

IN THE COURT OF APPEALS OF IOWA

No. 8-1022 / 07-2155
Filed March 26, 2009

TERMINAL PROPERTIES, INC.,
Member-Manager of Hampton
Propane Terminal, L.C.,
Plaintiff-Appellant,

vs.

HAMPTON PROPANE TERMINAL,
L.C., an Iowa limited liability company,
Defendant,

and

LAKES GAS COMPANY,
a Minnesota Corporation,
Defendant-Appellee.

Appeal from the Iowa District Court for Franklin County, John S. Mackey,
Judge.

Terminal Properties appeals from the decision of the district court
declaring Lakes Gas, purchaser of Hampton Propane Company, is entitled to a
\$260,000 credit for its purchase of a security agreement from Gulf Coast
Petroleum. **AFFIRMED.**

Thomas J. Houser and Christopher P. Jannes of Davis, Brown, Koehn,
Shors & Roberts, P.C., Des Moines, for appellant.

Jim D. DeKoster and Mark F. Conway of Swisher & Cohrt, P.L.C.,
Waterloo, for appellee.

Heard by Mahan, P.J., and Miller and Doyle, JJ.

MAHAN, P.J.

Terminal Properties appeals from the decision of the district court declaring Lakes Gas, purchaser of Hampton Propane Company, is entitled to a \$260,000 credit for its purchase of a security agreement from Gulf Coast Petroleum. For the reasons to be discussed, we affirm.

I. Background Facts and Proceedings.

Hampton Propane Company, L.C. (Hampton) executed an open-end real estate mortgage in June 1995 in favor of First National Bank of Hampton (First National) securing credit in the amount of \$415,000. Hampton was organized as a limited liability company in July 1995. At the times material to this appeal, Hampton had four members: Ray Energy, which held a 42.95% interest; Ken Fencil, who held a 24.06% interest; Terminal Properties, which held a 24% interest; and Dennis Ribbentrop, who held an 8.99% interest. In September 1998 Ken Fencil, Dennis Rippentrop, Dave Stevenson of Ray Energy, and Ted Vosburg of Terminal Properties each executed an individual guaranty with respect to the real estate mortgage.

Hampton was initially in the business of buying and selling propane, which it did from a facility in Hampton, Iowa. Hampton subsequently disengaged from that business and leased the facility to Ray Energy. Ray Energy purchased propane from several suppliers, including Gulf Coast Petroleum, Inc. (Gulf Coast), and re-distributed the propane to its customers.

Ray Energy purchased propane from Gulf Coast pursuant to a line of credit. By October 2000 Ray Energy's debt to Gulf Coast was such that Gulf Coast required Ray Energy to execute a \$1 million promissory note. By October

2001 Ray Energy's debt to Gulf Coast had increased to approximately \$1.6 million. Gulf Coast informed Ray Energy that it would not extend the line of credit any further unless Ray Energy executed a second promissory note and provided collateral in the form of a security interest in Hampton's assets.

On October 20, 2001, Ray Energy, by its president David Stevenson, executed a second \$1 million promissory note. The note memorialized Ray Energy's existing debt and extended its line of credit. That same date, October 20, 2001, Stevenson entered into a commercial security agreement on behalf of Hampton pledging certain assets of Hampton as collateral to secure the two \$1 million promissory notes executed by Ray Energy.

On December 28, 2001, Ray Energy, Fencl, and Rippentropp voted to ratify Stevenson's execution of the October 20, 2001 security agreement. Terminal Properties opposed ratification because it believed Hampton's assets should not be pledged to secure Ray Energy's debt. In this appeal, Terminal Properties challenges this ratification as ineffective, claiming it was precluded by conflicts of interest.

Ray Energy went out of business in April 2003. Ray Energy defaulted on its obligations to Gulf Coast. In May 2003 First National notified Hampton that it was in default under the real estate mortgage.

Lakes Gas initiated efforts to acquire Hampton's facilities in June 2003. Lakes Gas subleased the Hampton facilities from Ray Energy in July 2003. Effective December 1, 2003, Lakes Gas leased the Hampton facilities directly from Hampton. The lease was ratified by the same voting block that ratified the

security agreement—Ray Energy, Fencil, and Rippentropp. Again, Terminal Properties objected.

In October 2003 Gulf Coast filed suit against Ray Energy and Hampton seeking to foreclose on the security agreement.¹ Gulf Coast alleged that as of October 3, 2003, the principal amount of \$1 million was due, owing, and unpaid under the 2001 promissory note. It sought both a personal judgment against Ray Energy for \$1 million, and a judgment in rem against the collateral secured by the security agreement.

In November 2003 Hampton held two special meetings to address the Gulf Coast foreclosure action. Also in November 2003, Lakes Gas purchased First National's mortgage for \$318,000, along with the individual guarantees; the sum was to be credited against Lakes Gas's purchase price that it would pay for Hampton.

On December 11, 2003, Terminal Properties filed this action to dissolve Hampton, enter an injunction to preserve its assets, and to appoint a receiver for Hampton.² Hampton moved to dismiss the suit, and Fencil and Rippentropp joined the motion. Ray Energy filed its own motion to dismiss claiming that as a member, Terminal was not a proper party. Hearing on the request for injunctive relief was set for March 15, 2004.

On January 9, 2004, Hampton completed execution of a contract for deed, effective December 1, 2003, under which Lakes Gas would purchase all of Hampton's assets for \$730,000 payable as follows:

¹ We will refer to this suit as the foreclosure action.

² We refer to this action filed by Terminal Properties as the dissolution action.

- a. \$35,000 immediately upon execution of this agreement.
- b. Commencing on the first day of January, 2004, and on the same day of each month thereafter, the amount of \$100 shall be paid.
- c. All amounts owing hereunder shall, if not earlier due, become payable on January 1, 2006.
- d. All amounts owing hereunder shall, if not earlier due, become payable 30 days after the Seller has delivered to Buyer a [sic] evidence in a form satisfactory to Buyer that Seller holds good, marketable title to the property, as such title is defined by Iowa Statute and by the title standards . . . , subject only to the lien of any prior mortgage against such property which has been purchased by the Buyer, and further, that Seller is able to convey title to all assets purchased hereunder without lien or encumbrance.

In January 2004, in the foreclosure action, Gulf Coast filed a motion for summary judgment. Among the undisputed facts it cited were that the 2001 promissory note was matured, due, and payable; Ray Energy had failed to pay the note when due; the note and security agreement were in default; “there is now due, owing and unpaid as of October 3, 2003, the principal sum of \$1,000,000.00”; and Ray Energy had admitted \$1 million was due, owing, and unpaid under the 2001 note.

In February 2004 Gulf Coast sold and assigned all its rights, title, and interest in the promissory notes and the security agreement to Lakes Gas in exchange for \$260,000. Before Lakes Gas purchased the security agreement from Gulf Coast, Terminal Properties also engaged in negotiations with Gulf Coast in an attempt to purchase the security agreement for itself—without notice to other Hampton members. After selling its interest to Lakes Gas, Gulf Coast filed a notice in the foreclosure action that it had transferred its interest in the case to Lakes Gas. Lakes Gas was substituted as plaintiff, and Terminal Properties moved to intervene, asserting that if intervention was denied and

Lakes Gas prevailed, membership shares in Hampton would be “ultimately extinguished through judgment and judicial sale without the payment of fair value,” and Hampton’s assets would be lost.

On March 3, 2004, a special meeting of the members of Hampton was held. A resolution confirming and ratifying the contract for deed and lease agreement with Lakes Gas was approved by the voting block of Rippentropp, Fencl, and Ray Energy; Terminal Properties objected. There was also discussion about Lakes Gas’s acquisition of Gulf Coast’s lien and the fact the contract for deed required good title. Further discussion concerning Hampton’s possible defenses to Gulf Coast’s lien occurred. Following discussion, the following resolution was approved: “That Lakes Gas receive a \$260,000 credit against the purchase of assets of Hampton Propane Terminal by Lakes Gas Company provided it is confirmed that the \$260,000 was in fact paid by Lakes Gas Company to Gulf Coast Petroleum.” Rippentropp, Fencl, and Ray Energy voted in favor, Terminal Properties opposed.

In March 2004 Terminal Properties filed an amended petition in the dissolution action seeking judicial dissolution, an injunction to preserve the assets of Hampton, and appointment of a receiver. In May 2004 the court in the dissolution action entered a ruling enjoining Hampton “from disposing, transferring or in any manner conveying, pledging or encumbering any of its assets until further order of the court.” The pending motions to dismiss were denied, and a receiver was to be appointed.

With respect to the foreclosure action, following a hearing on the motion to intervene and Lakes Gas’s motion for summary judgment, the district court

entered personal judgment against Ray Energy. Terminal Properties was allowed to intervene. The matter proceeded to trial in April 2005, and at the close of Lakes Gas's evidence the district court granted Terminal Properties' motion for a directed verdict.

On May 30, 2005, the receiver filed a final report in the dissolution action noting the receiver had been unable to find an interested purchaser for the Hampton facilities. On June 6, 2005, a hearing was held in the dissolution action.

On July 22, 2005, the dissolution court entered an order stating in part:

In open court, the parties acknowledged their agreement to the sale of the assets of Hampton Propane Terminal, L.C., to Lakes Gas Company pursuant to the existing Contract for Deed, continued involvement by the Receiver to facilitate said sale, removal of the Receiver's bond after sale, deposit of the net sale proceeds in an interest bearing bank account, requirement of signatories from Plaintiff and Defendant Hampton Propane in order to disburse funds from said account; and a continuance of the hearing scheduled for June 15, 2005 to a later, but undetermined date.

The dissolution court ordered trial continued "until all matters relevant to the foreclosure case, LACV 003603, are resolved and all appeals are complete"; postponed action on the receiver's report until the sale was complete; dissolved the temporary injunctive relief "by agreement of the parties"; and ordered the parties to "proceed to sell the assets under the existing Contract for Deed."

On January 24, 2006, Lakes Gas sent Terminal Properties a draft closing statement pursuant to the contract for deed reflecting a \$260,000 credit for its cost to acquire the Golf Coast lien and a \$318,000 credit for its cost to acquire the real estate mortgage. Terminal Properties objected to the \$260,000 credit to Lakes Gas for its cost to acquire the Gulf Coast lien. On March 6, 2006, in the

dissolution action, Terminal Properties filed a motion to compel the sale of Hampton's assets without the allowance of the \$260,000 credit, and on April 14 Terminal Properties filed a motion to enjoin the sale to Lakes Gas with the credit.

On April 17, 2006, the dissolution court entered an order denying the motion to compel sale, noting "all parties wish to close the sale, but the main difference of opinion revolves around the payment by Lakes Gas of \$260,000.00 for the former Gulf Coast lien." The court wrote that "it appears a declaratory judgment is sought with respect to the fulfillment of the performance of the contract." By separate order entered the same date, the court also denied Terminal Properties' motion to enjoin the sale of Hampton's assets to Lakes Gas, stating:

With respect to [Terminal Properties'] motion to enjoin action, it is to be noted that the temporary injunctive relief previously granted by the court has been dissolved. All parties sought and received court approval for sale of Hampton Propane's assets in accordance with the previous executory contract for deed following the lack of any bona fide offer to purchase being presented to the receiver. The receiver's bond has been exonerated and he stands merely in a nominal capacity to facilitate the consummation of the agreement already reached between the parties. The order of approval of the sale is not a decree of dissolution pursuant to Section 409A.1302; it only confirms the agreement for sale. The parties, therefore, stand in the same position with respect to their own individual capacity to negotiate and finally conclude a sale of the assets of Hampton Propane, as they did prior to the issuance of temporary injunction, which relief [Terminal Properties] has abandoned.

On April 21, 2006, Hampton held a special meeting to address the sale of its facilities and Lakes Gas's purchase of the Gulf Coast security agreement.

On April 26, 2006, this court reversed the decision of the district court in the foreclosure action. *Lakes Gas Co. v. Terminal Prop., Inc.*, No. 05-1266 (Iowa

Ct. App. Apr. 26, 2006). This court concluded the district court erred in granting Terminal Properties' motion for a directed verdict, finding

a reasonable fact finder could determine, after viewing the evidence in the light most favorable to Lakes Gas and drawing all reasonable inferences, that there was at least \$1 million due and owing from Ray Energy under the 2001 promissory note.

Id. The case was remanded for further proceedings. Procedendo issued on June 5, 2006.

On June 23, 2006, a settlement agreement was executed on behalf of Hampton and Lakes Gas that authorized a credit to Lakes Gas for the \$260,000 paid to Gulf Coast. Terminal Properties objected to the settlement agreement. On July 11, 2006, Hampton executed a warranty deed and bill of sale conveying its assets to Lakes Gas.

Lakes Gas moved to voluntarily dismiss the foreclosure action without prejudice on August 2, 2006. Terminal Properties filed a resistance to the motion to dismiss. On December 27, 2006, the foreclosure court allowed the voluntary dismissal noting, "resolution of the lien action does not seem as if it will solve the reimbursement issue"; and "Lakes Gas would like to dismiss the action in order to avoid foreclosing on property that it has purchased." The court concluded the foreclosure action "became moot when Lakes Gas acquired the pledged collateral" and "a decision on the lien action, while tempting, is pointless considering that Lakes Gas does not want to foreclose on its own property."

On April 13, 2007, the dissolution court entered a case management order in which Terminal Properties was ordered to "file an ancillary declaratory judgment petition framing the issues herein." Terminal Properties filed a third

amended petition on May 1, 2007, requesting judicial dissolution and declaratory relief with respect to the validity of the prior security agreement entered into between Hampton and Gulf Coast and with respect to the agreement between Hampton and Lakes Gas for reimbursement of the \$260,000 credit given by Hampton to Lakes Gas in consideration of the amount Lakes Gas paid to acquire Gulf Coast's interest in the security agreement. Lakes Gas and Hampton answered. On August 31, 2007, Lakes Gas moved for summary judgment.

The dissolution court granted the summary judgment motion "with respect to any issues involving the validity of the Gulf Coast security agreement as the same is now moot due to the acquisition by Lakes Gas of its own collateral." The court denied the remainder of the motion, but limited the issue at trial to the "reimbursement issue with respect to both defendants."

At trial Ted Vosburg testified Terminal Properties was organized with the sole reason being to own membership in Hampton Propane. He stated that in 2001 Hampton was operating at a significant loss and all the members decided Hampton should be sold. Vosburg further testified that he disagreed with the other members that "to keep propane flowing through Hampton Propane Terminal would make it look like a going business and thereby make it more attractive to prospective buyers." He acknowledged, however, that had Ray Energy not been able to keep propane going through Hampton, operation of the facility would have halted and the members would have been solely responsible for the mortgage, taxes, and operating expenses of Hampton. Vosburg also acknowledged he had offered to purchase the Gulf Coast security agreement for himself—without informing the other members of Hampton—and, had that

occurred, he would have asserted his rights as a lien holder against the assets of Hampton. He did not dispute the price paid for Gulf Coast's interest (\$260,000) was a fair price.

David Busch testified on behalf of Lakes Gas about the history of its acquisition of Hampton. He testified that in negotiating the purchase of Hampton, "the only agreement we reached was that there appeared to be nothing that all four members of the Hampton Propane could agree upon no matter what it was." Busch testified that Terminal Properties would not consent to any sale that resulted in Terminal receiving less than \$250,000, which was the amount it had invested in the project. He further testified that Lakes Gas purchased the bank mortgage and Gulf Coast's interest in the security agreement in an effort to acquire Hampton free of liens.

On November 26, 2007, the district court found the settlement of the Gulf Coast lien for \$260,000 was in the best interests of Hampton. The court also found Terminal Properties' claims of conflict of interest with respect to the other member-managers of Hampton was "like the frog calling the garter snake green" in light of Vosburg's attempt to purchase the Gulf Coast lien position without disclosure to the other member-managers. The court declared the March 3, 2004 approval of \$260,000 credit to Lakes Gas was legal, valid, and binding; Hampton was to wind up its affairs in accordance with the settlement agreement reached with Lakes Gas in June 2006 and a final report by Hampton was to be filed, after which the court would issue a final decree of dissolution.

Terminal Properties appeals. In essence, Terminal Properties contends conflicts of interest precluded the ratification of the security agreement with Gulf

Coast and the later actions by Hampton members could not cure the invalidity of the pledge of Hampton's assets for Ray Energy's obligations.

II. Scope and Standard of Review.

How the parties tried this declaratory judgment action in the district court governs this court's scope of review. *Smith v. Bertram*, 603 N.W.2d 568, 570 (Iowa 1999). Terminal Properties argues the case was tried in equity and our review is therefore de novo. However, at trial the court ruled on objections as they were made, which is "the hallmark of a law trial, not an equitable proceeding." *Sille v. Shaffer*, 297 N.W.2d 379, 381 (Iowa 1980). We agree with Lakes Gas that our review is for correction of errors of law. See Iowa R. App. P. 6.4.

In a law action the district court's findings of fact have the effect of a special verdict and are binding on us if supported by substantial evidence. Iowa R. App. P. 6.14(6)(a). This court, however, is not bound by the district court's conclusions of law, and we may inquire into whether the district court's ultimate conclusions were materially affected by improper conclusions of law. *Smith*, 603 N.W.2d at 570.

III. Discussion.

Iowa Code chapter 490A (2001) governs the conduct of limited liability companies. Section 490A.706 sets forth the general standards of conduct for managers of a limited liability company and requires a manager to discharge the duties as a manager in "good faith" and "in a manner the manager believes to be in the best interests of the limited liability company." Iowa Code § 490A.706(1). These obligations are identical to the obligations owed by corporate officers and

directors to the company's shareholders. See generally *Cookies Food Prods., Inc. v. Lakes Warehouse Distrib., Inc.*, 430 N.W.2d 447, 451-53 (Iowa 1988) (discussing duties of care and loyalty to shareholders and noting that when there is self-dealing by a majority stockholder which is challenged, the majority stockholder has the burden to establish that they have acted in good faith, honesty and fairness). Generally, the decisions of corporate directors are presumed to be informed, made in good faith, and made in the best interests of the company. *Id.* at 453. By analogy, the decisions of limited liability member-managers are entitled to the same presumptions. The purpose of this business judgment rule "is to severely limit second-guessing of business decisions which have been made by those whom the corporation has chosen to make them." *Hanrahan v. Kruidenier*, 473 N.W.2d 184, 186 (Iowa 1991).

Section 490A.708 provides, in part:

1. A conflict of interest transaction is a transaction with the limited liability company in which a manager of the limited liability company has a direct or indirect interest. A conflict of interest transaction is not voidable by the limited liability company solely because of the manager's interest in the transaction if any one of the following is true:

a. The material facts of the transaction and the manager's interest were disclosed or known to the managers or a committee of managers and the managers or a committee of managers authorized, approved, or ratified the transaction.

b. The material facts of the transaction and the manager's interest were disclosed or known to the members entitled to vote and they authorized, approved, or ratified the transaction.

c. The transaction was fair to the limited liability company.

...

4. For purposes of subsection 1, paragraph "b", a conflict of interest transaction is authorized, approved, or ratified if it receives the vote of a majority of the members entitled to vote under this subsection. Interests owned by or voted under the control of a manager who has a direct or indirect interest in the transaction, and interests owned by or voted under the control of an entity described

in subsection 2, paragraph “a”, shall not be counted in a vote of members to determine whether to authorize, approve, or ratify a conflict of interest transaction under subsection 1, paragraph “b”. The vote of those members, however, is counted in determining whether the transaction is approved under other sections of this chapter. Members, whether or not present, that are entitled to be counted in a vote on the transaction under this subsection constitute a quorum for the purpose of taking action under this section.

Terminal Properties argues the December 2001 vote to ratify the Gulf Coast security agreement was not proper because it was based on the votes of interested members who were not entitled to vote. Terminal Properties contends Ray Energy and Ken Fencil had direct interests requiring they recuse themselves from the vote to ratify the security agreement.

Lakes Gas contends this issue is not properly before us as it was ruled moot by the district court. Lake Gas asserts the sole issue tried was the reimbursement issue. In response, Terminal Properties argues the reimbursement issue is “inescapably tied to the origin and effectiveness of the lien.” We disagree.

Because the members of Hampton on July 22, 2005, acknowledged in open court that they wished to proceed with the sale of Hampton to Lakes Gas pursuant to the contract for deed, we conclude the focus of this appeal is limited to—as it was in the district court—the issue of reimbursement for Lakes Gas’s purchase of Gulf Coast’s lien interest. See *Grinnell College v. Osborn*, 751 N.W.2d 396, 404 (Iowa 2008) (noting that appellate review is ordinarily limited to issues raised and decided by the district court).

Hampton Propane was not a profitable business. As early as 2001 the members of Hampton agreed it should be sold. Terminal Properties did not

agree with the other three members, however, in their conclusion that Hampton was worth more as an operating terminal than an idle one. Nonetheless, the majority of member-managers determined maintaining the flow of propane through the Hampton terminal was desirable, and this ultimately resulted in the security agreement with Gulf Coast.

The contract for deed required Hampton to provide clear title to Lakes Gas. Ted Vosburg of Terminal Properties acknowledged the contract for deed so required. There is no dispute the security agreement held by Gulf Coast was a lien against Hampton assets. There is also no dispute Lakes Gas paid Gulf Coast \$260,000 to settle Gulf Coast's lien against Hampton. Finally, there is no dispute \$260,000 was a fair price for the settlement of the lien.

The district court found:

It is true that at the inception of the case the court found, at least from the information known at that time, that possible conflicts of interest existed with respect to encumbering Hampton Propane's personal property by Ray Energy sufficient to support the issuance of a temporary injunction. Such temporary injunction, however, was dissolved when Terminal Properties agreed to the original sale to Lakes Gas. Here, the action by Hampton Propane in granting a \$260,000 credit to Lakes Gas for its purchase of the Gulf Coast security interest was approved by a majority of its members in view of the pending Gulf Coast litigation at the time of the March 3, 2004, member meeting, and confirmed again by the majority at a special members meeting held April 21, 2006, authorizing the most recent settlement agreement between Hampton Propane and Lakes Gas. The evidence quite clearly establishes that the settlement of the Gulf Coast lien for \$260,000 was in the best interests of the company given the extreme uncertainty over the nature, validity, and extent of the security interest held by Gulf Coast, and the enforceability of the same against Hampton Propane's major assets, i.e. fixtures being the liquid propane storage tanks.

The district court further found the action approving the \$260,000 credit did not entail any alleged conflicts of interest. These findings are supported by substantial evidence and are thus binding upon us.

Given that the member action to approve the credit to Lakes Gas was in the best interests of Hampton and was approved by a majority of Hampton's members, this court will not interfere. The district court did not err in concluding the action was legal, valid and binding. We affirm.

AFFIRMED.