to make additional capital contributions is that there are no negative consequences (dilution) to a member for not making an additional capital contribution. . . . There is nothing voluntary about making a capital contribution when you are forced to make the additional capital contribution because if you don't your proportionate ownership interest will be decreased (diluted). In other words, capital contributions become mandatory and required when the consequence of not making the capital contribution is decrease in your ownership interest (dilution) in the Company.

(App. I at 231).

The district court held that while Barkalow was not required to make such contributions, "he also cannot prevent other members from contributing additional capital under certain conditions." (*Id.* at 280 ("Tracy seeks instead to

force the Clarks to make loans to the Company while he is free to use his assets to make investments in his other enterprises.”)). In objecting to the purported contributions, the court held, Barkalow “is attempting to possess a veto power that prevents any additional capital being contributed into the Company unless he agrees to it (as a minority member).” (*Id.*). Barkalow is doing no such thing. He is just objecting to these contributions which violated the Certificate of Organization, frustrated his reasonable expectations as a minority member of the Company, and damaged him by diluting his interest in the Company down to a fraction of 1%.

3. The Capital Calls Were Not Supported by a Legitimate Business Purpose and Were Instead for the Purpose of Diluting Barkalow’s Interest in the Company.

The district court also held that the capital calls “were supported by a legitimate business purpose.” (*Id.*). Regarding the first call to repay the Shultz loan, the district court held that “Tracy cannot seriously dispute that there was as legitimate business purpose for the contributions, only whether the contributions should be considered loans or equity.” (*Id.*). Regarding the second call to repay the Clark family loans, the district court acknowledged that the loans were current, but that the “Clark entities had made demands for repayments of the loans, which had no set due date.” (*Id.*). The district court apparently deemed Clarks’ demand for repayment as the “legitimate business purpose” for the second capital call.

The court then stated that "Tracy fails to acknowledge that any time money or capital was needed for this LLC it was obtained from the Clarks or the Clark family entities," and that Barkalow "had not contributed one dollar towards this growing business and had for the majority of the time been treated as an equal partner. It is fair to say that the evidence clearly shows that Tracy was a difficult partner." (*Id.* at 280-81). The district court was simply wrong in finding that the Clarks and the Clark family entities were the sole source of money for the Company. As stated above, the Company also used bank loan financing and seller financing to acquire its properties. Furthermore, aside from the initial capital contributions, before the December 2015 contribution, all Clark family funds were loaned to the Company and booked as Company debt. The source of the debt financing should have had no impact on the internal dynamics of the Company and its members, nor the district court's analysis of whether Appellants oppressed Barkalow. Having control of the purse strings does not give majority members a basis for oppressing a minority member – even a "difficult" one – by diluting his membership interest down to below 2%.

a. Appellants Had Been Contemplating Diluting Barkalow's Interest Since 2013.

The district court erred in not recognizing the clear fact pattern presented at trial that Jeffrey Clark and Bryan Clark had been contemplating diluting Barkalow out of the Company since 2013, the year in which the relationship

between Barkalow and Jeffrey and Bryan Clark significantly deteriorated. (*See* Statement of Facts § II, *supra*). As explained above, in late 2013, Jeffrey Clark requested information from Company accountant Wagner on how to dilute Barkalow's interest in the Company. Wagner determined that if all Clark family debt (with the exception of $95,000 owed to Jeffrey Clark) was transferred "to equity as capital contributions," each of the Clark brothers' ownership interest in the Company would increase to 32.5% and Barkalow's interest would decrease to .83%. (App. II at 197). Of course the dilution analysis done by Wagner at Jeffrey Clark's request is exactly what played out when the Appellants were finally presented an opportunity to dilute Barkalow in 2015.

b. The 2015 Contributions.

When the Shultz loan came due in December 2015, the Clarks took advantage of the situation to proceed with diluting Barkalow's interest in the Company from twenty-five percent to one-tenth of one percent. (App. I at 436). While the Clarks claim that a member capital call was the only way in which to obtain funds to pay off the Shultz debt, the evidence and testimony submitted by Barkalow shows that the Company had other sources of funds available to it to pay the Shultz debt. (*See* Statement of Facts § IV, *supra*). Despite debt financing being available to fund the Shultz payoff, the Clarks chose to unilaterally contribute capital to pay off the Shultz debt without a member vote, and in doing

so, increased their ownership and diluted Barkalow's ownership in the Company. (App. I at 436). While the Clarks claim that they were not considering the effect on ownership interest when they made the contributions in 2015, Wagner's notes and Jeffrey Clark's email from that December 2015 time period show that dilution of Barkalow's interest was at the forefront of the Clarks' minds when they unilaterally contributed the funds to pay off the Shultz debt in December 2015.

c. The 2016 Contributions.

While the 2015 capital contribution was done to oppress Barkalow and dilute his interest, at least the Clarks could point to the Shultz payoff as a reasonable excuse for making the capital contributions. Appellants have no such reasonable excuse for diluting Barkalow's and Joseph Clark's interest in 2016. While Jeffrey and Bryan Clark claim that the Clark family loans were past due, in default, and in jeopardy of not being repaid because of Barkalow's refusal to honor their terms, as of January 2016, the Company was servicing the Clark family loans, the loans were not past due or in default, and the Company had a schedule pursuant to which it would repay the loans with interest over a 10-year period. (*See* Statement of Facts § V, *supra*).

The district court found that "the Clark entities had made demands for repayment of the loans, which had no set due date." (App. I at 280). But there

is no evidence corroborating that the Clark entities had made demands to Outside Properties for repayment of their loans, and certainly no evidence supporting the basis for such demands, given that the Company was repaying such loans pursuant to a 10-year amortization schedule. (*See* Statement of Facts § V, *supra*). In addition to wanting to further dilute Barkalow's interest in the Company, Appellants also put the interests of the Clark family and the Clark family entities before the interests of the Company and its other members, Barkalow in particular. The Company simply had no legitimate business reason to prepay the Clark family loans.

The evidence submitted at trial – and largely overlooked by the district court – proved that the actual reason for paying off these loans was to further dilute Barkalow out of the Company. (*See* Statement of Facts § V, *supra*). The Company's meeting minutes created by the Appellants' then-attorney, and e-mails between the e-mails between the Clarks' attorney, Paul Morf, and Wagner clearly show that the primary objective in making the 2016 contribution was to further dilute Barkalow. (*Id.*). Furthermore, Appellants funded at least part of this 2016 contribution from a loan from Iowa-Illinois Square LLC, one of the same Clark family entities that was paid off by the Company with funds from the 2016 contribution. (*Id.*). Joseph Clark did not participate in the 2016 contribution because borrowing money from one of the same sources of the original debt did

not make sense to him. (*Id.*). And he is correct, if the goal was to pay off Clark family debt, then borrowing from a Clark family entity to do so does not make any sense. Jeffrey and Bryan Clark's actions only make sense if their real goal was to find the necessary funds to be able to further dilute Barkalow through the contribution.

Given all of the above – that the Clark family loans were being serviced, were not past due or in default or in jeopardy of not being repaid; that Jeffrey and Bryan Clark borrowed the funds for the 2016 contribution from one of the same Clark entities that the Company was prepaying its existing loan; and that the e-mails subsequent the February 2016 meeting clearly show dilution of Barkalow was of primary concern to the Clarks' attorney and their accountant (also the accountant for the Company) – this Court should conclude that which the district court failed to, which is that the 2016 contribution was made for oppressing Barkalow, diluting his interest, and frustrating his reasonable expectations as a member of the Company.

The district court concluded that "Tracy understood he was a minority member when he joined Outside Properties as a member in 2009. . . . Tracy has had ample opportunity to get out of Outside Properties, which is all he is entitled to expect as a minority interest holder." (App. I at 281). But Barkalow has not had "ample opportunity" to exit Outside Properties with fair value for his

ownership interest. While the district court concluded that Appellants' offers at the 2016 meetings were "fair," they were far from it. Appellants made two offers, only one of which was an opportunity for Barkalow "to get out of Outside Properties." The Clarks first offered to buy out Barkalow for "undiscounted fair market value of his units," "with the fair market value of the other assets and liabilities of the Company to be based on the December 31, 2015, financial statement provided by the Company's accountant, Jason Wagner at RSM." (App. I at 406). But the year-end 2015 financial statement reflected the 2015 capital contributions by the Clarks which Barkalow objected to, and therefore any buyout figure would have reflected Barkalow's diluted ownership interest. (App. II at 22-24). The second offer was not a buyout, but to "to restore the Company to the initial posture of each of the four Members having equal 25% votes, if Tracy would agree to certain terms, including mutual global releases by all members and their respective entities." (App. I at 406). While not a buyout offer, this offer was an attempt get Barkalow to release his and his entities' claims against the Clarks in exchange for that which Barkalow understood he was already entitled to – his equal 25% ownership interest in the Company. It was not a fair offer, and this Court should not hold against Barkalow his rejection of these two offers.

Based on all of the above, the district court erred in not ordering that the member oppression required dissolution of the Company and recategorization of the contributions as loans.

IV. BREACH OF FIDUCIARY DUTY.

A. Preservation of Error.

Barkalow preserved error on this issue by presenting evidence regarding the Clarks' breach of fiduciary duties at trial, and by further briefing the legal issues in plaintiffs' Post-Trial Brief and Post-Trial Reply Brief. (App. I 113-15, 142-43, 250-52). The district court addressed the issue by denying Barkalow's claim in its Ruling. (App. I at 280-81).

B. Standard for Review.

"Breach of fiduciary duty is an equitable claim." *Weltzin v. Nail*, 618 N.W.2d 293, 299 (Iowa 2000). Therefore, this Court reviews *de novo* the district court's ruling. *Baur*, 832 N.W.2d at 668. In its review of factual findings, this Court gives weight to the lower court's findings, particularly on the credibility of witnesses, but this Court is not bound by the lower court's findings. *In re Trust of Trimble*, 826 N.W.2d 474, 482 (Iowa 2013). Review of a lower court's interpretation of statutory provisions is for correction of errors of law. *Id.*

C. Argument.

In order to recover on a breach of fiduciary claim, a claimant must show (i) the existence of a fiduciary relationship; (ii) defendants breached that fiduciary relationship; (iii) the breach of duty caused damage to the claimant; and (iv) the amount of damage. Iowa Civ. Jury Inst. 3200.1 (citing Restatement (Second) of Torts § 874). The members of an LLC owe each other and the company the duty of loyalty and the duty of care. Iowa Code §489.409. Majority members owe an obligation to minority members to conduct themselves in a manner that is not oppressive to the minority members. Majority members act oppressively when their actions frustrate the reasonable expectations of the minority members. *Baur*, 832 N.W.2d at 674.

For all of the reasons stated above, Appellants and Joseph Clark have breached their fiduciary obligations to Barkalow by engaging in oppressive conduct which resulted in the frustration of Barkalow's reasonable expectations. The Clarks frustrated the reasonable expectations of Barkalow to not be required to contribute additional capital and not have his ownership interest diluted. They did so by requiring Barkalow to contribute capital in 2015 and 2016 or face dilution of his ownership interest, and thereafter by unilaterally contributing capital without a legitimate business basis for doing so and for the sole (or predominant) purpose of diluting Barkalow's interest.

Without elaboration or any analysis of the expert testimony and evidence submitted at trial clearly evidencing Barkalow's damages based on dissolution, the district court held Barkalow "failed to provide evidence of his damages under the methodology required by the Iowa Supreme Court. (Ruling at 20, citing the Iowa Court of Appeals' *Baur* decision, *Baur v. Baur*, 885 N.W.2d 829, 2016 WL 4036105 (Iowa Ct. App. 2016)). Contrary to the district court's holding, Barkalow submitted detailed evidence supported by expert testimony as to how the Clarks' dilution of his interest has damaged him. Appellants', and, to a lesser extent, Joseph Clark's actions caused Barkalow's ownership interest (and corresponding net value) to be diluted exponentially. If the transactions at issue are allowed to stand, Barkalow's equity interest was diluted from 25% prior to the 2015 purported contribution, to just over 0.5% following the 2016 purported contribution. (App. II at 207 lists Barkalow's interest at 0.5005% but App. II at 208 lists Barkalow's interest at 0.5950%). This dilution has caused net value of Barkalow's membership interest to decrease from $477,163 (net value if contributions treated as loans with 30-year fixed rates of 3.85% (2015) and 3.65% (2016)) to $79,037 (net value if contributions treated as such). (App. II at 231 & 667; Trial Tr. Vol. 2, 65:14-71:25). If the Court's ruling does not result in the Company being dissolved and the recategorization of the contributions as loans, Barkalow seeks damages in

the amount of $398,126, which is the difference of net value of his ownership interest if contributions are treated as such instead of loans.

CONCLUSION

For the reasons stated above, this Court should affirm the district court's ruling dissolving Outside Properties, LLC and further ordering that the contributions be recategorized as loans, and that the members each be restored to their original 25% ownership interest. Alternatively, if the Court rules that the district court erred by ordering dissolution under the "reasonably practicable" standard, the Court should reverse the district court's ruling denying dissolution and equitable relief based on member oppression. Alternatively, if the Court overturns the district court on dissolution under the "reasonably practicable" standard, and affirms the district court's denial of relief based on member oppression, then the Court should reverse the district court's ruling on Barkalow's breach of fiduciary claim and remand directing the district court to enter judgment in Barkalow's favor in the amount of $398,126.

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I, Wesley T. Graham, hereby certify that I electronically filed the foregoing document with Clerk of the Supreme Court of Iowa using the Iowa Judicial System Electronic Document Management System, which will send notification of such filing to the counsel below on the 11th day of August, 2020.

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