THE STATE OF SOUTH CAROLINA
In The Supreme Court

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Jun 28 2024

S.C. SUPREME COURT

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas
The Honorable Clifton Newman

C.A. No.: 2015-CP-10-05463

The Boathouse at Breach Inlet, LLC, by and through its member, Laurence O. Stoney, Jr., ...Respondent,

v.

Richard S.W. Stoney, individually and as Member-manager of The Boathouse at Breach Inlet, LLC and Crew Carolina, LLC, Defendants

and

Theodore Stoney, Jr., individually and as Trustee for Richard Stoney, Jr. and Gregory G. Holmes, Third-Party Intervenors, of whom

Richard S. W. Stoney is .....Petitioner.

RETURN IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Did the Court of Appeals apply the correct standard of review?

2. Did the Court of Appeals apply the correct legal analysis in considering whether the Boathouse at Breach Inlet, LLC ("Company"), by and through its member, Laurence Stoney, had standing to bring this derivative action?

3. Did the Court of Appeals correctly find that dissociation of Laurence Stoney's personal membership interest in the Company was improper?

INTRODUCTION[1]

In this action, the Company, by and through its member, Laurence Stoney, seeks to restore more than $4,000,000 siphoned from the Company by Richard Stoney, individually and as Member-manager of The Boathouse at Breach Inlet, LLC and Crew Carolina, LLC ("Crew Carolina") (collectively, "Defendants"). After a non-jury trial, the trial court declined to award any relief "[b]ased upon the finding that Laurence Stoney is not an appropriate representative in this shareholder derivative action and that he should be dissociated from the Company[.]" (R. at 35). The Court of Appeals determined that Laurence had standing to pursue relief on the Company's behalf and remanded the derivative claims for a determination on the merits. The Court of Appeals also reversed the trial court's dissociation of Laurence based on its analysis of S.C. Code Ann. § 33-44-601(6)(iii) and its finding that "the Defendants and Intervenors did not meet their burden of showing it was not reasonably practicable to carry on the business with him." (App. at 105).

For the most part, the parties agree on the facts. The primary difference between them lies with where their focus is placed: Laurence looks to the management of the Company, and Richard looks to Richard individually and his other business ventures. Richard, however, is not the Company, and those other ventures were and are different entities with different members. Richard's strategy for managing his various businesses may have helped support Richard's lifestyle and helped keep some of his other businesses afloat, but it did not serve the Company. For a variety of reasons, Laurence is the only member likely to seek to vindicate the Company's rights. The Court of Appeals correctly centered its analysis on the Company and determined that

[1] In order to minimize confusion as between members of the Stoney family, this return will refer to individual family members by their first names.

Laurence had standing to pursue this action and should not be dissociated from his membership interest in it.

Richard makes no mention of Rule 242, SCACR, and the considerations listed there for the Court's review. This may be because there is no dissent in the decision of the Court of Appeals; there is no conflict with prior decisions of this Court; and there is no substantial constitutional issue or federal question. Although there is little South Carolina law on "class of one" derivative actions, Richard did not include this issue in his petition for rehearing and the decision of the Court of Appeals is consistent with Rule 23(b), SCRCP and prior South Carolina law discussing derivative actions. For these reasons, this case does not warrant discretionary review by this Court.

COUNTER-STATEMENT OF THE CASE[2]

On October 9, 2015, Laurence filed this derivative action on behalf of the Company against Defendants, asserting claims for breach of fiduciary duty, conversion, recovery for unlawful distributions, unjust enrichment, and an accounting. (R. at 43-60). The Company also sought to impose personal liability on Richard, punitive damages, and an award of attorney's fees and costs. (*Id.*). Defendants filed an answer on November 12, 2015, asserting a general denial, failure to state a claim, the statute of limitations, laches, lack of standing under multiple theories, the business judgment rule, waiver and estoppel, and unclean hands and demanding the recovery of attorney's fees and costs. (R. at 60-67)

This action was assigned to the Business Court on December 9, 2016. (R. at 1). On June 22, 2017, Company members Theodore Stoney, Jr. (Richard's brother, "Ted") and Gregory G. Holmes (Richard's friend) (collectively, "Intervenors") intervened on Defendants' behalf.

[2] Respondent incorporates his brief and reply brief before the Court of Appeals by reference.

On March 29, 2018, Defendants and Intervenors filed a motion to bifurcate this action into two phases, arguing that the issue of Laurence's standing as a representative plaintiff was distinct from the issues of Defendants' liability and damages. (R. at 191-206). With the parties' consent, the trial court conducted a preliminary trial on standing on December 13-14, 2018. On May 20, 2019, the trial court issued a preliminary order determining that Laurence had standing to serve as representative plaintiff for the Company such that the case could proceed to trial on the merits. (R. at 5-17). The order included conclusions of law that this action seeking to recover Company assets was correctly brought as a derivative action; that laches did not bar Laurence from maintaining this action; and that Laurence could maintain this action and fairly and adequately represent the interests of the Company even if he was not supported by the Company's other members. (*Id.*).

On January 7, 2020, Defendants filed a motion to dissociate, seeking to expel Laurence from the Company. (R. at 211-57). The trial court conducted a hearing on Defendants' motion to dissociate and, on February 24, 2020, issued an order preliminarily denying Defendants' motion. (R. at 18-20).

The case proceeded to trial on March 9-11, 2020. Notwithstanding its finding that the Company had suffered more than $4,000,000 in losses at the hands of Defendants, the trial court issued an order filed on July 7, 2020 denying the Company any relief for lack of standing on Laurence's part and granting the motion to dissociate Laurence. (R. at 21-37).

The Company filed a motion to alter or amend on July 16, 2020. In that motion, the Company sought to correct certain factual errors and omissions and to address the omissions and errors of law in the order, including the following:

> 1. The trial court did not address whether Richard had unclean hands, whether the business judgment rule applied to his actions, or whether his actions were permitted under the business judgment rule if it applied.

2. The trial court did not apply the correct analysis in finding that Laurence could not maintain this action on the Company's behalf.

3. The trial court erred in finding that Laurence could have filed an action in his individual capacity under S.C. Code Ann. § 33-44-410.

4. The trial court erred by disregarding the fact that the Company is the real party in interest—not Laurence in his individual capacity. Accordingly, the trial court erred in granting Defendants relief against Laurence in his personal, individual capacity.

5. In addition, the trial court erred by misapplying S.C. Code Ann. § 33-44-601(6)(iii), which strictly evaluates whether it is reasonably practicable for a business to continue to operate with a given member n granting the motion to dissociate.

6. The trial court further erred by permitting Defendants to assert their equitable claim for dissociation without addressing whether Richard has unclean hands.

(R. at 258-64). The trial court denied the motion by order filed August 10, 2020. (R. at 38). This appeal followed.

In a decision dated April 3, 2024, a unanimous panel of the Court of Appeals reversed and remanded the derivative claims, finding that Laurence had standing and that the trial court should proceed on the merits. (App. at 93-108). The Court of Appeals reversed the portion of the trial court's order granting the motion to dissociate. (*Id.*).

Richard filed a petition for rehearing on April 18, 2024 (App. at 109-31), which was denied by order dated April 29, 2024 (App. at 146-47). The petition for rehearing includes three arguments: (1) that the Court of Appeals improperly rejected the credibility determinations of the trial court (App. at 110-18); (2) that the Court of Appeals erred in finding that Laurence should not be dissociated (App. at 118-21); and (3) that the Court of Appeals made "extraneous findings" (App. at 122-31).

COUNTER-STATEMENT OF FACTS

The Company is a manager-managed LLC that operates a successful restaurant on the Isle of Palms, the Boathouse at Breach Inlet ("Breach Inlet"). (R. at 1146-79). It was formed in 1997, and the original members were Richard (80%), Ted (10%), Laurence (5%), and Richard Stoney, Jr. (5%, held in trust by Ted).[3] (*Id.*). Richard has been the Company's manager since its inception. (*Id.*).

Following the success of Breach Inlet, Richard sought to open other restaurants and food service businesses. (R. at 965:6-78:23, 990:15-19). These other restaurants and businesses were each owned by different LLCs, each of which had different members. (*Id.*).

As his portfolio grew, Richard formed Crew Carolina, a single-member LLC, wholly owned and controlled by Richard. (R. at 784:1-15, 967:7-18). Crew Carolina does not have an operating agreement, and it does not maintain corporate records or follow corporate formalities. (R. at 784:22-85:5, 790:25-91:5). Instead, Crew Carolina serves as Richard's "alter ego" for the purpose of moving funds from his successful restaurant, Breach Inlet, to his other ventures and to himself. (R. at 788:16-790:15).

According to the Company's financial records as of the time of trial, Richard owes the Company $42,835.19, and Crew Carolina owes the Company $4,194,264.66. (R. at 1128-29, 574:2-12). There was no plan or intention to repay these funds to the Company. (R. at 1186-88 at ¶ 3, 861:17-62:7, 913:19-14:20).

[3] Over time, the ownership interests changed, and by the time of trial, the ownership of the Company was as follows: Richard (55%); Ted (10%); Ted as trustee for Richard Stoney, Jr., Richard's son (5%); Lori Stoney, Richard's ex-wife (5%); Lori as trustee for Croft Stoney, Richard's daughter (5%); Laurence (5%); Holmes Capital Management, LLC (10%); MWC Properties, LLC (5%). (R. at 779:4-13).

By way of example, entries on the Company's general ledger booked as "Due From Richard Stoney" show that Richard used Company funds to host a friend from Italy; to take personal trips to the Bahamas, New York, Belgium, Chicago, and Key West; to buy feed for his polo horses; to pay the mortgage at Kensington Plantation; and to pay his personal taxes. (R. at 1122-24, 569:2-71:18, 648:22-49:9). Similarly, Company funds designated as "Due from Crew Carolina" were used for Richard's personal benefit, including funds used to pay for landscaping work at Kensington Plantation, to buy his girlfriend tickets to a fashion show, to fund his Christmas shopping, to pay his veterinary bills, and to write himself checks for "weekend cash." (R. at 1122-24, 650:5-52:14).

With respect to the use of Company funds to support Richard's other ventures, Chip Robinson, the Company's former controller, testified as follows: "Q. And isn't it true that the profits of [Breach Inlet] that you described as a cash cow and blood donor kept Richard's other [restaurant ventures] afloat? A. Yes." (R. at 853:25-54:3). This practice that Richard described as "robbing Peter to pay Paul" created cash flow problems for the Company, resulting in bounced checks and periods where the Company was unable to timely pay vendors and employees. (R. at 645:20-47:24, 854:4-56:10). In addition, the Company incurred interest charges and penalties for failure to pay taxes on time. (R. at 1127, 645:20-47:24).

Richard's attorney warned him as early as 2007 that his practice of self-dealing and comingling funds was inappropriate and instructed him to stop moving money from the Company to entities with different owners unless all of the Company's members agreed to it in writing. (R. at 515:5-18, 891:12-20, 429:25-33:6). In addition, in 2013, the Company's accountant, Dennis Jarvis, was concerned about the "Due From/Due To" and was worried the investors would "hold him accountable for it." (R. at 1186-88). As testified by Chip Robinson:

Q. I want to talk about the red flags and concerns raised by Mr. Jarvis. I believe your testimony [to] Mr. Barr was about how [the "Due From/Due To"] was booked. In fact, sir, he said to you that he had a real problem with "what's going on down there," and he was afraid that investors were going to "hold him accountable"?

A. Yes, sir.

. . .

Q. The CPA for the company was "freaking out" because he was scared that investors were going to hold him accountable?

A. Yes, sir.

Q. So in addition to your red flags that you raised to Richard where you told him it wasn't sustainable, Dennis Jarvis was waving red flags too, correct?

A. Correct.

Q. And the most important red flag was raised in 2007 when you understood from a legal standpoint that the practice needed to stop unless you got [approval] in writing from the members, correct?

A. . . . You're referring to our meeting with Mr. Pearlman, [the Company's lawyer]?

Q. Yes, sir.

A. Then yes, sir.

(R. at 890:15-91:20).

Richard ignored the advice of his accountant, controller, and attorney, and continued to move money out of the Company to make payments to himself and Crew Carolina without obtaining permission from the Company's members. (R. at 1122-24, 860:13-61:2). Instead, Richard instructed the Company's accountant "not to discuss the Due To/Due From with other members of the Boathouse and did not permit [him] to share the Company's tax returns with certain members, including Laurence Stoney." (R. at 1186-88 at ¶ 8).

The harm to the Company was not limited to the loans of Company funds to Richard and Crew Carolina. Breach Inlet sits on a waterfront property that is supported and protected by a bulkhead (a wooden sea wall). (R. at 761:19-22). Richard owns the real estate in his individual capacity, and the Company pays him rent. In 2011, Richard executed a lease agreement between himself and the Company. (R. at 1130-32). This lease (the "2011 Lease") provided that Richard was responsible for any bulkhead repairs. (*Id.*). In addition, the 2011 Lease gave the Company the unilateral right to extend the lease term in five-year increments to December 2035. (*Id.*).

In 2015, after Richard knew Laurence had retained counsel and sought additional information about the Company's dealings, Richard entered a new lease on behalf of himself and the Company (the "2015 Lease"). (R. at 1133-45, 756:5-24). In the 2015 Lease, Richard made three major changes to the 2011 Lease: (1) he replaced himself as landlord with 101 Palm Boulevard, LLC, a single-member LLC owned and controlled by Richard; (2) he altered the lease term so that it expired in 2020 (rather than being renewable through 2035); and (3) he shifted responsibility for any bulkhead repair, which was estimated to cost in the hundreds of thousands of dollars, from himself as landlord, to the Company as tenant. (*Id.*). Despite materially altering the Company's financial position to benefit himself, Richard concealed the existence of the 2015 Lease from the members of the Company. (R. at 766:9-17).

In addition, Richard took out a personal loan in 2008 in the amount of $1,677,331.89, plus interest. (R. at 1183-85). Without asking permission from the Company's members, Richard executed a guaranty on behalf of the Company securing that personal loan. (*Id.*). In 2012, after Richard defaulted, he caused the Company to enter a confession of judgment for $1,812,017.69 to prevent foreclosure on this personal debt. (R. at 1180-82, 817:14-18).

Lastly, Richard caused the Company to make distributions totaling $234,857.00 to Holmes and Cox when he did not make distributions to the Company's other members. (R. at 583:8-84:16, 1125).

Laurence brought this action on behalf of the Company in an attempt to right the wrongs committed at the Company's expense. These are not small matters and directly impact the Company and, in turn, derivatively impacted the value of the members' interests.

ARGUMENTS

I. The Court of Appeals applied the correct standard of review and was within its purview to find facts in accordance with its own view of the preponderance of the evidence. (Petition Questions Presented I and IV)

This action sounds in equity. *See Ballard v. Roberson*, 399 S.C. 588, 593, 733 S.E.2d 107, 109 (2012) (holding derivative actions arise in equity); *Park Regency, LLC v. R & D Dev. of the Carolinas, LLC*, 402 S.C. 401, 411, 741 S.E.2d 528, 533 (Ct. App. 2012) (finding request for dissociation of LLC member is in equity). As such, the Court of Appeals could "find facts in accordance with [its] own view of the preponderance of the evidence." *Straight v. Goss*, 383 S.C. 180, 191–92, 678 S.E.2d 443, 449 (Ct. App. 2009); *Inlet Harbour v. S.C. Dep't of Parks, Recreation & Tourism*, 377 S.C. 86, 91, 659 S.E.2d 151, 154 (2008). Indeed, the appellate courts have a *de novo* standard of review as to facts in equity cases. *Lewis v. Lewis*, 392 S.C. 381, 386, 709 S.E.2d 650, 652 (2011). "*De novo* review permits appellate court fact-finding, notwithstanding the presence of evidence supporting the trial court's findings." *Id.* at 390, 709 S.E.2d at 654-55. However, this Court is "not required to disregard the findings of the trial judge who saw and heard the witnesses and was in a better position to judge their credibility." *Straight*, 383 S.C. at 191–92, 678 S.E.2d at 449.

Richard recites that the "*de novo* standard of review does not relieve an appellant from demonstrating error in the trial court's findings of fact." *Lewis*, 392 S.C. at 385–86, 709 S.E.2d at

652. The authority underlying this quote, however, illustrates that this is not a separate requirement from the preponderance of the evidence standard, as follows:

> *See Crowder v. Crowder,* 246 S.C. 299, 301, 143 S.E.2d 580, 581 (1965) (citing *Forester v. Forester,* 226 S.C. 311, 85 S.E.2d 187 (1954)) ("It is now well settled that this court has jurisdiction in appeals in equity cases to find the facts in accord with our view of the preponderance or greater weight of the evidence, in the absence of a verdict by a jury; and may reverse a factual finding by the lower court in such cases when the appellant satisfies this court that the finding is against the preponderance of the evidence."); *Inabinet v. Inabinet,* 236 S.C. 52, 55–56, 113 S.E.2d 66, 67 (1960) (citing *Twitty v. Harrison,* 230 S.C. 174, 94 S.E.2d 879 (1956)) ("Our duty in equity cases to review challenged findings of fact as well as matters of law does not require that we disregard the findings below or that we ignore the fact that the trial judge, who saw and heard the witnesses, was in better position than we are to evaluate their credibility; nor does it relieve appellant of the burden of convincing this court that the trial judge erred in his findings of fact."); *Gilbert v. McLeod Infirmary,* 219 S.C. 174, 184, 64 S.E.2d 524, 528 (1951) ("We have jurisdiction in appeals in equity to find the facts in accord with our view of the preponderance or greater weight of the evidence, in the absence of verdict by jury."); *Wise v. Wise,* 60 S.C. 426, 449, 38 S.E. 794, 802–03 (1901) (McIver, C.J., dissenting and quoting *Finley v. Cartwright,* 55 S.C. 198, 33 S.E. 359 (1899)) ("Whatever differences of opinion may once have existed as to the rule which should govern where an appellant ... asks this court to reverse the findings of fact by the circuit judge in an equity case, it must now, since the decision in *Finley v. Cartwright* ... be regarded as settled 'that this court may reverse a finding of fact by the circuit court when the appellant satisfies this court that the preponderance of the evidence is against the finding of the circuit court.' ").

Id.

Contrary to the petition, the Court of Appeals did not disregard the trial court's factual findings and credibility determinations, but rather found that the trial court erred in failing to consider the other members motivations for opposing this action (App. at 102) and in failing to look beyond "the mere presence of economic and emotional conflict" in this LLC involving just a few members most of whom were related, rather than considering "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." (App. at 102-03). The opinion does not shy away from the facts relating to the bad blood between Richard and Laurence, and it includes an acknowledgement

that "animosity certainly exists between the parties." (*See* App. at 103). The Court of Appeals faults the trial court for reaching its result based solely on its finding that there was personal vindictiveness and disagrees, based on the preponderance of the evidence and the applicable law, with the trial court's conclusion that Laurence was acting in pursuit of personal gain. This is perfectly consistent with the applicable standard of review, the evidence in the record, and the briefing and argument before the Court of Appeals.

Richard also complains that the opinion of the Court of Appeals includes some language he deems "unnecessary" and "extraneous," citing a concurrence from *Blanford v. Mauterer*, 252 S.C. 146, 159, 165 S.E.2d 633, 640 (1969). As an initial matter, the issues on appeal were broader than just the standing issue. The Company also successfully challenged the dissociation ruling. Again, the Court of Appeals was free to find facts in accordance with its own view of the preponderance of the evidence. Further, Richard appears to concede that the testimony supports many of the statements that are the subject of his complaint.[4] He simply does not like the way the Court of Appeals phrased things.

[4] *See* Petition at Section IV, items 2, 3, 4, and 5, each of which concedes that there is evidence supporting the statement at issue. With respect to Section IV, items 1 and 6, Richard does not dispute that more than $4,000,000 was taken from the Company by himself and his single member LLC, he just disputes that his name is attached to those missing funds. With respect to Section IV, item 7, this conclusion appears in the discussion of dissociation, which was not remanded for further review.

II. The Court of Appeals correctly determined that Laurence could pursue derivative claims as a class of one. (Petition Question Presented II)

A. Richard waived this issue by failing to include it in his petition for rehearing.

Richard's petition for rehearing does not make any argument with respect to the legal analysis applied by the Court of Appeals in considering the standing issue. Accordingly, the arguments in Sections I(c) ("The Class of One" Issue, and Vindictive and Personal Motivations") and II ("This Court Should Grant Certiorari to Review These Issue of First Impression: Under the Generally Accepted Standards for Standing Articulated in the Fifth Circuit Court of Appeals Case of *Davis v. Comed*, and *Smith v. Ayres* a Purported Class Representative in a Shareholder Derivative Lawsuit May Lack Standing, Even in a "Class of One" Derivative Lawsuit, Where His Motives are Vindictive and Fro Personal Gain, Rather Than For the Benefit of the Company.") of the petition have been waived. Rule 242(d)(1), SCACR ("***Only*** those questions raised in the Court of Appeals and in the petition for rehearing shall be included in the petition for writ of certiorari as a question presented to the Supreme Court." (emphasis added)); Jean H. Toal *et al., Appellate Practice in South Carolina* 306 (3d ed. 2016) ("However, the petitioner may *only* include questions raised to the Court of Appeals and in the petition for rehearing to the Court of Appeals" (emphasis in original)).

B. The Court of Appeals correctly analyzed the standing issue.

The trial court found that there was undisputed evidence of loss to the Company in excess of $4,000,000. (R. at 28-29). Notwithstanding that finding, the trial court ruled that Laurence lacked standing to maintain this action on behalf of the Company. (R. at 33). This result was driven solely by the trial court's determination that Laurence was motivated, not by concern for the Company, but rather out of personal interest and vindictiveness toward Richard. (R. at 32-33). The Court of Appeals correctly focused its inquiry on the "totality of the circumstances," rather

than the relationship between Richard and Laurence and found that Laurence had standing to pursue this action. As stated by the Court of Appeals, "[t]o 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)." (App. at 105).

1. Laurence could not have brought this action in an individual capacity.

An LLC is an entity separate and distinct from its members. S.C. Code Ann. § 33-44-201. As a result, harm to the LLC must be pursued by way of a derivative action. *Park Regency, LLC,* 402 S.C. at 417, 741 S.E.2d at 536; *Wilson v. Gandis*, 430 S.C. 282, 311, 844 S.E.2d 631, 647 (2020).

Individual LLC members have only a limited ability to bring an action against an LLC itself or other members to enforce: "(1) the member's rights under the operating agreement; (2) the member's rights under this chapter; and (3) the rights that otherwise protect the interests of the member, including rights and interests arising independently of the member's relationship to the company." S.C. Code Ann. § 33-44-410. However, "[a] member of a limited liability company may maintain an action in the right of the company if the members or Managers having authority to do so have refused to commence the action . . . ." S.C. Code Ann. § 33-44-1101.

Laurence is not seeking to enforce his rights under the operating agreement or his rights under the LLC act or any other personal interest, nor is he seeking a remedy for any "loss [] separate and distinct from that of the [Company]." He seeks to make the Company whole. As such, this action could not have been brought in an individual capacity. The trial court erred in ruling otherwise as indicated by the Court of Appeals. (App. at 104 ("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 duty to the Company; therefore, the claims must be brought in a derivative action.")).

2. The Court of Appeals correctly determined that Laurence had standing to pursue this action on behalf of the Company.

The trial court found there was "undisputed evidence of [] loss" to the Company at the hands of Richard and Crew Carolina. (R. at 29). It excused that loss, however, because only one other member of the LLC (Richard's ex-wife, Lori Stoney) supported the derivative action. (*Id.*.).[5]

This LLC only has a few members, all of whom were closely associated with Richard (his brother, his children in trust, his cousin, and his ex-wife) or were receiving benefits from Richard's conduct (his business associates). Yes, a majority of the membership supported Richard and benefitted from his actions in breach of his fiduciary duties to the Company, but that does not mean Richard—the Company's manager and majority member—has an unfettered right to loot the Company. As set forth above, a derivative action is the only mechanism to make the Company whole and, in turn, to "adequately compensate[] the injured [member] by increasing the value of his [membership interest]." *See Brown v. Stewart*, 348 S.C. at 33, 46–51, 557 S.E.2d at 676, 683–85 (Ct. App. 2001).

With respect to the derivative relief sought in this case, the right to bring an action is governed by S.C. Code Ann. § 33-44-1101 and Rule 23(b)(1), SCRCP ("In a derivative action brought by one or more [] members to enforce a right [] of an unincorporated association, the [] association having failed to enforce a right which may properly be asserted by it, the complaint shall be verified and shall allege that the plaintiff was a [] member at the time of the transaction of which he complains []. . . . The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the [] members similarly situated in enforcing the right of the [] association . . . .").

[5] As stipulated by the parties, "Laurence O. Stoney is not similarly situated to any other member of the Boathouse at Breach Inlet, LLC." (R. at 207-08).

The Court of Appeals considered § 33-44-1101 and Rule 23(b) together with case law from other jurisdictions in determining that Laurence has standing as a "class of one." (App. at 99-105). In his petition, Richard does not so much disagree with the analysis, but rather contends that the Court of Appeals should have stopped its review and affirmed because there was evidence of personal vindictiveness between Richard and Laurence. Richard's argument fails to acknowledge the reality that a member of a member-managed LLC that has been mismanaged is highly likely to have personal animus toward the manager.

As discussed in other jurisdictions and by the Court of Appeals here, the "class of one doctrine" is particularly apt in the context of closely held companies. Such companies are ripe for malfeasance by self-interested managers, and the close ties between owners makes it difficult for minority members to challenge managerial wrongdoing for fear of further mismanagement or being expelled from the business. As explained by the Utah Supreme Court,

> In closely held corporations, it becomes easy for the majority shareholders to identify themselves as the corporation. . . . [W]e recognize that closely held corporations may be more vulnerable to malfeasance. . . . [T]he 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 Inv'rs, LLC v. Garrity, 216 P.3d 944, 951 (Utah 2009). The Texas Supreme Court similarly found,

> Furthermore, we question the wisdom of construing [Rule 23(b)(1)] in any manner which prevents a shareholder in a close corporation from enforcing his rights. Under the facts of this case, such an interpretation could deprive the corporation of any remedy it might have as the result of wrongs done it by the major shareholders.

Eye Site, Inc. v. Blackburn, 796 S.W.2d 160, 162–63 (Tex. 1990). If courts were to prevent a uniquely positioned member from standing as a class of one, that would "permit corporate looting and malfeasance in circumstances where all but one shareholder benefited personally from the

illegality . . . ." *Angel Inv'rs, LLC*, 216 P.3d at 950–51. Denying a class of one in a case such as this one would be patently inconsistent with the maxim that equity will not allow a wrong without a remedy. *See State ex rel. Daniel v. Strong*, 185 S.C. 27, 43, 192 S.E. 671, 678 (1937) ("Just as nature abhors a vacuum, so equity abhors a wrong without a remedy.").

Richard cites *Davis v. Comed*, 619 F.2d 588 (6th Cir. 1980) and *Smith v. Ayres*, 977 F.2d 946 (5th Cir. 1992) and urges that the Court adopt the analysis from these cases. *Smith* is inapplicable on its face because the parties have stipulated that no other members are similarly situated to Laurence. 977 F.2d at 949. *Davis* was cited by the Court of Appeals and provides a non-exclusive eight-factor test to determine if a representative plaintiff is "fairly and adequately" representing the interests of a company in a derivative action, as set forth below:

> Among the elements which the courts have evaluated in considering whether the derivative plaintiff meets [Rule 23's] representation requirements are: [1] economic antagonisms between representative and class; [2] the remedy sought by plaintiff in the derivative action; [3] indications that the named plaintiff was not the driving force behind the litigation; [4] plaintiff's unfamiliarity with the litigation; [5] other litigation pending between the plaintiff and defendants; [6] the relative magnitude of plaintiff's personal interests as compared to his interest in the derivative action itself; [7] plaintiff's vindictiveness towards the defendants; and, finally, [8] the degree of support plaintiff was receiving from the shareholders he purported to represent.

619 F.2d at 593-94. Both the trial court and the Court of Appeals cited *Davis*.

The analysis of *Davis* provided by the Virginia Supreme Court in *Cattano v. Bragg*, 727 S.E.2d 625 (Va. 2012) is helpful here. In that case, the minority member of a two-person law firm brought a derivative action to recover for harm to the business at the hands of its majority shareholder. The *Cattano* court cited a long list of cases where a class of one successfully sought to maintain a derivative action. *Id.* at 628. The court then considered the *Davis* factors, noting that these factors are "not exclusive and must be considered in the totality of the circumstances found in each case." *Id.* at 629 (quotation omitted).

The *Cattano* court then made the following ruling:

> While the present case contains economic antagonism as well as apparent animosity between the Firm's only two shareholders, we do not find this to be a determinative factor when evaluating a closely held corporation; nor do we find it determinative that the sole other shareholder does not support the derivative suit. To so hold would be to enact a de facto bar on derivative suits in two-shareholder corporations. Charged emotions and economic antagonism are virtually endemic to disputes in closely held corporations. Nevertheless, a single shareholder derivative claim is still possible, provided that the totality of the circumstances support a finding that the plaintiff's personal interests do not preclude the shareholder from fairly and adequately representing the corporation. In closely held corporations, we must look beyond the mere presence of economic and emotional conflict, placing more emphasis 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. The Court ultimately found that the minority shareholder could maintain suit based on the totality of the circumstances as follows:

> [T]he "totality of the circumstances" combine to show that Bragg "[f]airly and adequately represent[ed] the interests of the corporation" . . . . The remedy sought—the return of funds, misappropriated by an officer, to the corporation—is highly appropriate for a derivative claim. There is no evidence in the record of external parties motivating Bragg, and she is intimately familiar with the litigation. Bragg's additional individual claims—breach of contract and judicial dissolution—do not reflect an inappropriate conflict of interest. Significantly, as a portion of the funds returned would go to her upon dissolution, Bragg's personal interests are in line with those of the corporation, so that the return of assets to the Firm will clearly be vigorously litigated.

Id.

Similarly, in this case, it should not be disqualifying that Richard and Laurence do not get along. Especially where that disagreement, at least in part, flows from Laurence's efforts to restore Company assets and Richard's refusal to do so. If hostility alone were disqualifying, it would be rare case where a minority owner of a closely held business could pursue recovery on behalf of the business. The type of conduct at issue here—among other things, the loss of over $4,000,000 from the Company— will necessarily engender hard feelings on the part of the minority member.

The trial court did not perform this analysis and instead looked solely to its perception of vindictiveness and the support of other members that the parties stipulated Laurence was not representing. (R. at 31-33). The Court of Appeals considered the "totality of the circumstances" and reached a different conclusion. (App. at 101-04). Richard simply does not like the result of this analysis.

III. The Court of Appeals correctly reversed the trial court's order dissociating Laurence from the Company. (Petition Question Presented III)

Adding insult to injury, the trial court exercised its equitable powers to dissociate Laurence from the Company in its current, diminished state. S.C. Code Ann. § 33-44-601(6)(iii) permits a court to expel a member of a LLC only if that member "engaged in conduct relating to the company's business which makes it not reasonably practicable to carry on the business with the member."[6] Interestingly, Richard's petition does not cite the statute.

"[S.C. Code Ann. §] 33-44-702 outlines the procedure for a court to use when determining the fair value of a member's distributional interest when that interest is to be purchased by the company." *Wilson*, 430 S.C. at 312, 844 S.E.2d at 647. Under this statute, a trial court may "determine the fair value of the interest, considering among other relevant evidence the going concern value of the company, any agreement among some or all of the members fixing the price or specifying a formula for determining value of distributional interests for any other purpose, the recommendations of any appraiser appointed by the court, and any legal constraints on the company's ability to purchase the interest." S.C. Code Ann. § 33-44-702. Nothing in this definition allows the trial court to impute funds and value wrongly siphoned from the Company.

[6] Defendants did not move to expel Laurence from the Company for making it "not reasonably practicable to carry on the Company's business" until January 7, 2020, more than four years after Laurence filed this lawsuit. Common sense dictates that if it was not practicable to carry on the Company's business with Laurence Stoney, Defendants would have moved to expel him sooner.

That is the function of a derivative action. From Laurence's perspective "fair value" is not equitable unless the Company is made whole first.

By failing to remedy the losses to the Company and ordering dissociation, the trial court allowed Richard to profit from his wrongdoing while reducing the "fair value" to be paid to Laurence for his interest. For this reason, dissociation is not the "elegant, equitable solution" that Richard portrays it to be. Instead, dissociation would produce a result that is patently inconsistent with the overriding equitable principle that equity will not allow a wrong without a remedy. *State ex rel. Daniel*, 185 S.C. at 43, 192 S.E. at 678.

The Court of Appeals looked to the language of S.C. Code Ann. § 33-44-601(6)(iii) in determining whether the Defendants had met their burden of showing dissociation was warranted in this case. It also considered guidance from the Supreme Court of New Jersey's opinion in *IE Test, LLC v. Carroll*, 140 A.3d 1268, 1279 (N.J. 2016). As stated in *IE Test*, "LLC members seeking to [judicially] expel a fellow member . . . are required to clear a high bar [, and the Statute does not] authorize a court to dissociate an LLC member merely because there is a conflict."

In *IE Test*, one member of a three member LLC would not agree to execute an operating agreement such that the LLC could not obtain a line of credit or financing from a bank. *IE Test, LLC* at 1280. Despite the significant obstacle created by the dissenting member—making it impossible for the engineering company to borrow money to operate—the court refused to judicially expel the dissenting member because he did not engage in conduct with respect to the business that made it "not reasonably practicable" for the business to continue. *Id.*

In "ascrib[ing] to the statutory words their ordinary meaning and significance," the *IE Test* court reasoned that for it to expel a member, that member must have engaged in conduct such that "it must be unfeasible, despite reasonable efforts, to keep the LLC operating while the disputed

member remains affiliated with it." *Id.* at 1278. The court further observed that the statute was not "satisfied by the mere existence of a conflict among LLC members," and that:

> [T]he Legislature did not authorize a court to premise expulsion . . . on a finding that it would be more challenging or complicated for other members to run the business with the LLC member than without him. . . . Instead, the Legislature prescribed a stringent standard of prospective harm: the LLC member's conduct must be so disruptive that it is "not reasonably practicable" to continue the business unless that member is expelled.

Id. The court concluded that judicial expulsion is inappropriate if "the LLC can be managed notwithstanding [the dissenting member's conduct]." *Id.*

Laurence is a minority member of the Company with no access to or control over its operation or finances. He has been a passive investor in the Company since its inception in 1997, and the Company has been a successful venture. Nothing about Laurence's minority interest prevents the Company from conducting its business in the ordinary course. Richard disregards that fact and instead focuses again on the animosity between Laurence and himself and testimony that the parties do not want to be in business with each other. This does not rise to the level of impracticability contemplated by the statute.

Dissociation under § 33-44-601(6)(iii) is improper unless Defendants prove that it is unfeasible to keep Breach Inlet operational while Laurence is a member. To the contrary, Richard testified that based on first quarter sales he projected the Company to earn up to half a million dollars more in 2020 than in 2019. (R. at 748:12-18). Given Richard's testimony, under any test the Court might apply regarding the "reasonably practicable" standard, it is "reasonably practicable

to carry on the business" with Laurence as a passive investor. Accordingly, the Court of Appeals was correct in finding that dissociation was improper in this case.[7]

CONCLUSION

For all of these reasons, the petition does not raise any question for this Court's review under Rule 242, SCACR. Given the amount of time that has elapsed since this action was filed in 2015, the petition should be denied so that the derivative claims may finally be determined on their merits.

Respectfully submitted,

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[7] In addition, the trial court erred in awarding that relief against Laurence in his individual capacity and erred in awarding affirmative relief to the Defendants without addressing whether Richard had unclean hands as argued in Sections II(B) and (C) of Laurence's appellant's brief before the Court of Appeals.