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STATE OF NORTH DAKOTA

Case No.: 20140188

District Court No. 09-2012-CV-02902

IN THE SUPREME COURT

STATE OF NORTH DAKOTA

Sterling Development Group Three, LLC,
Sterling Development Group Eight, LLC,

Plaintiffs/Appellants,

v.

James D. Carlson,

Defendant/Appellee.

APPELLANTS' BRIEF and Addendum

DISTRICT COURT OF THE EAST CENTRAL JUDICIAL DISTRICT

THE HONORABLE STEVEN L. MARQUART PRESIDING

DISTRICT COURT NO. 09-2012-CV-02902

APPEAL FROM THE MEMORANDUM OPINIONS DATED MARCH 11, 2014 AND JUNE 25, 2014

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I. STATEMENT OF THE ISSUES

[¶1] Issue 1: The lower court erred in finding that the unambiguous Sterling Development Group Three, LLC and Sterling Development Group Eight, LLC Leases were contractually altered without consent, resulting in exoneration of James D. Carlson's Personal Guaranty obligations.

[¶2] Issue 2: The lower court abused its discretion by awarding costs in excess of that provided for by statute.

[¶3] Issue 3: The lower court abused its discretion by awarding costs for expert witness fees when the parties agreed to bifurcate the damages portion of the trial.

II. STATEMENT OF THE CASE

[¶4] Sterling Development Group Three, LLC ("Sterling Three") and Sterling Development Group Eight, LLC, ("Sterling Eight") commenced this action by service of the Summons and Complaint. Appendix page 10. The Complaint seeks to recover from James D. Carlson ("Carlson") on the personal guaranty obligations given in favor of Sterling Three and Sterling Eight for property in East Grand Forks, Minnesota. Appendix page 10. Sterling Three and Sterling Eight moved for summary judgment on August 30, 2013. Carlson conceded that the Personal Guaranty obligations are valid and enforceable as against James D. Carlson. However, Carlson argued that the Guaranty obligations are exonerated by alleged changes to the leases. The Court denied Sterling Three and Sterling Eight's motion for summary judgment, finding "a genuine issue of material fact exists as to whether Carlson consented to the modifications." Appendix page 285. The Court further stated that "[t]he parties do not dispute that changes occurred" to the leases Carlson guaranteed, and "the Court is satisfied that PRACS's obligations were altered." In fact, Sterling Three and Sterling Eight continued to dispute that alterations occurred.

[¶5] At the commencement of the bench trial the lower court advised the parties that it was reconsidering its prior order and would accept evidence on the issue of alteration as well as consent. The case was tried to the court on February 3 and 4, 2014. Following post-trial briefing, the lower court entered an order finding in Carlson's favor, and awarded costs to the prevailing party. Appendix page 487.

[¶6] Defendant filed its verified statement of costs, seeking costs in the amount of $11,899.97. Sterling Three and Sterling Eight objected to the cost judgment. Carlson conceded that travel costs of counsel are not permitted, but persisted in the claim for the remaining costs. The lower court heard Sterling Three and Sterling Eight's objection to costs on June 24, 2014, and entered an order on June 25, 2014 awarding Carlson costs in the amount of $7,069.30. Appendix page 495. An amended judgment was entered on July 1, 2014. Appendix page 499. Sterling Three and Sterling Eight appeal from both orders.

III. RELEVANT FACTS

[¶7] On November 9, 1999, Sterling Three entered into a 15-year lease agreement with PRACS ("Sterling Three Lease") for property located at 625 DeMers Avenue in East Grand Forks, MN. Appendix page 84. PRACS was owned and operated by James D. Carlson, and he signed the lease as President of PRACS. Simultaneous to executing the Sterling Three Lease, Carlson signed a Personal Guaranty for the Sterling Three building up to $2,000,000. Appendix page 142. The Sterling Three Lease was amended on April 14, 2004, to address remodeling. Appendix page 79. Carlson confirmed his Guaranty obligation. Appendix page 79.

[¶8] PRACS continued to expand its operations in East Grand Forks, MN. PRACS entered into another lease on April 14, 2004 with Sterling Eight, a separate entity from Sterling Three, for a separate building adjacent to the Sterling Three property ("Sterling Eight Lease").

Appendix page 109. The Sterling Eight Lease runs simultaneously with the Sterling Three Lease. Appendix page 79. Carlson signed a Personal Guaranty to Sterling Eight up to $2,000,000. Appendix page 145.

[¶9] Sterling Three and Sterling Eight built the buildings in East Grand Forks, MN to PRACS' design specifications at considerable cost. Appendix page 79. Carlson actively participated in the "build out" of these properties. Deposition of James D. Carlson, pages 26-27, lines 22-25, 1-4 (Docket #57). Carlson also participated in several meetings discussing the terms of the Sterling Three and Sterling Eight Leases. Carlson knew and understood that as a condition of entering into the "build out" leases, Sterling Three and Sterling Eight required a Personal Guaranty from him. Deposition of James D. Carlson, page 32, lines 11-16 (objection omitted) (Docket # 57).

[¶10] Carlson's obligation to pay Sterling Three and Sterling Eight was contingent only on the tenant's failure to pay rent. The tenant defaulted in March 2012. Sterling Three and Sterling Eight delivered Notice of Default to Carlson and demanded payment pursuant to the two Personal Guarantees.

[¶11] In 2006 Carlson entered into a Stock Purchase Agreement for the sale of PRACS to Cetero Contract Research. Appendix page 222. Pursuant to the terms of the Stock Purchase Agreement, Carlson requested Sterling Three and Sterling Eight sign Landlord Consent and Estoppel Certificates, acknowledging that there was a change in ownership of PRACS. Appendix paged 149 & 181. There is no dispute that these documents did not release Carlson from the personal guarantees. Further, the Stock Purchase Agreement identified Carlson's personal guaranty obligations, and required the purchaser to obtain releases. Appendix 281. No release of the Sterling Three or Sterling Eight Lease was ever secured.

[¶12] Carlson argued that his personal guaranty obligations to Sterling Three and Sterling Eight are exonerated due to alterations to the lease terms occurring after the sale of his interest in PRACS. Specifically, Carlson alleged Sterling Three and Sterling Eight agreed to a change in the lease terms pertaining to janitorial services, the calculation of the Consumer Price Index, and payment of the real estate taxes. The lower court found that alterations occurred without Carlson's consent. Sterling Three and Sterling Eight respectfully assert that the lower court erred as a matter of law.

IV. STANDARD OF REVIEW

[¶13] The standard of review of a written contract:

> Written contracts are construed to give effect to the parties' mutual intention when the contract was formed, and if possible, we look to the writing alone to determine the parties' intent. The interpretation of a written contract is a question of law, if the parties' intent can be determined from the language of the writing alone. Whether a written contract is ambiguous is a question of law, which we review independently. A written contract is ambiguous if rational arguments can be made for different interpretations. If a written contract is ambiguous, extrinsic evidence may be considered to determine the parties' intent, and the terms of the contract and the parties' intent are questions of fact.

Doeden v. Stubstad, 2008 ND 165, ¶ 14, 755 N.W.2d 859 (citations omitted).

[¶14] The North Dakota Supreme Court recently set forth the standard for the interpretation of a statute:

> The interpretation and application of a statute is a question of law, which is fully reviewable on appeal. Johnson v. Taliaferro, 2011 ND 34, ¶ 9, 793 N.W.2d 804. We have said: This Court's primary objective in interpreting a statute is to ascertain legislative intent. Baukol Builders, Inc. v. County of Grand Forks, 2008 ND 116, ¶ 22, 751 N.W.2d 191. Words of a statute are given their plain, ordinary, and commonly understood meaning unless a contrary intention plainly appears. N.D.C.C. § 1-02-02. Statutes are construed as a whole and are harmonized to give meaning to related provisions. N.D.C.C. § 1-02-07. If the language of a statute is clear and unambiguous, the letter of [the statute] is not to be disregarded under the pretext of pursuing its spirit. N.D.C.C. § 1-02-05. If the language of a statute is ambiguous, however, a court may resort to extrinsic aids to interpret the statute. N.D.C.C. § 1-02-39. Statutes must be construed to avoid absurd and ludicrous results. Stutsman County v. State Historical Soc'y, 371 N.W.2d 321, 325 (N.D. 1985). See N.D.C.C. § 1-02-38(3) and (4). We construe statutes in a practical manner, and we consider the context of statutes and the

> purpose for which they were enacted. McDowell v. Gillie, 2001 ND 91, ¶ 11, 626 N.W.2d 666.

Larson v. Norheim, 2013 ND 60, ¶ 9,830 N.W.2d 85 (citing Bragg v. Burlington Res. Oil and Gas Co. LP, 2009 ND 33, ¶ 8, 763 N.W.2d 481 (quotations omitted)).

[¶15] The standard of review to Appellant's appeal of the cost judgment is found in N.D.C.C. § 28-26-10:

> In actions other than those specified in sections 28-26-07, 28-26-08, and 28-26-09, costs may be allowed for or against either party in the discretion of the court. In all actions, when there are several defendants not united in interest and making separate defenses by separate answers and the plaintiff fails to recover judgment against all, the court may award costs to such of the defendants as have judgment in their favor.

V. LAW AND ARGUMENT

[¶16] A guaranty is "[A] promise to answer for the debt, default, or miscarriage of another person." N.D.C. C. §22-01-01(2). The guaranty is a direct liability:

> The contract of a guarantor is his own separate contract. It is in the nature of a warranty by him that the thing guaranteed to be done by the principal shall be done, and not merely an engagement jointly with the principal to do the thing… (Citations omitted.) A liability such as this, although it may result in requiring a guarantor to pay the note, is not predicated upon 'the terms of the instrument,' but upon a contract entirely separate and distinct.

Bank of Kirkwood Plaza v. Mueller, 294 N.W.2d 640, 643 (N. D. 1980) (quoting Northern State Bank v. Bellamy, 19 N.D. 509, 125 N.W. 888, 890 (1910)).

[¶17] A guaranty is a contract, the interpretation and construction of which are matters of law for the court. See Sorlie v. Ness, 323 N.W.2d 841, 844 (N.D. 1982). A contract should be interpreted so as to give effect to the mutual intentions of the parties "at that time of contracting," and "ascertained from the writing alone if possible." N.D.C.C. §§ 9-07-03, 9-07-04.

[¶18] Guaranty obligations are exonerated pursuant to N.D.C.C. § 22-01-15 if the original obligations of the principal are altered without the guarantor's consent. This section provides:

> A guarantor is exonerated, except insofar as the guarantor may be indemnified by the principal, if, by any act of the creditor without the consent of the guarantor:
>
> 1. The original obligation of the principal is altered in any respect; or
>
> 2. The remedies or rights of the creditor against the principal in respect thereto are impaired or suspended in any manner.

N.D.C.C. §22-01-15.

[¶19] In Ag Services of America, Inc. v. Midwest Investment Limited, 1998 ND 189, ¶17, 585 N.W. 2d 571, the court held that the original obligation of the principal was not altered, and the guarantor was not exonerated. In so doing, the court determined that "the alteration of a contract 'is a process wherein the parties make [a] change in the provisions of a contract.'" Id. at ¶10 (quoting Black's Law Dictionary 71 (5th ed. 1979) (Biteler's Tower Serv., Inc. v. Guderian, 466 N.W.2d 141, 143 (N.D. 1991)). The court recognized that, "A proposed change which never becomes effective will not release a guarantor." Id. (citing 38A C.J.S. Guaranty § 86 (1996)).

[¶20] Further, in Ag Services, the Supreme Court recognized that in order to exonerate a guarantor, an alteration of the original obligation must meet the essentials of a contract. Id at ¶11 (citing Thurber v. Fisher, 12 P.2d 481, 482 (Cal.App. 1932)). This Court's footnote to its citation of Thurber v. Fisher, 12 P.2d 481, 482 (Cal.App. 1932) is particularly instructive for purposes of determining whether or not an alteration has occurred. Id. n.1. This Court recognized that N.D.C.C. §22-01-15 was derived from §1551 of the Field Code proposed for New York in 1865, as was California Civil Code §2819. Id. Following this derivation, the court found that "California court decisions construing the Field Code section, while not binding, are entitled to respectful consideration, and may be 'persuasive and should not be ignored.'" Id. (citing Glatt v. Bank of Kirkwood Plaza, 383 N.W.2d 473, 477 n.4 (N.D. 1986), quoting Becker v. Becker, 262 N.W.2d 478, 483 (N.D. 1978)).

[¶21] North Dakota case law is instructive that in order to find an alteration to the obligation of the principal, the essential elements of a contract must be met.

[¶22] The elements of a contract are found in N.D.C.C. § 9-01-02:

> Requisites of contract.
> It is essential to the existence of a contract that there should be:
> 1. Parties capable of contracting;
> 2. The consent of the parties;
> 3. A lawful object; and
> 4. Sufficient cause or consideration.

[¶23] N.D.C.C. § 9-05-01 defines good consideration:

> Any benefit conferred or agreed to be conferred upon the promisor by any other person to which the promisor is not entitled lawfully, or any prejudice suffered or agreed to be suffered by such person, other than such as that person, at the time of consent, is lawfully bound to suffer as an inducement to the promisor, is a good consideration for a promise.

[¶24] Pursuant to N.D.C.C. §9-06-04 the statute of frauds requires contracts for the leasing of real property "for a period longer than one year" and an "agreement that by its terms is not to be performed within the year from the making thereof" be in writing to be valid.

[¶25] A guaranty is only exonerated if the original obligation is altered without the consent of the guarantor. This court in Estate of Murphy, 554 N.W.2d 432, 436 (N.D. 1996) recognized that consent can be implied through the conduct of the parties. Id. (citing Benson County Coop. Credit Union v. Central Livestock Ass'n., 300 N.W.2d 236, 241 (N.D. 1980)). This court further defined implied consent:

> Implied consent is "an inference arising from a course of conduct or relationship [**7] between the parties, in which there is mutual acquiescence or a lack of objection under circumstances signifying assent." Black's Law Dictionary 305 (6th ed. 1990); see also Benson County Coop. Credit Union v. Central Livestock Assn., 300 N.W.2d 236, 241 (N.D. 1980) (under the Uniform Commercial Code, "consent may be shown by implication arising from a course of conduct as well as by express words").

Murphy, 554 N.W. 2d at 436.

[¶26] At issue in this lawsuit are two separate leases, the Sterling Three Lease and the Sterling Eight Lease, as well as two separate and distinct Guaranty obligations. Carlson asserted that "the Sterling Plaintiffs and the tenant, PRACS, altered the leases…." Defendant's Post Trial Brief (Docket #242). Sterling Three and Sterling Eight are separate entities. Sterling Three and Sterling Eight constructed and own separate buildings, both of which were leased by PRACS. The lower court failed to distinguish between the two leases and two guarantees, lumping the alleged changes all together as suggested by Carlson.

[¶27] The lease terms are unambiguous, the interpretation of which is a matter of law. The leases must be construed to give the parties' intent effect. The lower court's opinion contains no analysis or discussion finding that either of the leases are ambiguous or that the alterations satisfy the elements of a contract modification.

Issue 1: The lower court erred in finding that the unambiguous Sterling Development Group Three, LLC and Sterling Development Group Eight, LLC Leases were contractually altered without consent, resulting in exoneration of James D. Carlson's Personal Guaranty obligations.

A. There Was No Contractual Alteration of the Lease Terms Regarding Janitorial Expenses

[¶28] The unambiguous terms of the Sterling Three and Sterling Eight Leases state that the tenant is responsible for the cleaning of the leased space, and payment thereof. Section 3.2.2 of both leases provides that the tenant is responsible for the cleaning in the demised premises:

> 3.2.2 Lessee services and expenses. Lessee shall be responsible for payment of, and shall be responsible for all cleaning for, the demised premises.

Appendix pages 84 & 109 (emphasis added).

[¶29] Sterling Three and Sterling Eight presented evidence that the tenant was directly billed for the cleaning in the tenant's demised premises. Appendix page 294. The annual billing statements contain a separate itemization for the janitorial services in the demised premises—

Janitorial Direct Expense. The CAM is a separate line item, and is not impacted by the cleaning expense allocated to the demised premises. Kevin Bartram testified as to the cleaning arrangements in the Sterling Three and Sterling Eight buildings:

> Q. And Sterling companies hired a cleaning company to clean the common area?
> A. That's correct.
> Q. And that company may have also cleaned the PRACS area?
> A. Correct.

Transcript of Proceedings, February 3, 2014, page 128, lines 20-25.

[¶30] Kevin Bartram further testified:

> Q. But the expense for the janitorial that was a direct bill to Sterling, was a direct bill then to PRACS?
> A. That's correct. The way that bill might change if the tenant, whoever the tenant was, decided they wanted cleaning less frequently or more frequently.
> Q. And if you estimated low, it was made up in payment at the end of the year?
> A. Correct.
> Q. Or if it was high --
> A. Yes. Correct.
> Q. -- it was also given a credit to PRACS then --
> A. Correct.
> Q. -- for the amount that was billed by the janitorial?

Transcript of Proceedings, February 3, 2014, page 130, lines 12-25.

[¶31] Sterling Three contracted with Thur-O-Clean, Inc. to clean the common areas. The property manager also engaged Thur-O-Clean to clean the tenant's demised premises on the tenant's behalf. Sterling Three had no obligation to secure the cleaning services for the PRACS space, but did so as a matter of convenience to PRACS. Thur-O-Clean billed the property manager for the number of hours spent in each of the tenant's demised premises, as well as the common area. Appendix page 364. The property manager passed the expense for demised premises cleaning directly on to PRACS. Appendix page 324. Common area cleaning expenses

were pro-rated for each tenant based on the total area leased, as provided for in the Sterling Three Lease. Margaret Asheim testified that the amount billed Sterling Three and Sterling Eight for the cleaning in the demised premises was "passed through" to the tenant as a separate itemization on the year end statements. The CAM or Common Area Maintenance line item was not affected.

[¶32] In 2008 the tenant sent an email to Sterling Three and Sterling Eight inquiring about the cleaning services. Appendix page 330. The tenant advised:

> We are exploring some different ways in our group to increase efficiencies, and are wondering if we are allowed in our contract to hire janitorial staff as employees rather than contract with an outside service. I know we currently pay for services in CAM's as a pass through, and we are exploring whether we can just pay for the services directly and have personnel on staff instead of having the CAM pass through. We have not made any decisions on anything- we are merely exploring options and know that we would have to ensure we complied with our lease agreement, which is why I am checking.

Appendix page 330 (emphasis added).

[¶33] Sterling Three and Sterling Eight responded:

> I have talked to Kevin Bartram, the owner of the PRACS property in EGF, and he said that it would be fine if you would like to hire your own janitorial services. Please let us know if and when this change would take place so that we can notify the current janitorial service and adjust the CAM prices. The only portion of janitorial that you will still be billed for in CAM will be for a portion of the common areas.

Appendix page 330.

[¶34] Shortly thereafter the cleaning service discontinued cleaning the PRACS' demised space, and the direct billing of the janitorial expense ceased. Appendix pages 312 & 314.

[¶35] The lower court erred when it found that "both the Sterling Three and Sterling Eight leases required Sterling to provide the janitorial service in the PRACS leased spaces and PRACS would be billed for said services by reconciliation of the common are maintenance (CAM) payment to Sterling." Appendix page 487 (emphasis added). The lower court further found that "In June of 2008, Cetero and Sterling Three and Sterling Eight agreed that Cetero could provide

the janitorial services. This, then, would also change the CAM payment to Sterling. This agreement altered the original lease agreements." Appendix page 487. The lower court found, as a matter of law that "When Cetero and Sterling Three and Sterling Eight agreed in June of 2008 that Cetero could now provide the janitorial services, which resulted in a change in the CAM payment to Sterling, this constituted an alteration of the original obligation." Appendix page 487.

[¶36] The cleaning in the PRACS space was not paid in the CAM, but rather as a separate line item in the amount of the bill from the contracted service for each space. The direct janitorial expense was "trued up" at the end of the year to coincide with the amount actually paid on the tenant's behalf. Transcript of Proceedings, February 4, 2014, page 284, lines 13-21.

[¶37] Consequently, after June 2008 the tenant was only billed for its share of common area janitorial in accordance with the Sterling Three Lease terms. Appendix pages 312 & 314.

[¶38] The tenant was ALWAYS responsible for cleaning the demised space, and for payment of the service. The tenant's cleaning of its demised space was in conformance with the unambiguous terms of the Sterling Three and Sterling Eight Leases. When the lessee inquired about the ability to "hire janitorial staff as employees rather than contract with an outside service," to save money, Sterling Three and Sterling Eight had no contractual basis to object. There was no need to ask. No permission was needed. The parties' did not intend to alter their obligations under the lease terms. The actual persons who did the cleaning in the demised premises may have changed, but the tenant remained responsible for the cleaning in its demised space. Carlson signed the Sterling Three and Sterling Eight leases, and therefore consented to their terms. Carlson's Guarantees were not exonerated.

B. The Sterling Three and Sterling Eight Leases Were Not Contractually Altered by the Consumer Price Index Adjustment Made In Conformance with the Contract.

[¶39] The Sterling Three and the Sterling Eight Leases tie the lease rate adjustments to the Consumer Price Index ("CPI"). The Sterling Three Lease provides that the rent will be adjusted every 5 years, and contains these provisions:

> 2.1.1 Lessee shall pay fixed minimum rent in accordance with the following terms: The base rent in years one through fifteen shall be as follows. In the first five years, base rent shall be $14.25 per square foot of actual leased space. The base rent shall be adjusted thereafter in accordance with the consumer price index as defined and described in paragraph 2.1.1.1, below. Said rent shall be paid in equal monthly installments. Based upon the approximate amount of leased square footage of 23,384 square feet, base rent for the first five years would amount to approximately $333,222.00 annually payable in equal monthly installments of $27,768.50.
>
> The base rent in years sixteen through twenty shall be adjusted in accordance with the consumer price index adjustments as defined and described in paragraph 2.1.1.1, below.

Section 2.1.1.1 provides, in relevant part:

> 2.1.1.1. Base Rent Adjustment. At the end of each five years (60 full calendar months) during the term of this lease, on the anniversary of the "Commencement Date" of this lease of each fifth year, the annual base rent for the subsequent five lease years shall be increased by an amount sufficient to provide Lessor, for each five year period during the term of this lease an annual base rent equal to the purchasing power of the annual base rent for the immediately preceding five years.
>
> Computation. Within 30 days after its publication and issuance, by the Bureau of Labor Statistics of the United States Department of Labor, Lessor shall deliver to Lessee, a true copy of the Revised Consumer Price Index-Cities (1967=100) (the Index) for the city of Minneapolis, Minnesota for "all items" for the first full calendar month immediately following the "Commencement Date" ("base month") and for the corresponding month of each fifth lease year thereafter. …
>
> Substitution. If at the time required for the determination of the additional rent, the Index is no longer published or issued, or either the Lessor or the Lessee believes that the Index does not accurately reflect a relationship to the base data an increase in the cost of living, the parties shall use any other Index that is generally recognized and accepted for similar determination of purchasing power.

Appendix page 84 (emphasis added).

[¶40] The first adjustment of the Sterling Eight Lease was written to coincide with the subsequent Sterling Three Lease CPI adjustment. Appendix page 138. The Sterling Three Lease and Sterling Eight Lease identify a specific "index" to be used as a basis for making the CPI adjustment, and also address the possibility that the particular index selected may not be available.

[¶41] The lower court erred as a matter of law when it found that the Sterling Three and Sterling Eight Lease terms had been altered by an alleged incorrect calculation of the CPI rent adjustment. Appendix page 487. The lower court found as a matter of law that "when Cetero agreed to the rental adjustment by looking at the CPI in 2010 and subtracting from it the CPI number from 2005 and dividing the difference in the 2005 number to get the percent increase, this was an alteration of the parties' original agreement." Appendix page 487. This finding is unsupported by any evidence.

i. The Sterling Three Lease Rate Amount was Adjusted in Accordance with the Sterling Three Lease Terms in 2005. Both the Sterling Three and Sterling Eight Lease Rent Amount were Adjusted in 2010 in Conformance with the Unambiguous Lease Contract.

[¶42] The first Sterling Three rent adjustment was made in December 2005. Margaret Asheim communicated the change to PRACS and outlined how the annual rate was adjusted. By letter dated December 1, 2005 Asheim explained that the index called for in the lease was not available, ". . . the 1967 Index is no longer updated." Appendix page 300. Asheim identified the index stated in the lease but noted that index had been changed from an annual index to a twice-a-year index. Asheim advised PRACS of her intent to use the current Minneapolis index, stating, "The current Minneapolis index is only calculated on a half-year and annual basis, so I am using the 'half 1' numbers to calculate the increase." Appendix page 300. Asheim provided a copy of the index showing an increase from 168.2 for half 1 in 2000 to 192.4 for half 1 in 2005,

and advised this "calculates to a 14.39% increase." Appendix pages 300 & 301. PRACS paid the rent based on this calculation without objection. Appendix pages 302, 303 & 304.

[¶43] The tenant did not contest the index selection or rent adjustment of the Sterling Three Lease in 2005. Steve Kiemele, Chief Financial Officer of PRACS, testified that PRACS was not "debating" or "contesting" the 2005 calculation. Transcript of Trial Proceeding, February 4, 2014, page 320, lines 4-15. There was simply no dispute that the CPI adjustment in 2005 was in accordance with the unambiguous lease terms. Carlson actually consented to the rent adjustment pursuant to the Sterling Three Lease terms in 2005.

[¶44] The Sterling Three Lease was adjusted again in 2010 in accordance with the unambiguous lease terms. There is no evidence to prove that the adjustment was made in error, or that an error in calculation resulted in an alteration of the Sterling Three Lease terms.

ii. The Sterling Eight Lease CPI Rent Adjustment Was Made In Accordance with the Unambiguous Lease Terms.

[¶45] The first Sterling Eight rent adjustment was written to coincide with the Sterling Three Lease CPI adjustment in 2010. By letter dated August 23, 2010, Keith Hanson, Property Manager of Sterling Three and Sterling Eight at the time, conveyed the new rate to the tenant, stating:

> Enclosed are invoices for the new rent payments for the original building and the building addition for September 1, 2010. Per the Lease Agreement, the annual rate shall be adjusted by the change in purchasing power every 5 years as shown in the Consumer Price Index from the first full month following the Commencement Date of September 1, 2000for the original building. The lease for the west addition was written to match the change in rent for the original building. As in 2005 we are using the first half number from the semi-annual report, as the 1967 index is no longer updated. I have attached a copy of this index showing the numbers that were used to calculate the increase.

Appendix page 307 (emphasis added).

[¶46] The tenant paid the increased rent for the Sterling Three and Sterling Eight Leases without objection.

[¶47] Carlson argues that Sterling Three and Sterling Eight changed the manner in which the CPI was calculated, resulting in exoneration of both personal guarantees:

> While there is no dispute that the lease agreements allow for rent adjustments, *see* Trial Exs. 1 and 3 at § 2.1.1.1, Plaintiffs' calculation of the adjustment was not in accordance with the leases' terms. Moreover, Carlson never approved, or even knew about the change in methodology.

Defendant's Post Trial Brief, at 8 (Doc. #242).

[¶48] Counsel asserted that the "contemplated adjustment, therefore, is an increase equal to the average increase over the proceeding five years." Counsel then went to great lengths to demonstrate how, in his opinion, the CPI should have been adjusted in 2010, resulting in the conclusion that "the 2010 base rent should have only increased by 4.21 percent." Counsel presented no evidence that the calculations were done in error, or that the CPI was calculated in 2010 differently than in 2005. Counsel testified at length about how the CPI should be calculated, and suggested an average would be correct. Transcript of Proceedings, February 4, 2014, page 280, lines 5-20. Margaret Asheim dispelled that interpretation, stating it is a simple math problem to determine the amount of change using the identified, agreed-upon index, and that to the best of her knowledge she calculated the CPI correctly in 2005. Transcript of Proceedings, February 4, 2014, page 288, lines 19-21. She agreed with counsel's statement as to how an average methodology would be applied, but did not state that his interpretation of the lease terms was correct. Transcript of Proceedings, February 4, 2014, page 280, lines 10-20. The Sterling Three Lease and the Sterling Eight Lease do not state the CPI is to be calculated on an average basis; the word "average" never appears in the leases.

[¶49] There is no evidence of any agreement between the tenant and the landlord to a change in methodology, as suggested by counsel. It is clear from the evidence that the parties did not intend to alter the lease terms with respect to the calculations. Keith Hanson advised the lessee

that he was calculating the CPI in accordance with the lease terms using the same index and manner of calculation as was used in 2005. Appendix page 307.

[¶50] Statements of counsel are not evidence and must be disregarded. N.D. Pattern Jury Instruction C 85.0. The lower court's acceptance of counsel's statements as to how the CPI should be calculated was in error. The finding of the lower court is not based on any evidence in the record and must be reversed.

[¶51] Even if the calculation in 2010 was done incorrectly, which Sterling Three and Sterling Eight dispute, the remedy would not be exoneration of Carlson's Personal Guaranty. Rather, recalculation of the amount of rent due may be appropriate. Carlson's Personal Guaranty of the Sterling Three Lease and the Sterling Eight Lease are not exonerated by an unproved, unsupported allegation of a calculation error. The lower court's finding that the CPI was calculated incorrectly, and that the alleged miscalculation resulted in an alteration of the lease terms, must be reversed.

C. Pursuant to the Unambiguous Sterling Three and Sterling Eight Lease Terms the Tenant is Responsible for the Real Estate Taxes.

[¶52] Pursuant to the unambiguous lease terms, the tenant is responsible for the real estate taxes levied on the property. Article IV, Section 4.1. of the Sterling Three Lease regarding Real Estate Taxes states:

> Lessee shall pay its proportionate share of real estate taxes and installments of special assessments against the property which have been certified for collection as of the Commencement Date of this lease as a part of the CAM expense as set forth in Article II, above.

Appendix page 84.

[¶53] The Sterling Eight Lease has a similar provision:

> Lessee shall pay its proportionate share of real estate taxes and installments of special assessments against the property which have been certified for collection as of the

Commencement Date of this lease as a part of the Maintenance expenses as set forth in Article II, above.

Appendix page 109.

i. The Tenant's Obligation to Pay the Real Estate Taxes Pursuant to the Sterling Three Lease was Not Altered.

[¶54] In 1999 Sterling Three received Tax Increment Financing ("TIF") from the city of East Grand Forks, MN for the development of the Sterling Three building. Tax Increment Financing is a well-recognized tool used by communities to incent development. The success of the TIF mechanism relies upon the property taxes actually being paid. It is the payment of the property taxes that generates "the incremental increase in taxes" paid to the government and the government, in turn, pays the increment to the developer. The lease tenant pays the property taxes, a portion of which is then remitted by the government to the developer as a "TIF payment."

[¶55] The Sterling Three TIF is not an issue in this lawsuit. The Sterling Three and Sterling Eight buildings are entirely separate and distinct properties. There is simply no question that there were two leases and two personal Guarantees. The tenant issued separate checks for the Sterling Three Lease and the Sterling Eight Leases, recognizing that they are in fact separate properties. Transcript of Proceedings, page 329, lines 22-25, page 330, lines 1-24.

ii. The Tenant's Obligation to Pay the Real Estate Taxes Pursuant to the Sterling Eight Lease Was Not Altered.

[¶56] On May 18, 2004, Sterling Eight entered into a Land Development and Purchase Agreement with the City of East Grand Forks, MN. Appendix page 349. The Purchase Agreement provides that the city of East Grand Forks will provide Sterling Eight "tax increment financing for the project of at least 75% of the net tax capacity for a period of not to exceed ten (10) years, …" Appendix Page 349. The agreement further provides that "the project will be a

pay as you go project with the first increment available in the first year of the full tax capacity." Appendix page 349. Finally, the agreement provides that Sterling Eight shall receive the TIF "regardless of any job or wage goals that might be applicable, under Minnesota law, including MSA §§116J.01 *et sequitor*." Appendix page 349 (emphasis added).

[¶57] On December 29, 2004, subsequent to Sterling Eight's separate agreement with East Grand Forks, MN, Carlson signed a JOBZ agreement with the State of Minnesota on behalf of PRACS. Appendix page 342. (emphasis added). M.S.A. §§116J.01 *et seq.* includes the JOBZ business incentive PRACS secured. The Sterling Eight TIF agreement overrides PRACS' JOBZ agreement.

[¶58] The TIF incentive and the JOBZ agreement are separate government tax incentive programs. The TIF is an incentive for building, available to the owner of the building for a specified duration. The JOBZ credit is provided as incentive to businesses to add jobs and equipment. There is no mention of either the TIF or the JOBZ credit in either of the lease contracts.

[¶59] Jim Richter, Executive Director of the Economic Development Housing Authority, the oversight entity for the Sterling Eight TIF and the PRACS' JOBZ agreement, testified that he did not anticipate the inherent conflict between the two programs. Transcript of Proceedings, February 4, 2014 page 339, lines 19-25, page 340, lines 1-6. Sterling Eight's prior agreement with East Grand Forks to receive a 75% tax increment financing (TIF) payment as an incentive for developing property in East Grand Forks, MN was compromised. When Jim Richter realized this conflict, he "brokered a deal" with PRACS and Sterling Eight such that Sterling Eight received the amount of the TIF to which it was entitled from PRACS, and PRACS received the

direct benefit of the JOBZ incentive. Sterling Eight received "the same deal" as before the JOBZ agreement. Appendix page 336. PRACS received a better deal. Appendix page 336.

[¶60] Sterling Eight identified the amount of the TIF on the annual expense summary as a separate line item. Appendix page 295. The number was derived from the amount calculated by Jim Richter. Margaret Asheim testified that the TIF amount had nothing to do with the lease payments for the following year and was never considered part of CAM:

> Q. (By Ms. Morris) Does the number you used for the value of the TIF impact or come into play with the CAM adjustment?
> A. Not with the CAM adjustment, no. I put it on this sheet as an accounting simplification, I guess, because rather than trading checks or doing something else. So when I calculated CAM, I did not use that.

Transcript of Proceedings, February 4, 2014, page 252, lines 21-25, page 253, lines 1-2.

[¶61] The identification of the TIF on the Sterling Eight annual statement was done as a matter of convenience to PRACS. The tenant's obligation to pay the real estate taxes pursuant to the Sterling Eight Lease terms did not change. Sterling Eight received nothing in exchange for agreeing to accept the amount of the TIF from the tenant as opposed to the city of East Grand Forks, MN. Transcript of Proceedings, February 3, 2014, page 123, lines 8-11.

[¶62] The JOBZ Business Subsidy Agreement states that "the qualified business plans to begin construction of its new facility in the Zone on JUNE, 2004, the Construction Date." Appendix page 342. Clearly the JOBZ Agreement pertained only to Sterling Eight. The Sterling Three Lease was not implicated as a result of the JOBZ application and the resolution of the conflict between the Sterling Eight TIF and the JOBZ credit. Transcript of Proceedings, February 3, 2014, page 199, lines 13-19. Jim Richter identified only the parcel number for Sterling Eight in his correspondence with PRACS and Sterling Eight. Appendix pages 315, 326, 336 & 338. Jim Richter confirmed that the Sterling Eight property was an entirely separate parcel and that the

JOBZ agreement only impacted the TIF for the Sterling Eight building. Transcript of Proceedings, February 4, 2014, page 340, lines 7-9, page 341, lines 23-25, page 343, lines 12-17.

[¶63] The lower court failed to recognize or even acknowledge that the JOBZ application signed by Carlson in 2004 impacted the TIF payment Sterling Eight was entitled to receive. It appears the lower court did not fully comprehend the interplay between the TIF payment Sterling Eight was entitled to receive and its priority over PRACS' JOBZ agreement. There is no evidence that there is a "reduction of the taxes caused by the tax increment financing." The amount of TIF is determined by the amount of real estate taxes collected. Jim Richter assisted Sterling Eight and PRACS reach an agreement to allow PRACS to receive the JOBZ benefit, and Sterling Eight receive the TIF. Carlson's Personal Guaranty of the Sterling Eight Lease is not exonerated. The lower court decision must be reversed.

D. Carlson Actually or Impliedly Consented to the Alleged Lease Alterations, if any.

[¶64] The issue of consent only arises if this court finds that there actually were contractual alterations to the Sterling Three and Sterling Eight Lease contracts. Sterling Three and Sterling Eight proved that there were no such contractual alterations. Sterling Three and Sterling Eight also proved that Carlson actually or impliedly consented to all of the alleged alterations. Carlson signed the Sterling Three Lease and Sterling Eight Lease as CEO of PRACS. Carlson was actively involved in the negotiation of both leases. Carlson knew and understood the terms of the Sterling Three and Sterling Eight Leases he signed. Carlson signed the Sterling Three Guaranty and the Sterling Eight Guaranty simultaneous to signing the leases. Carlson's consent was ongoing based upon his receipt of annual statements evidencing the Direct Expense-

Janitorial as a separate line item.[1] His consent is evidenced by his continued signatures on the checks paying the lease amounts, including the adjusted Sterling Three Lease payments following the CPI adjustment in 2005. Transcript of Proceedings, February 3, 2014, page 52, lines 3-10. Carlson's signature on the PRACS JOBZ agreement in 2004 proves his consent.

VI. COSTS

Issue 2: The lower court abused its discretion by awarding costs in excess of that provided for by statute.

[¶65] N.D.C.C. §28-26-06 allows a prevailing party to tax the opposing party for five specified classes of costs and disbursements, including (1) the legal fees of witnesses; sheriffs; clerks of the district court; the clerk of the supreme court, if ordered by the supreme court; process servers; and of referees and other officers; (2) the necessary expenses of taking depositions and of procuring evidence necessarily used or obtained for use on the trial; (3) legal fees for publication; (4) legal fees of the court reporter for a transcript of testimony when the transcript is used on motion for a new trial or in preparing a statement of the case; and (5) reasonable expert witness fees.

A. The Deposition Costs for James D. Carlson and Steve Kiemele Are Not Taxable Costs.

[¶66] N.D.C.C. §28-26-06 only allows the prevailing party to tax the non-prevailing party for the necessary expenses of taking depositions. In Matter of Estate of Dittus, 497 N.W. 2d 415, 421 (N.D. 1993), this court found that a party was not entitled to recover costs for attending a deposition as a deponent. Similarly, Sterling Three and Sterling Eight contend that Carlson is not entitled to recover any costs incurred for the depositions of Steve Kiemele and James

[1] Several annual statements were addressed directly to Dr. Carlson, and the attached Operating Expense Summaries clearly identified the janitorial in the demised premises as a direct expense to the PRACS. Appendix pages 321, 322, 323 & 324.

Carlson, including transcript copies. To award such costs was an abuse of the trial court's discretion.

B. Costs for the Conversion of Documents Are Not Taxable Costs.

[¶67] N.D.C.C. § 28-26-06 does not contemplate the conversion of documents "to database ready images" as taxable against the non-prevailing party. Sterling Three and Sterling Eight produced the documents electronically; Carlson's manipulation of the documents must be at his own expense.

C. The Court Trial Transcript to Prepare a Post-Trial Brief is Not a Taxable Cost.

[¶68] Carlson procured the trial transcript to prepare his Post Trial Brief. Sterling Three and Sterling Eight also procured the trial transcript at that time, at its own expense. Carlson then taxed the cost of the transcript. This is an impermissible cost under the terms of N.D.C.C. § 28-26-06. This section provides, in relevant part, for recovery of fees to the court reporter for transcript testimony "when such transcript is used on a motion for a new trial or in preparing a statement of the case; …" N.D.C.C. § 28-26-06. The preparation of the trial transcript for purposes of preparing a post- trial brief is simply not a taxable cost against the non-prevailing party. Taxing the transcript fee is an abuse of the lower court's discretion.

Issue 3: The lower court abused its discretion by awarding cost to Carlson for expert witness fees when the parties agreed to bifurcate the trial and Sterling Three and Sterling Eight's admissibility and credibility objections were preserved.

[¶69] Carlson identified Konrad Olson ("Olson") as an expert witness on the factual issue of mitigation of damages. In advance of trial, the parties agreed to bifurcate liability from damages, and the court entered an order on January 16, 2014 stating "A trial on damages will be scheduled at a later date, allowing time for the parties to file any motions relevant to damages in advance of trial." Appendix page 291 (emphasis added). Sterling Three and Sterling Eight's admissibility

and credibility objections were preserved. Carlson must bear the risk that the costs may not be recoverable if the damage phase of the trial is never had. To award the costs now is premature, in any event.

[¶70] Sterling Three and Sterling Eight objected that Carlson's expert witness should be disqualified from testifying as an expert in this case. As a commercial realtor, Olson does not possess "scientific, technical or other specialized knowledge [that] will assist the trier of fact to understand the evidence" as provided by N.D.R.Ev. 702. Affidavit of Jason Loos, ¶ 1 (Docket #264). Rather, Olson could only testify to what he would have done to market the properties. Olson testified that he has no experience negotiating property leases in East Grand Forks, Minnesota. Affidavit of Jason Loos, ¶ 1 (Docket #264). Olson further testified that there is no particular standard of care in the industry. Therefore, he could not opine that Sterling Three and Sterling Eight breached any such standard. Affidavit of Jason Loos, ¶1 (Docket #264).

[¶71] Further, Carlson's expert's opinion is biased. Olson testified that he represents Carlson for the sale of his properties in Fargo. Affidavit of Jason Loos, ¶ 1 (Docket #264). Olson's financial stake in the marketing and sale of Carlson's property is a clear conflict; exclusion of his testimony would have been an appropriate remedy had the trial not been bifurcated.

[¶72] Finally, Carlson's expert witness fees of $300 per hour are unreasonable. The expert's time spent researching and reviewing the market conditions, and brainstorming about possible marketing strategies, directly served Carlson's interest, and ultimately his own.

[¶73] Olson did not testify at trial, and Sterling Three and Sterling Eight contend his testimony would be excluded. The lower court abused its discretion by taxing costs relating to Olson at this juncture, if at all.

VII. CONCLUSION

[¶74] James D. Carlson signed both the Sterling Three and Sterling Eight Leases. He also personally guaranteed both leases. The leases and guarantees are unambiguous. In order to exonerate Carlson's Guaranty obligations, the tenant's obligation on both of the Sterling Three and Sterling Eight Leases must have been altered, without the consent of the guarantor. None of the alleged changes contractually altered the obligation of the principal. Furthermore, Carlson consented to the operation of the lease terms when he signed the leases. Carlson repeatedly received Annual Operating summaries and Carlson paid the rent. Carlson signed the JOBZ application which resulted in a conflict with the pre-existing TIF to which Sterling Eight was entitled. Carlson consented.to the terms of the Sterling Three and Sterling Eight Leases.

[¶75] Sterling Development Group Three, LLC and Sterling Development Group Eight, LLC respectfully request this court reverse the lower court's decision and find the Personal Guarantees enforceable. The matter must be remanded to the lower court for further proceedings related to damages.

[¶76] Sterling Development Group Three, LLC and Sterling Development Group Eight, LLC further respectfully request this court reverse the lower court's cost determination.

Dated this 30th day of July, 2014.

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CERTIFICATE OF COMPLIANCE

The undersigned, as attorney for Appellants Sterling Development Group Three, LLC, and Sterling Development Group Eight, LLC and as the author of the above brief, hereby certify, in compliance with Rule 32 of the North Dakota Rules of Appellate Procedure, that the brief was prepared with proportional typeface (Times New Roman) and the brief, excluding the table of contents, the table citations, and certificate of compliance, does not exceed 7,953 words.

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Case No.: 20140188

District Court No. 09-2012-CV-02902

IN THE SUPREME COURT

STATE OF NORTH DAKOTA

Sterling Development Group Three, LLC,
Sterling Development Group Eight, LLC,

Plaintiffs/Appellants,

v.

James D. Carlson,

Defendant/Appellee.

CERTIFICATE OF ELECTRONIC SERVICE

I hereby certify that on July 30, 2014, true and correct copies of the following documents:

Appellants' Brief

Appellants' Appendix

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CERTIFICATE OF ELECTRONIC SERVICE

I hereby certify that on August 5, 2014, true and correct copies of the following documents: **Revised Appellants' Brief, Revised Table of Contents to the Appendix and Appellants' Appendix Bates Stamp number 501** were served electronically upon the following:

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ADDENDUM

22-01-01. Definitions.
In this chapter, unless the context or subject matter otherwise requires:
1. A "continuing guaranty" means a guaranty relating to a future liability of the principal under successive transactions which either continue the liability or from time to time renew it after it has been satisfied.

- A "guaranty" means a promise to answer for the debt, default, or miscarriage of another person.

9-07-02. Language of contract governs if clear.
The language of a contract is to govern its interpretation if the language is clear and explicit and does not involve an absurdity.

9-07-03. Contract interpreted to give effect to mutual intention.
A contract must be so interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting so far as the same is ascertainable and lawful. For the purpose of ascertaining the intention of the parties to a contract, if otherwise doubtful, the rules given in this chapter are to be applied.

9-07-04. Intention ascertained from writing alone if possible.
When a contract is reduced to writing, the intention of the parties is to be ascertained from the writing alone if possible, subject, however, to the other provisions of this chapter.

22-01-15. When guarantor exonerated.
A guarantor is exonerated, except insofar as the guarantor may be indemnified by the principal, if, by any act of the creditor without the consent of the guarantor:
1. The original obligation of the principal is altered in any respect; or
2. The remedies or rights of the creditor against the principal in respect thereto are impaired or suspended in any manner.

9-01-02. Requisites of contract.
It is essential to the existence of a contract that there should be:
1. Parties capable of contracting;
2. The consent of the parties;
3. A lawful object; and
4. Sufficient cause or consideration.

9-05-01. Good consideration defined.
Any benefit conferred or agreed to be conferred upon the promisor by any other person to which the promisor is not entitled lawfully, or any prejudice suffered or agreed to be suffered by such person, other than such as that person, at the time of consent, is lawfully bound to suffer as an inducement to the promisor, is a good consideration for a promise.

9-06-04. Contracts invalid unless in writing - Statute of frauds.
The following contracts are invalid, unless the same or some note or memorandum thereof

is in writing and subscribed by the party to be charged, or by the party's agent:
1. An agreement that by its terms is not to be performed within a year from the making thereof.
2. A special promise to answer for the debt, default, or miscarriage of another, except in the cases provided for in section 22-01-05.
3. An agreement for the leasing for a longer period than one year, or for the sale, of real property, or of an interest therein. Such agreement, if made by an agent of the party sought to be charged, is invalid unless the authority of the agent is in writing subscribed by the party sought to be charged.
4. An agreement or promise for the lending of money or the extension of credit in an aggregate amount of twenty-five thousand dollars or greater.
5. An agreement or promise to alter the terms of repayment or forgiveness of a debt that is in an aggregate amount of twenty-five thousand dollars or greater.

28-26-06. Disbursements taxed in judgment.
In all actions and special proceedings, the clerk of district court shall tax as a part of the judgment in favor of the prevailing party the following necessary disbursements:
1. The legal fees of witnesses; sheriffs; clerks of district court; the clerk of the supreme court, if ordered by the supreme court; process servers; and of referees and other officers;
2. The necessary expenses of taking depositions and of procuring evidence necessarily used or obtained for use on the trial;
3. The legal fees for publication, when publication is made pursuant to law;
4. The legal fees of the court reporter for a transcript of the testimony when such transcript is used on motion for a new trial or in preparing a statement of the case; and
5. The fees of expert witnesses. The fees must be reasonable fees as determined by the court, plus actual expenses. The following are nevertheless in the sole discretion of the trial court:
a. The number of expert witnesses who are allowed fees or expenses;
b. The amount of fees to be paid such allowed expert witnesses, including an amount for time expended in preparation for trial; and
c. The amount of costs for actual expenses to be paid the allowed expert witnesses.
28-26-10. Costs in discretion of court.
In actions other than those specified in sections 28-26-07, 28-26-08, and 28-26-09, costs may be allowed for or against either party in the discretion of the court. In all actions, when there
are several defendants not united in interest and making separate defenses by separate answers and the plaintiff fails to recover judgment against all, the court may award costs to such of the defendants as have judgment in their favor.

RULE 702. TESTIMONY BY EXPERT WITNESSES
A witness who is qualified as an expert by knowledge, skill, experience, training, or education may testify in the form of an opinion or otherwise if the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue.