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**STATE OF MINNESOTA
IN COURT OF APPEALS
A16-1921**

David L. Phillips, Jr.,
Plaintiff,

Lisa Marie Phillips,
Appellant,

vs.

Diane L. Phillips,
Respondent,

Sheridan Properties, LLC,
Defendant,

and

3-Daves, LLC,
Third Party Defendant.

**Filed February 5, 2018
Affirmed
Reilly, Judge**

Rice County District Court
File No. 66-CV-14-790

Mark J. Schneider, Gary K. Luloff, Chestnut Cambronne PA, Minneapolis, Minnesota (for
appellant)

Peter W. Johnson, Excelsior, Minnesota (for respondent)

Considered and decided by Reilly, Presiding Judge; Worke, Judge; and Rodenberg,
Judge.

UNPUBLISHED OPINION

REILLY, Judge

In this appeal, appellant argues that the district court abused its discretion by declining to reform seven promissory notes. Appellant also challenges the district court's calculation of her interest in a limited liability company (LLC), and argues that respondent is not entitled to a contribution award due to unclean hands. Because the district court did not abuse its discretion in declining to reform the promissory notes or in finding that respondent does not have unclean hands, and because its calculation of appellant's LLC interest was not clearly erroneous, we affirm.

FACTS

In June 2005, David Phillips, Sr. (David Sr.) and his spouse, respondent Diane Phillips, formed a business, 3-Daves LLC (3-Daves), with David Sr.'s two sons and their spouses. 3-Daves was created to invest in and develop real estate. David Phillips, Jr. (David Jr.) and his wife, appellant Lisa Phillips, held joint ownership of a one-third membership interest in 3-Daves; David Larry Phillips (David Larry) and his wife, Michelle Phillips, held another one-third membership interest; and David Sr. and Diane held the remaining one-third membership interest in 3-Daves.¹

Each of the couples made initial capital contributions to 3-Daves. With that initial capital, 3-Daves acquired properties in Faribault, Dundas, and Lonsdale (the Properties). In 2008, 3-Daves decided to develop the Faribault property for residential renters. To this

¹ Appellant and respondent are referred to by their first names for clarity.

end, David Sr. and Diane advanced additional funds; these contributions were memorialized in a series of seven “Promissory Notes” (the Notes). 3-Daves was not a party to any of the Notes. Instead, David Jr., Lisa, David Larry, and Michelle signed the Notes individually as borrowers and guarantors.

In 2010, David Sr. died, and his governing and financial interests in 3-Daves passed to respondent, his wife, Diane. Soon after, David Jr., David Larry, and Michelle each filed for bankruptcy. Appellant Lisa did not file for bankruptcy, which left her and respondent as the remaining individuals with governing interests in 3-Daves. In 2011, Diane appointed herself chief manager of 3-Daves.

Around this time, mortgage holder New Market Bank began foreclosure proceedings on the Lonsdale property. Diane and New Market Bank reached a settlement for the Lonsdale property and some of Diane’s individual obligations. The settlement agreement required Diane to pay a sum of money to New Market Bank, including \$100,000 toward the balance on the Lonsdale property loan. New Market Bank also agreed to a new amortization schedule for the remaining \$160,000 balance on the Lonsdale property loan. After settling with New Market Bank, Diane transferred the Lonsdale property from 3-Daves to East View LLC, of which she was the sole owner and manager. East View LLC assumed the remaining \$160,000 balance on the Lonsdale property loan. Diane made repairs to the Lonsdale property and sold it for \$168,000, receiving \$1,598.60 in net proceeds.

In 2013, David Jr. and Lisa sold their principal residence, which was encumbered, in part, by a judgment lien held by Diane. David Jr. and Lisa sought a declaratory judgment

in district court that the proceeds of their home sale were exempt from liens under the homestead exemption. Diane filed a number of counterclaims, including a claim for default on the Notes and a claim for contribution for the settlement amount paid to New Market Bank for the Lonsdale property loan. Lisa argued that the Notes were intended to provide Diane priority to the proceeds from the sale of the property, and the parties never intended the Notes to function as promissory notes. Lisa then argued that she possessed a 50% governance interest in 3-Daves because she and David Jr. held their interest in a joint tenancy, and that Diane could not unilaterally act with regard to the Lonsdale property. Lisa also claimed Diane was not entitled to contribution because she came with unclean hands.

After a court trial, the district court granted Diane's claims and entered a judgment in favor of Diane for \$256,126.86. The district court determined that David Jr.'s bankruptcy filing severed his joint tenancy with Lisa. David Jr.'s governance interest in 3-Daves then terminated on his bankruptcy, and his 25% governing interest was split between Lisa and Diane, which left Diane with a 67% majority governing interest. Because Diane possessed a majority governing interest, she was authorized to transfer the Lonsdale property to Eastview LLC to protect the property from potential claims by creditors. This appeal followed.

DECISION

I. The district court did not abuse its discretion by declining to reform the Notes.

Lisa argues the district court abused its discretion when it declined to reform the Notes to effect her desired meaning. To support her position, Lisa argues that there was a mutual mistake between the parties, and they did not intend for the Notes to create a loan. According to Lisa, the parties understood that the Notes provided priority to Diane for the proceeds of a sale of any of the Properties.

Contract reformation is an equitable remedy. *SCI Minn. Funeral Servs., Inc. v. Washburn-McReavy Funeral Corp.*, 795 N.W.2d 855, 864 (Minn. 2011). Appellate courts review “equitable determinations for abuse of discretion.” *City of N. Oaks v. Sarpal*, 797 N.W.2d 18, 23 (Minn. 2011). A party seeking contract reformation for mutual mistake must prove that

(1) there was a valid agreement between the parties expressing their real intentions; (2) the written instrument failed to express the real intentions of the parties; and (3) this failure was due to a mutual mistake of the parties, or a unilateral mistake accompanied by fraud or inequitable conduct by the other party.

SCI, 795 N.W.2d at 865 (citation omitted). The elements must be established through “evidence which is clear and consistent, unequivocal and convincing.” *Id.* (citations omitted). The level of proof for contract reformation is a “high burden.” *Id.* (citation omitted).

Lisa’s argument fails on the third prong. Lisa has not shown with “unequivocal and convincing” evidence that there was a mutual mistake between the parties. *Id.* Lisa

testified that the Notes were to be repaid when any of the Properties were sold and that the proceeds would go to Diane first before being paid to the other members of 3-Daves. Lisa also testified that there were never discussions of a forced sale triggering repayment of the Notes. She claimed that no monthly payments were ever made on the Notes and that no interest-only payments were made either. Diane also testified that she understood the Notes were to be repaid upon the sale of one of the Properties and that the proceeds would be paid to her first before the other members of 3-Daves. However, Diane further testified that she thought of the Notes as “loans,” and that “we were making the loans to the four individuals, and they were responsible for it. And like I said, hopefully the properties would sell, we would all make some money.” Diane’s testimony supports the district court’s finding that there was no mutual mistake because respondent believed that the Notes created indebtedness.

Lisa also claims that there is “undisputed testimony” that the “boilerplate language was unintentionally included through the mutual mistake of both parties.” Diane testified that she chose the promissory note form because it would be “in the proper form” and “it was [her] intention that the note would be payable.” Diane’s testimony directly rebuts Lisa’s argument—Diane chose the form on purpose. On this record, the district court did not abuse its discretion in determining that Lisa failed to meet the “high” bar of “unequivocal and convincing” evidence that there was a mutual mistake between the parties. Thus, the district court did not err by awarding Diane judgment on the Notes. *See SCI*, 795 N.W.2d at 865.

II. Lisa failed to sustain her burden of showing that the district court erred by determining that Lisa and David Jr.'s joint tenancy was severed by David Jr.'s bankruptcy filing.

The district court determined that David Jr. severed David Jr. and Lisa's joint tenancy in their membership interest in 3-Daves by listing on his bankruptcy filing a "1/4 interest" in 3-Daves. Lisa argues the district court erred by determining that Diane and Lisa each took one-half of Dave Jr.'s governance interest when David Jr.'s bankruptcy caused his interest to terminate under statute. Because Lisa has mischaracterized the district court ruling and has failed to adequately show that the district court erred, we affirm.

The district court's ruling presents a mixed question of law and fact, because the court determined that the content of David Jr.'s bankruptcy filing evidenced a severance of the joint tenancy between David Jr. and Lisa.

We give the district court's factual findings great deference and do not set them aside unless clearly erroneous. However, we are not bound by and need not give deference to the district court's decision on a purely legal issue. When reviewing mixed questions of law and fact, we correct erroneous applications of law, but accord the [district] court discretion in its ultimate conclusions and review such conclusions under an abuse of discretion standard.

Porch v. Gen. Motors Acceptance Corp., 642 N.W.2d 473, 477 (Minn. App. 2002) (alteration in original) (quotations and citations omitted), *review denied* (Minn. June 26, 2002).

Each of 3-Daves' founding couples originally owned a one-third membership interest as joint tenants. It is undisputed that, upon David Sr.'s death, Diane became the

sole owner of a one-third interest in 3-Daves. It is also undisputed that, upon David Larry and Michelle's bankruptcy, their one-third interest in 3-Daves was split between the remaining couples. David Jr. and Lisa received an additional one-sixth interest, and Diane received an additional one-sixth interest. This left David Jr. and Lisa with a one-half interest as joint tenants and Diane with a one-half interest as a sole owner.

When David Jr. filed bankruptcy, he listed his interest in 3-Daves as a "1/4 interest." David Jr. reported \$1 as the value of his interest, and he sought an exemption for his interest under 11 U.S.C. § 522(d)(5)(2017). The district court here ruled that David Jr.'s bankruptcy *filing* severed the joint tenancy in his and Lisa's interest in 3-Daves, leaving him with a 25% individual interest. The district court then determined that his 25% governing interest in 3-Daves terminated upon his bankruptcy under Minn. Stat. § 322B.306, subd. 1(viii) (2016).

Lisa argues that the district court erred by ruling that the *termination* of David Jr.'s interest of 3-Daves under § 322B.306, subd. 1(viii) diminished appellant's interest in 3-Daves. Lisa mischaracterizes the district court's ruling. In actuality, the district court ruled that David Jr. *severed* the joint tenancy by claiming a 25% individual interest in 3-Daves in his bankruptcy *filing*. The district court then found that David Jr.'s resulting 25% interest was *terminated* by his bankruptcy under § 322.306, subd. 1(viii). Lisa does not address the issue of severance in her brief and did not properly characterize the posture of the district court ruling. Lisa offers no caselaw rebutting the district court's determination that the joint tenancy was severed by David Jr. claiming a 25% individual interest in 3-Daves in his bankruptcy filing. Because Lisa offers no authority to support her argument and

patently mischaracterizes the decision of the district court, we conclude that Lisa has not met her burden of showing that the district court erred. *See Jacobson v. Chicago & N. W. Ry. Co.*, 221 Minn. 454, 462, 22 N.W.2d 455, 461 (1946) (“The burden of showing error is on the appellant, and where, as here, he fails to sustain the burden, decision must go against him.”).

III. The district court did not abuse its discretion in rejecting Lisa’s unclean-hands argument.

Lisa argues that Diane is not entitled to contribution because she claimed equitable relief with unclean hands. Lisa contends that Diane acted with a bad motive when she transferred the Lonsdale property to Eastview LLC for personal benefit.

Contribution is an equitable remedy whereby two people who share a common burden must share in the cost of that burden. *Hammerschmidt v. Moore*, 274 N.W.2d 79, 81 (Minn. 1978). A person’s request for equitable relief may be denied if they seek relief with unclean hands, which is an action made “unconscionable by reason of a bad motive, or where the result induced by [their] conduct will be unconscionable either in the benefit to [themselves] or the injury to others.” *Peterson v. Holiday Recreational Indus. Inc.*, 726 N.W.2d 499, 505 (Minn. App. 2007), *review denied* (Minn. Feb. 28, 2007). This court reviews “equitable determinations for abuse of discretion.” *Sarpal*, 797 N.W.2d at 23.

Throughout the settlement process with New Market Bank, Diane believed she had a governing interest, which indicates that she did not believe she was doing anything wrong. Furthermore, Diane did not choose to transfer the Lonsdale property to Eastview LLC to benefit herself—the transfer was a condition of the settlement agreement with New

Market Bank. Diane's other properties involved with the New Market Bank settlement were also transferred to Eastview LLC. In fact, Eastview LLC was created to effectuate the settlement agreement. The district court did not err in determining that Diane did not possess a "bad motive" sufficient to show unclean hands. *See Peterson*, 726 N.W.2d at 505. Accordingly, the district court did not abuse its discretion by rejecting Lisa's unclean-hands argument and granting Diane's request for contribution.

Affirmed.