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7 # Superior Court of Washington for Clark County
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9 **Save Columbia CU Committee, John**
10 **Bucholtz, Steve Straub, and Robert Tice,** Plaintiffs,
11 vs.
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13 **Columbia Community Credit Union, Karen Martel, Edwin C. Bell, Dale Magers, William F. Byrd III, Robert M. Byrd,**
14 **Dennis McLachlan, Mark L. Ail, Connie**
15 **Jones, and Bruce Davidson,** Defendants.

No. 04-2-01341-4

Plaintiff's Response to Defendant's Motion for Dismissal or, in the Alternative, for Partial Summary Judgment

16
17 ## I. Introduction
18 Plaintiff Save Columbia CU Committee and the other above-named plaintiffs on
19 March 16, 2004, filed a Complaint for Declaratory Judgment and for Injunction against
20 Columbia Community Credit Union (**"CCCU"**) and its directors that stated, per CR 8(a) and
21 RCW Ch. 7.24, short and plain statements showing plaintiff's entitlement for declaratory or
22 other relief on the following claims:
23 (1) That five of CCCU's directors are ineligible to continue serving as directors (**"Term**
24 **Limits Claim"**);
(2) That CCCU's directors have breached, and are continuing to breach, their fiduciary
25 duties by impairing the corporate governance rights of Plaintiffs for their personal self-interests
26 (**"Fiduciary Duty Claim"**);
(3) That CCCU's directors have wrongly denied Plaintiffs access to corporate records
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1 and to corporate resources that permit Plaintiffs to communicate with other members of CCCU
2 (**"Access to Records Claim"**);
3 (4) That the conversion of CCCU into a savings bank is not permitted by applicable law
4 (**"No Enabling Law Claim"**); and
5 (5) That any conversion or merger of CCCU requires approval by two-thirds of its voting
6 members (**"Supermajority Vote Claim"**).
7 On April 5, 2003, CCCU moved for dismissal of all Plaintiffs' claims under CR 12(b)(6)
8 and, alternatively, moved for summary judgment under CR 56 on Plaintiffs' Term Limits Claim.
9 That motion was accompanied with a Memorandum of Points and Authorities (**"Defs' 4/5
10 Memorandum"**). This response first will address the applicable legal standard for deciding a
11 motion for dismissal under CR 12(b)(6) for failure to state a claim. Then it will apply that
12 standard to and discuss the Fiduciary Duty Claim, the Access to Records Claim, the No Enabling
13 Law Claim, and the Supermajority Voting Claim. Last, it will discuss the reasons to deny both
14 motions as to the Term Limits Claim.

15 **II. Standards for Denying Motions Under CR 12(b)(6)**

16 A motion under CR 12(b)(6) seeks dismissal "for failure to state a claim upon which
17 relief can be granted." The standards in Washington state for deciding, and usually denying, such
18 motions are clear. In *Bravo v. Dolsen Companies*, 125 Wn.2d 745, 888 P.2d 147 (1995), the
19 Washington State Supreme Court summarized the well-established law, at page 750:

20 > A dismissal for failure to state a claim under CR 12(b)(6) is appropriate only if "'it appears beyond doubt that the plaintiff can prove no set of facts, consistent with the complaint, which would entitle the plaintiff to relief.'" *Haberman v. WPPSS*, 109 Wn.2d 107, 120, 744 P.2d 1032, 750 P.2d 254 (1987) (quoting *Bowman v. John Doe,* 104 Wn.2d 181, 183, 704 P.2d 140 (1985) (quoting *Orwick v. Seattle,* 103 Wn.2d 249, 254, 692 P.2d 793 (1984))).
> CR 12(b)(6) motions should be granted only "'sparingly and with care'." *Haberman*, 109 Wn.2d at 120 (quoting *Orwick*, 103 Wn.2d at 254). "[A]ny hypothetical situation conceivably raised by the complaint defeats a CR 12(b)(6) motion if it is legally sufficient to support plaintiff's claim." *Halvorson v. Dahl,* 89 Wn.2d 673, 674, 574 P.2d 1190 (1978). Hypothetical facts may be introduced to assist the court in establishing the "conceptual backdrop" against which the challenge to the legal sufficiency of the claim is considered. *Brown v. MacPherson's, Inc.,* 86 Wn.2d 293, 298 n. 2, 545 P.2d 13 (1975).
> We have held that in determining whether such facts exist, a court may

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consider a hypothetical situation asserted by the complaining party, not part of the formal record, including facts alleged for the first time on appellate review of a dismissal under the rule. *Halvorson*, 89 Wn.2d at 675. Neither prejudice nor unfairness is deemed to flow from this rule, because the inquiry on a CR 12(b)(6) motion is **whether any facts which would support a valid claim can be conceived**. *See Halvorson,* 89 Wn.2d at 674-75. [Emphasis added.]

And in *Tenore v. AT&T Wireless Servs.*, 136 Wn.2d 322, 962 P.2d 104 (1998), that Court restated that standard, at page 329:

> Under CR 12(b)(6), a complaint can be dismissed for "failure to state a claim upon which relief can be granted." A dismissal under this rule involves a question of law which is reviewed de novo by an appellate court and is appropriate only if it appears beyond doubt that the plaintiff cannot prove any set of facts which would justify recovery. [[fn23] *Hoffer v. State*, 110 Wn.2d 415, 420, 755 P.2d 781 (1988), *aff'd*, 113 Wn.2d 148, 776 P.2d 963 (1989); *Bravo v. Dolsen Cos.*, 125 Wn.2d 745, 750, 888 P.2d 147 (1995).] In such a case, a plaintiff's allegations are presumed to be true and a court may consider hypothetical facts not included in the record. [[fn24] *Cutler v. Philips Petroleum Co.*, 124 Wn.2d 749, 755, 881 P.2d 216 (1994), *cert. denied*, 515 U.S. 1169, 115 S. Ct. 2634, 132 L. Ed. 2d 873 (1995).] **CR 12(b)(6) motions should be granted "sparingly and with care" and "only in the unusual case in which plaintiff includes allegations that show on the face of the complaint that there is some insuperable bar to relief.** [[fn25] *Hoffer*, 110 Wn.2d at 420 (quoting 5 CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1357, at 604 (1969)); *Orwick v. City of Seattle*, 103 Wn.2d 249, 254, 692 P.2d 793 (1984)." [Footnote citations inserted; emphasis added.]

E.g., *Postema v. Pollution Control Hearings Board*, 142 Wn.2d 68, 122, 11 P.3d 726 (2000). And in *Hoffer*, 110 Wn.2d at 421, the Court reviewed CR 12(b)(6) motion rulings, saying first:

> [O]ur task is to determine only if there is any possible set of facts for each claim under which recovery could be granted. In many instances the bondholders have alleged multiple theories under which they could recover under a single claim. Once we have determined that recovery for a single claim is possible under one theory or set of facts, we will not address the sufficiency of the other theories. Accordingly, we have not addressed all the parties' arguments concerning each claim.

So if "any possible set of facts"—even facts that "can be conceived"— might be found through pre-litigation discovery that would justify relief on a claim asserted, then the CR 12(b)(6) motion as to that claim must be denied.

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III. Fiduciary Duty Claim

CCCU is a cooperative society organized as a nonprofit corporation. RCW 31.12.015. Its members own the corporation and are entitled to receive their proportionate share of its assets in the event of its voluntary liquidation. RCW 31.12.474. The members elect its directors to manage its business and affairs. Washington case law established long ago that corporate directors and officers stand in a fiduciary relationship to their corporation and its shareholders/ members. *E.g., Tefft v. Schaefer*, 148 Wn. 602, 269 P. 1048 (1928); *Hudson v. Alaska Airlines*, 43 Wn.2d 71, 260 P.2d 321 (1953); *State ex rel. Hayes v. Keypoint Oyster*, 64 Wn.2d 375, 391 P.2d 979 (1964). The case law of other leading states is the same. *E.g., Toner v. Baltimore Envelope Co.*, 304 Md. 256, 268-69, 498 A.2d 642, 648 (1985) (Directors owe fiduciary duties to both the corporation *and* the shareholders.); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del.Supr. 1985) ("[O]ur analysis begins with the basic principle that corporate directors have a fiduciary duty to act in the best interests of the corporation's stockholders.")

Consistent with that corporate common law, CCCU's Disclosure Statement dated August 3, 2003 concerning its bank Plan of Conversion acknowledged., at page 3, that CCCU's Board of Directors recognized their *fiduciary duty to its members*, by saying, "In adopting the Plan, the Board of Directors, in exercising its *fiduciary duty to* the Credit Union and *its members*, considered the current environment and the following primary factors: ...." [Emphasis added.] Exhibit A of Schafer Declaration of 4/15, being filed with this response.

The CCCU members have various rights of corporate governance under Washington state law, including the Credit Union Act, RCW Ch. 31.12, under other statutes and the common law, and under CCCU's articles of incorporation and bylaws. The directors of CCCU have fiduciary duties to each member to not obstruct the exercise of their corporate governance rights over CCCU. The defendant directors breached that fiduciary duty by refusing, until ordered to do so by this Court on March 8, 2004, to call a special meeting as required by the petition presented to CCCU's officials by Plaintiffs on January 14, 2004. They then used CCCU funds and resources to prevent a fair and democratic recall election campaign. It is easy to conceive other facts, as well, that justify Plaintiffs' Fiduciary Duty Claim, for the Defendants plainly engaged in various acts that were intended to obstruct and impede the fair and democratic exercise by Plaintiffs of their rights of corporate governance over CCCU.

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Many judicial decisions have recognized that corporate directors have a duty *not* to use the power of their positions to interfere with the governance rights of their corporate principals— the shareholders or members—to have fair elections and votes. That duty recently was discussed by the Delaware Supreme Court in *MM Companies v. Liquid Audio*, 813 A.2d 1118 (Del. 2003), that concluded at 1132:

> The record reflects that the primary purpose of the Director Defendants' action was to interfere with and impede the effective exercise of the stockholder franchise in a contested election for directors. The Court of Chancery concluded that the Director Defendants amended the bylaws to provide for a board of seven and appointed two additional members of the Board for the primary purpose of diminishing the influence of MM's two nominees on a five-member Board by eliminating either the possibility of a deadlock on the board or of MM controlling the Board, if one or two Director Defendants resigned from the Board. That defensive action by the Director Defendants compromised the essential role of corporate democracy in maintaining the proper allocation of power between the shareholders and the Board, because that action was taken in the context of a contested election for successor directors. Since the Director Defendants did not demonstrate a compelling justification for that defensive action, the bylaw amendment that expanded the size of the Liquid Audio board, and permitted the appointment of two new members on the eve of a contested election, should have been invalidated by the Court of Chancery.
>
> One of the most venerable precepts of Delaware's common law corporate jurisprudence is the principle that "inequitable action does not become permissible simply because it is legally possible."[footnote to *Schnell v. Chris-Craft, Indus., Inc.,* 285 A.2d 437, 439 (Del.1971)] At issue in this case is not the validity generally of either a bylaw that permits a board of directors to expand the size of its membership or a board's power to appoint successor members to fill board vacancies. In this case, however, the incumbent Board timed its utilization of these otherwise valid powers to expand the size and composition of the Liquid Audio board for the primary purpose of impeding and interfering with the efforts of the stockholders' power to effectively exercise their voting rights in a contested election for directors. As this Court held more than three decades ago, "these are inequitable purposes, contrary to established principles of corporate democracy . . . and may not be permitted to stand."[*Id.*]

In *Blasius Industries, Inc. v. Atlas Corp.*, 564 A.2d 651 (Del.Ch. 1988), the Court observed the inapplicability of the business judgment rule to conduct that impedes shareholder governance rights, saying at 660:

> [A] decision by the board to act for the primary purpose of preventing the effectiveness of a shareholder vote inevitably involves the question who, as between the principal and the agent, has authority with respect to a matter of

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internal corporate governance. That, of course, is true in a very specific way in this case which deals with the question who should constitute the board of directors of the corporation, but it will be true in every instance in which an incumbent board seeks to thwart a shareholder majority. A board's decision to act to prevent the shareholders from creating a majority of new board positions and filling them does not involve the exercise of the corporation's power over its property, or with respect to its rights or obligations; rather, it involves allocation, between shareholders as a class and the board, of effective power with respect to governance of the corporation. This need not be the case with respect to other forms of corporate action that may have an entrenchment effect — such as the stock buybacks present in *Unocal*, *Cheff* or *Kors v. Carey*. Action designed principally to interfere with the effectiveness of a vote inevitably involves a conflict between the board and a shareholder majority. Judicial review of such action involves a determination of the legal and equitable obligations of an agent towards his principal. This is not, in my opinion, a question that a court may leave to the agent finally to decide so long as he does so honestly and competently; that is, it may not be left to the agent's business judgment.

In *Stahl v. Apple Bancorp, Inc.*, 579 A.2d 1115 (Del. Ch. 1990), the Court observed that it is the duty of the courts to nullify or remedy inequitable conduct by corporate directors, saying:

> It is an elementary proposition of corporation law that, where they exist, fiduciary duties constitute a network of responsibilities that overlay the exercise of even undoubted legal power. Thus it is well established, for example, that where corporate directors exercise their legal powers for an inequitable purpose their action may be rescinded or nullified by a court at the instance of an aggrieved shareholder. The leading Delaware case of *Schnell v. Chris-Craft Industries, Inc.,* Del.Supr., 285 A.2d 437 (1971) announced this principle and applied it in a setting in which directors advanced the date of an annual meeting in order to impede an announced proxy contest.
>
> Under this test the court asks the question whether the directors' purpose is "inequitable." An inequitable purpose is not necessarily synonymous with a dishonest motive. Fiduciaries who are subjectively operating selflessly might be pursuing a purpose that a court will rule is inequitable. Thus, for example, there was no inquiry concerning the board's subjective good faith in *Condec Corporation v. Lunkenheimer Company,* Del. Ch. , 230 A.2d 769 (1967) where this court held that the issuance of stock for the principal purpose of eliminating the ability of a large stockholder to determine the outcome of a vote was invalid as a breach of loyalty. . . . .
>
> Each of these cases dealt with board action with a principal purpose of impeding the exercise of stockholder power through the vote. They could be read as approximating a per se rule that board action taken for the principal purpose of impeding the effective exercise of the stockholder franchise is inequitable and will be restrained or set aside in proper circumstances.

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And in *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del.Supr. 1985), the Delaware Supreme Court observed that directors never may properly use corporate funds primarily out of a desire to perpetuate themselves in office, saying at page 955:

> In the board's exercise of corporate power to forestall a takeover bid our analysis begins with the basic principle that corporate directors have a fiduciary duty to act in the best interests of the corporation's stockholders. *Guth v. Loft, Inc.*, Del.Supr., 5 A.2d 503, 510 (1939). As we have noted, their duty of care extends to protecting the corporation and its owners from perceived harm whether a threat originates from third parties or other shareholders. But such powers are not absolute. A corporation does not have unbridled discretion to defeat any perceived threat by any Draconian means available. .... The restriction placed upon a selective stock repurchase is that **the directors may not have acted solely or primarily out of a desire to perpetuate themselves in office**. [Emphasis added.]

Discovery can be expected to reveal, and the exhibits attached to the Declaration of Doug Schafer in Support of TRO, filed in this proceeding on March 24, 2004, suggests that a number of the actions taken or authorized by the defendant directors were primarily out of a desire to perpetuate themselves in office in breach of their fiduciary duties to CCCU's members.

At page 8 of Defs' 4/5 Memorandum, Defendants make the bald claim that a derivative action "is the only proper way for a shareholder to assert a claim against a director for breach of fiduciary duty." Well, it depends upon whether the fiduciary breach harmed the corporation or harmed certain shareholders directly. In *Strougo v. Bassini*, 282 F.3d 162 (2nd Cir. 2002), the Federal Court of Appeals for the Second Circuit, in a thorough and thoughtful opinion approving direct shareholder claims for breach of fiduciary duty against directors of an investment company (a/k/a *mutual fund*), held at page 171, applying Maryland law:

> Where shareholders suffer an injury that does not stem from an injury to the corporation's business or property... the corporation lacks standing to sue, and Maryland's "distinct injury" rule allows shareholders access to the courts to seek compensation directly.
>
> Thus, under Maryland law, when the shareholders of a corporation suffer an injury that is distinct from that of the corporation, the shareholders may bring direct suit for redress of that injury; there is shareholder standing. When the corporation is injured and the injury to its shareholders derives from that injury, however, only the corporation may bring suit; there is no shareholder standing. The shareholder may, at most, sue derivatively, seeking in effect to require the corporation to pursue a lawsuit to compensate for the injury to the corporation, and thereby ultimately redress the injury to the shareholders.

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1 In the present proceeding, Plaintiffs' Fiduciary Duty Claim does not claim that CCCU as a
2 corporation suffered an injury, but that Plaintiffs and other shareholders suffered harm from
3 Defendants' actions. Thus, a direct shareholder action is appropriate.
4 Washington state's scant case law on shareholder claims for breach of fiduciary duty by
5 corporate officials *does* include one that permitted a direct shareholder action (not a derivative
6 one) against a nonprofit corporation's self-dealing president-director. *Lyzanchuk v. Yakima*
Ranches Owners Association, 73 Wn. App. 1, 10, 12, 866 P.2d 695 (1994).
7
8 **III. Access to Records Claim**

9 Plaintiffs claim a lawful right to examine and copy various records of CCCU.
10 Defendants, at page 10 of Defs' 4/5 Memorandum, flatly deny the existence of any such right,
11 and their actions to date of withholding CCCU's records have been consistent with their denial
12 of any such right. But the Settlement Agreement that CCCU entered into with the Washington
13 State Department of Financial Institutions ("DFI") on February 6, 2004, flatly directs CCCU to
14 make certain of its records available to its members. Exhibit A to Declaration of Linka K. Jekel,
15 Director - Division of Credit Unions, DFI.. (Filed March 8, 2004 in the related mandamus
16 proceeding, Case No. 04-2-00675-2.) The last sentence of paragraph 2.5 of that Settlement
17 Agreement states, "Columbia agrees to make its Bylaws reasonably available to members who
18 request a copy." One can readily conceive from this provision that Plaintiffs may be able,
19 through discovery, to present facts showing that CCCU has wrongfully refused Plaintiffs and
other members access to its bylaws, amendments to its bylaws, and/or other corporate records.
20 At page 10 of Defs' 4/5 Memorandum, counsel cites *State ex rel Wicks v. Puget Sound*
21 *Sav. & Loan Ass'n*, 8 Wn.2d 599, 113 P.2d 70 (1941), for the proposition that the common law
22 right of members of a state credit union to inspect its corporate records has been denied by the
23 Credit Union Act (RCW Ch. 31.12), as the *Wicks* court held inspection rights as denied by the
24 1933 state savings and loan association act. But the *Wicks* case is readily distinguishable not
25 merely due to the differences in the types of corporations and statutory schemes, but because the
26 *Wicks* court placed considerable weight on the fact that an inspection-rights provision in the
regulatory act adopted in 1933 by the legislature was vetoed by the governor and not overridden
27 by the legislature. The *Wicks* case appears to have been followed nationally only once or twice

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in its 63 years. It is essentially tied to the unique history of the 1933 legislation that it interpreted.

But the general common law of Washington and other states plainly permits the owners of a corporation—its shareholders/members—to inspect corporate records for proper purposes. In 1940 the Washington State Supreme Court discussed the corporate records inspection rights of an Arizona corporation's shareholder who had produced a copy of an Arizona statute allegedly granting him inspection rights. In *State ex rel. Grismer v. Merger Mines Corp.*, 3 Wn.2d 417, 101 P.2d 308 (1940), the court said at 420:

> **But even if the statute has been repealed, the common law right of a stockholder to examine the books and records of the corporation at proper times and for proper purposes remains.** *State ex rel.* ***Weinberg*** *v. Pacific Brewing & Malting Co.,* 21 Wn. 451, 58 P. 584, 47 L.R.A. 208; *Guthrie v. Harkness,* 199 U.S. 148, 50 L.Ed. 130, 26 S.Ct. 4.
>
> And, under the common law rule, as it prevails in most states, and under statutes similar to the Arizona statute, the burden of showing improper motives on the part of the shareholder in demanding an inspection of the books and records of the corporation is upon the defendant. It is presumed, until the contrary is shown, that the shareholder seeks the information for a proper purpose. *Ontjes v. Harrer*, 208 Iowa 1217, 227 N.W. 101; *Becker v. LeMars Loan & Trust Co.*, 217 Iowa 17, 250 N.W. 644; *Knox v. Coburn*, 117 Me. 409, 104 A. 789; *Dines v. Harris*, 88 Colo. 22, 291 P. 1024; *William Coale Development Co. v. Kennedy*, 121 Ohio St. 582, 170 N.E. 434. **This is the rule that prevails in this state.** *State ex rel.* ***Weinberg*** *v. Pacific Brewing & Malting Co.,* 21 Wn. 451, 58 P. 584, 47 L.R.A. 208; *State ex rel. Lee v. Goldsmith Dredging Co.,* 150 Wn. 366, 273 P. 196. And we will presume that the same rule prevails in Arizona, in the absence of evidence to the contrary. [Emphasis added.]

A comprehensive survey of the national corporate common law on the inspection rights of shareholders was presented in *Tucson Gas & Electric Company v. Schantz*, 5 Ariz. App. 511, 428 P.2d 686 (1967). The court wrote, at 513-14:

> The common law rule as to a shareholder's right of inspection is that every shareholder has the right, by reason of his interest therein, to inspect the books and papers of a corporation at reasonable times and places and for proper purposes. 5 Fletcher, Cyclopedia Corporations § 2214 (1952). It is thus seen that this right is not an absolute one but rather a qualified one. The basis of a shareholder's right to inspect the books and records of a corporation is his ownership of the corporate property and assets through his ownership of shares; as an owner, he has the right to inform himself as to the management of the corporate property by directors and officers who are his trustees in direct charge of the property. *Guthrie v. Harkness,* 199 U.S. 148, 26 S.Ct. 4, 50 L.Ed. 130

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(1905); *William Coale Development Co. v. Kennedy,* 121 Ohio St. 582, 170 N.E. 434 (1930); *Wise v. H.M. Byllesby & Co.,* 285 Ill. App. 40, 1 N.E.2d 536 (1936); *State ex rel. Boldt v. St. Cloud Milk Producers' Ass'n,* 200 Minn. 1, 273 N.W. 603 (1937); 5 Fletcher, Cyclopedia Corporations § 2213 (1952); *State ex rel. Lowell Wiper Supply Co. v. Helen Shop, Inc.,* 211 Tenn. 107, 362 S.W.2d 787 (1962). As stated in *William Coale Development Co., supra*:

> "Can anything be plainer than the fact that the owner of property has a clear right to inspect his own property? When the owner of property selects an agent or agents to care for and manage his property, how can that act be held to clothe the agent with power to manage the owner as well as to manage the property, and to prevent the owner from even looking at his own property except he do so pursuant to the rules and restrictions promulgated by the agent, who was wholly without power or authority to formulate any such rules or regulations? Are we to forget and abandon all the law pertaining to the relation of principal and agent?"

Generally speaking, the right of a stockholder extends to all books, papers, contracts, minutes or other instruments from which he can derive any information that will enable him to protect his interest. 5 Fletcher, Cyclopedia Corporations § 2239 (1952); 18 Am.Jur.2d Corporations § 199; Annotations: 22 A.L.R. 24, 82; 43 A.L.R. 783, 788; 59 A.L.R. 1373, 1380; 80 A.L.R. 1502, 1514; 174 A.L.R. 262, 286; 18 C.J.S. Corporations § 506.

This common law right of inspection is a remedial right which exists independently of statute. *State ex rel. G.M. Gustafson Co. v. Crookston Trust Co.,* 222 Minn. 17, 22 N.W.2d 911 (1946). Statutes providing for a shareholder's right of inspection have been construed as enlarging or extending the common law right rather than as a restriction or abrogation of the right of inspection. 18 Am.Jur.2d Corporations § 179; 18 C.J.S. Corporations § 502; 5 Fletcher, Cyclopedia Corporations § 2215 (1952); *Bishop's Estate v. Antilles Enterprises,* 252 F.2d 498 (3d Cir. 1958); *State ex rel. Grismer v. Merger Mines Corporation,* 3 Wn.2d 417, 101 P.2d 308 (1940); *State ex rel. McClure v. Malleable Iron Range Co.,* 177 Wis. 582, 187 N.W. 646, 22 A.L.R. 5 (1922); *State ex rel. Lowell Wiper Supply Co. v. Helen Shop, Inc., supra*; *Texas Infra-Red Radiant Company v. Erwin,* 397 S.W.2d 491 (Tex.Civ.App. 1965); *Matter of Steinway,* 159 N.Y. 250, 53 N.E. 1103, 45 L.R.A. 461 (1899).

And the highest New York appellate court similarly has recognized the common law inspection rights of shareholders of a federal savings and loan association, in *Matter of Ochs v. Wash. Hgts. F.S. & L. Assn.*, 17 N.Y.2d 82, 268 N.Y.S.2d 294, 215 N.E.2d 485 (1966), saying at 86:

> [A] Federal savings and loan association is an instrumentality of the United States and, more precisely, a creature of the Home Owners' Loan Act of 1933. For this reason no New York statute is directly applicable to the supervision and control

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> of its internal management. However, the enactment in this State of such statutory corporate controls as the Business Corporations Law (1875), the General Corporation Law (1892), the Stock Corporation Law (1892) and the Business Corporation Law (1961) in no way diminished the common-law safeguards already existent in this area of shareholder inspection. This court clearly so held in *Matter of Steinway* (159 N.Y. 250, 264-265 [1899]). As Judge Vann wrote: "We do not think that the statute now in force is exclusive, or that it has abridged the common-law right of stockholders with reference to the examination of corporate books. By enabling a stockholder to get some information in a new way, it did not impliedly repeal the common-law rule which enabled him to get other information in another way, for the courts do not hold the common law to be repealed by implication, unless the intention is obvious. By simply providing an additional remedy the existing remedy was not taken away. The statute merely strengthened the common-law rule with reference to one part thereof, and left the remainder unaffected." See, also, the recent case of *Sivin v. Schwartz* (22 A.D.2d 822 [2d Dept., 1964]) wherein the court stated that "In our opinion, that statute is not exclusive; and any stockholder, including one not of record, has a common-law right to inspect the stock books if the inspection is sought in good faith and for a valid purpose." [Citations omitted.]

Washington statutes codifying certain shareholder inspection rights can be found at RCW Ch. 23B.16, RCW 24.03.135, and RCW 30.12.025, but none of them preclude a shareholder's common law inspection rights as recognized in *Grismer* and *Weinberg, supra.*

V. The No Enabling Law Claim

At page 10 of Defs' 4/5 Memorandum, Defendants seek dismissal of the No Enabling Law Claim because, "Plaintiffs do not allege that Columbia is undergoing a conversion or that one is imminent or planned." The legal standard for review of CR 12(b)(6) motions requires no factual allegation, but only that such a set of facts is *conceivable*. Though discovery may reveal more telling facts, the facts that now are public suggest that Defendants' bank conversion plans may not be abandoned. They formally adopted their Plan of Conversion by resolutions on April 15, 2003 *after studying the conversion proposal for nine months*. Letter (pg. 3) of CCCU Counsel Brian Witt dated January 13, 2004, (**"Witt Letter"**) being Exhibit A to Declaration of Doug Schafer in Support of Motion for Summary Judgment on Term-Limited Directors Issue filed April 2, 2004 in this proceeding. That Plan of Conversion with its adopting resolutions is Exhibit B to Schafer Declaration of 4/15.

After the National Credit Union Administration ("NCUA") announced by letter of

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January 29, 2004, that it disapproved of the manner the membership vote on the Plan of Conversion was handled, Defendants the next day announced in a news release that they "might decide to place the vote before our membership again." Exhibit C to Schafer Declaration of 4/15. Defendants subsequently negotiated the Settlement Agreement with DFI that included a provision, at paragraph 2.5, that limited CCCU's power to amend its bylaws "until after Columbia's Annual Meeting in 2005 or conversion of Columbia to another form of charter, whichever occurs first." That plainly suggests that Defendants' plans to convert CCCU "to another form of charter," such as that of a bank, have not been abandoned.

What's more, the Federal Deposit Insurance Corporation's formal order dated October 10, 2003, approving CCCU's application for bank deposit insurance does not expire for one year from that date. Exhibit D to Schafer Declaration of 4/15. Again, that suggests that Defendants' charter conversion options for CCCU remain open.

Thus, the readily available evidence suggests that the Defendants have not completely abandoned their plan of converting CCCU to a savings bank or "another form of charter."

Also at page 10 of Defs' 4/5 Memo, Defendants ever-so-briefly suggest that Plaintiffs' No Enabling Law Claim should be dismissed based upon their lack of standing or the absence of a justiciable controversy.

In *Grant Co. Fire Prot. Dist. v. Moses Lake*, 145 Wn.2d 702, 42 P.3d 394 (2002), the Court addressed the *standing* requirement in the context of a declaratory judgment claim, saying at 712:

> Standing to seek a declaratory judgment is addressed by statute, the Uniform Declaratory Judgments Act (UDJA), chapter 7.24 RCW:
>
> > A person . . . whose rights, status or other legal relations are affected by a statute, municipal ordinance, contract or franchise, may have determined any question of construction or validity arising under the instrument, statute, ordinance, contract or franchise and obtain a declaration of rights, status or other legal relations thereunder.
>
> RCW 7.24.020. To establish harm under the UDJA, a plaintiff must present a justiciable controversy premised on allegations of harm personal to him/her that are substantial and not conjectural or speculative. *Walker v. Munro*, 124 Wn.2d 402, 411, 879 P.2d 920 (1994). The common law doctrine of standing clarifies the statutory right, prohibiting a litigant from raising another's rights. *Id.* at 419.
>
> This court has established a two-part test to determine standing under the UDJA. The first part of the test asks whether the interest the complainant seeks to

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protect is "'arguably within the zone of interests to be protected or regulated by the statute or constitutional guarantee in question.'" *Save a Valuable Env't v. City of Bothell,* 89 Wn.2d 862, 866, 576 P.2d 401 (1978) (quoting *Ass'n of Data Processing Serv. Orgs., Inc. v. Camp,* 397 U.S. 150, 152-53, 90 S.Ct. 827, 25 L.Ed.2d 184 (1970)). The second part of the test considers whether the challenged action has caused "injury in fact" to the complainant. *Id.*

The focus of the "zone of interest" test is whether the statute was designed to protect the interests of the plaintiff. In evaluating standing to challenge a previous version of chapter 35.13 RCW, this court held that "[i]t is undisputed that the residents of the area proposed for annexation would have standing to raise the equal protection claim." *City of Seattle v. State,* 103 Wn.2d 663, 669, 694 P.2d 641 (1985). This court has held that residents operating a business and owning property within an area to be annexed have a clear interest in the proceedings and have standing. *State ex rel. Thigpen v. City of Kent,* 64 Wn.2d 823, 825, 394 P.2d 686 (1964). *See also Seattle*, 103 Wn.2d at 669 (holding that both residents and municipalities acting on behalf of their residents have standing to raise constitutional issues).

The "injury in fact" test focuses on whether a plaintiff has suffered an actual injury. It is axiomatic that parties whose financial interests are affected by an action have suffered injury. *Seattle Sch. Dist. No. 1 v. State*, 90 Wn.2d 476, 493, 585 P.2d 71 (1978) (holding that a school district has standing when legislation involves "actual financial restraints"); *see also Am. States Ins. Co. v. Breesnee,* 49 Wn. App. 642, 645-46, 745 P.2d 518 (1987) (holding that injured party's uninsured motorist carrier had standing in declaratory judgment action between responsible party and his liability insurer).

And in the case of *Lawson v. State*, 107 Wn.2d 444, 730 P.2d 1308 (1986), the Washington State Supreme Court discussed the requisite elements for a *justiciable controversy* in the context of a declaratory judgment case, saying at 460:

Absent issues of major public importance, a "justiciable controversy" must exist before a court's jurisdiction may be invoked under the Uniform Declaratory Judgments Act, RCW 7.24.020. *DiNino v. State ex rel. Gorton,* 102 Wn.2d 327, 330, 684 P.2d 1297 (1984).

A "justiciable controversy" is

(1) . . . an actual, present and existing dispute, or the mature seeds of one, as distinguished from a possible, dormant, hypothetical, speculative, or moot disagreement, (2) between parties having genuine and opposing interests, (3) which involves interests that must be direct and substantial, rather than potential, theoretical, abstract or academic, and (4) a judicial determination of which will be final and conclusive.

DiNino, at 330-31 (quoting *Clallam Cy. Deputy Sheriff's Guild v. Board of Clallam Cy. Comm'rs,* 92 Wn.2d 844, 848, 601 P.2d 943 (1979)). All four of these elements must be satisfied or the case must be dismissed; otherwise, the

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court steps into the prohibited area of advisory opinions. *DiNino v. State ex rel. Gorton, supra* at 331.

Given that a conversion of CCCU to a state savings bank would strip Plaintiffs of all of their rights of corporate governance over CCCU and would strip them of their legal right to share in the liquidation proceeds of any future liquidation of CCCU, it plainly appears that the standing and justiciable controversy tests are met. And whether or not either test is otherwise met, Division II of the Washington Court of Appeals very recently held that the "overlapping" standing and justiciable controversy showings are unnecessary if the claim sought to be adjudicated is an issue of *major public importance*. In *Kightlinger v. Public Utility Dist. No. 1*, 119 Wn. App. 501, 81 P.3d 876 (2003), the appellate court (upholding this trial court) declared it of substantial public concern the issue of whether a Clark County public utility district had authority to repair appliances other than those it sold, since "The issue reaches beyond Clark County. Other PUDs, statewide, could engage in the same or similar businesses." 119 Wn. App. at 508 n.3.

Given that CCCU alone has about 60,000 members, and that three other substantial Washington state credit unions already have purported to convert in the last three years to bank charters and more purported credit union-to-bank conversions are possible, the issue of whether such conversions are permitted by Washington state law is of major public importance.

The No Enabling Law Claim should not be dismissed under CR 12(b)(6).

VI. The Supermajority Vote Claim

On pages 2 and 10 of Defs 4/5 Memorandum, Defendants treat the No Enabling Law Claim and the Supermajority Vote Claim as a single claim for purposes of Defendants' motion to dismiss under CR 12(b)(6). While they are two separate and distinct claims, the reasoning and analysis given above why the former ought not be dismissed under CR 12(b)(6) are also applicable to the latter. It is worth noting (in the public interest) that Plaintiff's legal theory for challenging Defendants' claimed power to *invoke* the laws of foreign jurisdictions—substituting them for the laws of Washington state—as to "powers and authorities in corporate governance matters" under RCW 31.12.404 would also apply to similar so-called *parity provisions* that DFI has arranged in recent years to be included within the following RCW sections: 30.04.215 (for

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commercial banks), 30.04.217 (for bank trust departments), 30.08.155 (for trust companies), 31.13.020 (for corporate credit unions), 32.08.142 (for mutual savings banks), 32.08.146 (for mutual savings banks), 32.08.155 (for mutual savings banks), 32.08.157 (for mutual savings banks), 33.12.012 (for savings associations), and 33.12.014 (for savings associations).

Adjudication of Plaintiffs' Supermajority Voting Claim is of major public importance.

VII. The Term Limits Claim

In partial response to Defendant's motion for summary judgment (and for dismissal under CR 12(b)(6)), Plaintiffs trust the Court will consider Plaintiffs' Motion for Summary Judgment of Term-Limited Directors and Memorandum in Support Thereof, filed on April 2, 2004, in this proceeding (**"Plaintiffs' S/J Motion"**). In addition to it, Plaintiff will respond below to Defendants' defenses to the Term Limits Claim raised at pages 3-5 and 11-13 of Defs' 4/5 Memorandum.

Defendants assert the doctrine of judicial estoppel bars Plaintiffs from seeking enforcement of CCCU's Bylaws term-limit qualification for directors because Plaintiffs had referred to the challenged directors in prior pleadings to this court as "directors." Under the circumstances, that is a silly argument. Defendants and their respected counsel have consistently claimed that they are properly holding their CCCU directorships, and they have not readily revealed information (even when requested) that would enable CCCU members to ascertain if their tenure as directors is consistent with the Bylaws term-limit director qualification provision.

Plaintiffs first sought to bring about their removal by means of the special meeting vote, but the manner in which Defendants conducted, and campaigned against, the recall vote left them claiming entitlement to their directorships. Accordingly, Plaintiffs now are seeking judicial enforcement of the CCCU Bylaws term-limit qualification for directors provision. Plaintiffs have taken no inconsistent positions that warrant the application of the judicial estoppel doctrine.

Even if the five challenged CCCU directors are found ineligible to continue serving as directors, their recent service in those directorships may have been as "de facto" directors. The de facto director doctrine is widely recognized by courts as applicable to save from invalidation actions taken by individuals while acting as corporate directors when it later is learned that they were not eligible to be in their position. The South Dakota Supreme Court described and applied

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that doctrine in *Forest Home Cemetery v. Dardanella Fin. Corp.*, 329 N.W.2d 885 (1983), saying at 888:

> The law is clear that the actions of "de facto" directors of a corporation are valid and binding as to third parties. Henn, Law of Corporations § 206 (1970); 19 Am.Jur.2d Corporations § 1103 (1965). A "de facto" director is one in possession of and exercising the powers of the office under the claim and color of an election or appointment although he is not an officer or director "de jure." 19 Am.Jur.2d Corporations § 1100 (1965). Though an individual elected as a director of a corporation may fail to meet the statutory requirement of owning stock in the corporation, that individual may act as a de facto director. *Id.* at § 1102. Here, Forest Home's directors did not initially own lots in the cemetery as required by SDCL 47-29-6. They were, however, in the possession of and exercising the powers of the office of directors under the claim and color of appointment and thus were "de facto" directors. As "de facto" directors, their action in initiating this quiet title suit is valid.

It should be noted, however, that a recent opinion by the Washington Court of Appeals, Div. II, ruled *invalid* the actions of a nonprofit corporation's architectural control committee the members of which did not meet the qualifications stated in the corporation's own bylaws. *Hartstene Pointe Maintenance Ass'n v. Diehl*, 95 Wn. App. 339, 979 P.2d 854 (1999). No mention was made in that opinion of the de facto director or officer doctrine.

On page 5 of Defs' 4/5 Memorandum, Defendants argue that the CCCU term-limits Bylaws language "is properly construed as acting prospectively only." The starting point of analysis is the statute that permits state credit unions to impose qualifications for directors. RCW 31.12.235(3) states:

> (3) A director must meet any qualification requirements set forth in the credit union's bylaws. If a director fails to meet these requirements, the director shall no longer serve as a director.

The Revised Model Nonprofit Corporation Act (ABA Bus. L. Section, M. Hone, Reporter; 1987) provides at Section 8.02, "All directors must be individuals. The articles or bylaws may prescribe other qualifications for directors." And the Official Comment to that section states the common corporate law rule, "If a qualification adopted after the director's term commences would disqualify a director, it cannot be enforced until after the end of the directors's term." Thus, a newly adopted qualification limiting a director's service on the board could not be applied to an incumbent director until after the end of their current term—but would be enforced

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1 at the next election for their position, possibly barring the incumbent from re-election.

2 Such an application of the term-limit director qualification provisions in CCCU's Bylaws
3 makes good sense. One must assume that the purpose why the CCCU Board of Directors in
4 November 1999 adopted the term limits Bylaws amendments was to bring cause a healthy
5 degree of turnover on the board of directors. At that time, incumbent director Connie Jones was
6 one year into her seventh three-year term, so the application of the new qualification provision to
7 her at the next election for her position would require her to retire at the end of that seventh term
8 in March 2002 with 21 years of board service. For incumbent director Bob Byrd, then in his
9 third term (but his first term having been only two years so presumably not counted as a full
10 term), the new qualification provision would require his retirement from the board in March of
11 2003 with 11 years of service. For incumbent director Dennis McLachlan, then in his third
12 three-year term, the new qualification provision would require his retirement from the board in
13 March 2001 with 9 years of board service. For incumbent director Mark Ail, then in his second
14 term, the new qualification provision would require his retirement from the board in March,
15 2003, with nearly 9 years of board service (assuming his first term of two-and-a-half years is
16 counted as a full term). For incumbent director William Byrd III, then in his second term, the
17 new qualification provision would require his retirement from the board in March, 2004 with
18 about 9.5 years of board service.

19 In contrast, if the interpretation that Defendants *now* are suggesting were applied to the
20 challenged directors—to only count their terms beginning with their next re-election after
21 November 1999—the effect of the 1999 term-limit Bylaws amendment would have been to limit
22 Connnie Jones to **30 years**; Bob Byrd to **20 years**; Dennis McLachlan to **20 years**; Mark Ail to
23 **15.5 years**; and Wm. Byrd III to **15.5 years**. Such a result would have been patently inconsistent
24 with the very purpose for adopting the term limit director qualification—to cause a healthy
25 degree of turnover on the board.

26 If the 1999 term limit director qualification provision is given the natural application
27 suggested above—applying to each candidate in each election after its adoption—then
challenged directors Connie Jones, Bob Byrd, Dennis McLachlan, and Mark Ail are no longer
serving lawfully on CCCU's board, and William Byrd III would now be at the end of his period
of permitted service and ineligible to seek re-election at the upcoming 2004 annual meeting.

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At page 12 of Defs' 4.5 Memo, Defendants claim that the now alleged intent of the members of CCCU's 1999 Board of Directors should control. But since corporate bylaws are recognized as a contract between the corporation and its shareholders/members, and since CCCU denies its members access to its Board meetings or records of them, its seems that the unilateral and secret intent of CCCU's directors ought be of little significance. Of controlling significance should be the plain meaning to be gleaned from the term limit director qualification provision by any CCCU member who now obtains a copy of its Bylaws and reads that provision. In stark contrast to public laws that are made in the open, where evidence of true legislative intent can be documented and archived for public retrieval, the secrecy surrounding CCCU's Board of Directors actions means that evidence of their actual intent in amending the Bylaws may never be known.

At page 13 of Defs' 4/5 Memorandum, Defendants claim support for their interpretation of term limit director qualification provision from the fact that the incumbents have been elected without opposition at each annual meeting of the CCCU members. While "elected" may be the proper corporate term, no actual election has occurred in decades, it appears from a review of the many years of annual meeting minutes included in the Stipulation re Term of Board Service of Board Members (the undersigned having yet seen but a draft of that Stipulation). In actuality, the Board's nominating committee always re-nominates only the incumbent directors, and no member has ever undertaken the onerous task of collecting 500 member signatures on a petition to nominate another board candidate. So at each annual meeting, at which the average attendance was but 54 (per the Witt Letter, page 1), the Chair simply declared the committee-nominated incumbent directors to be re-elected by acclamation. That "re-election" procedure was certainly not a membership mandate for any incumbent director.

For the reasons explained above and in the Plaintiff's S/J Motion, the Defendant's motion for summary judgment and motion to dismiss under CR 12(b)(6) should be denied.

Date: April 15, 2004

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