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December 1, 2023

Clerk of the Court
CALIFORNIA COURT OF APPEAL, THIRD DIVISION
601 W. Santa Ana Blvd.,
Santa Ana, CA 92701

Re: Case Name: ***Wardak v. WLOW Partners, LLC***
Case No. G061606
Submission: Appellant's Supplemental Letter Brief (Corrected Version)

Dear Sir or Madam:

In the above case, I represent the Appellant, Bastel Wardak. On his behalf, I now submit the corrected version of Appellant's Supplemental Letter Brief in response to the Court's briefing order of November 17, 2923, which invited the parties to submit letter briefs that give their answers to three queries.

The original version of this brief had various formatting problems and required minor, non-substantive corrections. It is otherwise identical to the original version, which I filed yesterday, November 30, 2023.

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Dated: December 1, 2023

Respectfully submitted,

By: *William Markham*

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I. EXECUTIVE SUMMARY

Wardak's Response to Query No. 1. Wardak's answer to query no. 1 is "Yes."

1. Respondent Dwaine K. Dirks breached various fiduciary duties that he owed to WLOW Partners, LLC under section 17704.09(b)–(c) by having it adopt the Second Operating Agreement in May, 2015.[1] (*See* pp. 17–31, 33–34, 39–51, *infra*.)

2. This agreement superseded WLOW's prior agreements and saddled WLOW with problematic funding and penalty provisions (the "Joint-Funding Clause" and the "Forfeiture Provisions"), which Dirks supplied, insisted on including in the agreement, and could and did misuse to advance his own improper purposes at WLOW's expense. (*See* pp. 18–22, n.5, *infra*.)

3. In particular, Dirks misused these provisions to: (a) prevent Wardak from providing WLOW its required funding; (b) disband and dissolve WLOW at a time when Wardak could and would have fully funded its property development; (c) strip WLOW of its property and other assets; and (d) transfer these assets to a competitor that Dirks and Omar owned and operated. (*See* pp. 19–27, *infra*.) By this conduct, Dirks breached the following fiduciary duties that he owed to WLOW: the duty of loyalty under section 17704.09(b); the duty to hold in trust under

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1 All statutory references in this brief are made to various sections of the Corporations Code.

section 17704.09(b)(1); the duty to avert conflicts-of-interest under section 17704.09(b)(2); and the duty not to compete under section 17704.09(b)(3). (*See* pp. 29–34, 42–45, *infra.*)

4. Dirks also used the Second Operating Agreement to overstate his capital contributions to WLOW and later used the inflated figure to support a demonstrably unfounded claim against WLOW for reimbursement of his capital account. He also presented another demonstrably unfounded claim against WLOW, seeking repayment of a loan that he claimed to have made to it, but apparently had never made. By these two claims, which he lacked any reasonable basis to assert, Dirks sought more than $1.3 million from WLOW's damage award of $1.5 million. By all of these acts, Dirks breached his fiduciary duty to account to WLOW, which is codified at section 17704.09(b)(1). (*See* pp. 39–47, *infra.*)

Wardak's Response to Query No. 2. Wardak's answer to query no. 2 is also "Yes."

1. Dirks breached various fiduciary duties that he owed to WLOW under section 17704.09(b)–(c) by exercising his right under the Second Operating Agreement to dissolve WLOW and take sole ownership of its membership interests and therefore its assets. (*See* pp. 31–49, *infra.*)

2. Dirks breached his fiduciary duties of loyalty and care under section 17704.09(b)–(c) by disbanding and dissolving WLOW at the very time when Wardak was ready, willing, and able to furnish all of its required funding on the same terms and

conditions that it had previously accepted when Wardak and Omar were supposed to provide the funding jointly. If WLOW had received this funding, it would have completed its property development. By refusing Wardak's offer and dissolving WLOW, Dirks acted in a manner that was directly contrary to WLOW's interest. By these acts, Dirks breached his duty of loyalty to WLOW, which is codified at section 17704.09(b). (*See* pp. 19–27, 33–34, *infra*.)

3. By taking WLOW's assets, Dirks breached his fiduciary duty under section 17704.09(b)(1) to hold these assets in trust for WLOW's sole benefit. (*See* pp. 34–39, *infra*.)

4. By taking WLOW's assets, Dirks also breached his fiduciary duty of care under section 17704.09(c), since his acts qualified as "intentional misconduct." (*See* pp. 48–49, *infra*.)

5. By dissolving WLOW and taking its assets, Dirks also breached his fiduciary duty to avert conflicts-of-interest with WLOW (codified at section 17704.09(b)(2)) and his fiduciary duty to refrain from competing against WLOW (codified at section 17704.09(b)(3)). *See* pp. 47–48, *infra*.)

6. Specifically, Dirks' dissolution of WLOW and taking of its assets without consideration disserved WLOW's interest and instead served Dirks' own interest and the interest of LJS Placentia Partners, LLC, which Dirks and Omar formed and used to hold, develop, and earn substantial profits from the property development that Dirks took from WLOW. *(See id*.)

7. By taking WLOW's assets and putting them to rival use, and by diverting profits that WLOW otherwise would have earned, Dirks breached the following fiduciary duties that he owed to WLOW: the duty to avert conflicts-of-interest under section 17704.09(b)(2); and the duty to refrain from competing under section 17704.09(b)(3). (*See (See id*.).

Wardak's Response to Query No. 3. Wardak's answer to query no. 3 is "No."

1. The Second Operating Agreement imposed no limitation (reasonable or otherwise) of Dirks' duty of care under section 17704.09(c).

2. The Second Operating Agreement did not expressly deem specific types or categories of activities to be permitted by Dirks' duty of loyalty under section 17704.09(b).

3. The Second Operating Agreement did not ratify any act or transaction performed by Dirks that, absent ratification, would have constituted a breach of Dirks' duty of loyalty under section 17704.09(b).

4. Such provisions might have been included in the Second Operating Agreement as permitted by the predecessor version of section 17701.10(c)(14)–(15), which was in effect when that agreement was made. Had there been any such provision, Wardak would have challenged it as allowed by law. But there was no such provision, much less one that met the requirements of former section 17701.10(c)(14) or (15). The Second Operating Agreement therefore did not absolve Dirks of the clear breaches

of fiduciary duty that he committed in this case. (*See* pp. 49–51, *infra*.)

To explain these answers, Wardak offers the following statement of the controlling law and then his analysis of the Court's three queries.[2]

II. THE CONTROLLING LAW

A. Section 17704.09 Imposes Fiduciary Duties of Loyalty and Care on Members of Member-Managed LLCs and Managers of Manager-Managed LLCs

Section 17704.09(a) imposes certain fiduciary obligations on the following persons: (1) all members of a "member-managed" LLC (*see* § 17704.09(a)); and (2) any manager of a "manager-managed" LLC (*see* § 17704.09(f)).

Wardak refers to all such persons as "managers" in this brief.[3]

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[2] To avoid repetitive briefings, this submission does not provide a separate statement of relevant facts, but presents facts and supporting citations as required to make specific points or to provide context. Wardak's Opening Brief presents a complete statement of the relevant facts and supporting citations to the record. (*See id*. pp. 18–36, n.1, n.2.) Wardak's Reply Brief presents facts and supporting citations as required to reply to Dirks' and Omar's Opposition Briefs. (*See* Wardak's Reply Brief, pp. 15–27, 32–34, n.4.)

[3] A manager-managed LLC is managed solely by its manager, who can be a member, but need not be. A majority of the members can vote to remove a manager. *See* § 17704.07(c); *see* (continued...)

Specifically, all managers owe the following fiduciary duties to the LLC and its other members: (1) the duty of loyalty codified at section 17704.09(b); and (2) the duty of care codified at section 17704.09(c). *See* § 17704.09(a), (f).

Dirks served as WLOW's manager from the time he formed WLOW in mid-2013 ((7AA 1138–1141)) until he cancelled its legal existence in December, 2019 (7AA 1153). He therefore owed these duties whether or not WLOW was member-managed or manager-managed. *See* § 17704.09(a), (f).

B. A Manager's Duty of Loyalty

Under section 17704.09(b), a manager owes a fiduciary duty of loyalty to his LLC and its other members.[4]

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[3](...continued)
also Swart Enterprises, Inc. v. Franchise Tax Bd. (2017) 7 Cal.App.5th 497, 510 (explains the distinction between member-managed and manager-managed LLCs). To qualify as a manager-managed LLC, an LLC must state in its operating agreement that it will be a manager-managed LLC. *See* § 17704.07(a) ("A limited liability company is a member-managed limited liability company unless the articles of organization contain the statement required by [section 17702.01(b)(5)]"); § 17702.01("If the limited liability company is to be manager-managed, the articles of organization shall contain a statement to that effect."). WLOW's operating agreements established that Dirks served as WLOW's sole manager and alone held a manager's powers, but they did not expressly state that WLOW was a manager-managed LLC. (7AA 1163–1172, 1211–1243.)

[4]
Section 17704.09(b) was enacted in 2016 and has been examined only in a few published decisions. But it is the successor of a closely similar statute (Corp. Code, § 17153) and is also closely similar to the statute that codifies business partners'
(continued...)

Substantively, this duty is the same as the duty of loyalty that governs dealings between partners. *Compare* § 17704.09(b) *with* § 16404; *see also Feresi v. The Livery, LLC* (2014) 232 Cal.App.4th 419, 425 ("The manager of an LLC has a fiduciary duty and owes to the members of the LLC the same duties of loyalty and good faith as a partner owes to the partnership and its partners.").

Above all, the duty of loyalty set forth at section 17704.09(b) requires a manager to show "unfaltering loyalty and honesty" in his dealings with the LLC and its other members. *See Feresi,* 232 Cal.App.4th at 425–426 (under section 17704.09(b), "[t]he animating principle of a fiduciary's duties to his charges is unfaltering loyalty and honesty.").

To this end, a manager must fulfill four specific fiduciary obligations, which are codified as subparts of section 17704.09(b). These fiduciary obligations each have a well-understood meaning in the case law and are as follows:

- The *duty to account,* which is codified at section 17704.09(b)(1);
- The *duty to hold in trust*, which is also codified at section 17704.09(b)(1);

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[4](...continued)
fiduciary duties (Corp. Code, § 16404). Decisions that have interpreted and applied those statutes thus offer doctrines and rules that have persuasive authority in cases that arise under section 17704.09.

- The *duty to avert conflicts-of-interest,* which is codified at section 17704.09(b)(2); and
- The *duty not to compete*, which is codified at section 17704.09(b)(3).

A manager's duty of loyalty imposes no further obligation. *See* § 17704.09(b) (a manager's duty of loyalty is "limited" to the four specific duties set forth at subparts 1-3 of section 17704.09(b)).

Lastly, a manager's duty of loyalty should be considered in light of its historical origins. The duty and its related fiduciary obligations were originally developed at common law to govern a trustee's dealings with his beneficiary. These duties were later adapted to govern dealings between business partners. *See BT-I v. Equitable Life Assurance Society of the United States* (1999) 75 Cal.App.4th 1406, 410–1411("Partnership is a fiduciary relationship, and partners are held to the standards and duties of a trustee in their dealings with each other.").

C. A Manager's Duty of Care

A manager of an LLC, when acting in this capacity, owes a fiduciary duty of care that is breached if he engages in "grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." (§ 17704.09(c)). Each of these terms likewise has a well-understood meaning in the case law.

III. ANALYSIS

In this section, Wardak presents the legal analysis that he developed to arrive at his answers to the Court's three queries.

A. Dirks Used the Second Operating Agreement to Favor His Own Interests over WLOW's Interests

To all appearances, Dirks and his close friend Omar misused the Joint-Funding Clause and Forfeiture Provisions to shut down WLOW, extinguish Wardak's 25% membership interest in WLOW's property development, set up their own company, and have it complete the property development begun by WLOW. (*See* Wardak's Opening Brief, pp. 21–36.) That, at least, is what they ended up doing. (*See* pp. 19–27, *infra; see also* Wardak's Opening Brief, pp. 23–36.)

The evidence in the record, which is cited and fully explained in Wardak's Opening Brief at pp. 23–36, supports a strong inference that Dirks and Omar put this scheme into effect from the time they urged Wardak to accept the Second Operating Agreement and made express representations to him to induce his acceptance.[5]

If, as seems highly probable, Dirks engaged in such a scheme while serving as WLOW's manager, then he indisputably

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[5] Dirks insisted on having an agreement along the lines of the Second Operating Agreement (7AA 1235–1237; 1RT 143:22 – 146:14; 3RT 545:21 – 546:24, 547:16–21) and worked with an attorney to prepare it (7AA 1174, 1203; 1RT 144:4-13; 145:24 – 146:8). He and Omar made express representations to Wardak in writing and orally to induce him to accept it. (7AA 1203-1204; 1RT 144:14 – 146:14, 150:3 – 152:14, 152:25 – 153:10, 155:10 –156:3; 3RT 405:6 – 406:6, 409:24 – 410:10, 411:23 – 412:12, 471:13 – 474:18; 478:10 – 479:6; *see also* Wardak's Opening Brief, pp. 25–26.)

breached his fiduciary duty of loyalty to WLOW. *See Enea*, 132 Cal.App.4th at 1564 ("It is hornbook law that in forming [a partnership] the partners obligate themselves to share risks and benefits and to carry out the enterprise with the highest good faith toward one another–in short, with the loyalty and care of a fiduciary.")

It is not necessary, however, to prove these points to show that Dirks breached his duty of loyalty to WLOW. It suffices to show that he repeatedly sought to promote his own interest at the expense of WLOW's interest, whatever his interest might have been at the time. *McMillin v. Eare* (2021) 70 Cal.App.5th 893, 912 ("A trustee also owes a duty of loyalty in that he has a duty to administer the trust solely in the interest of the beneficiaries; this duty is frequently invoked as protection against creating conflicts between a trustee's fiduciary duties and personal interests."); *see also Leff v. Gunter* (1983) 33 Cal.3d 508, 514.

1. How Dirks Used the Second Operating Agreement to Undermine WLOW's Interest

On this last point, the evidence is unanswerable and conclusively demonstrates that Dirks interpreted and enforced the Joint-Funding Clause and Forfeiture Provisions to serve purposes that were *inimical* to WLOW's interest, which was to procure its required construction funding, complete its property development, operate it, and eventually sell it to generate profits. (7AA 1138 at second recital; 1141, 1154 at § 3.b; 1211 at § 3.b; 1222–1225; 3RT 466:3-16, 538:6 – 539:9)

Dirks, who understood what lay in WLOW's interest, used the Joint Funding Clause and Forfeiture Provisions to *defeat* it rather than advance it. The most noteworthy instances were as follows:

a. Dirks insisted on an unreasonable interpretation of the Joint-Funding Clause in order to *prevent* WLOW from receiving from Wardak the funding that it required to complete its property development. (7AA 1181–1182, 1188–1189; 3RT 560:23 – 561:2.) According to Dirks, the Joint-Funding Clause was an "all-or-nothing" provision, which he maintained Wardak was powerless to perform after Omar defaulted. (*Id*.) On this ground, Dirks rejected Wardak's unambiguous offer to cure Omar's default and provide *all* of WLOW's required funding on the same terms and conditions that WLOW had already accepted for joint-funding provided by both Wardak and Omar. (7AA 1181-1184, 1188-1189; 1RT 163:1 – 166:4; 3RT 560:23 – 561:2.)

b. By adopting an unreasonable, inequitable interpretation of the Joint-Funding Clause to reject Wardak's tender of full performance, Dirks deprived WLOW of readily available, full funding and thus *undermined* WLOW's interest rather than advance it.[6] (*Id*.)

c. If Dirks had wished to advance WLOW's interest, he would have looked for a way to accept this tender. Nor need he

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6 This matter is fully explained and substantiated with citations to the record in Wardak's Opening Brief, pp. 26–29.

have looked very hard, since his all-or-nothing interpretation of the Joint-Funding Clause was at best a possible, if inequitable construction, not an inevitability or a manifest expression of the parties' clear intent to have Wardak and Omar invest in equal parts or not at all. (*See* Wardak's Opening Brief, pp. 44–47.) But rather than find a simple way to advance WLOW's project, Dirks essentially ignored Wardak's successive entreaties and ongoing tender of performance from mid-June to the latter part of September, 2015.

d. Finally, on September 18, 2015, Dirks wrote a reply to Wardak's attorney. (7AA 1188–1189.) In it, he declared that Omar and Wardak had been in default under the Joint-Funding Clause since May 22, 2015, announced that he had "suspended" WLOW's property development, and gave notice that he would "dissolve [WLOW] as outlined in [the Forfeiture Provisions]." He also indicated that he had or would convert Omar and Wardak's prior funding of WLOW to a no-interest loan. (7AA 1188–1189.)

e. By proceeding in this manner, Dirks arguably became the "100% Owner" of WLOW and acquired "100% Ownership" of WLOW's membership interests, and Omar and Wardak arguably lost their membership interests (25% apiece). (7AA 1215, at § 11.) The wording of the Forfeiture Provisions is ambiguous on this point (*id.*), but thereafter Dirks acted as though he had become the sole owner of WLOW. (7AA 1188–1189, 1198–1199, 3RT 417:22 – 418:2, 424:15-23, 459:6-12, 566:13 – 568:5.)

f. It is impossible to reconcile these acts with Dirks' fiduciary duty to protect and advance WLOW's interest, which above all was to complete the construction of its property development by procuring funding to pay for its capped-fee construction contract. (7AA 1138 at second recital; 1141, 1154 at § 3.b; 1211 at § 3.b; 1222–1225; 3RT 466:3-16, 538:6 – 539:9.)

g. WLOW had no interest in insisting that its funding come in equal shares from both Wardak and Omar, or not at all. Nor did it have any interest in having its manager suspend its operations, dissolve it, and take aggressive, hostile measures against a willing funder who sought a way to provide its funding over his fixed opposition. Dirks' conduct therefore cannot be reconciled with a *bona fide* intent to fulfill his fiduciary duties to WLOW.

h. Whatever might have been Dirks' purpose, it clearly was not to protect and advance WLOW's interest, but on the contrary to accomplish some other end that was inimical to WLOW's interest. That is enough to find him liable to WLOW for breach of the duty of loyalty. *Cf. McMillin*, 70 Cal.App.5th at 912; *Leff*, 33 Cal.3d at 514.

2. Why Dirks Undermined WLOW's Interest: To Shut Down WLOW, Exclude Wardak, and Transfer WLOW's Property Development to a New Company that He and Omar Would Form

After Dirks dissolved WLOW, he took no further action until May, 2016. The likely explanation is provided by the early procedures in this case, which Wardak initiated in response to

Dirks' notice of default on September 24, 2015. (7 AA 1320 at ROA No. 2.)

Shortly after bringing the case, Wardak recorded a notice of lis pendens against WLOW's property (7 AA 1320 at ROA No. 10), which remained encumbered by a trust deed that WLOW had given to Omar and Wardak on June 4, 2013 to secure their ongoing funding of its operations from mid-2013 to May 15, 2015 (7AA 1242). As of May 15, 2015, the amount of this funding was $605,537.80. (7AA 1227.) Wardak was entitled to collect one-half of this sum,[7] all of which remained secured by WLOW's trust deed. 7AA 1242.

Dirks filed a motion to expunge Wardak's notice of lis pendens on November 20, 2015 (7 AA 1320 at ROA No. 12). The parties thereafter litigated motions concerning the propriety of Wardak's recording and whether the prevailing party on this issue, Dirks, was entitled to a fee award. (7 AA 1320–1324 at ROA Nos. 12–13, 17, 30–32, 34, 37–38, 40, 47, 56, 59, 61–62, 64,

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[7] At trial, Omar admitted under cross-examination that (1) to provide funding for WLOW, Omar and Wardak had their company emit funds; (2) Omar and Wardak were each one-half owners of this company, and they each owned one-half of the funds that their company emitted for WLOW's use; (3) for unknown reasons, Omar funneled a substantial part of these funds through various shell corporations that he operated; and (4) regardless, Omar and Wardak were each entitled to collect one-half of WLOW's debt to them. *Compare* 7AA 1205-1206 *with* 1RT 116:14-24; 181:18-26, 183:17 – 186:24; 2RT 205:21 – 206:6, 295:15-24, 330:14-18; 3RT 395:18:5 – 397:2, 397:11-16, 398:15 – 399:10, 413:15-23, 414:7-10; *see also* Wardak's Opening Brief, pp. 31–33.

78, 80, 84, 91.) This stage of the case ended when the Superior Court granted Dirks' motion for a fee award on June 29, 2016. (7AA 1324 at ROA No. 91.)

It was only towards the end of this period when Dirks and Omar performed the acts and transactions that all but announced their well-coordinated scheme to exclude Wardak from WLOW's property development, in which he had already invested more than $300,000 from mid-2013 to mid-2015 (i.e., one-half of the funds that WLOW owed to him and Omar). Wardak briefly summarizes these matters below, having described them at greater length in his Opening Brief. (*Id*., pp. 21-36.)

a. Omar Intervenes in April, 2016 to Support Dirks' Position. On April 20, 2016, Omar moved to intervene in the proceedings below, seeking two judicial declarations from the Superior Court. The first would confirm that he and Wardak had defaulted under the Joint-Funding Clause, so that Dirks was entitled to enforce the Forfeiture Provisions (i.e., dissolve WLOW, take sole ownership of its membership interests, and restate its debt to Omar and Wardak on the singularly one-sided terms in his favor that appear in the Forfeiture Provisions). The second would confirm that Omar had provided $541,228.21 of the $605,538 in overall funding that WLOW had received from him and Wardak (i.e., he claimed to have furnished $440,337.77 from his own funds, plus one-half of the funds provided by a company

in which he and Wardak each held one-half ownership interests.) (1AA 53–56 at ¶¶ 1–3, 10–14, 16, Prayer for Relief.)[8]

b. *Dirks and Omar Conduct a Fraudulent Escrow Transaction*. On May 19, 2016, Dirks and Omar initiated an escrow transaction in order to disencumber WLOW's property from Omar and Wardak's trust deed – i.e., the trust deed that secured their funding of WLOW from mid-2013 to mid-2015. (7AA 1190.) This escrow transaction was completed and WLOW's property was disencumbered of the trust deed on June 23, 2016. (7AA 1209.)[9]

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At trial, Omar conceded under cross-examination that in fact his proper share of the overall funding was $302,769, plus interest, rather than the $541,228.21 that he asked the Superior Court to allocate in his favor in a judicial declaration. *See* n. 7, *supra*.

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During this escrow transaction, Omar submitted materially false statements to the escrow officer to reduce Wardak's share of the payoff proceeds and to reduce the sum that WLOW was required to pay to perform the transaction. In consequence, Wardak was underpaid by $123,900, and WLOW disencumbered its property by paying only $193,837.47 instead of the full amount of the secured debt, which was $635,665. (7AA 1208, 1RT 116:14-24; 181:18-26, 183:17 – 186:24; 2RT 205:21 – 206:6, 295:15-24, 330:14-18.) Omar loaned the payoff amount to WLOW so that it could fund the transaction. (3RT 566:16-18.) The jury found that by this escrow transaction Omar had converted $123,900 of Wardak's funds and in so doing had breached a contractual obligation to Wardak. (6AA 1123.) A full statement of this matter appears in Wardak's Opening Brief at pp. 31–33.

c. *Dirks Forms LJS Placentia*. On the same date as the escrow transaction was consummated (June 23, 2016), Dirks formed LJS Placentia. (7AA 1197).

d. *Dirks Conveys WLOW's Property to LJS Placentia.* About two weeks later, on July 7, 2016, Dirks had WLOW convey its property to him by quitclaim without paying any consideration. (7AA 1199.) Immediately afterwards, Dirks conveyed this property by quitclaim to LJS Placentia. (7AA 1198.) Dirks treated the conveyance as his capital contribution to LJS Placentia (3RT 567:19-21) and testified that at the time the property was worth more than $1 million (3RT 567:22–25).

e. *Dirks and Omar Reveal Their Agreement to Own and Operate LJS Placentia by Themselves*. According to Dirks, he and Omar agreed in June or July, 2016 that they would co-own LJS Placentia and have it complete the property development begun by WLOW. (3RT 417:22 – 418:2, 488:2 – 489:9, 567:1 – 568:5.) Regardless of when they reached this agreement, the two of them became members of LJS Placentia with nearly equal membership interests. (3RT 424:15-23, 567:1-18, 567:26 – 568:5.) Thereafter, they had LJS Placentia complete the property development (3RT 568:19-21) and earn net revenues in excess of $2.2 million from an equity cash-out (7AA 1200) and a subsequent sale of the property for more than $5 million (7AA 1201).

f. *Dirks and Omar Split LJS Placentia's Profits Only Between Themselves*. Dirks and Omar each received one-half of LJS Placentia's profits from this venture (3RT 417:22 – 418:2,

488:2–489:9, 567:26–568:21), which the jury fixed at $1.5 million (6AA 1123), and which the Superior Court ruled were supported by substantial evidence in the record (6AA 1087).

g. *Connecting the Confusing Dots*. On the whole, this property development entailed many confusing transactions, but they all point in only one direction: Dirks, Omar, and Wardak began the venture in 2013 by forming WLOW, in which Dirks held a 50% stake and the other two each held a 25% stake. (7AA 1138-1139.) Wardak and Omar, who are related (1RT 58:9-23, 71:10-20, 77:23 – 78:11), had a bitter falling out over an unrelated business dispute (1RT 78:12 – 80:1; 3RT 423:16 – 424:11). Dirks and Omar, who are uncommonly close, longtime friends and co-venturers (1RT 81:13-17; 3RT 393:2 – 394:22, 420:10-20), apparently decided at some point to shut down WLOW, terminate Wardak's ownership interest in its property development, transfer the development to a new company, complete it, and keep its profits to themselves. To this end, they misused the Joint-Funding Clause and Forfeiture Provisions set forth in the Second Operating Agreement.

Whatever grievances Dirks held in this matter against Wardak, nothing gave him license to subvert his fiduciary duties and pro-actively undermine the LLC that he was charged with managing. But that is what he did, and he therefore breached his fiduciary duties.

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3. The Joint-Funding Clause and Forfeiture Provisions Were Drafted to Accomplish Dirks' Own Purposes, not to Protect WLOW.

The Joint-Funding Clause and Forfeiture Provisions that Dirks had WLOW adopt were apparently *intended* to serve his improper purposes rather than WLOW's legitimate ones, as is made clear by the following points:

a. The Joint-Funding Clause was imprecise and ambiguously worded in a manner that arguably allowed Dirks to assert (in bad faith and unreasonably) that it was an all-or-nothing provision. (7AA 1214–1215, § 11; 3RT 560:23 – 561:2.)

b. WLOW's interest, however, was to obtain the required funding, not to insist that Wardak and Omar each furnish one-half of it, or else WLOW must disband. (7AA 1138 at second recital; 1141, 1154 at § 3.b; 1211 at § 3.b; 1222–1225; 3RT 466:3-16, 538:6 – 539:9.) Indeed, WLOW's interest in procuring funding was *frustrated* by Dirks' all-or-nothing interpretation of the Joint-Funding Clause, which prevented Wardak from providing all of WLOW's required funding. (7AA 1181–1182; 3RT 560:23 – 561:2.)

c. The Forfeiture Provisions (summarized at length in Wardak's Opening Brief, pp. 24–25) were shockingly one-sided in Dirks' favor. (7AA 1214–1215 at § 11; 1218 at § 24(v).) They were so one-sided that, even if Dirks did not intend to misuse them from the start, he had a strong incentive to enforce them if he had a colorable basis for doing so. To benefit from these provisions, however, Dirks must declare Wardak and Omar's default under

the Joint-Funding Clause, cancel their membership interests in WLOW without compensation, and dissolve WLOW. (7AA 1214–1215 at § 11; 1218 at § 24(v).)

d. WLOW's interest, however, was not to have itself dissolved and lose its assets to its manager, but rather to procure the funding that it needed to complete its property development, where it planned to rent apartments for a time before finally selling the entire development. (7AA 1138 at second recital, 1141, 1154 at § 3.b, 1211 at § 3.b, 1222–1225; 3RT 466:3-16.) These interests were neither protected nor furthered by the Forfeiture Provisions, which on the contrary richly rewarded Dirks for shutting down WLOW, dissolving it, becoming the sole owner of its membership interests, and using its assets as he wished. (7AA 1214–1215 at § 11; 1218 at § 24(v).)

e. The Forfeiture Provisions thus served to confer a windfall on Dirks, rather than protect WLOW's interest. In fact, these provisions unreasonably exposed WLOW to needless dissolution, the entire loss of its assets, and the diversion of its future profits. (7AA 1214–1215 at § 11; 1218 at § 24(v).)

f. If it is assumed, *arguendo*, that WLOW's appropriate response to Omar's default under the Joint-Funding Clause would have been to wind up its affairs and dissolve itself, WLOW's appropriate remedies must have included, *inter alia*, an option either to sell its unfinished property development as a going concern or to liquidate its assets for fair-market value. *See*

§ 17707.05; *cf. Trahan v. Trahan* (2002) 99 Cal.App.4th 62, 74 ("We are unaware of any case in which liquidation value was found to mean something other than either valuation of the corporation as a going concern in liquidation or the piecemeal valuation of the company's assets and liabilities as of the valuation date.") Thereafter, WLOW must have disbursed the sale or liquidation proceeds according to the order of priority set forth at section 17707.05 and restated in the Second Operating Agreement. (7AA 1216 at § 14(c), 1218 at text beneath § 24(vi).)

g. WLOW's manager, Dirks, would have been charged with a fiduciary duty to perform these transactions solely for WLOW's benefit. *See Everest Investors 8 v. McNeil Partners* (2003) 114 Cal.App.4th 411, 424 ("A partner's fiduciary duty extends to the dissolution and liquidation of partnership affairs, as well as to the sale by one partner to another of an interest in the partnership."); *Dickson, Carlson & Campillo v. Pole* (2000) 83 Cal.App.4th 436, 445 ("The partners of a dissolved partnership owe each other a fiduciary duty to complete the partnership's unfinished business.").

h. The Forfeiture Provisions rode roughshod over these standard, mandatory practices for winding up and dissolving an LLC or partnership. Instead, they authorized Dirks to become the "100%" owner of all membership interests in WLOW (7AA 1214–1215 at § 11; 1218 at § 24(v). Thereafter, he acted as though he had absolute leave to take and dispose of WLOW's assets as he wishes without giving consideration or providing notice and an

accounting (7AA 1198–1199; 1RT 171:2-15, 172:3 – 173:7, 174:3-–19; 3RT 488:2-11, 488:18 – 489:9), and apparently without concern for possible obligations to WLOW's outside creditors or its excluded former member, Wardak. (7AA 1198–1201; 3RT 417:22 – 418:2, 488:2 – 489:9, 567:26 – 568:21.)

i. More broadly, the Forfeiture Provisions imposed shocking penalties on Omar (in theory) and Wardak (in fact), but omitted to provide reasonable remedies to protect WLOW, and instead were principally or solely calculated to *confer windfall benefits on Dirks*. (7AA 1188–1189, 1214–1215 at § 11; 1218 at § 24(v).)

Dirks never should have burdened WLOW with such an operating agreement. (*See also* Wardak's Opening Brief, pp. 23–31, 33–36.)

By doing so, and by using it to further his own interest at the expense of WLOW, Dirks breached the duty of loyalty that he owed to WLOW under section 17704.09(b). *See Feresi*, 232 Cal.App.4th at 425; *Jones*; 112 Cal.App.4th at 1540; *Enea*, 132 Cal.App.4th at 1564.

B. By Dissolving WLOW and Taking Its Assets, Dirks Favored His Own Interest Over WLOW's Interest

Before Dirks could enforce the Forfeiture Provisions to accomplish his apparent purposes, he required Omar and Wardak's breach of the Joint-Funding Clause. (7AA 1214–1215 at § 11; 1218 at

§ 24(v).)

That was a finding that Dirks could make, if at all, only by unreasonably preventing Wardak from performing the Joint-Funding Clause on his own after Omar defaulted. (*See id*.) That is precisely what Dirks did. (*See* pp. 19–27, *supra*.)

By so acting, Dirks *undermined* WLOW's interest rather than advance it. Under the circumstances, WLOW's interest plainly lay in accepting Wardak's timely offer to provide its entire funding. (*Id*.) At a minimum, Dirks should have made a reasonable effort to procure this funding.[10]

Dirks chose instead to disregard Wardak's tender of performance and offer to cure Omar's default. More than three months after Wardak first proffered them (7AA 1182–1184, 1186–1187), Dirks finally provided a substantive response: he elected to dissolve WLOW and enforce the other Forfeiture Provisions. (7AA 1188–1189; 1RT 166:1 – 167:11.)

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[10] Wardak timely tendered his one-half share of the funding, timely re-tendered it after an inadvertent complication arose, and timely offered to cure Omar's default. (1RT 156:1-16, 157:3-11, 158:15 – 159:10, 160:11-20, 161:1 – 166:4; 3RT 479:2-8; 7AA 1173, 1182–1184, 1186–1187). The specific sequence of events is set forth in detail and with citations to the record in Wardak's Reply Brief, p. 17, n.4. Dirks unsuccessfully argued below that Wardak failed to provide his one-half share of the funding. This allegation was the basis for his cross-claims against Wardak for breach of contract, intentional misrepresentation, and negligent misrepresentation. (2AA 316–324.) The jury rejected these claims and found that Wardak had fulfilled his contractual obligations. (6AA 1104–1105.)

A manager who had a faithful regard for WLOW's interest would not have proceeded in such a manner. WLOW had a promising property development and had already procured its entitlements, building permits, and construction plans (*see* n. 11, *infra*), and it had an option to accept a master construction contract to have all construction work performed within a fixed budget (7AA 1218 at § 11, 1222–1225; 3RT 530:5-11). WLOW was not a failed venture. It was not forced out of business.

If Dirks or WLOW's other two members concluded that they were divided by irreconcilable differences, the law would have afforded them appropriate remedies. *See* § 17707.03 (states grounds for a judicial dissolution of an LLC; § 17707.4 (prescribes procedures for winding up an LLC); § 17707.5 (prescribes how an LLC must hold or disburse its assets in order to wind up its affairs). But Dirks chose a different plan, which he pursued to WLOW's detriment. (*See* pp., 19–27, *supra.*)

Dirks thus breached his duty of loyalty to WLOW when he exercised his right under the Forfeiture Provisions to dissolve it and take sole ownership of its membership interests and assets. *See Feresi*, 232 Cal.App.4th at 425; *Jones*; 112 Cal.App.4th at 1540; *Enea*, 132 Cal.App.4th at 1564.

C. In His Dealings with WLOW, Dirks Failed to Act with "Unfaltering Loyalty and Honesty"

In the above matters, which were all interconnected, the least that can be said is that Dirks did not act with "unfaltering

loyalty and honesty" in his dealings with WLOW. (*See* Wardak's Opening Brief, pp. 21–36.)

On this ground alone, Dirks breached his duty of loyalty to WLOW. *See Feresi*, 232 Cal.App.4th at 425 (stating that the duty of loyalty under section 17704.09(b) requires "unfaltering loyalty and honesty" and is the same duty that business partners owe to one another); *cf. Enea v. Superior Court* (2005) 132 Cal.App.4th 1559, 1564 ("[I]n all proceedings connected with the conduct of the partnership every partner is bound to act in the highest good faith to his copartner and may not obtain any advantage over him in the partnership affairs by the slightest misrepresentation, concealment, threat or adverse pressure of any kind."); *BT-I*, 75 Cal.App.4th at 1411 ([A partner's fiduciary duty of loyalty] "extends to all aspects of the relationship and all transactions between the partners. Each partner occupies the position of a trustee to the other with regard to all the partnership transactions, including the transactions contemplated by the firm and constituting the object or purpose for which the partnership was formed.").

D. Dirks Breached His Duty to Hold WLOW's Property in Trust

The duty of loyalty obliges a manager to hold in trust for his LLC "any property, profit, or benefit" that the manager acquires while conducting or winding up the LLC's business or that the manager develops by using the LLC's property. *See*

§ 17704.09(b)(1). An LLC's property specifically includes its commercial opportunities. *See id.*

Dirks breached this duty when he took WLOW's property and other assets without paying anything and delivered them to LJS Placentia (7AA 1188-1189, 3RT 417:22–418:2, 488:2–489:9, 566:13–568:5).[11] LJS Placentia thereafter completed the property development begun by WLOW, earning substantial profits from the venture (7AA 1200-1201; 3RT 417:22 – 418:2, 488:2 – 489:9, 567:26 – 568:21), which Dirks and Omar kept for themselves, each taking a one-half share. (3RT 417:22 – 418:2, 488:2 – 489:9, 567:26 – 568:21.)

These acts were brazen instances of a breach of the duty to hold in trust. When winding up WLOW's affairs, Dirks never had any lawful right or equitable claim to confiscate WLOW's assets and use them as he wished without paying for them. *Cf. Prince v. Harting* (1960) 177 Cal.App.2d 720, 727 ("A partner has no right to deal with partnership property other than for the sole benefit of the partnership. There are many other cases to the same effect, and the principle is universally recognized and applied, both in California and in other states.").

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At the time, WLOW held the following substantial assets: (1) a real property whose value at the time was over $1 million, according to Dirks' testimony (3RT 567:19-25); (2) land entitlements to build multi-unit residential units on the property (7AA 1214 at § 11); (3) building permits (7AA 1227); and (4) construction plans (7AA 1223–1225).

On the contrary, Dirks owed a fiduciary obligation to hold WLOW's assets solely for WLOW's benefit. *See* § 17704.09(b)(1). After he gave notice of WLOW's dissolution, he owed a fiduciary duty to observe all required procedures and to disburse WLOW's assets according to law. *See* § 17707.05 (requires that an LLC, when winding up its activities, use its assets first to pay outside creditors' claims, then to pay members' claims and reimburse their capital contributions, and then to distribute any remainder to its members according to their respective membership interests); *see also* § 17704.05(1) (forbids an LLC to make a distribution to any member that renders it unable to pay its obligations to non-member creditors for ordinary business expenses); § 17707.04 (establishes obligatory procedures and notice requirements for winding up an LLC); *cf. Everest Investors,* 114 Cal.App.4th at 424 (a partner must fulfill his fiduciary duty of loyalty to the partnership while it is wound up and dissolved).

To purchase WLOW's assets, Dirks could have tendered his capital credit at WLOW as part of his payment, but he could not walk off with them without paying anything or providing an accounting, as he chose to do. *See* § 17707.05; *cf. Everest Investors*, 114 Cal.App.4th at 424 ("A partnership is an entity separate and apart from the partners of which it is comprised, and it is the partnership entity which owns its assets, not the partners.").

As noted above, the Second Operating Agreement included boiler-plate provisions that governed WLOW's "Termination and

Dissolution": these provisions obliged Dirks to sell all of WLOW's assets for fair-market value and disburse the proceeds in the standard order of priority (described above). (7AA 1218–1219 at text beneath § 24(vi).)

Dirks' election to convey WLOW's assets to himself after wrongfully dissolving WLOW and without paying for them thus constituted an open-and-shut case for breach of his fiduciary duty to hold WLOW's assets in trust. *See* § 17704.09(b)(1); *see also* § 17707.05; *cf. Everest Investors*, 114 Cal.App.4th at 424; *Prince*, 177 Cal.App.2d at 727.

Indeed, a partner breaches his duty of loyalty and renders himself liable in tort if he "destroys" the partnership (or LLC) and takes all of its assets for his own use. *See Barlow v. Collins* (1958) 166 Cal.App.2d 274, 278 (the usual requirement of an accounting and dissolution is waived when "the wrongful acts complained of are not only a breach of contract but constitute a tort, and this is especially true where the tort is of such a nature that it not only terminates the partnership but wrongfully destroys it, and where the erring partner converts to his own use its entire assets.").

That is precisely what Dirks did in this case. Its distinguishing feature is that, immediately before he did so, he had his LLC adopt an operating agreement that purported to authorize him to do so. But this authorization was directly contrary to numerous other provisions in the same agreement (*see* pp. 49–51, *infra*), and it depended upon the occurrence of a condition precedent (a breach of the Joint-Funding Clause) that

he caused to occur by his unreasonable, "all-or-nothing" interpretation of its meaning. (*See* Wardak's Opening Brief, pp. 29–31.)

Lastly, Dirks previously suggested that WLOW's assets principally consisted of the property that he contributed to it, and that by taking the property from WLOW he only reclaimed what belonged to him. (7AA 1235–1237.)

This argument fails as a matter of law. *See Bardis v. Oates* (2004) 119 Cal.App.4th 1, 13 ("It is no answer that the proceeds from self-dealing might be deemed 'fair compensation' to the faithless partner.")

The argument also fails on the merits: when Dirks contributed the property to WLOW, he received in exchange a capital credit of $465,000 at WLOW. (7AA 1141.) Thereafter, Omar and Wardak paid him $191,475.14 to "draw down" this capital credit (7AA 1227), and they also paid $210,140.93 to retire a personal loan taken by Dirks that encumbered the property at the time (*id.*). Omar and Wardak also contributed another $191,475.14 to WLOW for building permits, preliminary construction, and miscellaneous development costs claimed by Dirks (*id.*). In all, they contributed $605,538 to fund WLOW's property development from mid-2013 to mid-2015 (*id.*). All three of WLOW's members thus provided substantial value to WLOW.

Dirks had no prerogative to flout his fiduciary, statutory, and contractual obligations after he needlessly dissolved WLOW

rather than accept Wardak's funding of its property development. *cf. Everest Investors,* 114 Cal.App.4th at 424

By taking WLOW's assets and conveying them to LJS Placentia, Dirks breached his fiduciary duty to WLOW to hold its assets solely for its benefit. *See* § 17704.09(b)(1).

E. Dirks Breached His Duty to Account to WLOW

The duty of loyalty obliges a manager "to account" to his LLC. At a minimum, he must make timely, adequate disclosures of his transactions and dealings with the LLC, as well as any debt that he owes to the LLC or that the LLC owes to him. *See* § 17704.09(b)(1); *cf. Pool-O'Connor v. Guadarrama* (2023) 90 Cal.App.5th 1014, 1029 ("Trustees are under an obligation to render to their beneficiaries a full account of all their dealings with the trust fund, and where there has been a negligent failure to keep true accounts, or a refusal to account, all presumptions will be against the trustee upon a settlement.") (quoting *Purdy v. Johnson* (1917) 174 Cal. 521, 527.)

As shown below, Dirks unambiguously breached his duty to account by the following practices, acts, and omissions: (1) misreporting his capital contributions and capital withdrawals; (2) omitting to keep capital accounts for Omar or Wardak; (3) presenting unfounded claims for payment from WLOW's damage award; and (4) failing to provide any kind of accounting of the assets that he unjustifiably took from WLOW.

1. Dirks' Unreliable Accounting of His Capital Account at WLOW

Dirks gave inconsistent, irreconcilable figures for the balance of his capital account at WLOW. (5AA 860, 888–889; 7AA 1141, 1150-1151, 1215; 1 ARA 17–19; 3RT 463:18 – 464:2; 468:1-4; 504:23 – 505:11; 554:7-11; 567:19-25).

Dirks' most recent statement was that, as of September 24, 2021, his capital account at WLOW was $349,000 – i.e., WLOW owed him this sum to reimburse his capital contributions to it. (5AA 888–889.) This assertion was demonstrably unfounded. Instead, the evidence discloses the following matters:

a. Dirks received a capital credit of **$465,000** upon contributing the property to WLOW in 2013. (7AA 1141.)

b. In mid-2013, Omar and Wardak paid $210,140.93 to retire a personal loan taken by Dirks that encumbered the property when he contributed it to WLOW. (7AA 1227; 1RT 104:20 – 105:4.) One-half of this sum, or $105,070.46, should have been deducted from Dirks' capital account at WLOW.[12]

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When a partner contributes an encumbered property to a partnership, the partnership assumes liability for the loan secured by the encumbrance, and each partner bears this liability according to his partnership interest. When Omar and Wardak paid off the loan that encumbered WLOW's property, Dirks was relieved of liability for 50% of this expenditure, since he held 50% of WLOW. This sum therefore should have been deducted from Dirks' capital account. *See* 26 CFR § 1.752-1 ("Treatment of partnership liabilities.").

c. On January 1, 2015, Dirks added $170,475.14 to his capital account at WLOW, claiming without documentation that this figure was the sum of his payments for WLOW's building permits (7AA 1150). At the same time, he deducted from his capital balance the sum of Omar and Wardak's draw-downs as of January 1, 2015 ($152,000), but not one-half of their payoff of his loan ($105,070.46). Accordingly, he stated that his capital account at WLOW as of January 1, 2015 was **$389,475.14.** (7AA 1151.)

d. Dirks never identified, nor could he, any other capital contribution that he ever made to WLOW.

e. By May 15, 2015, Dirks had received from Omar and Wardak draw-downs of this capital contribution whose total amount was $191,475.14. (7AA 1227.) By then, Dirks had also received from Omar and Wardak the sum of $53,751.86 to reimburse him the expense of purchasing WLOW's building permits (7AA 1227). Dirks even acknowledged that they were the ones who had funded WLOW's purchase of its required permits (7AA 1235).

f. If, as Dirks appeared to acknowledge, Omar and Wardak were the parties who paid for all of WLOW's building permits, Dirks' capital account on May 15, 2015 was **$168,454.40**, which is the difference between (1) his original capital contribution of $465,000; and (2) the sum of withdrawals from this contribution, which were Omar and Wardak's draw-downs ($191,475.14) and one-half of their expense to pay off the loan that secured the property ($105,070.46). If Dirks is credited with

paying $170,475.14 for WLOW's building permits, as he claimed without substantiation, then his capital account on this date was **$338,929.54**, which is the (1) the sum of Dirks' contributions of the property ($465,000) and his claimed permit fees ($170,475.14); *less* (2) the sum of Omar and Wardak's draw-downs ($191,475.14) and one-half of their expense to pay off the loan that secured the property ($105,070.46). On no possible telling could Dirks' capital account at WLOW have been any higher, even if Dirks is given the benefit of the doubt on all points.

g. Inexplicably, Dirks stated in the Second Operating Agreement that, as of May 15, 2015, the balance of his capital account at WLOW was **$541,475.14**. (7AA 1215.) At best, this statement is unreliable and unfounded.

h. Confusing matters further, Dirks testified at trial that the total cost of WLOW's building permits was approximately $250,000. (3RT 466:4–6.)

i. At trial, Dirks testified that the property was worth more than $1 million in July, 2016 when he took it from WLOW. (7AA 1198; (3RT 567:19-25.) Immediately afterwards, he gave it to LJS Placentia (7AA 1199), and at around the same time he and Omar agreed to treat it as his capital contribution to LJS Placentia (3RT 566:13–568:5). Dirks must therefore have deducted at least $1 million from his capital account at WLOW

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when he withdrew the property from it and contributed it to LJS Placentia.[13]

j. The upshot is that, even according to Dirks' own inflated figures, his capital account at WLOW was *deeply in the red* after he took its property and contributed it to LJS Placentia.

Dirks also omitted to record capital contributions for Omar or Wardak even though they had provided substantial capital sums, including $53,751,86 for permit fees (7AA 1227), $94,675.41 for construction work (*id.*), and $25,698.59 for additional construction work (*id.*). If Dirks had a reason to omit these apparent contributions, he made no notation of it anywhere. In all, Omar and Wardak each provided $302,768.90 to WLOW as of May 15, 2015 (7AA 1214 at §11, 1227), but Dirks gave no credit

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The property's value upon its withdrawal from WLOW was its fair-market value at the time. This method of valuation was required by the Second Operating Agreement, which states the following in the text beneath § 24(vi): "Any property distributions in kind in liquidation shall be valued and treated us though the properly was sold and cash proceeds distributed." (7AA 1218–1219.) This valuation was also required by law. *Cf. De Luz Homes v. County of San Diego* (1955) 45 Cal.2d 546, 561–562 (For purposes of assessing the value of a real property, the "standard" measure is "the price that property would bring to its owner if it were offered for sale on an open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other. It ... might be called the market value of property for use in its present condition."); *Trahan*, 99 Cal.App.4th at 74 (when a corporation appraises the value of its assets in order to wind up its affairs, the total value of its assets is "either valuation of the corporation as a going concern in liquidation or the piecemeal valuation of the company's assets and liabilities *as of the valuation date*.") (emphasis supplied).

to either of them in their accounts, which remained at $00.00 (7AA 1214 at § 11).[14]

2. Dirks' Presentation of Unfounded Claims for Payment from WLOW's Damage Award

After the jury trial, Dirks stated to the Superior Court on July 15, 2021 that the total of his unreimbursed capital contributions to WLOW was **$541,475.14**. (5AA 860.) He therefore demanded payment of this amount from WLOW's damage award. (5AA 861.)

On September 24, 2021, Dirks modified his request, stating that the amount of his unreimbursed capital contributions to WLOW was **$349,000.** (5AA 888–889.) He demanded that this sum be paid from WLOW's damage award. (*Id.*)

These claims lacked *any* reasonable basis. Dirks' only capital contributions to WLOW were the property, land entitlements, building permits, and construction plans. (7AA 1141, 1150-1151; 3RT 463:18 – 464:2, 468:1-4, 504:23 – 505:11, 554:7-11, 567:19-25). In July, 2016, he *took* these assets from WLOW (7AA 1199), gave them to LJS Placentia (7AA 1198; 3RT

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During trial, Wardak testified and Omar conceded under cross-examination that they had jointly contributed their funds, each owned one-half of these funds, and were each entitled to 50% of whatever reimbursement WLOW would make to them after Dirks cancelled their membership interests. (*Compare* 7AA 1205-1206 *with* 1RT 116:14-24; 181:18-26, 183:17 – 186:24; 2RT 205:21 – 206:6, 295:15-24, 330:14-18; 3RT 395:18:5 – 397:2, 397:11-16, 398:15 – 399:10, 413:15-23, 414:7-10).

568:19-21), and claimed them as his capital contribution to *LJS Placentia* (3RT 567:19-25; 1 ARA 17–19).

To oppose this claim, Wardak conducted a comprehensive analysis of the matter and reached the following conclusions:

a. By express agreement with Omar, Dirks transferred his capital account at WLOW to LJS Placentia when he transferred the property from the one to the other. (3RT 566:13 – 568:5.)

b. Omar thereafter paid down Dirks' capital account at LJS Placentia by paying Dirks draw-downs of $8,500 per month until the property was sold in February, 2019. (*id*).

c. By then, the amount of Dirks' capital account at LJS Placentia could have been no higher than **$146,150.38** (1 ARA 17–19).

d. Dirks did not leave behind a capital account at WLOW. But if he had done so, it must have been a large deficit, since he had withdrawn the property (7AA 1199), which he valued at more than $1 million (3RT 566:13 – 568:5), as well as WLOW's other assets – its land entitlements (7AA 1214 at § 11), building permits (7AA 1227), and construction plans (7AA 1223–1225). In fact, he transferred all of these assets to LJS Placentia, where he treated them as his capital contributions. (1 ARA 17–19; 3RT 566:13 – 568:5).

Dirks' accounting of his capital account at WLOW was therefore unreliable, and his claims for payment from WLOW's damage award were unfounded. He thus breached his fiduciary

duty to account to WLOW. *See* § 17704.09(b)(1); *cf. Pool-O'Connor v. Guadarrama* (2023) 90 Cal.App.5th 1014, 1029.

Dirks also requested that the Superior Court allocate to him from WLOW's damage award the sum of **$951,234.65** to reimburse a loan of $635,665.78 that he claimed to have made to WLOW at 10% interest on June 20, 2016. (5AA 859–860). Wardak's close examination of the record, which he submitted to the Superior Court and has placed in the record before this Court, disclosed that Dirks' purported loan to WLOW was apparently a fiction and had never been made. (1 ARA 11–17.)

Without deciding these matters, the Superior Court rejected Dirks' requested claims against WLOW's damage award after finding that they were "unjust." (6AA 1101.)

These matters were intimately connected with WLOW's adoption of the Second Operating Agreement, which set forth Dirks' inflated statement of his capital account (7AA 1214 § 11), and also with Dirks' dissolution of WLOW and taking of its assets (3RT 566:13 – 568:5).

In connection with these matters, Dirks failed to give WLOW candid, timely accounts of his transactions with it and presented unfounded claims against it despite his fiduciary duty to account under section 17704.09(b)(1).

The duty to account, in turn, is a subpart of the duty of loyalty under section 17704.09(b). By his above conduct, Dirks breached it. *See Feresi*, 232 Cal.App.4th at 425 (stating that the duty of loyalty under section 17704.09(b) requires "unfaltering

loyalty and honesty" and is the same duty that business partners owe to one another); *cf. Enea*, 132 Cal.App.4th at 1564.

3. A Faithless Manager Cannot Fulfill the Duty to Account

It is open to question whether Dirks, after enforcing the Forfeiture Provisions, could have fulfilled his fiduciary duty to account to WLOW. This duty, like the other fiduciary obligations set forth at section 17704.09(b)(1)–(3), are subparts of the duty of *loyalty*. It seems doubtful that a faithless manager, having ransacked his LLC, can fulfill any part of his duty of loyalty by candidly avowing his ill-motivated self-dealing. *See Feresi,* 232 Cal.App.4th at 425–426; *cf. Enea,* 132 Cal.App.4th 1564.

F. Dirks Breached the Duty to Avert Conflicts of Interest and the Duty Not to Compete

While managing WLOW, Dirks took the above steps for his own immediate benefit and for the ultimate benefit of a rival firm that he and Omar formed (LJS Placentia). (*See* pp. 19–27, *supra*.)

On this separate ground, Dirks breached his duty of loyalty to WLOW, which forbade him to have any dealing with WLOW while acting for another who had an adverse interest, including his own private interest (*see* § 17704.09(b)(2)). This duty also forbade him to compete against any business or commercial activity operated by WLOW (*see* § 17704.09(b)(3)). *Cf. Everest Investors,* 114 Cal.App.4th at 424–425 ("A partner may not dissolve a partnership to gain the benefits of the business for himself, unless he fully compensates his copartner for his share of

the prospective business opportunity."); *Bardis v. Oates* (2004) 119 Cal.App.4th 1, 13 ("As managing partner, Oates was prohibited from engaging in self-dealing in any way, shape or form. The law does not permit a fiduciary to deal with himself in any transaction in his individual capacity."); *Jones v. Wells Fargo Bank* (2003) 112 Cal.App.4th 1527, 1540 ("Partnership is a fiduciary relationship, and partners may not take advantages for themselves at the expense of the partnership."); *Heller Ehrman LLP v. Davis Wright Tremaine LLP* (2018) 4 Cal.5th 467, 480 ("Under our partnership law, partners cannot compete with their firm during the partnership....").

G. Dirks Breached His Duty of Care

A manager, when acting on behalf of the LLC, must not engage in "grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." *See* § 17704.09(c). This obligation is characterized as a fiduciary duty in section 17704.09(a).

By his above acts, which he took while acting as WLOW's manager, Dirks engaged in "intentional misconduct." To all appearances, he deliberately supplied and then abused the Second Operating Agreement's funding and forfeiture provisions to frustrate WLOW's efforts to procure funding, to disband and dissolve WLOW, and to give away its assets to himself and then to a rival company (LJS Placentia). (*See* pp. 19–27, *supra*.)

Alternatively, Dirks acted with gross negligence by having WLOW adopt the Second Operating Agreement despite its

inclusion of an ambiguous funding clause and problematic forfeiture provisions that seemingly promoted his own interest at WLOW's expense.

If Dirks did not act with intentional misconduct in this matter, then his conduct can only be described as grossly negligent, since it is a rare manager of an LLC who will invoke a doubtful interpretation of an ambiguous contractual provision to prevent his LLC from receiving mission-critical funds, then invoke its failure to do so as cause to disband and dissolve it, take away all of its assets, and make no provision for its winding up and dissolution. *See People v. Bennett* (1991) 54 Cal.3d 1032, 1036 ("Gross negligence is the exercise of so slight a degree of care as to raise a presumption of conscious indifference to the consequences. (....) The test is objective: whether a reasonable person in the defendant's position would have been aware of the risk involved.")

Dirks thus breached his duty of care to WLOW in violation of section 17704.09(c) by managerial conduct that severely harmed WLOW and was either intentional or grossly negligent.

H. Dirks' Enforcement of the Forfeiture Provisions Entailed Serial Breaches of His Fiduciary, Contractual, and Statutory Duties to WLOW

The Forfeiture Provisions in the Second Operating Agreement conferred on Dirks discretionary powers to perform various acts and transactions (described in full in Wardak's Opening Brief, pp. 23–25.) These acts and transactions were largely irreconcilable with his other obligations under the Second

Operating Agreement. Indeed, he could not perform them without committing a material breach of the Second Operating Agreement. *Compare* (7AA 1214–1215 at § 11, 1218 at § 24 (v) *with* 7AA 1214–1219 at §§ 9, 17, 19, 22, 24 (below subpart (vi)).

Nevertheless, Dirks opted to enforce the Forfeiture Provisions by canceling Wardak's membership interest in WLOW, disbanding and dissolving WLOW, and taking sole ownership of its membership interests and therefore its assets.

By performing these acts and transactions, Dirks openly breached the following contractual obligations that he was charged with performing under the Second Operating Agreement:

1. Dirks' obligation to take no act that would prevent WLOW from carrying on its business. ((7AA 1214 at § 9(g)(2).)

2. Dirks' obligation to possess and assign rights in WLOW's property only for WLOW's benefit. (7AA 1214 at § 9(g)(4).)

3. Dirks' obligation to record and keep title to all of WLOW's assets only in WLOW's name. (7AA 1217 at § 22.)

4. Dirks' various obligations upon the proposed sale, sale, or transfer of any member's membership interest. (7AA 1216 at § 17.)

5. Dirks' obligation to hold WLOW's real property in WLOW's name until any capital gain from its sale could be treated as a long-term capital gain under federal law. (7AA 1216–17 at § 19.)

6. Dirks' obligation upon WLOW's dissolution to liquidate all assets held by WLOW and to disburse the liquidation proceeds so far as possible to pay its debts to outsiders, its debts and capital reimbursements to members, and *pro rata* distributions to its members. (7AA 1216 at § 14(c), 1218–1219 at text beneath § 24(vi)). This obligation tracked the statutory requirements for LLCs set forth at section 17707.05. (*See* pp. 29–31, *supra*.)

As WLOW's manager, Dirks was obliged to fulfill these obligations in accordance with his fiduciary duties of loyalty and care under section 17704.09(b)–(c). His enforcement of the Forfeiture Provisions, however, plainly and directly breached each of these obligations as well as his parallel statutory obligations under section 17707.05.

The Forfeiture Provisions thus authorized Dirks to perform acts and transactions that, once performed, would constitute material breaches of his fiduciary, statutory, and contractual duties to WLOW. That is precisely what happened when Dirks performed these acts.

I. The Second Operating Agreement Did Not Modify Any of Dirks' Fiduciary Duties

The Second Operating Agreement did not purport to modify any of Dirks' fiduciary duties to WLOW (reasonably or otherwise), nor did it absolve his clear breaches of these duties (by a proper ratification or otherwise). These points are explained in this section.

The Second Operating Agreement was executed on May 15, 2015. At the time, it could have expressly limited the reach of Dirks' fiduciary duties to WLOW and its other members in accordance with the predecessor version of section 17701.10(c)(14)–(15).[15]

Accordingly, the Second Operating Agreement could have imposed "reasonable" limitations of Dirks' duty of care under section 17704.09(c). *See* § 17701.10(c)(15). It also could have declared, within reason, that certain acts or transactions that Dirks was authorized to perform in the future would not constitute a breach of his duty of loyalty under section

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In this section of the brief, all statutory references made to section 17701.10 refer to the predecessor version in effect when WLOW adopted its Second Operating Agreement on May 15, 2015. Like the current version, this statute permitted an LLC's operating agreement to establish rules and procedures that governed "relations among the members ... and between the members and the limited liability company." (*See id*., (a)(1).) Section 17701.10(a)(2) also permitted rules and procedures that governed a manager's "rights and duties" (*see id*., (a)(2)). Even so, an LLC's operating agreement could not "eliminate the duty of loyalty, the duty of care, or any other fiduciary duty." *See id*., (c)(4). At most, it could "[i]dentify specific types or categories of activities" that did not violate any duty of loyalty, so long as the exclusion of these activities was not "manifestly unreasonable." *See id.,*(c)(14)(A). An LLC's operating agreement could also "[s]pecify the number or percentage of members that may authorize or ratify ... a specific act or transaction that otherwise would violate the duty of loyalty [codified at section 17704.09(b)]," provided that these members first received a "full disclosure ... of all material facts." *See* 17701.10(c)(14)(B). Lastly, an LLC operating agreement could reasonably "reduce" the duty of care codified at section 17704.09(c). *See* § 17701.10(c)(15).

17704.09(b). *See* § 17701.10(c)(14)(A). Any such limitation of Dirks' duty of care would have been enforceable if found to be reasonable, and any such carve-out from his duty of loyalty would have been enforceable so long as it was not found to be "manifestly unreasonable." *See id.*, (c)(14)(A)–(15).

California's law of partnerships, however, suggests that contractual limitations of a manager's fiduciary duties, even if permitted under section 17701.10(c)(14)–(15), should be narrowly construed and upheld only when truly reasonable and consistent with a manager's usual fiduciary dealings with his LLC. *Cf. Everest Investors,* 114 Cal.App.4th at 424 ("The fiduciary obligations of a general partner with respect to matters fundamentally related to the partnership business cannot be waived or contracted away in the partnership agreement.").

The Second Operating Agreement also could have included an express ratification of Dirks' past or future acts or transactions that, absent ratification, would constitute a breach of his duty of loyalty under section 17704.09(b), so long as the ratification was made by a majority of WLOW's members after they had received a full disclosure of all material facts. *See* § 17701.10(c)(14)(B). Lastly, the Second Operating Agreement could have established a procedure by which such ratifications might be made in the future. *See id*.

WLOW's Second Operating Agreements lacked any such limitation or ratification. It did not purport to limit, modify, circumscribe, or excuse any part of Dirks' fiduciary duties under

section 17704.09(b)–(c). (*See* 7AA 1211–1243.) Nor did it include an express ratification (by a qualified majority or otherwise) of acts or transactions performed by Dirks that, absent ratification, would constitute a breach of his duty of loyalty. (*Id*.) Rather, the Second Operating Agreement was silent on these points. (*Id*.)

If Dirks committed any breach of a fiduciary duty, it was not absolved by any provision in the Second Operating Agreement.

Nor can the Forfeiture Provisions be construed as a *de facto* carve-out from Dirks' fiduciary duties, as is made clear by the following points.

1. Any such carve-out would have been unreasonable for all the reasons given above and therefore invalid. *See* § 17701.10(c)(14)(A) (permits carve-outs from a manager's duty of loyalty if not "manifestly unreasonable"); *id*., (c)(15) (permits "reasonable" limitations of a manager's duty of care).

2. The Second Operating Agreement did not expressly acknowledge or even hint that its Forfeiture Provisions authorized Dirks to take acts or transactions that might constitute a breach of a fiduciary duty that he owed.

It is impossible, then, that the Second Operating Agreement could have placed such acts and transactions beyond the purview of Dirks' duty of loyalty or limited Dirks' duty of care.

As worded, section 17701.10(c)(14)(A) and section 17701.10(c)(15) appear to require an express reference to any such limitation or ratification. *See id*. A manager cannot

surreptitiously include provisions in an operating agreement that authorize him to breach his fiduciary duties. *See* § 17701.10(c)(14)–(15). *See also Feresi,* 232 Cal.App.4th at 425–426; *cf. Enea,* 132 Cal.App.4th 1564; *cf. Everest Investors,* 114 Cal.App.4th at 424 (a partner cannot use a contract to waive his fiduciary duties to the partnership for "matters fundamentally related to the partnership business.").

The Second Operating Agreement did not make any sort of disclosure that would permit a majority of WLOW's members to ratify any act or transaction that might otherwise constitute a breach of the duty of loyalty. (7AA 1211–1243). But before such a ratification could have been made, an LLC's members must receive a full disclosure of "all material facts," and then a majority of them can ratify "a specific act or transaction that otherwise would violate the duty of loyalty." *See* § 17701.10(c)(14(B).

There is nothing of the sort in the Second Operating Agreement. (7AA 1211–1243.) Rather, Dirks merely juxtaposed the Joint-Funding Clause and Forfeiture Provisions next to standard boiler-plate provisions in an otherwise unremarkable operating agreement for an LLC. (7AA 1214–1215 at § 11, 1218–1219 at § 24.)

If the Second Operating Agreement had included any such limitation or ratification, Wardak would have objected on one or more of the above grounds. As it happens, Wardak need not raise any such objection because the Second Operating Agreement did

not purport to modify any of Dirks' fiduciary duties (reasonably or otherwise) or ratify any of his acts or transactions that otherwise would have constituted a breach of his duty of loyalty (with sufficient disclosures or otherwise).

Wardak's answer to the Court's last query is therefore "No."

IV. CONCLUSION

In sum, Dirks committed various breaches of his fiduciary duties to WLOW by having it adopt the Second Operating Agreement, by dissolving it and taking its assets, and by performing various acts and transactions that were indissociable from these matters. None of these breaches of duty was absolved by any provision in the Second Operating Agreement.

For all of the foregoing reasons, Wardak's responses to the Court's first and second queries are "Yes" and "Yes," and his response to the Court's third query is "No."

Lastly, the undersigned hesitated before submitting such a lengthy letter brief, but he surmised that the Court's three queries raise issues of paramount importance in this appeal and wished to address them fully and carefully.

Dated: December 1, 2023

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that the computer program used to prepare this brief indicates that this brief contains 11,359 words, including footnotes, and excluding my firm's letterhead, the table of contents, the table of authorities, the signature blocks, this certificate of compliance, and the certificate of service.

I further certify that font used in this brief is Roman-type (Century Schoolbook) and 13 points in size.

Dated: December 1, 2023

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CERTIFICATE OF SERVICE

I, the undersigned, declare that I am over the age of eighteen years and am not a party in this civil action. My business address is 402 West Broadway, Suite 400, San Diego, CA 92101.

On the date indicated below, I served this document, which is entitled "Appellant's Supplemental Letter Brief (Corrected Version)" on the attorneys for all parties in this action other than Plaintiff-Appellant, whom I represent. Their names, addresses, and other contact information are as follows:

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I accomplished this service by causing an officially approved provider of filings and services, TrueFiling, to serve this document on the above-listed attorneys by electronically transmitting it to each attorney's above-listed e-mail address.

I declare under penalty of perjury that the foregoing matters are true and correct. Executed at San Diego, California on December 1, 2023.

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