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SC Court of Appeals

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM GREENVILLE COUNTY
Court of Common Pleas, Business Court Program

R. Lawton McIntosh, Circuit Court Judge

Appellate Case No. 2020-001645
Case No. 2019-CP-23-00998

McMillan Pazdan Smith, LLC, ... Plaintiff/Counterclaim Defendant-Respondent,

v.

Donza H. Mattison,. . . . . Defendant/Counterclaimant-Appellant,

---

Donza H. Mattison, in a Derivative Capacity on Behalf of McMillan Pazdan Smith, LLC,. . . . . Third-Party Plaintiff-Appellant,

v.

Rondald G. Smith, Joseph M. Pazdan, Brad B. Smith, and Chad C. Cousins.. . . . . Third-Party Defendants-Respondents.

SUPPLEMENTAL BRIEF OF APPELLANT

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Pursuant to the Clerk's letter of June 5, 2024, Appellant, Donza H. Mattison, by and through her undersigned counsel, hereby submits this Supplemental Brief of Appellant to discuss the applicability of the holdings in Boathouse at Breach Inlet, LLC, by and through its member, Laurence O. Stoney, Jr. v. Stoney, 442 S.C. 633, 900 S.E.2d 483 (Ct. App. 2024), to the instant case. As set forth in detail below, the Stoney case is directly on point with respect to several of Appellant's arguments and fully supports Appellant's position that the Circuit Judge erred in granting summary judgment to Respondents/Third-Party Defendants in the derivative action brought by Appellant to remedy the alleged self-dealing and breaches of fiduciary duty by the managing members and COO of McMillan Pazdan Smith, LLC. Judge (soon to be Justice) Verdin's opinion in Stoney is a thorough and well-researched survey of derivative action case-law from other jurisdictions and fills a void of published appellate case-law on derivative actions in South Carolina. Under the standards expressly adopted by the Court in Stoney, the facts in the record in this case, taken in the light most favorable to Appellant, simply do not meet Respondents' burden to establish that Appellant would not fairly and adequately represent the interests of similarly situated members of the LLC in this derivative action, particularly if she is the only similarly situated member of the company as a "class of one."

As a preliminary observation, the procedural posture of the Stoney case was very different than that presented here. The Stoney case was an appeal from a full-blown, non-jury trial. Id. at 643, 900 S.E.2d at 489. Because the case was a matter of equity, the applicable standard of review allowed the appellate court to take its own view of the evidence in the record. Here, the appeal is from the dismissal of a case on summary judgment, when the facts in the record must be construed

in the light most favorable to the non-moving party, Appellant. Accordingly, the application of the holdings from Stoney is actually much more favorable to Appellant in the instant case.

From a factual standpoint, the Stoney case involved very analogous material facts to those presented here: a minority member of a closely held LLC, with less than 5% ownership interest, brought a derivative action on behalf of the LLC against the managing member, who had used the LLC to pay for personal expenses, to the tune of over $4 million dollars from the LLC with no realistic prospect of paying the money back; the managing member, who owned the real estate leased to the LLC restaurant, nefariously provided unfavorable lease terms to the LLC and shifted responsibility for repairing a bulkhead to the LLC; the managing member refused to let all of the other members see the financial records of the company; the managing member repeatedly said that he expected the other co-owners simply "to trust him"; and plaintiff was the only member of the LLC (other than the defendant's ex wife) who expressly supported the derivative action. Id. at 639-43, 900 S.E.2d at 486-88. The Stoney plaintiff's derivative action complaint alleged that the managing member of the LLC breached his fiduciary duties and authorized unlawful distributions to certain members not in accordance with their ownership shares.

The Stoney opinion held that a single dissenting shareholder of a corporation or member of an LLC can bring a derivative action on behalf of the corporate or company entity, under appropriate circumstances, even if that derivative action plaintiff does not have any support from any other shareholder or member. In other words, the Stoney court validated Appellant's ability to bring a derivative action against Respondents where, like here, all other members of the firm have disavowed such a claim. Under the holding of Stoney, the lack of support from other members of the LLC is not dispositive and does not, in and of itself, preclude a single member from bringing a

derivative action on behalf of the company. The key issue is whether, "in the totality of the circumstances," the purported derivative action plaintiff can "fairly and adequately" represent the interests of the company on whose behalf she is suing. The two fundamental questions as clearly stated by Stoney are whether the derivative plaintiff "'will vigorously pursue the suit and [whether] the remedy sought is in the interests of the corporation.'" Id. at 648, 900 S.E.2d at 491 (quoting Cattano v. Bragg, 727 S.E.2d 625, 629 (Va. 2012)).

The Court of Appeals in Stoney expressly adopted the eight-factor test from Davis v. Comed, Inc., 619 F.2d 588, 593-94 (6th Cir. 1980), and the "totality of the circumstances" approach from the Virginia Supreme Court's decision in Cattano, in evaluating whether the derivative plaintiff can "fairly and adequately" represent the company's interests. Stoney, 442 S.C. at 645-47, 900 S.E.2d at 489-90. The degree of support from similarly situated shareholders or members is only one of the eight Davis v. Comed factors. The Stoney decision recognized that a court should not accept affidavits or statements from other non-majority members rejecting the derivative action at face value; instead, the court "must consider the other members' motivations for opposing [the derivative] action," such as personal gain or fear of retaliation. Id. at 647, 900 S.E.2d at 491. The Stoney opinion favorably cites to the Ninth Circuit's decision in Larson v. Dumke, 900 F.2d 1363, 1368 (9th Cir. 1990), which observed that the other, non-defendant shareholders "may have been motivated by individual interests, rather than the good of the corporation." Here, the fact that all of the other members of MPS were still employed by MPS and that Respondents thus had the power to set their bonuses and to terminate or continue their employment renders the boilerplate statements expressing disagreement with the derivative action essentially meaningless. Not only was Ms. Mattison in the unique position as the only member of the firm who did not have to fear retaliation by the Third-

Party Defendants in her employment or compensation, she also had much greater access to the financial records of MPS than any other non-managing member of the firm, after she obtained such documents as part of the valuation process for her membership units following her resignation of employment.

The Stoney opinion validates a number of arguments that Appellant made in her previous briefs, primarily under Arguments 1 and 6. For example, Appellant made the identical "plain language" argument based on the wording of S.C. Code Ann. § 33-44-1101 and Rule 23(b)(1), SCRCP, that a single shareholder or member can bring a derivative action. Compare Final Br. of App., at 37, with Stoney, 442 S.C. at 644, 900 S.E.2d at 489 ("[U]nder the plain language of the statute and applicable rule, as single member of a limited liability company can bring a derivative action."). The Stoney case also cited with approval a number of cases that were relied upon by Appellant, including Angel Investors, LLC v. Garrity, 216 P.3d 944 (Ut. 2009); Jordan v. Bowman Apple Prods. Co., 728 F. Supp. 409, 412 (W.D. Va. 1990); Brandon v. Brandon Const. Co., 776 S.W.2d 349, 352 (Ark. 1989); Larson v. Dumke, 900 F.2d 1363, 1368 (9th Cir. 1990); Halsted Video, Inc. v. Guttillo, 115 F.R.D. 177, 179 (N.D. Ill. 1987); and HER, Inc. v. Parenteau, 770 N.E.2d 105, 112–13 (Ohio Ct. App. 2002).

The Stoney opinion discusses at length, and adopts the reasoning of, the Utah Supreme Court's decision in Angel Investors, which "recognize[d] that closely held corporations may be more vulnerable to malfeasance. Majority shareholders of closely held corporations have increased control over the corporation because they likely serve on the corporation's board; their dual roles can make malfeasance easier to conduct as well as justify. Likewise, the nature of a closely held corporation, where there is often a small number of shareholders and many of those may have close ties to each

other, lessens the likelihood that a minority shareholder will speak out against corporate malfeasance." Angel Investors, 216 P.3d at 951. In the Angel Investors case, the purported derivative plaintiff owned one percent of the corporation, and all of the other owners submitted affidavits stating that they did not support the Angel Investors' derivative action. Id. at 948. The Angel Investors court relied heavily on the Ninth Circuit case of Larson v. Dumke, which held that "a plaintiff may proceed with a derivative suite as a class of one where every other 'non-defendant shareholder has an economic interest in supporting the current management.'" Angel Investors, 216 P.3d at 950 (quoting Larson, 900 F.2d at 1368). The Stoney court was particularly concerned that "[i]gnoring the opposing shareholders' motivations [for not supporting the derivative action] could 'permit corporate looting and malfeasance in circumstances where all but one shareholder benefit personally from the illegality or are at risk of personal detriment were the malfeasance brought to light.'" Stoney, 442 S.C. at 647-48, 900 S.E.2d at 491 (quoting Angel Investors, 216 P.3d at 951) (emphasis added). Again, in our case, Ms. Mattison was the only member of MPS who was not also an employee of MPS at the time this derivative action was brought and who could act without fear of retaliation, intimidation, or retribution; therefore, she has standing to bring this action as a valid class of one.

The Stoney court also recognized that an individual shareholder of a corporation or a member of an LLC generally cannot bring a direct action against another shareholder, member, or manager for a loss that belongs to the company, unless that individual shareholder or member has a loss that is "'separate and distinct' from that of the company." Stoney, 442 S.C. at 650, 900 S.E.2d at 492. The Stoney court observed that "Laurence's claims in this action involved losses to the Company, rather than to his own membership interest, and also involve Richard's alleged breach of his

fiduciary duties to the Company; therefore, the claims must be brought in a derivative action. To deny Laurence standing in the derivative action would deny him and the Company a remedy, which we find is not the intent of Rule 23(b)(1)[, SCRCP]." Id. at 651, 900 S.E.2d at 493. Here, as Appellant previously argued in her final briefs, she could not have brought a direct action against the Third-Party Defendants because the losses belong to MPS, not her individually, since her losses were not "separate and distinct" from those of MPS. (Final Br. of App., at 40) (citing Ward v. Griffin, 295 S.C. 219, 221, 367 S.E.2d 703, 703-04 (Ct. App. 1998)). Accordingly, if Appellant were denied standing as an appropriate representative of MPS in this derivative action, the alleged malfeasance by Third-Party Defendants could not be remedied at all.

All of the Davis v. Comed factors other than the degree of support from other shareholders favor a finding that Ms. Mattison would "fairly and adequately" represent the interests of MPS in the derivative action. These are all factual matters, which again must be viewed in the light most favorable to Appellant at this stage of the proceedings. Although Respondents have tried to paint Ms. Mattison as vindictive towards the managing members of the firm, there is nothing in the record to support the Circuit Court's finding in that regard. Nevertheless, the Stoney court specifically recognized that "'[c]harged emotions and economic antagonism are virtually endemic to disputes in closely held corporation.'" Stoney, 442 S.C. at 648, 900 S.E.2d at 491 (quoting Cattano, 727 S.E.2d at 629). The Stoney court held that in addressing a derivative action involving a closely held company like MPS, the court must focus more on "'whether the totality of the circumstances suggest that the plaintiff will vigorously pursue the suit and that the remedy sought is in the interest of the corporation.'" Id. (quoting Cattano, 619 S.E.2d at 629). There can be no doubt that Ms. Mattison has been, and will continue to be, a vigorous pursuer of the wrongdoers in this case and that

recovering on the allegations of self-dealing and breaches of fiduciary duty she has made against the managing members, if proven to be true, would be in the interests of MPS as a separate corporate entity apart from its managing members. There is no conflict between Ms. Mattison's individual interests and those of MPS that would impede or interfere with her ability to pursue these claims. Accordingly, she is a proper derivative action plaintiff and should have been allowed to pursue this case on behalf of MPS in a derivative capacity.

CONCLUSION

In sum, the Stoney case presents compelling additional legal support for Appellant's arguments in this appeal. For all of the foregoing reasons, as well as for the reasons previously articulated in Appellant's prior briefs, Appellant respectfully requests that this Court reverse the Circuit Court's order granting summary judgment against Appellant on her derivative action.

Respectfully submitted,

June 20, 2024

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PROOF OF SERVICE

I certify that I have served the Supplemental Brief of Appellant on Respondents, McMillan Pazdan Smith, LLC, Rondald G. Smith, Joseph M. Pazdan, Brad B. Smith, and Chad C. Cousins, by email on June 20, 2024, addressed to their following attorneys of record: Samuel W. Outten and Miles Coleman, Nelson Mullins Riley & Scarborough LLP, 2 W. Washington St., Suite 400, Greenville, SC 29601; Thomas H. Keim, Jr. Ford Harrison, 100 Dunbar St., Suite 300, Spartanburg, SC 29306; and A. Mattison Bogan, Nelson Mullins Riley & Scarborough, LLP, 1320 Main St., 17th Floor, Columbia, SC 29201.

[Signature of Counsel on Following Page]

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