STATE OF MICHIGAN

SAGINAW COUNTY CIRCUIT COURT

BUSINESS COURT

GUILLERMO MEDINA and
LILY SELLS,

Plaintiffs,

v.

EDWARD J. DeGROAT,

Defendant.

Case No. 20-041728-CB

Judge: M. Randall Jurrens (P27637)

OPINION FOLLOWING BENCH TRIAL ON LIABILITY

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Plaintiffs assert claims against defendant related to a partnership all three are in with others.

Following a bench trial[1], the court took the matter under advisement and subsequently received counsels' written arguments.

For the reasons stated in this opinion, while appreciating the legal issues raised by plaintiffs, the court is unpersuaded the admitted evidence warrants imposing liability on defendant.

[1] The parties agreed to bifurcate trial, limiting this first phase to the issue of liability and saving to another day, if needed, the issue of damages.

Background

From testimony[2] and exhibits[3] received during trial, plus written joint stipulated facts submitted before trial, the court understands:

[2] The only witnesses were the three parties: plaintiffs Guillermo Medina and Lily Sells, and defendant Edward J. DeGroat.

[3] The court admitted the following exhibits:

Plaintiffs' Ex 1:	Towne Centre Investments Partnership Agreement
Plaintiffs' Ex 2:	January 27, 2003 Quit Claim Deed from defendant's daughter, Janet M. Goodchild, "whose address is 4901 Towne Centre #140, Saginaw, Michigan 48604"
Plaintiffs' Ex 5:	October 3, 2011 promissory note obligating the partnership to repay a $35,500 loan from defendant's wife, Nancy DeGroat, together with 5% interest
Plaintiffs' Ex 6:	December 1, 2011 promissory note obligating the partnership to repay a $67,445.73 loan from defendant's wife, together with 5% interest
Plaintiffs' Ex 9:	March 7, 2018 appraisal report prepared by Weiss Appraisal Service Inc.
Plaintiffs' Ex 14:	table of the partnership's net income and distributions (1986-2019)
Plaintiffs' Ex 18:	August 19, 1994 letter from defendant to his partners outlining terms of recently signed lease with the State of Michigan, Department of Social Services (at $14.50/sq ft, plus $3.00/sq ft to cover buildout costs), with an invitation for any partner(s) to loan $50,000 (to be re-paid with 10% interest) needed to fund buildout costs
Plaintiffs' Ex 20:	plaintiffs' expert's report (but not actually tendered to the court)
Plaintiffs' Ex 22:	defendant's expert's report (but not actually tendered to the court)

In late 1986, plaintiff Medina, his son, Marlow Medina, defendant, and four others formed a partnership to purchase and operate a 3-story office building known as the Vanguard Building located at 4901 Towne Centre Road in Saginaw Township. To document their association, everyone signed a partnership agreement drafted by defendant (Plaintiffs' Ex 1).

In addition to designating defendant as the managing partner, material provisions of the agreement include:

> 5.01 Initial Contributions. The initial capital of the partnership shall consist of a total of five hundred twenty-six thousand eight hundred and no/100 ($526,800.00) dollars contributed as follows:
>
> | Name of Investor | Amount of Initial Contribution | |
> |---|---|---|
> | EDWARD J. DEGROAT | $ 207,728.00 | 70½ % |
> | JAMES P. PHILLIPS | $ 75,712.00 | 7 % |
> | DARRELL L. BROWN | $ 54,080.00 | 5 % |
> | VOSS M. STAEHLING | $ 32,448.00 | 3 % |
> | GUILLERMO MEDINA | $ 108,160.00 | 10 % |
> | JAMES W. PITT | $ 32,448.00 | 3 % |
> | MARLOW MEDINA | $ 16,224.00 | 1 ½ % |
>
> 6. Profits and Losses. In the event of a loss by the partnership, the Investors shall be entitled to share in such loss in the same proportion as their contributions to the partnership. In the event of any profit earned by the partnership from any source other than the sale or other disposition, the Investors shall share in such profit in the same proportion as their contributions to the partnership. In the event of any profit realized from the sale or disposition of the office building the Investors shall first receive the amounts of their capital accounts, and any profit over and above the capital accounts shall be distributed to the Investors in proportion to their capital accounts as to their percentage of ownership.
>
> 7.03 Duties of Managing Partner. Managing Partner shall be responsible for and have the authority to exercise all rights and privileges of the owners under the Partnership Agreement and to take all necessary action and steps for complying with any of the requirements of the operation and leasing of the office building. Managing Partner shall also keep the partnership books and be responsible for the preparation and filing of the necessary tax returns for the partnership.

Although participating in discussions and considering the possibility, plaintiff Sells[4] ultimately opted to not buy into the partnership; although, early on, she did loan the partnership money.

Since inception, as managing partner, defendant has been solely responsible for the partnership's day-to-day affairs, leasing office space in the building, keeping the partnership's books and records, and making partnership distributions. With regard to the latter, defendant has distributed profits to the partners monthly based on the percentages stated in ¶ 5.01 of the partnership agreement (i.e. not based on dollars actually contributed).[5]

Defendant testified his inflated 70.5% share (rather than the 39.43% share of his actual initial contribution) reflects the burden of managing the partnership's daily operation, including leasing the building's rental space without taking a realtor's commission[6].

Since the partnership's formation (and even before[7]), defendant occupied office space in the building; initially occupying Suite 140 (approximately 1,000 square feet) for which he paid rent equal to one-half of market rate, until moving in 2010 to Suite 225 (912 square feet) where he has paid no rent. Although defendant's use of office space was open and known[8], he did not affirmatively inform plaintiffs of the particulars of the arrangement, including the amount of rent,

[4] Although since divorced, Guillermo Medina was married at the time to Lily Sells.

[5] The partnership appears to have been profitable, distributing profits aggregating $6,501,472 from 1986 through 2019 (Plaintiffs' Ex 14), plus $60,000 in each of 2020 and 2021.

[6] Defendant is a real estate broker, although in recent years generally limiting his services to properties in which he holds an interest (e.g. the Vanguard Building).

[7] Even prior to the partnership's acquisition, defendant occupied office space in the Vanguard Building by arrangement with the prior owner.

[8] Plaintiffs met with defendant in his Vanguard Building office both pre- and post-partnership formation.

which he based on spending one-half of his time on unrelated business ventures in the early years, while in the latter years devoting full time to the Vanguard Building.

In 2007, plaintiff Medina, estimating the building's value at $8 million, offered to sell his partnership share to defendant and/or the other partners for $800,000 (but nothing came of it).

In 2008, Sells acquired Marlow Medina's partnership interest by assignment.[9]

In his capacity as managing partner, defendant procured and repaid three loans from his wife to finance building repairs and improvements:

- October 3, 2011 loan in the amount of $35,500 due and payable, together with interest at the rate of 5%, compounded annually, on December 3, 2011 (Plaintiffs' Ex 5)

- December 1, 2011 loan in the amount of $67,445.73 due and payable, together with interest at the rate of 5% compounded annually, in 37 equal monthly installments (Plaintiffs' Ex 6)

[9] The parties stipulated Sells acquired the partnership interest of her son in 2008 by written assignment and defendant testified he signed the document also to indicate his consent to the transfer of Marlow's interest to Sells (although no documentary evidence to this effect was admitted). However, there is no evidence that all partners consented to Sells becoming a member of the partnership as required by MCL 449.18(g) (or, alternatively, plaintiffs' counsel's suggestion to the contrary notwithstanding, that the requirements for withdrawal/sale under ¶ 9.01 of the partnership agreement were observed); unless the parties' stipulation that defendant "ratified and approved [the assignment] in writing [ ] in his capacity as managing partner" falls within his authority under ¶ 7.03 of the partnership agreement "to exercise all rights and privileges of the owners". Assuming so, it demonstrates the agreement's broad delegation of partners' authority to defendant.

If defendant's authority as managing partner did not extend to consenting to admission of a partner into the existing partnership, the court notes that MCL 449.27(1) provides (emphasis added):

> ***A conveyance by a partner of his interest in the partnership does not*** of itself dissolve the partnership, nor, as against the other partners in the absence of agreement, ***entitle the assignee***, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or ***to require any information or account of partnership transactions, or to inspect the partnership books***; ***but it merely entitles the assignee to receive*** in accordance with his contract the ***profits to which the assigning partner would otherwise be entitled***[.]

- April 2018 loan in the amount of $45,000 due and payable, together with interest at the rate of 3%, over four years (undocumented)

Defendant did not inform plaintiffs of these partnership debts (or their repayment).

Applicable Partnership Principles

Partners stand in a fiduciary relationship to each other. *Penner v DeNike*, 288 Mich 488, 490; 285 NW 33 (1939). As fiduciaries,

> courts [ ] impose on them obligations of the utmost good faith and integrity in their dealings with one another in partnership affairs. Partners are held to a standard stricter than the morals of the marketplace and their fiduciary duties should be broadly construed, connoting not mere honesty but the punctilio of honor most sensitive. The fiduciary duty among partners is generally one of full and frank disclosure of all relevant information. Each partner has the right to know all that the others know, and each is required to make full disclosure of all material facts within his knowledge in any way relating to the partnership affairs. [*Band v Livonia Assoc*, 176 Mich App 95, 113-114; 439 NW2d 285 (1989)]

Further illustrating of the degree of fidelity required among partners, *Johnson v Ironside*, 249 Mich 35, 45; 227 NW 732 (1929) (quoting *Lata v Kilbourn*, 150 US 524) observed:

> The general principles on which the court proceeded admit of no question, it being well settled that one partner cannot, directly or indirectly, use partnership assets for his own benefit; that he cannot, in conducting the business of a partnership, take any profit clandestinely for himself; that he cannot carry on the business of the partnership for his private advantage; that he cannot carry on another business in competition or rivalry with that of the firm, thereby depriving it of the benefit of his time, skill, and fidelity, without being accountable to his copartners for any profit that may accrue to him therefrom; that he cannot be permitted to secure for himself that which it is his duty to obtain, if at all, for the firm of which he is a member; nor can he avail himself of knowledge or information which may be properly regarded as the property of the partnership, in the sense that it is available or useful to the firm for any purpose within the scope of the partnership business.

These principles are now codified in the Uniform Partnership Act, *MCL 449.1 et seq.*:

> Partners shall render on demand true and full information of all things affecting the partnership to any partner or the legal representative of any deceased partner or partner under legal disability. [MCL 449.20]
>
> Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any

> transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property[.] [MCL 449.21(1)]

Consistent with its common law antecedents, MCL 449.20 has been broadly interpreted as imposing a duty to disclose all known information that is significant and material to the affairs or property of the partnership. *Jaffa v Shacket,* 114 Mich App 626, 640; 319 NW2d 604 (1982).

The remedy for a partner's breach of fiduciary duty to other partners is to place the wronged partners in the economic position that they would have enjoyed but for the breach. *Gilroy v Conway,* 151 Mich App 628, 637; 391 NW2d 419 (1986) ("[MCL 449.21] defines identically the partnership fiduciary duty and the remedy for its breach, i.e., to account").

Analysis

Allocation of Distributions

Plaintiffs claim defendant misappropriated profits by paying them only 10% and 1½%, respectively, while distributing 70½% to himself (Plaintiffs' Post-Trial Brief, pp 4-5).

Specifically, plaintiffs argue the partnership agreement's directive that profits be distributed to partners "in the same proportion as their contribution to the partnership" (Plaintiffs' Ex 1, ¶ 6) refers to monies actually paid in (e.g. $108,160, $16,224, and $207,728), resulting in 20.53% and 3.08% shares for plaintiffs, respectively, and a 39.43% share for defendant (Plaintiffs' Post-Trial Brief, pp 5, 7-8; Plaintiffs' Reply Brief, pp 1-4).

Conversely, consistent with his trial testimony, defendant argues that, while "clumsy", the partnership agreement distinguishes between the partners' capital account (stated in dollars) and the allocation of profits (stated by percentage) (Plaintiffs' Ex 1, ¶ 5.01) (Defendant's Post-Trial Brief, pp 1-2, 4-10).

"The main goal of contract interpretation generally is to enforce the parties' intent." *Burkhardt v Bailey*, 260 Mich App 636, 656; 680 NW2d 453 (2004). "[W]hen the language of a

document is clear and unambiguous, interpretation is limited to the actual words used, and parol evidence is inadmissible to prove a different intent." *Id*. However, " 'a written instrument is open to explanation by parol or extrinsic evidence when it is expressed in short and incomplete terms, or is fairly susceptible of two constructions, or where the language employed is vague, uncertain, obscure, or ambiguous, and where the words of the contract must be applied to facts ascertainable only by extrinsic evidence, a resort to such evidence is necessarily permitted.' " *Klapp v United Ins Group Agency, Inc*, 468 Mich 459, 470; 663 NW2d 447 (2003), quoting *Edoff v Hecht*, 270 Mich 689, 695-696; 260 NW 93 (1935).

Here, ¶ 6 of the parties' agreement provides that partners are to share in the profits "in the same proportion as their contributions to the partnership". In turn, ¶ 5.01 of the agreement describes each partner's "Amount of Initial Contribution" in terms of both dollars and percentages. While this two-fold description might be fine (albeit redundant) if mathematically correct, the agreement's assignment of percentages significantly adjusts the proportions, enhancing defendant's while diminishing his partners, including plaintiffs. Without more, the conflicting provisions render ¶ 5.01 ambiguous. *Coates v Bastian Bros, Inc*, 276 Mich App 498, 503; 741 NW2d 539 (2007). This ambiguity regarding the proportion of each partners' contribution then casts a shadow on how to properly distribute profits under ¶ 6. Accordingly, the court is justified in looking beyond the language of the document and considering extrinsic evidence to determine the parties' intent. *Shay v Aldrich*, 487 Mich 648, 667-668; 790 NW2d 629 (2010).

Here, from the beginning, defendant has distributed profits to the partners based on the percentages assigned in ¶ 5.01 of the partnership agreement. This course of conduct, over a period

of decades, is compelling evidence of the parties' intent.[10] As observed in *Klapp* , 468 Mich at 478-479 (cleaned up):

> How the drafting party has interpreted ambiguous contractual language in the past is certainly relevant in determining what the parties intended such language to mean. The meaning of a provision in a contract whose language is ambiguous must be ascertained in the light of all of the relevant circumstances, including the meanings accepted by the parties. There is no doubt that evidence of practical interpretation by the parties is admissible as an aid in the determination of the meaning to be given legal effect.
>
> Where parties by such a uniform course of conduct for a long time have given a contract a particular construction, that construction will be adopted by the courts.
>
> The practical interpretation given to contracts by the parties to them, while engaged in their performance and before any controversy has arisen concerning them, is one of the best indications of their true intent.

Moreover, the long-honored practice of distributing profits based on assigned percentages notwithstanding, defendant testified this method for allocating profits was "agreed-upon" in the first instance. Conversely, although plaintiffs testified they did not recall being informed profits were being distributed this way, they did not assert defendant told them to the contrary. And, interestingly, at least as of 2007 when he offered to sell his interest, plaintiff understood he was entitled to only 10% (not 20.53%).

Accordingly, the court will adopt the construction the parties have given their agreement since the beginning, allocating profits based on assigned percentages.[11]

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[10] The court notes that no other partners have joined plaintiffs in suing defendant for misappropriating profits, nor appeared as witnesses to express concurrence in plaintiffs' proposed interpretation of the partnership agreement.

[11] The court is not unaware that plaintiffs argue ambiguities must be construed against the drafter (Plaintiffs' Post-Trial Brief, pp 8-9; Plaintiffs' Reply Brief, pp 4-6). This is known as the rule of contra proferentem. However, the rule of *contra proferentem* "is only to be applied if all conventional means of contract interpretation, including the consideration of relevant extrinsic

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Accordingly, the court concludes that defendant's distribution of partnership profits has not violated any duty due plaintiffs.[12]

Office Use

Plaintiffs additionally claim defendant breached his fiduciary duty by using building office space to conduct non-partnership business (Plaintiffs' Post-Trial Brief, p 12). The court concurs that a partner's un[der]compensated use of partnership property potentially violates fiduciary duties owed other partners. *Johnson*, 239 Mich 35, at 45.

However, here, defendant testified he paid rent equal to 50% of the then-going rate when he used office space for non-partnership business 50% of the time, and only stopped paying rent altogether when he began devoting his office time exclusively to partnership business in 2010. Without more, the court is not persuaded to impose liability for office space used openly and exclusively in furtherance of partnership business, nor when the nominally sized space[13], already

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evidence, have left the [factfinder] unable to determine what the parties intended their contract to mean." *Klapp*, 468 Mich at 471. "In other words, the rule of *contra proferentem* should be viewed essentially as a "tie-breaker," to be utilized only after all conventional means of contract interpretation, including the consideration of relevant extrinsic evidence, have been applied and found wanting." *Klapp* at 472. It is a rule of "last resort". *Petersen v Magna Corporation*, 484 Mich 300, 312; 773 NW2d 564 (2009). Here, a conventional means of contract interpretation -- use of extrinsic evidence -- renders use of a tie-breaker unnecessary.

[12] As a practical matter, if the court were to unwind the past 35 years and require defendant recalculate, disgorge, and redistribute profits (even if limited to just plaintiffs), the partnership would presumably then need to address foregone commissions or other compensation for non-managing partner services defendant understood were being subsumed into an enlarged share of profits.

[13] According to a March 19, 2018 appraisal report (Plaintiffs' Ex 9), the Vanguard Building contains 51,086 square feet of rentable space. According to trial testimony, Suite 140, used for the first 24 years by defendant, for the benefit of both the partnership and himself, approximates 1,000 square feet (or 1.96% of the building's total rentable space), and Suite 225, used by defendant exclusively for partnership purposes since 2010, approximates 780 square feet (or 1.52% of total rentable space).

occupied by the partnership, is contemporaneously used for defendant's own benefit in exchange for payment of market-rate rent.

Family Loans

Plaintiffs previously claimed defendant engaged in self-dealing by borrowing money from and paying interest to his own family members (Complaint, ¶ 25; and Plaintiffs' Trial Brief, p 3). While alluding to this claim in a section title (Plaintiffs' Post-Trial Brief, p 10), and passing references to "self-interested" transactions and "self-dealing" (Plaintiffs' Post-Trial Brief, pp 1 and 12), plaintiffs failed to develop the argument. Without more, the issue is deemed abandoned. *Mitcham v Detroit*, 355 Mich 182, 203; 94 NW2d 388 (1959).[14]

[14] But even if the issue is considered, it is doubtful that a loan from a family member, ipso facto, constitutes actionable self-dealing. Rather, it would seem plaintiffs need to demonstrate how a transaction in which a partner has an interest violates a recognized standard.

In this regard, although the court is not aware of partnership law on point, by analogy, it notes that in the realm of Michigan business corporations, "[a] transaction in which a director or officer is determined to have an interest shall not, because of the interest, be enjoined, set aside, or give rise to an award of damages or other sanctions, in a proceeding by a shareholder or by or in the right of the corporation, if the person interested in the transaction establishes * * * [t]he transaction was fair to the corporation at the time entered into", *MCL 450.1545a* (and Michigan law governing nonprofit corporations and limited liability companies is in accord, *MCL 450.2545a* and *MCL 450.4409*).

Here, there was no evidence demonstrating how the loan transactions with defendant's wife (two at 5% and one at 3%) were not "fair" to the partnership when entered into, including, particularly, in comparison to interest rates then-available in the market and the ability of alternate lenders to advance funds in time to meet the partnership's requirements (e.g. roof repairs were time sensitive). So, even if considered, plaintiff's assertion of defendant's self-dealing, while theoretically possible (assuming one's spouse is equivalent to oneself), would be factually speculative.

Interestingly, when borrowing from plaintiff Sells, circa 1987, the partnership paid her 12% interest.

Also interesting (albeit admittedly in 1994, similarly years before the 2011 and 2018 loans from

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Conclusion

Plaintiffs request the court impose liability for defendant's allocation of partnership profits, use of partnership office space, and familial borrowing. However, considering the admitted facts and applicable law, the court is not persuaded defendant has breached any contractual, common law, or statutory duty as alleged.[15]

Accordingly, the court is entering a judgment of no cause of action.

Date: January 26, 2022

/s/ (P27637)
M. Randall Jurrens, Business Court Judge

his wife), defendant, on behalf of the partnership, offered a 10% rate of return to partners if they would loan money to fund buildout costs for an incoming tenant (Plaintiff's Ex 18), but there were no takers.

[15] Under the circumstances, the court need not consider the parties' statute of limitations arguments (Plaintiffs' Post-Trial Brief, pp 13-15, Defendant's Post-Trial Brief, pp 15-17, and Plaintiffs' Reply Brief, pp 8-9), nor the bifurcated issue of damages.