

IN THE SUPREME COURT

STATE OF NORTH DAKOTA

Donna Watts, Jack Watts, Georgia Bonderenko,)
Mabel Brauer, Gaylen Erck, Vickie Erck, Rodney)
Getzlaff, Kathy Getzlaff, Harlon Getzlaff, Dennis)
Hensen, LaVonne Hensen, Delton Hust, Holly Hust,)
Dennis Jacobsen, Christie Jacobsen, Bruce Johnson,)
Diane Johnson, Judith Koponen, Wayne)
Krzmarzick, Darrel Loftesnes, Theresa Loftesnes,)
Eugene Neiss, Melanie Wanner, Mark Rustad, Rena)
Rustad, Jim Soltis, Rita Stomvoll, John Stomvoll,)
Jim Suydam, Bonnie Suydam, Clara Thompson,)
Larry Voltz, Diane Voltz, Natalie Wade, Shawn)
Weigel, LaRinda Weigel, Lynn Wood, Vernon F.)
Bohara, Elinda Kay Bohara, Laverne Mikkelson as)
Trustee of Ann C. Bonebrake Trust, and Carol)
Uecker,)

Plaintiffs-Appellants,)

vs.)

Magic 2 x 52 Management, Inc., a North Dakota)
corporation, B K Properties, L.L.C., a North Dakota)
limited liability company, Herslip Construction, Inc.,)
a North Dakota corporation, Kenneth Herslip,)
individually, and doing business as Herslip)
Restaurants, Bradley Wells, and Mark Guttormson.)

Defendants-Appellees.)

Supreme Court
Case No. 20110145

APPEAL FROM LETTER OPINION ENTERED MARCH 25, 2011
BY THE HONORABLE WILLIAM W. MCLEES, NORTHWEST JUDICIAL
DISTRICT, WARD COUNTY, NORTH DAKOTA, CIVIL NO. 51-07-C-00280

BRIEF OF APPELLANT

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STATEMENT OF THE ISSUE

(1.) Whether the District Court's determination it lacked the authority under applicable law to grant Appellant's requested post-judgment relief of piercing the corporate veil and awarding punitive damages on the basis of pre-judgment and post-judgment fraudulent conveyances, waste, and other wrongful conduct by Appellees, none of which was at issue at trial, was in error.

STATEMENT OF THE CASE

(2.) Appellants, comprising a majority of the limited partners of Magic 2 x 52 Limited Partnership ("Magic Partnership") commenced this derivate action on behalf of Magic Partnership against Appellees seeking the removal of Magic 2 x 52 Management, Inc. ("Magic Management") as the general partner of Magic Partnership, and requesting monetary damages from the Appellees on the basis of breach of fiduciary duties, breach of contract, misappropriation/conversion of partnership property, fraud, and other violation of North Dakota law. Appellants also requested the District Court pierce the corporate veil of the corporate defendants and requested an award of punitive damages on the basis of fraud. At all relevant times, Appellee Ken Herslip was an officer, director and controlling shareholder of Appellees.

(3.) Shortly following commencement of this action, the District Court granted the Appellants' motion for removal of Magic Management as general partner of Magic Partnership pending trial, appointed a neutral receiver for Magic Partnership, and ordered an accounting of Magic Partnership. Following completion of the accounting, the District Court permitted the limited partners to vote, in accordance with the partnership agreement, on whether to remove Magic Partnership as general partner of Magic Partnership. A

majority of the limited partners voted to replace Magic Management with plaintiff Donna Watts as general partner of Magic Partnership. Donna Watts remains the sole general partner of Magic Partnership to this day.

(4.) Following a bench trial, judgment in favor of Magic Partnership was entered on April 19, 2010 pursuant to Honorable William W. McLees' Opinion of the Court issued March 31, 2010 (App. 64-112), upholding the limited partners' removal of Magic Management as the general partner of Magic Partnership, and awarding monetary damages to Magic Partnership against Magic Management, Herslip Construction and BK Properties on the basis of breach of contract, breach of fiduciary duties, fraud, and violation of the North Dakota Uniform Limited Partnership Act. The District Court entered an Amended Judgment on May 11, 2010 awarding Magic Partnership recoverable costs and disbursements against Herslip Construction, Magic Management and BK Properties for an Amended Judgment of \$192,355.46, and further judgment and pre-judgment interest against Magic Management and Herslip Construction in the amount of \$222,047.68. (App. 113-14.) Despite noting evidence of fraud existed to support an award of punitive damages against the Appellees, the District Court exercised its discretion not to award punitive damages. The District Court also denied Appellant's request to pierce the corporate veils of the judgment debtors.

(5.) During the course of the prior litigation, as well as following entry of judgment, Appellees engaged in fraud by conveying Appellee's assets and business opportunities to other Herslip controlled entities, and otherwise committing waste of corporate assets for the malicious purpose of preventing Appellant's collection upon the judgment. The financial

condition of the Appellees was not at issue, nor was discovery permitted on Appellees' financial condition, in the underlying litigation.

(6.) Following diligent and unsuccessful attempts by Appellants to collect upon the judgment, and following discovery of the fraudulent conveyances and waste, Appellants filed a post-judgment motion with the District Court requesting the Court pierce the corporate veils of the judgment debtors to hold Ken Herslip personally responsible, and requesting an award of punitive damages, on the basis of the fraudulent conveyances and waste of corporate assets – additional conduct not at issue in the prior litigation in this case.

(7.) The District Court denied Appellants' post-judgment motion to pierce the corporate veil and for punitive damages on the basis the appeals period had already expired relative to the March 31, 2010 Opinion, and on the basis the deadline for Appellants to request post-judgment relief pursuant to Rules 59 and 60 of the North Dakota Rules of Civil Procedure had also expired. The District Court concluded the Appellants were not entitled to "a second bite of the apple as to these two issues," without addressing any of the newly presented evidence of pre-judgment and post-judgment fraudulent conveyances and waste on the part of the Appellees which justifies the relief requested. The District Court sympathized with Appellants' plight but concluded it was without authority to grant the Appellants' requested remedy under the North Dakota Rules of Civil Procedure in this action. The District Court instead intimated the remedy requested must be pursued in a separate action.

(8.) The specific issue presented on appeal, therefore, is whether the District Court's determination it lacked the authority to grant the Appellant's requested relief in this action was in error. The District Court's decision was in error as Appellants' requested relief is not dependent upon an appeal or modification of the underlying judgment pursuant to Rules 59

or 60. The District Court had the inherent power to award the requested post-judgment relief. Appellants request a determination of error on appeal and request the matter be remanded to the District Court for determination, or in the alternative, that this Court pierce the corporate veil and find Ken Herslip personally liable on the judgment, and also award punitive damages to Magic Partnership.

STATEMENT OF FACTS

I. DISTRICT COURT'S LETTER OPINION

(9.) Judge William W. McLees' Letter Opinion entered March 25, 2011 at issue provides as follows:

Counsel:

Having considered the Plaintiffs' motion to Pierce the Corporate Veil and for Punitive Damages, or, in the Alternative, to Compel Discovery and Attendance at a Deposition, as well as the Herslip Defendants' Response to that motion, the Court finds that an appropriate basis has *not* been shown for granting that portion of the Plaintiffs' motion pertaining to piercing the corporate veil/punitive damages-----and that portion of the Plaintiffs' motion will be *denied*.

In this regard, the Court first observes that Judgment was entered in this case on April 19, 2010. NOTE: An Amended Judgment was entered, addressing taxable costs, on May 11, 2010. The Judgment was based on a forty-seven page Opinion of the Court, dated March 31, 2010. As part of the Court's opinion, the Court specifically denied the Plaintiffs' request to pierce the corporate/limited liability veils of the Defendants Herslip Construction, Inc., ("HCI"), Magic 2x52 Management, Inc. ("Magic Management"), and BK Properties, L.L.C. ("BK Properties"), and set forth in detail the rationale for its decision as to this issue. As part of the Court's opinion, the Court also specifically *denied* the Plaintiffs' request for an award of punitive damages, and set forth in detail the rationale for its decision as to this issue.

The Court further observes that the Plaintiffs did not file a motion for new trial under Rule 59 of the North Dakota Rules of Civil Procedure, nor have they sought relief from the Judgment under Rule 60 of those same rules. Finally, the Plaintiffs did not appeal any aspect of the Court's decision to the North Dakota Supreme Court. Under any circumstances, the April 19, 2010, Judgment (as amended relative to taxable costs), is *final* as to all issues decided by the Court in this matter---including the issues the Plaintiffs now want this Court to re-visit, *piercing the corporate veil* and *punitive damages*. In making this determination, the Court finds that the line of

cases (i.e. *Coughlin Construction Co., Inc. v. Nu-Tec Industries, Inc.*, 2008 ND 163, 755 N.W.2d 867; *Axtmann v. Chillemi, et al.*, 2007 ND 179, 740 N.W.2d 838, *Hamilton v. Hamilton*, 410 N.W.2d 508 (N.D. 1987); and, *Jablonsky v. Klemm*, 377 N.W.2d 560 (N.D. 1985)) relied upon by the Plaintiffs simply do not allow them – **in this action** – a “second bite at the apple” as to these two issues.

The Court further finds, with respect to that portion of the Plaintiffs’ motion seeking an order from the Court to compel discovery and the attendance (of the Defendant Kenneth Herslip) at a deposition, that the Plaintiffs are rightfully entitled to examine (at deposition) the Defendant Kenneth Herslip (“Herslip”) in relation to the business and affairs of the Defendant BK Properties----and that portion of the Plaintiff’s motion will be *granted*.

While the Herslip Defendants have informed opposing counsel, over the past several months, that Herslip has been incapacitated as the result of ongoing medical problems and therefore unable to sit for a deposition, the Plaintiffs have provided the Court with information (the accuracy/reliability of which is essentially not disputed by the Herslip Defendants) from which it can reasonably be concluded that Herslip was at least well enough to attend a corporate franchise convention sponsored by Buffalo Wild Wings Corporation in Dallas, Texas, which was held from February 26, 2011, through March 2, 2011. While opposing counsel and this Court may not have a full understanding as to what restrictions Herslip is facing as a result of his medical condition, the fact that he was able to travel a considerable distance from home, and participate in convention activities over several days, certainly causes this Court to question why Herslip can tolerate one activity (i.e., travel/convention) and not the other (i.e., a deposition).

Accordingly, the Court ORDERS that the Herslip Defendants make Herslip available for a deposition, in relation to the business and affairs of BK Properties, no later than June 1, 2011---unless Herslip’s treating physician certifies to this Court, under penalty of perjury, that Herslip’s medical condition will not allow him to participate in a deposition on or before this date.

As for that portion of the Plaintiffs’ motion which asks the Court to compel the Defendants HCI and Magic Management to comply with the Plaintiffs’ post-judgment discovery requests, the Court finds that any such order from this Court would be in violation of the automatic stays now in place as a result of the bankruptcy filings on these two entities. Otherwise stated, unless and until the automatic stays are vacated, this Court has *no authority* to require HCI or Magic Management to comply with the Plaintiffs’ post-judgment discovery requests.

The Court also concludes that any post-judgment discovery conducted by the Plaintiffs will be properly limited to the business and affairs of the three judgment debtors in this case, HCI, Magic Management and BK Properties.

Finally, while the Court is by no means unsympathetic to the Plaintiffs' plight----in the sense that they unquestionably have the right to be made whole for the wrongs done to them by the three judgment debtors in this case, and the Plaintiffs' collection efforts thus far appear to have been wholly unsuccessful----the Court cannot provide the Plaintiffs with a remedy when none exists under the applicable law/rules.

IT IS SO ORDERED.

(App. 115-17 (emphasis in original).) The District Court's Letter Opinion is in error as it incorrectly interprets Appellants' motion as a request for the District Court to re-visit issues determined at trial and incorrectly determines the District Court lacks the authority to grant the post-judgment relief requested by Appellants based upon ongoing fraudulent conduct on the part of the Appellees, none of which was at issue prior to entry of judgment.

II. EVIDENCE SUPPORTING APPELLANTS' REQUESTED RELIEF

A. Fraudulent Conduct by Herslip Defendants Before Judgment Awarded

(10.) Pursuant to the March 31, 2010 Opinion following a bench trial, the District Court determined, in relevant part, the Appellees breached every fiduciary duty owed Magic Partnership and its limited partners (March 31, 2010 Op. at ¶ 3, App. 92-93) and committed fraud (March 31, 2010 Op. at ¶ 9, App. 101-02) when Magic Partnership's then general partner, Magic Management secretly sold real property owned by Magic Partnership to BK Properties (a company wholly owned and managed by Ken Herslip and formed shortly prior to, and for purposes of, this transaction), for significantly less than fair market value. Shortly following this transaction, Ken Herslip, through BK Properties, sold the land to a third party for a significant gain. The District Court also determined, pursuant to the March 2010 Opinion Herslip Construction overcharged Magic Partnership on the construction of the Denny's Restaurant in Minot (March 31, 2010 Op. at ¶ 4, App. 94-97), and Magic Management violated North Dakota law and its contractual obligations to Magic Partnership

and its limited partners by failing to produce Magic Partnership records to limited partners upon reasonable request, and engaging in numerous instances of “stonewalling” the limited partners (*Id.* at ¶ 1, App. 79-83). Based upon these findings, the District Court entered an Amended Judgment on May 11, 2010 awarding Magic Partnership recoverable costs and disbursements against Herslip Construction, Magic Management and BK Properties for an Amended Judgment of \$192,355.46, and further judgment and pre-judgment interest against Magic Management and Herslip Construction in the amount of \$222,047.68. (Amended Judgment, App. 113-14.) In other words, the total judgment amount against Herslip Construction and Magic Management totals \$414,403.14, plus post judgment interest at 6.5% per annum.

B. Herslip’s Wrongful Conduct Since Judgment Awarded

(11.) Appellants’ submitted to the District Court the following additional evidence of wrongdoing by Ken Herslip in support of their request to pierce the corporate veil to hold Ken Herslip personally liable for the judgment debts of Magic Management, Herslip Construction and BK Properties. To avoid duplication and for clarity, a general overview of additional evidence of wrongdoing is being provided in this facts section, with additional evidence being presented in the argument directly.

1. Immediately Upon Entry Of Judgment, Herslip Forms Herslip Management, LLC And Transfers Thereto Herslip Construction’s Construction Business, Management/Administrative Services Business, And Goodwill

(12.) On May 9, 2010, just over one month after the District Court awarded judgment to Magic Partnership, Herslip opened a new North Dakota business, namely Herslip Management, LLC. *See* North Dakota Secretary of State Corporate Details for Herslip

Management, LLC. (Exh. A.¹) A company profile of Herslip Management, LLC published by Manta.com (Exh. B) provides the following description of Herslip Management, LLC:

Herslip Management, LLC is a private company categorized under Construction, Repair, and Dismantling Services and located in Minot, ND. Current estimates show this company has an annual revenue of 220,000 and employs a staff of approximately 5.

Business Categories

Construction, repair, and dismantling services in Minot, ND
Oil/Gas Field Services
Oil and Gas Pipeline and Related Structures Construction
View newly formed U.S. businesses

Company Contacts

Kenneth Herslip

(Exh. B). In addition, the following information regarding Herslip Management, LLC is available at Yellowpages.com:

Categories

General Contractors, Building Contractors-Commercial & Industrial, Home Builders, Altering & Remodeling Contractors, Home Repair & Maintenance, Air Conditioning Contractors & Systems, Heating Contractors & Specialties

AKA

Herslip Management, LLC, Herslip Construction, Inc.

(Exh. C). Herslip Management, LLC not only provides all of the construction services previously performed by Herslip Construction, Inc., **it is also portraying itself as also being known as Herslip Construction.** See North Dakota Secretary of State Corporate Details for Herslip Construction, Inc. (Exh. HH)(listing nature of business as “general contractor/construction”). This is conclusive proof of fraudulent transfers of business

¹ All exhibits referenced in this brief are attached to the Affidavit of Shawn A. Grinolds dated January 7, 2011 (Docket # 549).

opportunities, as well as the goodwill of Herslip Construction to Herslip Management, LLC. As discussed in the argument below, this is also clear and convincing evidence of fraud.

(13.) In addition, during litigation in this case, Herslip Construction received significant income from managing restaurants and other properties owned by entities controlled by Ken Herslip and/or his spouse, Janelle Herslip, including, but not limited to Herslip Restaurants, BK Properties, LLC, GHW Enterprises, LLC, LaMore Restaurants Group, LLC, Grand Restaurants, LLC, and Wings of Minot ND, LLC. In order to avoid Appellants' garnishment upon the revenues received by Herslip Construction for the management/administrative services provided these entities, Herslip transferred all of this business to Herslip Management, LLC. LaMore Restaurants Group, LLC's (controlled by Herslip) written response to Appellants' subpoena requesting information evidencing management fees paid by LaMore to any person or entity, including, but not limited to Herslip Construction, Inc., Herslip Management, LLC and/or any entity in which Ken or Janelle Herslip was involved and/or had an ownership interest, establishes this point, and provides:

This request seeks information far beyond the scope of post-judgment discovery as to the judgment debtors Magic 2 x 52 Management, Inc., B K Properties, LLC, and Herslip Construction, Inc. The general financial position, including the tax returns of LaMore, along with Ken and Janelle Herslip, are not relevant to such collection efforts. **LaMore states during the pendency of this action through May, 2010 it paid a monthly management fee to Herslip Construction, Inc., in exchange for general administrative, office and bookkeeping services provided by Herslip Construction through its employees. The fees were paid month-to-month for services provided and not pursuant to contract.** The fees paid in each year were as follows:

2007	\$14,510
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2008	\$51,697
2009	\$55,753
2010	\$14,157

LaMore did not have other financial dealings with Herslip Construction during that time and has received no payments or assets from Herslip Construction. **When Herslip Construction became a judgment debtor and was subject to collection efforts, Herslip Construction could no longer provide the services required by LaMore as its assets were subject to levy and payments from LaMore for services provided were subject to garnishment.** Among other things, in early May, 2010, Herslip Construction was served with a writ of execution and its bank accounts were subject to garnishment.

Accordingly, LaMore ceased making payments to Herslip Construction in May 2010, and Herslip Construction filed for bankruptcy in June, 2010. LaMore now obtains its general administrative, office and bookkeeping services from Herslip Management and pays a monthly fee for that service. Monthly fees paid from June, 2010, through the end of the year totaled \$57,002. The fees for services per month have increased as LaMore added a second Denny's restaurant in Sioux Falls in 2010. LaMore does not have a contract with Herslip Management. As with Herslip Construction, LaMore has received no payments or assets from Herslip Management. LaMore will undertake to find the checks evidencing the payments detailed above but some of the checks may no longer be available.

(LaMore Restaurant Group, LLC's Objections and Response to Subpoena Duces Tecum at pp. 2-3, attached to correspondence from Randall J. Bakke to Judge McLees (Docket # 558)(bold added).)

2. Two of the Three Herslip Defendants Against Whom Judgment Was Awarded File For Bankruptcy

(14.) On June 9, 2010, Herslip Construction and Magic Management each filed Chapter 7 petitions with the Bankruptcy Court in North Dakota. During a creditors meeting held on September 17, 2010, Herslip disclosed that on or about July of 2008, (during the course of litigation in this case, and when it became evident Appellants would likely prevail on their claims against the Herslip Defendants), Herslip ceased the ongoing business of Herslip Construction and began winding up its affairs, allegedly due to his poor health. *See* audio

recording of bankruptcy creditors meeting (Exh. D). As a result of this decision, the gross income of Herslip Construction dropped from \$2.375 million in 2008 to just \$350,000 in 2009. *See* Herslip Construction's Chapter 7 Statement of Financial Affairs at ¶ (Exh. E). Herslip also admitted at the creditors meeting that Herslip Construction likely would not have filed for bankruptcy if Magic Partnership had not been awarded a judgment against Herslip Construction in this case.

(15.) Appellants respectfully submit Herslip intentionally and with malice has committed waste of Herslip Construction, a valuable asset (including its goodwill) for the sole purpose of defrauding Magic Partnership and its limited partners. Ken Herslip did not attempt to sell Herslip Construction or attempt to take any other action to preserve its assets or goodwill value. Instead, he simply stopped doing business under the name Herslip Construction and transferred significant assets and revenue sources, including customers for which Herslip Construction previously performed managerial/administrative services, to other entities controlled by Herslip and/or his spouse (including, but not limited to, Herslip Management, LLC), as well as directly to Herslip and his spouse in the guise of alleged compensation. As indicated in Herslip Construction's Profit & Loss Statement for 2008, and as elaborated upon in the argument below, the company used to provide managerial/administrative services for Herslip Restaurants, BK Properties, GHW Enterprises, LLC, LaMore Restaurants Group, LLC, Grand Restaurants, LLC, and Wings of Minot ND, LLC, but quit doing so once it became apparent the Appellants would obtain a significant Judgment against Herslip Construction.

3. Herslip's Continued Shell Game Of Setting Up Multiple Business Entities To Avoid Liabilities Such As Appellants' Judgment

(16.) Herslip has continued business as usual following his decision to cease the operations of Herslip Construction. Herslip's establishment of Herslip Management, LLC discussed above is but one example of many. Recently, on or about September 20, 2010, Ken Herslip, through a South Dakota company he owns called LaMore Restaurants Group, LLC, opened another new Denny's restaurant in Sioux Falls, South Dakota. *See* Press Release issued by Denny's Corporation on September 20, 2010 (Exh. F). Herslip also owns several other restaurants in North Dakota, South Dakota and Montana under the name Herslip Restaurants, among others. Ken Herslip, personally or through his spouse, Janelle Herslip, owns controlling interests in numerous entities through which he continues to actively conduct business as usual, including through Herslip Family Properties, LLP, Herslip Restaurants, LaMore Restaurants Group, LLC, GHW Enterprises, LLC, BK Properties, LLC, Grand Restaurants, LLC (organized in North Dakota effective May 9, 2007), Herslip Management, LLC, a North Dakota limited liability company organized on May 9, 2010, and Wings of Minot ND LLC (organized in North Dakota effective February 11, 2008 (Exh. II)). There may be others as well. As discussed below, Herslip has refused to cooperate with post-judgment discovery relative to Herslip Construction, Magic Management, and other entities in which he and/or his wife have controlling interests. Herslip is playing a shell-game with his assets through these artificial entities.

4. Continued Stone Walling Tactics By Herslip

(17.) Ken Herslip has also continued his stonewalling tactics with respect to Appellants' attempts to obtain information regarding the judgment debtors Herslip Construction and Magic Management. Shortly after Appellants' obtained judgment in this case, on May 3, 2010, Appellants served upon the Appellee judgment debtors post-judgment discovery

requests pursuant to Rule 69 of the North Dakota Rules of Civil Procedure (Exhs. G, H and I). On June 8, 2010, BK Properties served its responses (Exh. J) to Appellants' discovery requests revealing all of its assets are essentially fully leveraged – nothing to levy upon. On June 9, 2010 (about the time discovery responses were due), Herslip Construction and Magic Management both filed Chapter 7 bankruptcy petitions with the intention of dissolving the corporations. *See* U.S. Bankruptcy Court, North Dakota, Docket Sheet re: Bankruptcy Petition # 10-30713 (Herslip Construction, Inc.)(Exh.K); U.S. Bankruptcy Court, North Dakota, Docket Sheet re: Bankruptcy Petition #10-30714 (Magic 2 x 52 Management, Inc.)(Exh. L). Ken Herslip has used these filings as a basis not to respond to Appellants' post-judgment discovery requests despite the fact corporate debtors cannot obtain a discharge of debts in bankruptcy. *See* Correspondence from Todd Zimmerman to Shawn Grinolds dated June 14, 2010 (Exh. M)(advising Herslip Construction and Magic Management will not participate in post-judgment discovery due to automatic stay in bankruptcy proceedings). Appellants obtained orders (Exhs. N and O) from the Bankruptcy Court on November 24, 2010 authorizing Rule 2004 examinations of Herslip Construction and Magic Management. On November 24, 2010, Appellants' counsel advised Herslip's counsel that in light of these Orders, Herslip's objections to Appellants' written discovery requests had no merit. *See* Correspondence from Randall J. Bakke to Todd Zimmerman dated November 24, 2010 (Exh. P). Regardless, Herslip continues to stonewall the Appellant' attempts to obtain relevant post-judgment information from the judgment debtors, and has provided no answers or documents responsive to Appellants' Rule 69 request relative to Herslip Construction or Magic Management. The District Court denied Appellant's request to compel written discovery from Herslip Construction and Magic

Management and entities in which either Herslip or his spouse have had a controlling interest at any time since October of 2006 when Appellants put Herslip on notice of Appellants' intention to sue.

(18.) Prior to the District Court's Letter Opinion, Appellants' counsel had attempted to schedule Ken Herslip's deposition since July 20, 2010. *See* Correspondence from Randall Bakke to Todd Zimmerman dated July 20, 2010 (requesting deposition of Ken Herslip for collection purposes in August or September of 2010)(Exh. Q). As Herslip would not agree to a deposition in August or September, Appellants' counsel, after conferring with Herslip's counsel, scheduled Ken Herslip's deposition for December 1, 2010. *See Notice of Deposition of Kenneth Herslip and Subpoena Duces Tecum* dated November 18, 2010 (Exh. R); correspondence from Randall Bakke to Todd Zimmerman dated November 5, 2010 (Exh. S); correspondence from Todd Zimmerman to Randy Bakke dated November 8, 2010 (Exh. T). Herslip served objections to the subpoena duces tecum (Exh. U) refusing to provide any information relative to Herslip Construction and Magic Management on the grounds they had filed for bankruptcy. Herslip's counsel also advised Herslip would be unable to attend his deposition on December 1, 2010 due to health issues. *See* Correspondence from Todd Zimmerman to Randall J. Bakke dated November 24, 2010 (Exh. V). Due to the asserted health issues, the December 1 deposition was postponed until December 21, 2010. *See Amended Notice of Deposition of Kenneth Herslip and Amended Subpoena Duces Tecum* dated December 2, 2010 (Exh. W). On December 3, 2010, and again on December 14, 2010, Herslip's counsel again advised Ken Herslip would be unable to attend the December 21, 2010 scheduled deposition due to his health issues (Exhs. X and Y). As alleged support for the assertion Herslip is unable to attend his deposition is

correspondence from his treating physician dated November 30, 2010 (Exh. Z) advising Herslip underwent emergency surgery on November 20, 2010, that Herslip will require one more surgery, and that Herslip will require six months to recuperate. Notably, Herslip's treating physician does not state Herslip is unable to participate in his deposition during his alleged prolonged period of recuperation. Despite Herslip's continued assertions of health problems allegedly precluding his appearance at a deposition in this action, including at the February 22, 2011 hearing before the District Court on Appellants' motion at issue, Herslip was none-the-less capable of attending a Buffalo Wild Wing's convention in Dallas, Texas a few days later from February 25, 2011 through March 2, 2011. See Buffalo Wild Wings 2011 Convention Schedule, attached to correspondence from Randall J. Bakke to Judge McLees dated March 4, 2011 (Docket #557). During the convention, Herslip was photographed with Dallas Cowboys cheerleaders and participated in a golf tournament (allegedly only driving the golf cart). See photographs attached to Docket # 557. Upon consideration of this evidence, the District Court ordered Herslip to appear for a deposition on or before June 1, 2011 unless his health care provider certified his inability to do so under penalty of perjury. (App. 116.) The District Court limited the scope of any such examination to only BK Properties on the basis discovery as to Herslip Construction and Magic Management was subject to an automatic stay in the bankruptcy proceedings. (App. 116.)

5. Appellants' Unsuccessful Collection Attempts

(19.) Appellants have diligently attempted to collect upon their judgments against the judgment debtors in this case. In addition to service of the Rule 69 discovery requests, to which no response has been received from Herslip Construction or Magic Management, the

Ward County Sheriff's office has also been unable to collect upon any of the numerous writs of execution issued at the request of Appellants' counsel. *See* Sheriff's Returns (Docket #'s 534, 535, 536, 537, 542, 543). The only exception has been the Sheriff's levy upon a small amount (\$3,104.11) held in the business checking account of Herslip Construction at Bremer Bank-Minot on May 28, 2010 (prior to June 9 bankruptcy filings). Due to Herslip Construction's filing for bankruptcy, the Sheriff's office deposited said funds with the District Court. Other specific assets Appellants have sought levy upon include a Cadillac Escalade titled in the name of Herslip Construction, and a Certificate of Deposit owned by BK Properties in the amount of \$254,614.68. As evidenced by correspondence from Ken Herslip to Lt. Brent Renaud of the Ward County Sheriff's Office dated July 23, 2010 (Exh. AA) as well as the Sheriff's Return dated August 26, 2010 (Docket #'s 542, 543), when execution upon the certificate was attempted, Herslip contended the "certificate of deposit no longer exists," without further elaboration as to what happened to it. The subject certificate had been listed on BK Properties year-end balance sheet of December 31, 2009. As stated, Appellants have not had an opportunity to depose Herslip to inquire as to the disposition of this sizeable asset.

(20.) With respect to the Cadillac Escalade, Appellants were able to determine substantial equity existed in the vehicle. As evidenced by email correspondence between Appellants' counsel and Lt. Renaud (Exh. BB), arrangements for levy upon the Cadillac had been arranged, however, Herslip Construction's bankruptcy filing prevented the levy. The Cadillac has been sold in the bankruptcy proceedings for an unknown amount. **Appellants have not received a single penny either from the judgment debtors directly, or pursuant to the ongoing bankruptcy proceedings.** Herslip's fraudulent conduct both pre-

and post-Judgment clearly warrant piercing the corporate veil and finding Kenneth Herslip personally liable for judgment debts owed Magic Partnership by Magic Management, Herslip Construction and BK Properties.

ARGUMENT

I. STANDARD OF REVIEW

(21.) The District Court's determination it lacked the authority under applicable law to grant the relief requested by Appellants involves strictly a question of law. This Court reviews questions of law under the de novo standard on the entire record. *Sailer v. Sailer*, 2010 ND 185, ¶ 7, 788 N.W.2d 604.

II. THE DISTRICT COURT HAS THE POWER TO GRANT THE RELIEF REQUESTED BY APPELLANTS IN THIS ACTION

(22.) The District Court misinterpreted Appellants' motion as a request for a new trial under Rule 59, or relief from judgment under Rule 60 of the North Dakota Rules of Civil Procedure. Appellants are not asking for a new trial or reversal of the existing judgment in this action. Instead, Appellants are requesting Ken Herslip, a party to this action, be held personally responsible for the judgment debt of Herslip Construction, Magic Management and BK Properties, and awarding punitive damages due to his personal ongoing fraudulent conduct of transferring debtor assets to other entities in which he and/or his wife have controlling interests, all for the malicious purpose of frustrating Appellants' collection efforts. While Appellants believe sufficient evidence of fraud was presented at trial to justify piercing the corporate veil, Appellants' current motion is based upon additional pre-judgment and post-judgment fraudulent and malicious conduct

by Ken Herslip, through his controlled entities, which was not at issue at the trial, to be considered in conjunction with the prior findings of fraud.

(23.) Appellants had no opportunity to present the pending arguments at the trial in this action. While the District Court previously declined Appellants' request to pierce the corporate veil, and exercised its discretion not to award punitive damages after determining Herslip's fraudulent conduct supported such an award, such determinations were necessarily based solely upon the information available and relevant to the issues then being addressed by the District Court at trial. Asset transfers by the Appellees were simply not relevant at trial in this case. It was not until the liability of the judgment debtors was determined at trial that the issue of fraudulent conveyances became relevant. As discussed below, evidence of pre-judgment and ongoing post-judgment fraudulent conduct by Herslip exists which justifies holding Herslip personally liable for the judgment, and justifying an award of punitive damages against him.

(24.) Appellants are not limited to proceeding under Rules 59 and 60 of the North Dakota Rules of Civil Procedure as illustrated by the fact the North Dakota Supreme Court has previously pierced the corporate veil of judgment debtors based upon fraudulent transfers occurring post-judgment. By way of example, and under very similar circumstances as presented to this Court, in *Axtmann v. Chillemi*, 2007 ND 179, 740 N.W.2d 838, the North Dakota Supreme Court pierced the corporate veil of a corporate judgment debtor, post-judgment, and held the sole shareholder personally liable for the corporation's judgment debt on the basis of post-judgment fraudulent transfers made to another corporation formed by the sole shareholder post-judgment. While a separate lawsuit to pierce the corporate veil was brought in *Axtmann*, such was only

required because the sole shareholder was not a party to the prior lawsuit in which the original judgment was obtained. In other words, a separate lawsuit was required in *Axtmann* for the Court to obtain jurisdiction over the sole shareholder and the newly formed corporation. In the present case, Ken Herslip has always been a party to this action and therefore, there is no need to commence a new lawsuit in order for the District Court to address Appellants' requested relief. Query what purpose, other than delay and waste of resources, would be accomplished by commencement of a separate lawsuit. In fact, considering the extensive factual background of this case of which Judge McLees is already familiar, a significant detriment to the parties would result if the separate lawsuit should be assigned to a different judge.

(25.) Simply stated, Rules 59 and 60 are not designed to address post-judgment fraud by a judgment debtor and are instead designed to address fraud occurring at or prior to trial. Rules 59 and 60 simply have no application to Appellants' motion and there is no need to vacate the existing judgment in this action. Even assuming, *arguendo*, a modification of the existing judgment were necessary to grant Appellants the relief requested, which is denied, the District Court has the equitable power to do so outside of Rules 59 and 60. *See Hamilton v. Hamilton*, 410 N.W.2d 508, 515 (N.D. 1987)(courts have inherent power to grant relief from judgment in equity in the interests of justice when procedural requirements of Rule 60 are not met). The District Court has the power to hold Herslip personally accountable for fraudulent transfers of assets to entities controlled by him and/or his wife in this action.

(26.) In addition to the District Court's inherent power to hold Herslip personally accountable for his fraudulent conduct, North Dakota's Uniform Fraudulent Transfer Act

also provides the District Court with the power to hold Herslip personally liable for assets fraudulently transferred for his own benefit. *See* N.D.C.C. § 13-02.1-08(2)(providing creditors may recover judgment for the value of assets transferred up to the amount of the creditor's claim against the first transferee of the asset or the person for whose benefit the transfer was made or any subsequent transferee); N.D.C.C. § 13-02.1-10 (providing unless displaced by the provisions of the Uniform Fraudulent Transfer Act, the principles of law and equity, including, among others, the law of fraud, supplement their provisions). Herslip has transferred valuable assets belonging to Herslip Construction to other entities in which he and/or his wife have controlling interests. Among these assets are the goodwill of Herslip Construction (*see* post-judgment yellowpages.com advertisement for Herslip Management, LLC, formed post-judgment, asserting Herslip Management, LLC is also known as Herslip Construction, Inc. (Exh. C)), numerous lucrative management agreements Herslip Construction used to be a party to, as well as outright preferential cash transfers to Herslip, his wife, and their controlled entities at a time when Herslip Construction was insolvent and Appellants' claims were known.

III. EVIDENCE PRESENTED SUPPORTS AWARD OF REQUESTED RELIEF

(27.) The standard in deciding whether to pierce the corporate veil of an artificial entity and find its shareholders, members or partners liable is well-settled. Eight separate factors to consider in determining whether to pierce the corporate veil were addressed by the Supreme Court of North Dakota in *Coughlin Construction Co., Inc. v. Nu-Tech Industries, Inc.*:

“[I]nsufficient capitalization for the purposes of the corporate undertaking, failure to observe corporate formalities, nonpayment of dividends, insolvency of the debtor corporation at the time of the transaction in question, siphoning of funds by the dominant shareholder, nonfunctioning of other officers and directors, absence of corporate records, and the existence of the corporation as merely a façade for individual dealings.”

755 N.W.2d 867, 873 (N.D. 2008); *See also Hilzendager v. Skwarok, et.al.*, 335 N.W.2d 768, 774 (N.D. 1983) (internal citations omitted). The Court in *Hilzendager* also stated “when the notion of legal entity is used to defeat public convenience...**protect fraud**, or defend crime, the law will regard the corporation as an association of persons.” 335 N.W.2d 768, 774 (emphasis added).

(28.) Further, in *Jablonsky v. Klemm*, the Court added that “an element of injustice, inequity or fundamental unfairness must be present” in order for the Court to pierce the corporate veil and find an individual personally liable. 377 N.W.2d 560, 564 (N.D. 1985).

(29.) The Fourth Circuit Court of Appeals, in applying the same factors listed above, appropriately noted that unfairness may be shown by demonstrating any number of the above-referenced factors, “which, *all fitting into a picture of basic unfairness*, has been regarded fairly uniformly to constitute a basis for an imposition of individual liability under the doctrine [of piercing the corporate veil]”. *Id.* (emphasis added).

A. **The District Court Previously Determined Appellees Engaged In Fraudulent Conduct With Respect To The Handling Of Entrusted Property Belonging To Magic Partnership, Justifying Piercing The Corporate Veil**

(30.) In paragraph 9 of this Court’s March 2010 Opinion, the District Court addressed the Appellants’ request for an award of punitive damages against the Herslip Defendants on the basis of fraud. After discussing the elements required to prove fraud, the District

Court determined “there is little question that the evidence in relation to the Herslip Defendants’ handling of the excess lot plus transaction would support a claim for exemplary (punitive) damages” Although the District Court exercised its discretion in not ultimately awarding Appellants punitive damages, the District Court none-the-less determined the Appellees had committed fraud relative to the excess lot plus transaction. This alone, without more, is sufficient to hold Ken Herslip, the officer, director and owner of Magic Management, Herslip Construction and BK Properties, personally liable for the judgment held by Magic Partnership. Such a result is only just under the circumstances.

(31.) As explained by this Court in *Axtmann v. Chillemi*, 2007 ND 179, 740 N.W.2d 838 in holding the officers of a corporation personally liable for the judgment entered against the corporation found to have committed fraud:

The officers and directors of a corporation generally are not liable for the ordinary debts of a corporation. Organizing a corporation to avoid personal liability is a legitimate goal and is one of the primary advantages of doing business in the corporate form. . . . [H]owever, this Court [has] also said that when the notion of a corporate entity is used to defeat public convenience, **justify wrong, protect fraud**, or defend crime, the law regards the corporation as an association of persons.

* * *

Proof of fraud is not a necessary prerequisite for disregarding the corporate entity, but an element of injustice, inequity, or fundamental unfairness must be present before a court may properly pierce the corporate veil and that element of unfairness may be established by the showing of a number of requisite factors for piercing the corporate veil. The essence of the requirement for fairness is that an individual cannot hide from the normal consequences of carefree entrepreneuring by doing so through a corporate shell.

Id. at ¶¶ 12-13 (bold added)(citations omitted). In other words, the limited liability protections generally available to the officers and directors of a corporation are not

available to protect fraud or other wrongful conduct. Officers and directors of corporations are generally held personally liable for their wrongful/fraudulent conduct and North Dakota case law consistently establishes where fraud is present, the corporate veil will be pierced. *See e.g. Axtmann v. Chillemi*, 2007 ND 179 (piercing corporate veil on basis of fraud); *Intercept Corp. v. Calima Financial, LLC*, 2007 ND 180, 741 N.W.2d 209 (piercing corporate veil of limited liability company on basis of fraud); *Jablonsky v. Klemm*, 377 N.W.2d 560 (1985)(piercing corporate veil due to undercapitalization, insolvency, and siphoning off of funds).

(32.) While the case law clearly indicates fraud is not required to pierce the corporate veil, in the present case, Magic Partnership's judgment against Magic Management, Herslip Construction and BK Properties is based upon fraudulent conduct on the part of Kenneth Herslip personally. Herslip, through these artificial entities, defrauded Appellants by secretly transferring entrusted property owned by Magic Partnership to an entity (BK Properties) he secretly created for this purpose, and then, within one month of transferring title to BK Properties, said entity sold the entrusted property to a third-party for a substantial gain, all to Herslip's private benefit and to the detriment of Magic Partnership and its limited partners. Herslip is using these artificial entities to protect his personal wrongdoing and to protect fraud. There can be no question the plaintiffs in this derivative action, limited partners who invested significant portions of their personal assets in Herslip's schemes, have not been treated fairly by Herslip and that he is using corporate shells to avoid paying the judgment Appellants obtained against the Herslip controlled entities. His additional actions during the litigation and post-judgment of discontinuing the operations of Appellee Herslip Construction and allowing it to wither

away without any attempt to preserve its value, either through its sale as a going concern, by continuing its operations, or by otherwise failing to provide for payment of its debts, further demonstrates his use of these artificial entities to further defraud Magic Partnership and its limited partners. Herslip also continues to stone-wall the Appellants by failing to produce requested information relevant to Appellants' collection efforts. This ongoing wrongful conduct by Herslip materially prejudices Magic Partnership and its limited partners. The judgments owed by the judgment debtors to Magic Partnership are substantial. Appellees' wrongful conduct should not be condoned and Ken Herslip should be held personally liable to Magic Partnership for the judgment against Magic Management, Herslip Construction and BK Properties in the interests of justice, equity and consistent with fundamental fairness.

B. During The Litigation And Post-Judgment In This Case, Appellees Engaged In Additional Fraudulent Conduct By Intentionally Diminishing The Assets Of The Judgment Debtors For The Purpose Of Defrauding Magic Partnership And Its Limited Partners

(33.) In addition to the discussion of fraud as a basis for piercing the corporate veil, this Court in *Axtmann* also discussed lack of capitalization of a corporation as justification for piercing the corporate veil, as follows:

This Court has also recognized that the attitude toward piercing the corporate veil is more flexible in tort than in contract, because the creditor has an element of choice inherent in a voluntary contractual relationship where the ordinary tort case forces the debtor-creditor relationship upon the creditor by the occurrence of an unexpected tort. In tort cases, particular significance is placed on whether a corporation is undercapitalized, which involves an added public policy consideration of whether individuals may transfer a risk of loss to the public in the name of a corporation that is marginally financed. In *Jablonsky v. Klemm*, 377 N.W.2d 560, 566 (N.D. 1985)] this Court explained the obligation for adequate capitalization:

[t]he obligation to provide adequate [risk] capital begins with incorporation and is a continuing obligation thereafter * * * during the

corporation's operations. In *Briggs Transp. Co. v. Starr Sales Co.*, 262 N.W.2d 805, 810 (Iowa 1978) the court stated:

If a corporation is organized and carries on business without substantial capital in such a way that the corporation is likely to have no sufficient assets available to meet its debts, it is inequitable that shareholders should set up such a flimsy organization to escape personal liability. The attempt to do corporate business without providing any sufficient basis of financial responsibility to creditors is an abuse of the separate entity and will be ineffectual to exempt the shareholders from corporate debts. It is coming to be recognized as the policy of the law that shareholders should in good faith put at the risk of the business unencumbered capital reasonably adequate for its prospective liabilities. If capital is illusory or trifling compared with the business to be done and the risks of loss, this is a ground for denying the separate entity privilege.

Axtmann v. Chillemi, 2007 ND at ¶ 14. In the present case, in 2008, during the course of litigation in this matter, Herslip, as an officer, director and controlling shareholder, made the decision to discontinue the operations of Herslip Construction. His decision to do so was based upon malice and his intention not to pay Magic Partnership for sums then claimed due the limited partnership, sums which he had reason to believe would be or were likely to be awarded against the Appellees.

(34.) Counsel for Appellants first advised Herslip of Appellants' intention to commence suit in this action in October of 2006. See correspondence from Randall Bakke to Ken Herslip dated October 6, 2006 (Exh. CC). The action was actually commenced in January of 2007. According to the financial statements and/or tax returns of Herslip Construction (Exh. DD), Herslip Construction's gross income, net earnings, total assets and total equity (assets minus liabilities) have changed as follows since 2006:

<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
-------------	-------------	-------------	-------------	-------------

Total Income	1,957,724	757,839	2,375,664*	350,990*
	102,546*			
Net Earnings	337,997	(148,812)	195,744	**
Total assets	804,851	271,975	400,014	**
	359,573*			
Total Equity	460,464	41,851	220,386	**
	(212,876)*			

* Per Chapter 7 Statement of Financial Affairs at ¶ 1 (Exh. E).

** Herslip Construction's 2009 financial statements have been requested in discovery but inappropriately not produced by Herslip or his counsel.

(35.) When Herslip made the decision to discontinue operations of Herslip Construction, Herslip Construction had a track record of sufficient earnings to cover its debt to Magic Partnership. Herslip Construction had also been in operation for roughly fourteen years (incorporated in December of 1994) and had developed significant goodwill value. Out of spite, Herslip simply chose to sink the ship to prevent any recovery by Magic Partnership on its judgment. Herslip made no effort to sell the company, or to hire someone else to manage it for him. No effort was made to preserve its value and to make sure it was adequately capitalized in light of the corporation's anticipated liabilities. Instead, he did the exact opposite by taking actions to diminish the capital of the corporation for the express purpose of defrauding Magic Partnership and its limited partners. As disclosed by Herslip in his Statement of Financial Affairs relative to

Herslip Construction's bankruptcy petition² at paragraph 3, Herslip reduced the available assets in the corporation and gave himself as an alleged creditor of Herslip Construction favorable treatment by paying alleged loans owed to himself, his wife Janelle, and entities controlled by them during the course of this case. The bankruptcy disclosures only disclose payments made within one year of the petitions filing (in other words, additional preferential transfers during the course of this litigation may have been made for which information has not yet been provided in response to Appellants' post-judgment discovery requests), summarized as follows:

<u>Payee</u> Remaining	<u>Date of payment</u>	<u>Amt. Paid</u>	<u>Owed</u>
Ken and Janelle	1/22/10 – loan repayment	\$5,322.58	\$0.00
Janelle	7/10/09 – loan repayment	2,700.00	0.00
Wings of Minot, ND (controlled by Ken And Janelle)	Various For trade payables	1,501.34	0.00
GHW Enterprises, LLC (owned by Ken And Janelle)	Various - for rent	31,998.38	0.00
Herslip Restaurants LLC (controlled by Ken and And Janelle)	Various	\$489.74	0.00
Herslip Restaurants LLC	8/19/09 – loan repayment	9,789.43	0.00

² In 1992, Ken and Janelle Herslip obtained a Chapter 7 discharge in bankruptcy (Exh. JJ) , and filed for bankruptcy for Jennings Lumber, a company in which Herslip had an ownership interest.

Ken Herslip	7/31/09 – loan repayment	\$1,000.00	0.00
Ken Herslip	12/21/09 – reimbursement	34.80	0.00
Total		\$ 52,836.27	

These disclosures establish Ken Herslip gave himself and his wife, and their controlled entities preferential treatment over Magic Partnership by paying them off, in full, thereby contributing to the corporation's current insolvency (negative equity). Again, these disclosures only relate to transactions occurring within one year prior to Herslip Construction's filing of its bankruptcy petition and there may have been numerous additional preferential transfers not yet disclosed by the Appellees, despite Appellants' outstanding discovery requests for such information.

(36.) Herslip's bankruptcy petition also discloses Herslip Construction paid Ken Herslip \$59,470.80 and his wife Janelle Herslip \$31,823.04 in salary for the year prior to filing the bankruptcy petition. Recall that Herslip stated during the creditors meeting he essentially discontinued the operations of Herslip Construction on or about July of 2008, well over one year prior to the filing of the bankruptcy petition. Query why he would continue to pay himself and his wife over \$90,000 per year for a corporation which was no longer actively engaged in business. Herslips were simply draining the corporation dry to prevent any collection by Appellants. Failing to take any action to preserve the value of Herslip Construction, including its goodwill value, either by continuing operations on his own or through hired management, or through a sale for its fair market value, or by having the corporation pay alleged debts owed Ken and his wife or entities they control before payment of Magic Partnership, constituted malicious waste for the sole purpose of defrauding Appellants.

(37.) Appellants' respectfully submit the intentional diminishment of capital in a corporation is much more egregious than a failure to contribute adequate capital to a corporation. As stated in *Axtmann*, "the attitude toward piercing the corporate veil is more flexible in tort than in contract." The pre and post judgment fraud committed by the Herslip Defendants is/was a tort forced upon Magic Partnership and its limited partners. Piercing the corporate veil to hold Ken Herslip personally liable for the judgments against Magic Management, Herslip Construction and BK Properties is further justified on this basis.

C. **Appellees Have Transferred Business Opportunities Which Would Have Benefited The Judgment Debtors To Other Entities In Which Ken Herslip Or His Spouse Have Controlling Interests, All For The Purpose Of Defrauding Magic Partnership And Its Limited Partners**

(38.) Despite its name, Herslip Construction's activities were not limited to construction. The corporation received significant income from managing restaurants and other properties owned by entities controlled by Ken Herslip and/or his spouse, Janelle Herslip, including, but not limited to Herslip Restaurants, BK Properties, LLC, GHW Enterprises, LLC, LaMore Restaurants, Grand Restaurants, LLC, and Wings of Minot ND, LLC. Herslip Construction's management/administrative fee income in this regard was as follows since 2006:

<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
123,497	178,000	245,714	**

** Herslip Construction's 2009 financial statements have been requested in discovery but wrongly not produced by Herslip or his legal counsel.

(39.) It is believed these entities continue to receive managerial/administrative services, only now through other Herslip controlled entities, including Herslip Management, LLC.

In other words, Herslip has transferred these valuable business opportunities previously belonging to Herslip Construction to other entities he controls for the purpose of frustrating Magic Partnership's ability to collect on its judgment.

(40.) Since Herslip made the decision to discontinue the operations of Herslip Construction in 2008, and discontinued the operations of Magic Management, Herslip has continued business as usual, albeit through other artificial entities in which he and/or his spouse have controlling interests. By way of example, prior to 2008, Herslip would utilize Herslip Construction to build restaurants for other entities in which he had an interest. The Minot Denny's, owned and operated by Magic Partnership, is one example where Herslip Construction built the restaurant later managed by Magic Management. Herslip continues to build and manage restaurants post 2008, albeit through other entities in which he and/or his spouse have controlling interests. On or about July of 2010, Herslip opened a new Denny's restaurant in Great Falls, Montana through an entity called Herslip Restaurants. *See* internet article entitled "Denny's Restaurant to Open in Great Falls this Weekend" (Exh. EE). On or about September 20, 2010, Herslip opened a new Denny's restaurant in Sioux Falls, South Dakota through an entity called LaMore Restaurant Group, LLC. *See* Press Release from Denny's Corporation dated September 20, 2010 (Exh. F). Herslip also owns GHW Enterprises, LLC, a North Dakota limited liability company, which has a stated business purpose of rental and development. *See* North Dakota Secretary of State Corporation Details for GHW Enterprises, LLC (Exh. FF). GHW is characterized online as a nonresidential construction company. *See* Company Profile for GHW Enterprises, LLC available at Manta.com at Business Categories (Exh. GG). As discussed in the facts above, one month after the District

Court awarded judgment to Appellants, Herslip also opened a new North Dakota business on May 9, 2010, namely Herslip Management, LLC. *See* North Dakota Secretary of State Corporate Details for Herslip Management, LLC. (Exh. A). A company profile of Herslip Management, LLC published by Manta.com (Exh. B) provides the following description of Herslip Management, LLC (formed after judgment entered in this case):

Herslip Management, LLC is a private company categorized under Construction, Repair, and Dismantling Services and located in Minot, ND. Current estimates show this company has an annual revenue of 220,000 and employs a staff of approximately 5.

Business Categories

Construction, repair, and dismantling services in Minot, ND
Oil/Gas Field Services
Oil and Gas Pipeline and Related Structures Construction
View newly formed U.S. businesses

Company Contacts

Kenneth Herslip

(Exh. B). In addition, the following information regarding Herslip Management, LLC is available at Yellowpages.com (Exh. C):

Categories

General Contractors, Building Contractors-Commercial & Industrial, Home Builders, Altering & Remodeling Contractors, Home Repair & Maintenance, Air Conditioning Contractors & Systems, Heating Contractors & Specialties

AKA

Herslip Management, Llc, Herslip Construction, Inc.

(Exh. C). This is conclusive proof of blatant fraud. Herslip Management, LLC was formed one month after Appellants obtained their judgment in this case and performs essentially identical services as were previously being performed by Herslip Construction, Inc. The alleged basis Ken Herslip gives for discontinuing the operations of Herslip Construction, Inc. is he has been sick. If he was too sick to continue the

construction and related operations of Herslip Construction, Inc., query how he is able to continue those identical services through Herslip Management, LLC. As indicated on Manta.com (Exh. B), Herslip Management, LLC's estimated annual revenues are \$220,000. That estimate is likely very low considering the company has only been in existence since May of 2010. Incredibly, and perhaps the most conclusive evidence of fraud, is the fact Herslip Management, LLC's yellow pages advertisement (Exh. C) indicates it is also known as Herslip Construction, Inc., obviously to divert the goodwill of Herslip Construction, Inc. to Herslip Management, LLC. Herslip continues to engage in construction and managerial/administrative services, previously performed by Herslip Construction, albeit through other artificial entities.

(41.) As discussed in the preceding paragraph, as the officer, director and owner of Herslip Construction, Herslip had an obligation to make sure Herslip Construction was adequately capitalized to meet its current and anticipated liabilities. The claims of Magic Partnership were anticipated liabilities of Herslip Construction at the time Herslip made the decision to wind up Herslip Construction. In fact, the decision to wind up Herslip Construction was made precisely to frustrate Magic Partnership's ability to collect on its claims. This is wrongful conduct which should not be condoned by the Court and justifies holding Ken Herslip and his wife Janelle Herslip, co-owners of Herslip Construction, personally liable to Magic Partnership for the judgment debts of Magic Partnership, Herslip Construction and BK Properties.

D. Herslips' Fraudulent And Malicious Conduct Justifies An Award Of Punitive Damages

(42.) Herslips' wrongful conduct discussed herein is also more than sufficient justification for imposition of punitive damages under N.D.C.C. § 32-03.2-11, which provides, in relevant part, as follows:

1. In any action for the breach of an obligation not arising from contract, when the defendant has been guilty by clear and convincing evidence of oppression, **fraud, or actual malice**, the court or jury, in addition to the actual damages, may give damages for the sake of example and by way of punishing the defendant.

(bold added). As discussed, during the creditors meetings held in the bankruptcy proceedings, Herslip testified he would not have filed for bankruptcy had it not been for the Appellants' judgment in this case. *See* audio recording of bankruptcy creditors meeting (Exh D). The evidence discussed in this brief, alone, constitutes clear and convincing evidence of fraud and/or actual malice on the part of the Herslips justifying an award of punitive damages.

(43.) Considering the Appellants' judgment against Herslip was based upon fraud, and considering Herslip's continued fraud during the litigation and continuing into the collection proceedings (ongoing over a long period of time), and further considering the substantial economic hardship Herslip has caused Magic Partnership by his fraudulent conduct, Appellants respectfully submit the maximum allowable punitive damage award of \$250,000 (N.D.C.C. § 32-03.2-11(4)) is in order to have the desired effect of deterring similar wrongful conduct by Herslip, and others, in the future. As discussed, Herslip and his wife have controlling interests in numerous sizeable business entities, including in the restaurant and construction industries. Herslip has, and continues to, profit from his ongoing fraudulent conduct in an amount well in excess of \$250,000 (first year estimated

annual income of Herslip Management LLC of \$220,000 alone). It will take a sizeable award to have the desired punitive and deterrent effect.

E. Herslip Has Wrongfully And Intentionally Refused To Comply With Plaintiffs' Post-Judgment Discovery Requests With Respect To Herslip Construction, Magic Management, And Other Entities In Which Herslip And/Or His Spouse Have Controlling Interests, All Of Which Are Directly Relevant To The Issues Of Fraudulent Transfers, Capitalization And Waste

(44.) As discussed in detail in paragraph II(B)(3) above, on May 3, 2010, Appellants' counsel served post-judgment discovery requests upon the Appellee judgment debtors pursuant to Rule 69. While BK Properties responded to the discovery requests by revealing all of its assets were fully leveraged, Herslip Construction and Magic Management objected to the discovery requests on the basis they were filing Chapter 7 bankruptcy petitions. They each filed for bankruptcy on June 9, 2010. Although corporate entities cannot obtain a discharge of debts in bankruptcy, and despite the fact Appellants' have obtained orders from the bankruptcy court authorizing discovery from Herslip Construction and Magic Management, Herslip Construction and Magic Management have inappropriately asserted they are not required to comply with the discovery requests due to the pending bankruptcy proceeding.

(45.) As discussed above in paragraph II(B)(4), beginning on July 20, 2010, counsel for Appellants began requesting available dates for the deposition of Ken Herslip for purposes of post-judgment collection. Ultimately, a deposition date of December 1, 2010 was scheduled. Due to alleged health issues, Appellants agreed to post-pone Mr. Herslip's deposition. An amended deposition notice (Exh. W) was served to conduct Mr. Herslip's deposition on December 21, 2010. Ken Herslip's counsel again advised Mr.

Herslip will not be attending the December 21 deposition due to alleged ongoing health issues.

(46.) Ken Herslip is intentionally refusing to produce any information relative to Herslip Construction, Magic Management and other entities in which he or his spouse have controlling interests. He continues to “stone-wall” the limited partners of Magic Partnership, just as he did for years – leading to the underlying litigation in this case. Appellants clearly have a right to question Mr. Herslip and to obtain discovery answers and documents regarding his management of the judgment debtors, his decision to discontinue their operations, the operations of other entities in which he or his spouse have controlling interests, as well as business opportunities, assets and liabilities transferred between them.

F. Other Bases For Piercing The Corporate Veil

(47.) As stated, Appellees have wrongfully refused to comply with Appellants’ post-judgment discovery requests or otherwise produce information directly relevant to the issue of transfers/waste committed for purposes of defrauding its judgment creditor, Magic Partnership. Herslip has evaded Appellants’ attempts to depose him regarding these issues on the basis of alleged health issues he is experiencing. In the event this Court is not satisfied the information presented is sufficient to justify holding Ken and Janelle Herslip (or Ken Herslip alone) personally liable for the judgment debts owed Magic Partnership by Magic Management, Herslip Construction and BK Properties, Appellants respectfully request remand to the District Court with direction to compel Ken Herslip’s compliance with Appellants’ Rule 69 discovery requests and compelling his attendance at a deposition for questioning regarding not only the judgment debtors, but

also any and all entities in which either Ken or Janelle have had a controlling interest since October of 2006, so Appellants may submit a supplemental brief in support of their motion with additional evidence in support thereof.

IV. CONCLUSION

(48.) For the foregoing reasons, Appellants request the District Court's determination it lacked authority to grant Appellants' requested relief in this action be found in error and the case be remanded to the District Court for determination of the issues presented in *Plaintiffs' Motion to Pierce the Corporate Veil*.

(49.) In the alternative, Appellants request *Plaintiffs' Motion to Pierce the Corporate Veil* be granted and Kenneth Herslip be found personally liable for the judgment debts owed Magic Partnership by Herslip Construction, Inc., Magic 2 x 52 Management, Inc. and BK Properties, LLC. In addition, Appellants request an award of punitive damages against Kenneth Herslip on the basis of clear and convincing evidence of fraud and/or actual malice. In the further alternative, Appellants request an order compelling Ken Herslip's compliance with Appellants' outstanding Rule 69 discovery requests and further compelling his attendance at a deposition for questioning regarding not only the judgment debtors, but also any and all entities in which either Ken or Janelle Herslip have had a controlling interest since October of 2006 and permitting Appellants an opportunity to submit a supplemental brief in support of this motion thereafter.

Dated this 14th day of June, 2011.

SMITH BAKKE PORSBORG
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CERTIFICATE OF COMPLIANCE

(50.) The undersigned, as attorneys for the Plaintiffs/Appellants in the above matter, and as the authors of the above brief, hereby certify, in compliance with Rule 32(a) of the North Dakota Rules of Appellate Procedure, that the above brief was prepared with proportional type face and that the total number of words in the above brief, excluding words in the table of contents, table of authorities, signature block, certificate of service and certificate of compliance totals 10,352.

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(51.) I hereby certify that a true and correct copy of the foregoing Appellants' Brief was on the 14th day of June, 2011, emailed to the following:

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Appellants' Brief