

VERMONT SUPERIOR COURT

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CIVIL DIVISION

Case No. 118-12-20 Lecv

Hirschak vs. Hirschak et al

ENTRY REGARDING MOTION

Title: Motion for Preliminary Injunction; Renewed Motion for Preliminary Injunction

(Motions: 1; 3)

Filer: Christopher D. Roy; Christopher D. Roy

Filed Date: December 03, 2020; March 29, 2021

The motion is DENIED.

The parties to this case are three brothers and the LLC they formed in 2018 when they purchased their father's business when he retired. Disagreements developed and this is the second lawsuit between them. The first resulted in a settlement, but further disagreements developed. In this suit, the Plaintiff brother, Garret, claims breach of fiduciary duty and seeks dissolution and winding up of the LLC. The other two brothers, Toby and Tyler, have counterclaimed for breach of fiduciary duty, unjust enrichment, and expulsion of Garret from the LLC.¹ All parties acknowledge that the three-member business cannot continue as is, as the three brothers cannot work together, and the LLC needs to be wound up or restructured. They have not agreed on terms. This motion seeks an injunction as to conduct of the business prior to final resolution.

Their father had operated the business in three divisions. Real estate and commercial personal property divisions were operated out of Morrisville, and the auto division was operated in Williston. When the brothers set up the business, each was to be responsible for one of the three divisions. Garret was allocated responsibility for the auto division which involved conducting regular auto auctions. After about two years, Toby and Tyler stopped paying his compensation and made management decisions without him, and later removed him from the role.

In this suit Garret filed a Motion for a Preliminary Injunction and a Renewed Motion in which he seeks reinstatement as the manager of the auto division, compensation equal to the amounts his brothers receive in the form of salary, prohibition against making company decisions without notice to and involvement of him, and provision of weekly financial reports. A Partial Stipulation was filed and issued as an Order on May 17, 2021.

¹ Because all of the brothers (and their father) have the same surname, the court uses first names for clarity.

An evidentiary hearing on the remaining issues in the Motion and Renewed Motion was held on December 20, 2021 and January 31, 2022. Based on the evidence presented, the court makes the following findings of fact.

Facts

The brothers' father, Thomas Hirschak, ran the company from the 1970's until 2018, when he retired. His wife, Terry Owen, began as a bookkeeper for the company 38 years ago, but for the last 15-20 years she oversaw its finances at a supervisory level as well as doing other work in the business. The company had a bookkeeper, but Terry Owen supervised the bookkeeper and financial reports, and the company utilized an accountant at the end of the year. All three brothers worked in the company as they grew up. Eventually, Garret left for other work and has done well financially. He and his wife own a real estate company that employs 400 people (MSI), and a second related company (SDI). Toby and Tyler both continued to work in their father's business, which was called The Thomas Hirschak Company.

The three brothers bought the company and its assets from their father on September 4, 2018. Toby and Tyler would most likely not have been able to afford, on their own, to buy the business from their father when he retired. Garret contributed \$300,000 as a down payment on the purchase of the real estate, and has made other cash contributions for operational expenses as well, which he estimates total around \$800,000. He testified that critical to his agreement to become a member was an agreement made between the brothers that he claims was ratified in December of 2019 and September of 2020. It was that each of the three would receive equal compensation from the business.

At the time of purchase, the brothers formed Hirschak Brothers LLC² (hereinafter LLC) and signed an Operating Agreement, but the evidence shows that they also made other agreements about how the business would be run that are not apparently documented. They agreed that each would be responsible for one of the divisions: Tyler for real estate, Toby for commercial, and Garret for auto. They would each receive an equal amount in compensation from the business, but Garret would take his distribution in the form of payments to his separate business, MSI, as a "subcontractor," and Toby and Tyler would take theirs as employees. Garret testified that the reason for his subcontract was that it would save 13% in taxes. Toby claims that there was no "formal" agreement for equal compensation. The lack of documentation does not mean an agreement was not reached. Although there is apparently no written agreement, the evidence supports a finding that the brothers did make that agreement, as that is what happened for over a year. Garret operated the auto division and MSI received payment on contract invoices of \$2,400 per week for the auto division and \$255 per week for each of the commercial and real estate divisions.

² Apparently the LLC continues to do business under the name of The Thomas Hirschak Company.
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Another agreement they made, not in writing but carried out and undisputed, was that rather than continuing the financial management of the business the way it had been done by their father, Garret's company, MSI, would handle all financial management as well as human resources and information technology matters. It already had personnel doing those functions for its own business purposes, and it would presumably save costs to have it handle these functions for the LLC. Thus, all the books were managed out of MSI. Terry Owen continued to be involved in the business for about a year, conducting auctions and helping with business operations and transition, but she no longer had any role in financial management. She was aware of the work of Melanie at MSI regarding finances, and respected her work. At the end of 2019, Terry Owen stopped working in the business altogether and joined her husband in Florida.

Throughout the end of 2018 and all of 2019 and much of 2020, all bookkeeping, accounting, and financial management functions were done by MSI. Occasionally each of the brothers asked for MSI and/or SDI, to provide some other services, which it did, and MSI or SDI billed the LLC. For example, if the cars at the auto auction site in Williston needed the snow brushed off, MSI or SDI provided a worker and billed the LLC. Similarly, Toby and Tyler requested services for their divisions to be performed by MSI, for which it billed the LLC. Toby and Tyler had little involvement in overall finances and did not inspect bills or accounts. Garret managed the financial organization and operation of the new LLC. The evidence suggests Garret did not provide them with much financial information, and they did not ask for it. None of the three brothers kept track of hours worked, but each received regular and equal distributions from the LLC, although Garret's was paid to MSI pursuant to invoices from MSI to the LLC.

In the latter part of 2019, Toby and Tyler began to look at the invoices from MSI paid by the LLC, and they began to question whether the LLC was being overbilled by MSI. They began to think that Garret was enriching his own businesses at the expense of the LLC. There was a shortage of cash at the end of 2019, and the LLC stopped paying bills from MSI and SDI. Shortly thereafter, in March of 2020, Covid caused all business operations to change significantly. For a time, no auto auctions could be held. Eventually, auctions were resumed online. However, the business overall suffered during the Covid period and relations between the brothers soured. In May of 2020, Garret wrote an email to Toby and Tyler stating that he did not see that "it's going to work with 3 of us as owners. . . The company can't sustain the current model and we haven't been able to agree on a path forward." (Ex C) He made a proposal to sell his shares. In July of 2020 he made another proposal to restructure the company.

In August of 2020, Toby and Tyler filed the first lawsuit. It ended rather quickly with a Settlement Agreement (Ex. 2) that provided that: all financial records would be moved from Garret's MSI business office to the LLC's business office on Cadys Falls Road in Morrisville, all members would have equal access to all financial accounting records, Garret would "maintain his status as an Independent Contractor for compensation purposes," and an independent audit of the company's finances and accounts would be conducted as soon as possible.³ Toby testified

³ The terms of the Settlement Agreement show that various brothers are also members of other entities that are not part of this lawsuit but were part of the financial investigation and report.

that although there was a written agreement for Garret to continue to be an independent contractor, there was no agreement as to the amount of payment. He appears to believe that because no amount was agreed upon, none needs to be paid. Garret believes this provision was a confirmation of the prior agreement for equal compensation.

Toby and Tyler assumed responsibility for managing finances. They hired a bookkeeper. In September of 2020, Toby and Tyler decided that they wanted to change the way the brothers were compensated. The LLC would no longer make equal monthly distributions to the three brothers; rather, it would only pay each as an employee based on hourly rates requiring that each brother keep track of his work time. Garret declined to agree to this change. His position was that a fundamental reason that he agreed to become part of the business and contribute so much cash to it was that all three brothers would receive equal compensation regardless of the differences in their roles, work hours, and cash contributions. Garret did not keep records of hourly work time, and Toby and Tyler stopped paying MSI altogether.

Toby and Tyler made management decisions without consulting Garret, including taking out a second Covid-related loan on behalf of the LLC, changing the 401(k) supplier, and changing a tax account.

The bookkeeper Toby and Tyler hired worked for 4-5 months but she did not work out as the work was "over her head." She left and financial records were not in good shape. Garret, who was working but not receiving compensation through MSI, filed this lawsuit in December of 2020. Thomas Hirschak (father) and Terry Owen learned about the interpersonal and financial troubles of the brothers' business. Mr. Hirschak had financed his sons' purchase, and the LLC continued to owe him money. He asked for accounting and recordkeeping files, presumably assuming that there would be files and reports of the type kept when he owned the business, and there were no comparable reports.

In January of 2021, Toby and Tyler told the employees that they had removed Garret as manager of the auto division. On February 3, 2021, they sent him a letter stating that he was not an employee of the LLC and was not entitled to compensation, and they would not pay MSI invoices. They clearly stated that they were making this business decision (there had apparently been no formal meeting of members). They said he was entitled to receive financial statements and "to attend the Company's management meetings held each Monday morning at 8:30." (Ex. E) Garret has continued to assert his claim to monthly distributions from the LLC on a contract basis through MSI, and MSI sends monthly bills. Terry Owen returned to work with Toby and Tyler in early 2021. She reinstated the accounting routines that the former business had used. She is clear, as is everyone, that the three brothers cannot sustain a business working relationship and their joint business has to be terminated in some manner.

In April of 2021, pursuant to the Settlement Agreement the accountant submitted a report that stated that for the years 2018-2020, related party expenses (amounts paid to entities in common ownership with members, such as MSI and SDI) were properly supported with invoices and spreadsheets, although prearranged services and costs related to those invoices were not documented. This is consistent with the evidence that Toby and Tyler had left all financial

matters, including billing practices between the LLC and MSI, up to Garret, who had documented everything with invoices but had not discussed with the others terms of how much would be paid for what items or services. They now suspect him of feathering his own nest. He claims he was responsible for significant responsibilities for financial matters during the early period of the new business and its setup and transition to new practices, and that if his company had not provided those services, the LLC would have had to hire them to be done elsewhere.

MSI and SDI claim unpaid invoices and have filed a separate lawsuit in docket number 21-CV-01922 against the LLC in which they seek to collect on invoices.

Garret testified that he has received LLC financial statements since Toby and Tyler took over, but that they are infrequent and incomplete. He attended Monday morning management meetings for a while, but stopped in September of 2021 after finding it difficult to get information. He concluded that the meetings consisted mostly of reviewing upcoming schedules and that that was not when substantive management decisions were made.

Garret testified that he was not seeking to be the permanent manager of the auto division; rather he wants to settle differences and turn the business over to Toby and Tyler. Garret believes that Toby and Tyler are benefitting by making the business look profitable and paying themselves accordingly, while not paying him anything or reimbursing him for his cash inputs and that therefore they are making profits off his back. He believes that they have no incentive to reach resolution because they can just draw out the period of not paying him anything while enjoying the profits resulting from not doing so. Toby believes that Garret is deliberately sending invoices and demanding payment to drive up the debt in order to be able to maximize the amount he claims is due him so that the company will have to be dissolved and he can wind up with its assets.

Toby testified that financial reports are given to Garret every two weeks. Garret claims they are not complete. He specifically identified amortization and bills payable as not having been included in profit and loss statements. Toby appears to take the position that Garret can ask for what he wants. Toby also testified that he did not object to providing weekly reports.

In sum, Garret claims that he only agreed to be a part of this close business and to provide cash to make the purchase of the business from their father possible, and to subsequently make other cash infusions, because of the agreements made to induce his participation, specifically: that he would run the auto division, that each brother would receive equal compensation, that he would participate in management, and that he would have access to all financial information. He seeks a preliminary injunction to enjoin Toby and Tyler and the LLC from departing from these obligations to him, at least until such time as the business relationship is terminated. He claims that without an injunction, Toby and Tyler are getting a "free ride" by not paying him anything or reimbursing him for his contribution while they are enjoying the profitability that results from not meeting obligations.

Toby and Tyler claim that the Operating Agreement does not entitle any member to employment, and that Garret had the opportunity to be paid for work done on an hourly basis but he has declined the opportunity. They also do not want him working in the business any more.

Analysis

The case is before the court at this point for decision on Garret's request for a preliminary injunction. "The movant bears the burden of establishing that the relevant factors call for imposition of a preliminary injunction." *Taylor v. Town of Cabot*, 2017 VT 92, ¶ 19, 205 Vt. 586. Those factors are: (1) the threat of irreparable harm to the movant; (2) the potential harm to the other parties; (3) the likelihood of success on the merits; and (4) the public interest. *Id.* The terms of a preliminary injunction Garret is seeking are that he be reinstated as the person responsible for the auto division, that he receive the same compensation as his brothers, that he be given the opportunity to participate in management, and that he receive weekly financial reports.

Reinstatement as Manager of the Auto Division.

Irreparable harm. Evidence shows that Garret was seeking to terminate his business relationship with the LLC as early as May of 2020. His own testimony was that he is not seeking to be the permanent manager of the auto division, but rather to get his "position" back of receiving equal money from the LLC as well as to resolve terms for winding up. He is not seeking to regain an opportunity for work, but rather payment for his willingness to invest and participate in this business. This is manifest in his complaint for dissolution and his testimony. Since his objective is payment, a money remedy would be sufficient, and he has not shown that lack of reinstatement to the management role prior to final resolution will cause irreparable harm.

Potential harm to others. All parties are clear that the best future for everyone is termination of the three-brother business partnership. Reinstatement of Garret as manager of the auto division would be a step backward and would likely promote discord that would be counterproductive to business productivity and relations, which is not in the interests of any of the brothers or the public.

Likelihood of success on the merits. Since all parties seek to terminate their business relationship, as their pleadings and evidence show, likelihood of success in obtaining reinstatement is not shown.

Public interest. Public policy is reflected in 11 V.S.A. Chapter 25, Subchapters 6 and 7, which provide for a winding up process for nonfunctional business organizations.

Summary. None of the factors support reinstatement of Garret to the role of responsibility for the auto division.

Compensation payments in the same amount as Toby and Tyler

Irreparable harm. The invoices Garret continues to send from MSI demonstrate a claim for compensation in the same amount previously paid, whereas the argument he has made is for compensation in an equal amount to the amounts paid Toby and Tyler. These amounts are presumably based now on hours worked, and it is unknown what those amounts are and whether Toby and Tyler receive the same or different amounts. In any event, the remedy for a successful claim would be a judgment for money damages for loss of compensation. Garret has not shown irreparable harm in support of injunctive relief on this claim.

Potential harm to others. Toby and Tyler may consider that the LLC would be harmed by having to pay for services not being performed. Garret argues that the business only exists because he put money into it in reliance on the incentive of receiving the same compensation as his brothers. In view of the fact that a money judgment would be the available remedy, this factor does not support the request for a preliminary injunction.

Likelihood of success on the merits. Garret is seeking compensation payable to MSI under a contract between the LLC and MSI, and MSI is not a party to this suit.⁴ Garret chose to take compensation from the LLC in the form of payment to a separately organized, owned, and controlled business organization under a contractual relationship, and presumably enjoyed tax benefits as a result. Since it is MSI, and not Garret personally, that seeks compensation and is the entity that would be entitled to it, it is questionable whether Garret could succeed in compelling compensation to MSI within the framework of this case. Even if Garret as a member has standing to seek enforcement of the 2018 agreement, there is no evidence of a contract between MSI and the LLC signed by an authorized representative on behalf of the LLC, and thus enforcement in 2022 of an agreement made in 2018 may not be available under the statute of frauds, 12 V.S.A. §181 (4). Garret also relies on the Settlement Agreement of August 2020, which specifically provided for him to “maintain his status as an Independent Contractor for compensation purposes.” The fact that no specific amount was stated and the word “maintain” was used favors Garret’s argument that at least that some amount was contemplated. Garret’s real argument is that the reason he should continue to receive payments through MSI is that he only agreed to become a member and provide capital and cash infusions in reliance on the inducement that he would receive compensation equal to that of his brothers. The evidence did not include details of any original agreement sufficient for the court to find a likelihood of success on the merits. This, combined with the fact that a money remedy is available for this aspect of the claim, means that this factor does not support the issuance of a preliminary injunction.

Public interest. It is predictable that informal management agreements among business partners in a close business made at the time the business is created may need to be adjusted with experience as the business develops and as external circumstances affect the business. Unless there is an enforceable contract compelling some action, public interest as set forth in 11 V.S.A.

⁴ MSI and SDI are also seeking compensation against the LLC in the separate lawsuit in 21-CV-01922, presumably based on the same invoices upon which Garret relies in this suit.

§4054 favors members of a member-managed LLC being able to modify practices through management decisions pursuant to their Operating Agreement. In addition, the public interest strongly favors promptly proceeding to a resolution of terms between LLC members when they do not agree about fundamental management issues. 11 V.S.A. Chapter 25, Subchapters 6 and 7.

Summary. Garret has not met the burden of proving that the factors support the issuance of a preliminary injunction compelling monthly payments to MSI in either the amount previously paid or some unknown amount currently received by one or both of the other brothers.

Prohibition against management decisionmaking without notice to and involvement of Garret

This claim appears to have been at least partially resolved by the Partial Stipulation and Order issued May 17, 2021. The evidence shows that Toby and Tyler made management decisions on their own from August of 2020 through January of 2021. However, on February 3, 2021 they sent Garret a letter stating that management meetings would be held Monday mornings at 8:30 and they acknowledged that he was entitled to attend. (This letter was sent after Garret filed this Motion for Preliminary Injunction, in which he sought such relief.) It appears that the filing of the motion prompted recognition of his right to notice of management meetings. The Partial Stipulation and Order of May 17, 2021 specifically provided for the relief requested on this claim.

Garret did attend Monday meetings until he stopped in September of 2021 based on his own conclusion that they were primarily scheduling meetings. However, the evidence of what actually happened at those meetings is thin, and there is no evidence of major management decisions having been made after February of 2021 outside of those meetings. Garret's failure to attend scheduled management meetings after September 2021, together with the absence of any evidence of decisions made outside of those meetings, together with the Order of May 17, 2021, show that none of the four factors support the issuance of an injunction on this claim.

Provision of financial reports to Garret

This claim appears to have been resolved by the Partial Stipulation and Order issued May 17, 2021, which provided for Garret to receive weekly backup of the company's QuickBooks reports. Garret testified that the reports he has received are incomplete in that they do not take into account certain components that he believes should be included. However, he did not provide specific evidence of having requested identified items. Garret remains a member and is entitled by the terms of the Operating Agreement and the Settlement Agreement to have access to all financial information. Toby's testimony that reports are provided to Garret every two weeks, rather than weekly was unrefuted, but Toby agreed to provide such reports weekly. Based on the terms of the Operating Agreement, Settlement Agreement, Order of May 17, 2021, and Toby's agreement to provide reports weekly, injunctive relief is not necessary.

Order

For the foregoing reasons, the Motion for a Preliminary Injunction is *denied*.

The attorneys shall submit a stipulation for a pretrial scheduling order by **March 1, 2022**.

Electronically signed pursuant to V.R.E.F. 9(d) on February 14, 2022 at 10:05 AM.



Mary Miles Teachout
Superior Court Judge