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STATE OF MONTANA
Case Number: DA 18-0657

IN THE SUPREME COURT OF THE STATE OF MONTANA

Cause No. DA 18-0657

WILLIAM ("BILL") D. HARRISON and **HARRIET ("SHERRIE") A. HARRISON**, individually and as husband and wife,

Plaintiffs,

v.

THOMAS ("TOM") D. HARRISON and **KIMBERLY ("KIM") HARRISON**, husband and wife; and **LINCOLN ROAD RV PARK, INC**., a Montana corporation,

Defendants and Counter-Plaintiffs,

v.

WILLIAM ("BILL") D. HARRISON and **HARRIET ("SHERRIE") A. HARRISON**, individually and as husband and wife,

Counter-Defendants.

and

JON BOUSER, KIMBERLY BOUSER, individually and as husband and wife, **ERICK BRODSHO, HEATHER BRODSHO**, individually and as husband and wife, **GORDON BROWN**, **LYNDEE BROWN**, individually and as husband and wife, **PAUL CHATRIAND, TAMRAH CHATRIAND**, individually

and as husband and wife, **KENDALL CUNNINGHAM, ABIGAIL CUNNINGHAM**, individually and as husband and wife, **REBECCA SMITH EANES, JOSEPH FOWLER, FRANK GONZALEZ, TRACY GONZALEZ**, individually and as husband and wife, **HEATHER HARRINGTON, ROBERT HOLLIDAY, ZACHARY KOZAK, CHERIE LOFTON, JOSEPH MARINER, RICHARD NEWBY, KRISTEN NEWBY**, individually and as husband and wife, **ROBIN ROUSE, ALLEN TARYN ROUSE**, individually and as husband and wife, **IAN STEFFAN, JESSICA STUART, LINDSAY ZELL, EMILIANO CUAUTEMOC ZELL**, individually and as husband and wife, **GV75, LLC**, a limited liability company,

Plaintiffs/Appellees

v.

THOMAS ("TOM") D. HARRISON and **KIMBERLY ("KIM") HARRISON**, husband and wife; and LINCOLN ROAD RV PARK, INC., a Montana corporation,

Defendants/Appellants.

BRIEF OF APPELLANTS

ON APPEAL FROM THE MONTANA FIRST JUDICIAL DISTRICT COURT,
LEWIS AND CLARK COUNTY, THE HONORABLE MIKE MENAHAN, PRESIDING

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STATEMENT OF ISSUES PRESENTED FOR REVIEW

Whether the District Court erred when it ordered the Appellants, both individual shareholders of the Corporation, to each pay $25,000 (for a total of $50,000) to be used for on-going expenses of the Corporation operated by a court-appointed Receiver, when the on-going expenses are disputed by the shareholders, the issues have yet to be litigated, and the shareholders are not individually liable for the debts of the Corporation.

STATEMENT OF THE CASE

This dispute involves a small, family-owned corporation that operated a motor home park and subdivision in the Helena valley. The shareholders, Bill and Sherrie Harrison, parents to Tom Harrison and his wife Kim, also shareholders, suspected that Tom and Kim were mismanaging the corporation. Bill and Sherrie filed suit complaining, among other things, that Tom and Kim used corporate funds to pay personal expenses, failed to address concerns regarding the Grand Valley Estate Homeowner's Association, and failed to finalize the Grand Valley Estates Subdivision with Lewis and Clark County. Bill and Sherrie sought the appointment of a Receiver, which was granted, and Charla Taylor was appointed as Receiver. Charla Taylor then purchased the RV Park and its assets after a settlement agreement was entered into between Bill and Sherrie and Tom and Kim.

Meanwhile, the Grand Valley Estate Homeowners intervened in the lawsuit. The Receiver engaged in efforts to wind down the affairs of the corporation, including finalization of the subdivision approval. Charla Taylor suddenly and unexpectedly passed away and her sister, Rita Cortright, took over as Receiver.

On August 30, 2018, Cortright sought "further instruction" from the Court prior to her dismissal regarding payments of additional costs and fees. A hearing was held and the District Court issued the order now on appeal requiring Tom and Kim to individually pay debts of the Corporation.

STATEMENT OF THE FACTS

Bill and Sherrie Harrison are husband and wife. Tom and Kim Harrison were formerly husband and wife, but have divorced due in large part to the stresses of this litigation.[1] Tom is the only son of Bill and Sherrie. In 1993, the Lincoln Road RV Park, Inc. (hereinafter referred to as "the Corporation") was incorporated for the purpose of developing a residential major subdivision, the "Grand Valley Estates Subdivision," and an adjacent motor home park, the "Lincoln Road RV Park." Bill, Sherrie, Tom, Kim and two other individuals, the Wyricks, were shareholders when the Corporation

[1] *Marriage of Harrison*, CDR 2016-462, filed in the First Judicial District Court.

was first incorporated. Bill and Sherrie later purchased the Wyricks' shares, leaving Bill, Sherrie, Tom and Kim as the sole shareholders of the Corporation. *Complaint*, ¶¶ 1-7; *Amended Answer*, ¶¶ 1-7; *Doc.*[2] 1 and 39.

In August of 2008, the Grand Valley Estates Subdivision's restrictive covenants were filed with the Lewis and Clark County Clerk and Recorder's Office. In September 2009, the Grand Valley Estate Homeowner's Association ("GVHOA") was incorporated. *Ryan Casne Affdvt.*, ¶ 4, Defendants Exhibits 3, 4, and 5; *Doc.* 145.

In December of 2015, Bill and Sherrie filed suit against Tom and Kim after bank statements and other documents received by them raised questions about the management of the Corporation by Tom and Kim. *Doc.* 1. Bill and Sherrie sought the appointment of a receiver for the Corporation, and on December 15, 2015, the District Court issued its *Order Appointing Receiver* over the Corporation. *Doc.* 16, 23. The Order directed the Receiver to "preserve, protect, and liquidate" the Corporation's assets while paying all expenses in the ordinary course of business of the Corporation. *Doc.* 23.

On January 29, 2016, Tom and Kim filed their Amended Answer and Counterclaims against Bill and Sherrie. *Doc.* 39.

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[2] The abbreviation "Doc" refers to the docket entry in the District Court's Case Register Report.

On February 19, 2016, Tom and Kim filed a motion to terminate the Receiver. *Doc.* 41.

On April 19, 2016, the property owners in the Grand Valley Estates Subdivision (the "Homeowners") filed a motion to intervene in the case, asserting the Corporation breached the covenants, committed negligence, negligent misrepresentation, constructive and actual fraud involving the completion of the subdivision and its water and sewer system. The Homeowners also sought to pierce the corporate veil between the Corporation and the Shareholders.[3] *Doc.* 73, 74, 75.

An initial mediation between Bill, Sherrie, Tom, and Kim – the Shareholders – was held on August 30, 2016, and Tom and Kim withdrew their motion to terminate the Receiver's appointment. The parties also stipulated to the Receiver marketing and selling the RV Park. *App.* E.

The Receiver then purchased the Corporation's principal asset, the RV Park, with the Parties' and the District Court's approval. *Doc.* 100. The sale closed on March 1, 2017. The Receiver also completed a number of tasks to secure the necessary approvals to complete the subdivision as well as the water and sewer system that is the subject of the Homeowners' Complaint to

[3] On May 31, 2017, the District Court granted the motion to intervene by the Intervenor Homeowners. *App.* D; *Doc.* 115.

intervene.

The First Settlement Agreement

On March 15, 2017, the Shareholders attended a second mediation. The Receiver did not attend the mediation. Counsel for the Homeowners attended to monitor the negotiations, but did not actively participate. As a result of that mediation, Bill and Sherrie and Tom and Kim reached a settlement with, among others, the condition that within seven calendar days of execution, the sum of $50,000 (double the budgeted amount) would be segregated and used by the Receiver to complete a defined set of tasks identified by the Homeowners. By segregating twice the budgeted amount to complete the task list and then conveying all of their shares in the Corporation to Tom and Kim, the agreement was an incentive for Tom and Kim to finish those tasks as quickly and cost-effectively as possible.

Following that mediation, on April 5, 2017, Bill, Sherrie, Tom and Kim jointly moved the Court for an order approving the Settlement Agreement, a copy of which was attached to the motion as Exhibit A. *Doc.* 105. Under the terms of the first Settlement Agreement, $50,000 would be reserved and all remaining cash assets of the Corporation would then be distributed 60 percent to Bill and Sherrie, and 40 percent to Tom and Kim. Then, after the distributions, Bill and Sherrie would sell their shares to Tom and Kim for

$1.00, leaving them as the sole shareholders of the Corporation. The purpose of the $50,000 was to address uncompleted tasks for Grand Valley Estates that the Homeowners wanted completed. However, because they had not yet been granted leave to intervene, there was no accommodation in the first Settlement Agreement for claims asserted by the Homeowners. The first Settlement Agreement also required removal of the Receiver and dismissal of the lawsuit with prejudice. Completion of the tasks would then fall to Tom and Kim as the sole shareholders.

On May 16, 2017, a hearing was held on the motion to approve the Settlement Agreement. *Doc.* 114.

On May 31, 2017, the District Court issued its *Order on Pending Motions* granting the Homeowners' motion to intervene and denying the joint motion to approve the first Settlement Agreement. *Doc.* 115; *App.* D. The Court also determined that it would be premature to discharge the Receiver, as there was no substantial guarantee that the remaining subdivision tasks would be completed by Tom and Kim. In its order, the District Court stated:

> Although *the Receiver does not have a direct duty to protect the interest of the Residents* [Homeowners], this is a Court of both law and equity. Mont. Const. art. VII, § 4. Approving the settlement agreement at this junction would be inequitable to the Corporation and to the Residents. Because the law does not appear to provide the Court authority to unilaterally amend a settlement agreement, the Court will deny the Receiver's motion to amend and approve the settlement agreement. Accordingly, the Shareholder's motion to approve the agreement and

> discharge the Receiver and to dismiss the case will also be denied. (Italics added.)

App. D at 7; *Doc*. 115.

The Second Settlement Agreement

After the *Order on Pending Motions* was issued the parties continued to negotiate a resolution that would result in distributions being made to the shareholders with sufficient funds held in reserve to address the claims of the Homeowners. After careful consideration of the alternatives, it was eventually agreed between all parties that the Receiver would maintain control of approximately $ 34,000 for the purposes of addressing the claims of the intervening homeowners. A second Settlement Agreement was reached containing those terms. *Doc*. 119 and 120; *App*. C.

The second Settlement Agreement was similar to the first Settlement Agreement. Bill and Sherrie and Tom and Kim agreed to a 60/40 share split and the Receiver was authorized to distribute 97.16% of the cash on hand, which would result in approximately $34,082.81 held in reserve. Those funds would be used by the Receiver to "pay all Corporate Expenses." It was agreed that "the term Corporate Expenses shall include the following: i.) all expenses arising from or related to completion of the Grand Valley Estates Subdivision ('Subdivision'); ii.) all expenses arising from or related to completion of the Subdivision's corresponding water/sewer system; iii.) all expenses arising

from or related to the review and drafting of amended and enforceable organizational documents, bylaws, and covenants related to operation of the Subdivision, water/sewer system and the Grand Valley Estates Homeowner's Association ('HOA'); and iv.) all expenses arising from or related to transfer of all real and personal property required for the GVE Homeowner's sole operation, ownership and control of the Subdivision, water/sewer system, and HOA." *App.* C, p. 2, ¶ 3. In addition, Bill and Sherrie agreed to pay the Homeowners the sum of $24,621.48, which were all of the attorneys' fees incurred by the Homeowners. The Homeowners would release Bill and Sherrie and dismiss them from the lawsuit. The payment obligation by Bill and Sherrie and the release by the Homeowners was contingent on all twenty-eight of them executing the second Settlement Agreement. If all twenty-eight did not execute the second Settlement Agreement, then Bill and Sherrie had no payment obligation and were not released.

When the second Settlement Agreement was executed, the Parties and their counsel and the Homeowners calculated that $ 34,082 should be sufficient to cover the remaining tasks and fees.

A hearing was held on September 12, 2017, and the District Court approved the Settlement Agreement. *App.* B; *Doc.* 123. The District Court also directed the Receiver to execute the Settlement Agreement (*App.* B, p. 2,

¶ 1) and further ordered that "the remaining claims by the Intervenor Homeowners shall remain to be litigated in the case." *Id.*, ¶ 5. The Receiver and her counsel signed the Settlement Agreement the same day. *App*. C, p. 8; see also, *Hrg. Trans.*, 54:7 to 57:6.

Nearly a year later, on August 30, 2018, the Receiver filed her "Application for Further Instruction from the Court Regarding Final Action Prior to Dismissal of the Receiver" in which she asked for additional funds: (1) to bring the subdivision "in compliance with DNRC permit requirements;" (2) payment of legal fees for intervenors; and (3) to pay pending IRS taxes and penalties. *Doc*. 140, p. 6. The Receiver requested that the Court "issue a judgment against each of the individual shareholders" to "insure payment by the respective parties" and that "based on the substantial amount of the distribution paid to Tom and Kim Harrison, and the nature of the unpaid taxes, the responsibility for any taxes and penalties determined to be owed to the IRS could be equitably split between them. *Id*., p. 8.

The Homeowners responded that they believed that the Corporation and "Tom and Kim Harrison remain liable for the costs associated with remedying deficiencies in the subdivision." *Doc*. 142, p. 4.

Tom and Kim objected on the following grounds:

1. The corporate veil bars the individual shareholders from being

responsible for corporate debts. It further has not been established that Tom and Kim were personally liable for those costs. No scheduling order has been established in the Homeowners' case, no discovery has been undertaken, no motions have been filed, there has been no trial, and the evidentiary record before the District Court is such that there is no factual or legal basis for holding Tom and Kim individually responsible for paying any of those costs. To hold Tom and Kim Harrison responsible for any of these costs is premature because their liability has not been established as either a matter of fact or a matter of law.

2. The payment of attorneys fees are only allowable in certain situations, and this is not one of them. There is no statute, contract, or equitable basis for an order requiring Tom and Kim to pay these costs.

3. The subdivision already had workable and enforceable Articles of Incorporation, By-Laws, and Restrictive Covenants. It is beyond the scope of ¶ 3 of the Settlement Agreement for the Homeowners or the Homeowners Association to utilize corporate funds to amend those documents when they already existed. The Homeowners should have been required to submit a non-redacted invoice of the legal services provided so as to determine what exactly was done.

4. The Grand Valley Estates Subdivision was already completed.

The Subdivision's water and sewer system was designed and certified by a professional engineer. It was then subsequently approved by both Lewis and Clark County and DEQ and has been in full use for years by the individual Homeowners. Whatever permitting disputes exist between the Bureau of Reclamation and the DNRC are beyond the scope of subdivision approval and the Homeowners Association should bear the expense of that permitting.

5. There are adequate funds in the Grand Valley Estates Homeowners Association account to pay Homeowners's fees and costs. The Receiver controls the funds in the account and she can utilize those funds for the very purpose they were intended: the general benefit of the subdivision homeowners. *Doc*. 144 and 145.

A hearing was held on September 21, 2018. The Receiver's counsel stated that the remaining issues for resolution included: (1) the water use permit; (2) the IRS tax issue; and (3) money for a "final accounting." *Hrg Trans.*, 6:25 to 9:9. Bryan Gartland, the Helena Regional Manager for DNRC, testified about the DNRC permit, which does not allow the Homeowners to water their lawns. They can only use water for interior use. *Id*., 11:17 to 13:25. Gartland testified that while DNRC administers the Montana Water Use Act, which includes water rights and water use, DNRC does not have any involvement in the approval of a water system that is

submitted to DEQ for approval. Nor does DNRC have any involvement with the county approval process, except, perhaps, to "review and comment on the means of diversion or the general system or pump specifications for a well." *Id.*, 41:23 to 43:8.

The Receiver for the Corporation, Rita Cortright, testified that as of September 20, 2018, the Corporation had a checkbook balance of $2,721.76. However, it had the following outstanding invoices:

- Doug Williams, CPA, for the Harrisons'[4] 2017 tax preparation in the amount of $1,675;
- Jackson, Murdo, and Grant billing that totals $7,204;
- Luxan and Murfitt for September hours in the amount of $4,368;
- the Receiver's estimated time for the month of September at $400;
- potential IRS taxes and penalties in the amount of $3,068 in taxes owed, and a potential penalty of $2,354.85;
- payment of property taxes on the four common areas for Grand Valley Estates Subdivision in the possible amount of $2,127.44; and

[4] Which was inaccurate, since the Harrisons had their own accountant from Anderson Zurmeuhlen, Tiffany Hanson, to prepare their taxes.

- To finish up the Receiver's work she would have an audit prepared.

Id., 50:19 to 52:16. The Receiver also controls the checking account for the Grand Valley Estates Homeowners Association.[5] Even though the Receiver had signed a Settlement Agreement to set aside $34,082.81 for the payment of corporate expenses, they were asking for another $18,475 in corporate costs. *Hrg. Trans.*, 54:7 to 57:6.

The District Court's Order

On November 9, 2018, the District Court filed its Order now on appeal. *App*. A; *Doc*. 149. In its order, the District Court made the following relevant findings:

> 12. Pursuant to the terms of the settlement agreement, the Receiver paid Tom and Kim Harrison $545,227.39, and, pursuant to the terms of the settlement agreement, they became the sole shareholders in the corporation, with 50 percent ownership each.[6]

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[5] According to the Receiver's Report for December 2018, the Grand Valley Homeowner's Association checking account had a balance of $29,376.69 on December 31, 2018. *Doc*. 167, GVA p. 1.

[6] That finding was clearly erroneous. Tom and Kim were paid $454,786.68.

13. The Receiver testified that the known unresolved debts of the Lincoln Road RV Park, Inc., will require funding in the following estimated amounts:

a.	IRS taxes and Penalties	$6,000 to $8,000
b.	Estimated cost for DNRC water mitigation	$500 to $10,000
c.	Remaining amount owed as legal fees for Intervenors[7]	$7,204.00

The District Court then determined that under its equitable powers it had the legal authority to fashion an equitable remedy appropriate to the circumstances of the case. The Court reasoned:

> If the assets of a corporation have been distributed in liquidation, a claim may be enforced against a shareholder to the extent of the corporate assets distributed to the shareholder. Mont. Code Ann.§§ 35-1-936 and -937(2)(b). A shareholder may become personally liable for the acts or debts of the corporation by reason of that shareholder's own acts or conduct. Mont. Code Ann.§ 35-1-534(2).
>
> Where the liability for the IRS taxes and penalties was

[7] The District Court ordered that these attorney's fees be paid from the GVHOA funds. The attorneys' fees issue is therefore not a part of this appeal.

> incurred during the time that the Shareholders were in control of the corporate bank accounts (prior to appointment of the Receiver in December 2015) and the liability was incurred based on their own acts and conduct, they can be held jointly responsible for payment of that debt. Further, because the shareholders sold the subdivision lots based on availability of appropriate irrigation rights, they can be held personally responsible for the ongoing corporate obligation of paying the cost of providing a valid water use permit for the subdivision.
>
> The Court approved a distribution to Shareholders Kim Harrison and Thomas Harrison of over a half million dollars as part of the 2017 Partial Settlement Agreement.

App. A, 8:4-20. The District Court then ordered both Tom and Kim each to provide $25,000.00 to the Receiver to be used to pay the ongoing expenses of the corporation or they would be held in contempt. *Id*., 9:1-10.

Tom and Kim timely appealed.

STANDARD OF REVIEW

This Court's duty upon review of equity cases and proceedings of an equitable nature is to review all questions of fact arising upon the evidence presented in the record, whether the evidence is alleged to be insufficient or

not, and to determine the same, as well as questions of law. § 3-2-204(5), MCA. There is in that statutory requirement for this Supreme Court's appellate review a measure of protection for the losing party coming to the Court on appeal in equity cases. *Daniels v. Thomas, Dean & Hoskins, Inc.* (1990), 246 Mont. 125, 134; 804 P.2d 359, 364.

Equitable remedies are reviewed for an abuse of discretion. *Ruegsegger v. Welborn* (1989), 237 Mont. 317, 321, 773 P.2d 305, 308 (1989). In order to establish an abuse of discretion, "the appellant must demonstrate that the district court acted arbitrarily without conscientious judgment or exceeded the bounds of reason." *Seltzer v. Morton*, 2007 MT 62, ¶ 65, 336 Mont. 225, 154 P.3d 561.

A district court's findings of fact are reviewed to determine if they are clearly erroneous. *In re Marriage of Olson*, 2008 MT 232, ¶ 20, 344 Mont. 385, 194 P.3d 619. "A finding is clearly erroneous if it is not supported by substantial evidence, the district court misapprehended the effect of the evidence, or [a] review of the record convinces [this Court] the district court made a mistake." *Id.* A district court's conclusions of law are reviewed de novo to determine if they are correct. *Id.*

SUMMARY OF THE ARGUMENT

There is no evidence in the record upon which to base a legal conclusion

of personal liability sufficient to pierce the corporate veil and the District Court abused its discretion in-so-doing. The District Court was also clearly erroneous when it found that it approved a distribution to Shareholders Kim Harrison and Thomas Harrison of over a half million dollars as part of the 2017 Partial Settlement Agreement, and that Tom and Kim sold the subdivision lots based on availability of appropriate irrigation rights. The District Court was also legally incorrect when it determined that the Homeowners' claims should at this juncture be enforced against Tom and Kim to the extent of the corporate assets distributed to them under §§35-1-936 and 937(2)(b), MCA, and that they are personally liable for the acts or debts of the corporation by reason of their own acts or conduct. §35-1-534(2), MCA.

ARGUMENT

The District Court abused its discretion when it utilized its equitable powers and required Tom and Kim to personally provide funds to pay corporate debts or be held in contempt.

* * * * *

1. There was no legal basis to require Tom and Kim to each personally pay $25,000 for Corporate debts and costs.

It is well settled under Montana law that a corporation has a separate

and distinct identity from its stockholders. *Moats Trucking Co., Inc. v. Gallatin Dairies, Inc.*, 231 Mont. 474, 477, 753 P.2d 883, 885 (1988).

§ 35-1-534(2)(a), MCA provides that "a shareholder who is active in a corporation *is not personally liable for the acts or debts of the corporation* except that a shareholder may become personally liable by reason of that shareholder's own acts or conduct." (Italics added.) As such, shareholders are not personally liable for the acts of a corporation unless the distinction between the corporation and the shareholder is disregarded, i.e., unless the "corporate veil" is pierced. *Peschel Family Trust v. Colonna*, 2003 MT 216, ¶¶21-42, 317 Mont. 127, ¶¶21-42, 75 P.3d 793, ¶¶21-42.

Here, the District Court expressly rejected the first Settlement Agreement where the parties sought to set aside $50,000 to "complete the remaining tasks regarding the subdivision, sewer, and water systems." *App. D*, 3:18-20, 8:2-3. Instead, after a negotiated settlement, both the District Court *and* the Receiver decided that they preferred instead for the Corporation to "retain $34,000 to finish certain tasks and address potential liabilities involving the Intervenor Homeowners." *App.* B, p. 2. This was the result of numerous discussions and careful and thoughtful consideration of the scope of the remaining issues. See, *Doc.* 106, p. 3, ¶¶ 8 and 10 (Receiver "[h]ad multiple discussions with Scott Svee regarding outstanding issues of

concern for the GVE homeowners and status of Receiver's completion of tasks to date . . . Discussed the terms of the settlement agreement reached by the four shareholders and its impact on the Receivership"); *Doc.* 113, p. 2, ¶ 4 ("[h]ad multiple discussions with Scott Svee regarding outstanding issues of concern for GVE homeowners, and status of Receiver's completion of tasks to date"); *Doc.* 122, p. 2 ("Telephone conferences with Candace Payne and Scott Svee regarding questions from homeowners represented by Scott"). By agreeing to $34,000, both the Receiver and the District Court waived any claim to additional funds for the purpose of dealing with any further issues relating to the subdivision. After resolving the matter pursuant to a negotiated Settlement Agreement, it is unfair and a violation of Tom and Kim's limited liability protection under § 35-1-534(2)(a) for the Receiver to run back to the Court asking for more money, and for the District Court to order that Tom and Kim personally pay $25,000 each.

Count 7 of the Homeowners' Complaint alleges a claim for individual liability and to pierce the corporate veil. *Doc.* 75, p. 11, ¶¶ 80-83. The District Court's September 12, 2017, order approving the settlement agreement expressly stated that "the remaining claims by the Intervenor Homeowners shall remain to be litigated in the case." *App.* B, p. 3, ¶ 5. There has been no scheduling order in the Homeowners' case, no discovery

has been undertaken, no motions have been filed, there has been no trial, and the evidentiary record before the District Court does not establish a factual or legal basis for holding Tom and Kim individually responsible for paying any of the costs claimed by the Receiver. The affidavits that have been filed in the case (Docs. 7, 8, 9, 10, 11, 18, 18, 29, 21, 22, 36, 43, 44, 48, 49, 50, 51, and 52) do not assert facts relative Tom or Kim's "own conduct" sufficient to hold them personally liable for the Corporation's debts. The only evidentiary hearing ever held in the entire case occurred on September 21, 2018, and that consisted only of the brief testimony of Bryan Gartland and Rita Cortwright. Neither witness talked about Tom or Kim's "own acts or conduct." There was further no evidence before the District Court that "the shareholders sold the subdivision lots based on availability of appropriate irrigation rights." Aside from conclusory statements of fact, the District Court neither cited nor discussed specific evidence in the record supporting those findings or any evidence that would suffice to pierce the corporate veil.

Furthermore, the finding that the Court approved a distribution to Tom and Kim "of over a half million dollars as part of the 2017 Partial Settlement Agreement" is clearly erroneous. In fact, $80,592.12 attributed to Tom and Kim were tax payments to the IRS and the Montana Department of Revenue made by the Receiver long before the Settlement Agreement was ever

negotiated or approved. See, *App*. F; *Doc*. 94 (Exhibit D, pp. and 5 (Check Nos. 1302, 1306, 1307, 1308, 1309, 1310); *Doc.* 106, Exhibit B, p. 1 ("Thomas and Kimberly Harrison Distribution $27,570.60"); and *Doc*. 113, Exhibit B, p. 1 ("Thomas and Kimberly Harrison Distribution $80,592.12"). Tom and Kim only received $454,786.68.

In short, the District Court's findings were clearly erroneous. They were not supported by any substantial credible evidence. An evidentiary hearing was never held, and nobody ever testified to any of Tom or Kim's own acts or conduct that might be sufficient to pierce the corporate veil.

The District Court was also incorrect as a matter of law when it relied upon §§ 35-1-936 and -937(2)(b) for the proposition that "if the assets of a corporation have been distributed in liquidation, a claim may be enforced against a shareholder to the extent of the corporate assets distributed to the shareholder." *App*. A, 8:4-6. Neither of those statutes apply to this situation.

§ 35-1-936, MCA, outlines the procedure for the disposition of known claims against a dissolved corporation. § 35-1-937, MCA provides for unknown claims against a dissolved corporation. Neither statute applies here because the Corporation has not been dissolved. The statutes furthermore only set forth the procedure and deadlines for the filing of claims before they are barred. There is a distinction between filing a claim, and prevailing in

litigation so that a judgment may be entered and enforced. That hasn't happened here, and as stated above, a scheduling order is not even in place yet. The District Court placed the proverbial cart before the horse by ordering Tom and Kim to personally pay $25,000 each for the payment of corporate expenses before there has been any kind of determination that the corporation is liable, much less that the corporate veil should be pierced holding Tom and Kim personally responsible for that payment.

2. The IRS taxes and penalties.

As for the Corporation's tax liability and penalties, it is basic that S corporations are taxed as if they were partnerships rather than corporations. The primary benefit offered by S corporations is a means to avoid the taxation of income both to the corporation as a separate entity and again to the stockholders as dividends when distributed. Therefore, when an S corporation makes a distribution of its earnings and profits to its stockholders, the distribution is taxed to the stockholders as a dividend. 26 U.S.C. § 316(a). S corporation money distributions are taxable to shareholders as dividends to the extent of the current year's earnings and profits. However, to the extent that the taxable income of a Subchapter S corporation exceeds money distributions for the current year, the difference is also taxed directly to the shareholders at their personal rates rather than

being taxed to the corporation as a separate entity. 26 U.S.C. § 1373(b); see also *De Treville v. United States*, 445 F.2d 1306, 1308-09 (4th Cir 1971). Any tax liability of the Corporation therefore passes through to Tom and Kim. That is why the Receiver made $80,592.12 in tax payments as set forth above and attributed them as distributions to Tom and Kim. For a Subchapter S corporation like Lincoln Rd. RV Park, Inc., the tax liability flows through to Tom and Kim. This means that it is an obligation that Tom and Kim must deal with personally, and it is not a matter for the Receiver or for the Corporation. If it is, then the tax constitutes an impermissible double tax. *Byrne v. Comm'r*, 361 F.2d 939, 942 (7th Cir.1966).

The point is, the Corporation's tax liability, if any, is not a matter for the Receiver to deal with. It is a matter for Tom and Kim to attend to personally. That is most likely why the Receiver could not provide the Court any specific information when she testified at the September 21, 2018, hearing. The District Court therefore abused its discretion when it ordered Tom and Kim to pay $25,000 each for the Corporation's alleged tax liability.

As to the tax penalties, it is crystal clear that shareholders are not personally liable for the payment of a corporation's tax penalty. *In re Tax Refund Litig.*, 766 F. Supp. 1248, 1258 (Dist.Ct. E.D.N.Y. 1991), affrm'd *In re Barrister Assocs. v. United States (In re MDL-731--Tax Refund Litig. of*

Organizers & Promoters of Inv. Plans Involving Book Props. Leasing), 989 F.2d 1290, 1305, n. 5 (2nd Cir. 1992). The District Court therefore also abused its discretion when it ordered Tom and Kim to pay $25,000 each for the Corporation's alleged tax penalty.

CONCLUSION

The District Court's order must be reversed and vacated. The matter should be remanded to the District Court with instructions to proceed forward with the litigation involving the Homeowners.

DATED this 1st day of February, 2019.

By: s/ Palmer Hoovestal
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CERTIFICATE OF COMPLIANCE

Pursuant to Rule 27 of the Montana Rules of Appellate Procedure, I certify that this principal brief is printed with a proportionately spaced Century Schoolbook text typeface of 13 points; is double-spaced except for footnotes and for quoted and indented material; and the word count calculated by WordPerfect is 5,130 words, and not averaging more than 280 words per page, excluding caption, table of contents, table of authorities, certificate of compliance, and certificate of service.

DATED this 1st day of February, 2019.

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CERTIFICATE OF SERVICE BY E-FILING

I hereby certify that on the 1st day of February, 2019, I duly served a true and correct copy of the foregoing **BRIEF OF APPELLANTS** on the counsel listed below by e-filing or email, to:

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APPENDIX

Order on Receiver's Application for Further Instruction (Nov. 9, 2018). . . . . A

Order Approving Partial Settlement Agreement (Sept. 12, 2017). . . . . B

Mutual Release and Settlement Agreement (Aug. 8, 2017). C

Order on Pending Motions (May 31, 2017). . . . . D

Mediation Agreement (Aug. 30, 2016). . . . . E

Tax Payments. . . . . F

Electronically Signed By: Palmer A. Hoovestal
Dated: 02-05-2019