NELSON MASANG,
Plaintiff,

v.

SAM Y. MASANG,
Defendant.

CIVIL ACTION NO. 10-039

Supreme Court, Trial Division
Republic of Palau

Decided: March 18, 2011

[1] **Corporations and Partnerships:** Dissolution

Where a partnership is "at will," any partner may dissolve it as long as the dissolving partner gives notice to the copartner of the intent to dissolve the partnership.

[2] **Corporations and Partnerships:** Dissolution

Actual dissolution of a partnership vitiates any need for judicial dissolution.

[3] **Corporations and Partnerships:** Dissolution

Dissolution does not end the partnership, but instead commences a period of winding up.

[4] **Corporations and Partnerships:** Winding up

Typically, the wind-up involves selling the business's assets, paying its debts, and distributing the net balance, if any, to the partners in cash according to their interests.

[5] **Corporations and Partnerships:** Accounting

An accounting typically runs hand-in-hand with dissolution and winding up. An accounting is an action to determine the rights and liabilities of the partners. The goal of an accounting is to ascertain the value of the partners' interest in the partnership as of a particular date, typically the date of dissolution, and to determine the existence of any profits or losses.

[6] **Corporations and Partnerships:** Accounting

Actions for accounting of partnership assets and liabilities lie in equity.

[7] **Corporations and Partnerships:** Accounting

Where neither party established that he was denied access to business records and an accounting prior to trial, there is no right to a court-ordered accounting.

[8] **Corporations and Partnerships:** Receipt of assets

The liabilities of the partnership are to be resolved prior to any partner receiving part of the firm's assets.

[9] **Corporations and Partnerships:** Misappropriation of assets

One partner cannot generally maintain an action at law against a copartner for a misappropriation of partnership moneys.

[10] **Corporations and Partnerships:**

Wrongful dissolution

No claim for wrongful dissolution will lie where partnership was one at will.

[11] **Damages:** Punitive Damages

Punitive damages is defined as damages, other than compensatory or nominal damages, awarded against a person to punish him for his outrageous conduct and to deter him and others like him from similar conduct in the future.

[12] **Damages:** Punitive Damages

Factors to be considered in assessing punitive damages include the character of the defendant's act, the nature and extent of the harm to the plaintiff that the defendant caused or intended to cause and the wealth of the defendant.

[13] **Damages:** Punitive Damages; **Corporations and Partnerships:** Availability of punitive damages

Punitive damages in a partnership context are awarded based on malice or acts undertaken with wanton and reckless disregard to the rights of others.

Counsel for Plaintiff: Kevin Kirk
Counsel for Defendant: Mark P. Doran

ALEXANDRA F. FOSTER, Associate Justice:

I. FINDINGS OF FACT

In February 2004, Plaintiff Nelson Masang approached his adoptive brother, Defendant Sam Masang,[1] to form a partnership to sell automotive parts. (Pl.'s Ex. 2.) As a long-time businessman, Sam had the money and business acumen, and Nelson had the specific knowledge and contacts within the NAPA automotive parts industry. The business, NS Auto Parts Supply International ("NS Auto Parts"), was a sub-distributor for NAPA brand auto parts in Palau under an agreement with Bisnes-Mami Inc., a Guam corporation. The agreement specified that Nelson and Sam were each 50% owners of the business. The business was located on Sam's property, and he was paid $2,000 per month in rent. Nelson was the managing partner of NS Auto Parts, receiving a monthly salary of $2,400.[2] Sam was not involved in the day-to-day operations, but he regularly reviewed business records to keep apprised of the sales, inventory and payments.

NAPA (through Bisnes-Mami, Inc.) provided NS Auto Parts with inventory and computers. Sam and Nelson took out loans to cover payments for inventory, staffing and other expenses. In June 2006, Sam and Nelson "rearranged" their debts and secured a $308,394.57 loan from the National Development Bank of Palau (NDBP). This new loan was motivated in part by a requirement to pay $249,000 to Bisnes-Mami, Inc. for inventory. As collateral for the loan, Sam mortgaged his property in Malakal,

[1] Because the parties share the same last name, the Court will distinguish them by using their first names.

[2] Nelson was the right choice for managing partner since he had worked for NAPA distributorships and subdistributorships both in Guam and Palau for 12 years before starting this business in 2004.

including his buildings and his home, and Sam and Nelson executed a chattel mortgage over the assets and inventory of NS Auto Parts. Both Sam and Nelson are jointly and severally liable for repayment of the loan.

While NS Auto Parts was able to service its debts, and cover its employees' salary and overhead costs, it was not a profitable endeavor. Sam received rent and Nelson his salary, but the parties never split any business profits.

In June 2006, Nelson borrowed $4,000 from the NS Auto Parts to purchase a van. Soon thereafter, he turned the van over to the partnership as a delivery vehicle. $ 150 was deducted from his biweekly paycheck to repay that loan, even after the van had been bequeathed to NS Auto Parts. Sales in 2008 and 2009 were particularly poor. Although Nelson concedes that the business was not profitable, he could not recall specifics about how much money the business was losing each month, nor could he recall how much money the company paid on its monthly debts. He testified that the accountant prepared the checks, and he signed them. Sam held several conversations with Nelson about the poor profitability of their joint endeavor, but Sam did not volunteer ideas for maximizing revenue or minimizing liabilities. At no point did Sam warn Nelson that he was going to end the partnership if it did not turn the corner and become profitable.

On March 20, 2009, Sam sent Nelson a letter stating, in relevant part, that NS Auto Parts has not been a profitable business since its inception, and that he faced the possibility of losing his property, as well as the inventory of the store, upon foreclosure. (Pl.'s Ex. 31.) With that, Sam wrote that he had "no choice" but to relieve Nelson of his duties as manager:

> Effective as of Friday, March 27, 2009, you will be on 'paid' leave and will not need to go to the Auto Parts Store until further notice, or as you may be needed .... I also formally request you to provide me with all keys for all locks for the doors, and any keys for any filing cabinets or other locks for the premises, by March 27th. After the assessment by NAPA representatives, they will help me to make a decision as to whether or not the NAPA Auto Parts Store will remain open, or will be permanently closed.
>
> . . . . After receiving the assessment from the NAPA representatives, I will be able to decide if we will need to dissolve our partnership arrangement, and we will need to settle accounts between us relating to the NAPA Auto Parts business.

Nelson was surprised by Sam's letter—according to Nelson, although Sam had previously complained of nonexistent profits, he had not pinned that problem on Nelson's management of the business. After several attempts at speaking with Sam proved fruitless, Nelson retained legal counsel. (Pl.'s Ex. 33.)

On March 27, 2009, Sam sent another

letter to Nelson stating, in relevant part:

> After 5:00 PM today, I will put a chain and padlock on the door of the store until further notice. Furthermore, our partnership together will terminate immediately by next week, unless you cooperate in full according with my letter to you dated March 20, 2009. In addition, if you do not respond by Monday morning, March 30, 2009, then NS Auto Parts will remain closed until we liquidate all assets and liabilities of the company.

Sam followed through on his threat and locked Nelson out of the business on March 27, 2009, because apparently Nelson did not "cooperate in full." Nelson did not attempt to return to work after Sam locked the doors on March 27. Further, Nelson did not "respond" to Sam's satisfaction by March 30. Nelson received his last paycheck on that date. After March 27, Sam assumed all assets and liabilities of the partnership, but did not liquidate them as promised. Instead, Sam entered a new NAPA distribution agreement with the successor to Bisnes-Mami, Inc., in May 2009.

Sam contends that while he attempted to work with Nelson regarding the wind-up, Nelson refused to respond. Conversely, Nelson contends that Sam simply took possession of the partnership assets and failed to provide him with an accounting or payment.

II. ANALYSIS AND CONCLUSIONS OF LAW

A. Parties' Claimed Damages and Relief

The parties seek relief on several grounds. In his complaint, Nelson seeks:

> (1) judicial dissolution of the partnership;
> (2) an accounting by the defendant of all dealings and transactions involving the partnership since March 27, 2009;
> (3) an order requiring liquidation of all partnership property and the proceeds divided among the parties according to their interests; and
> (4) "compensatory damages, punitive damages, and attorneys fees."

In his counterclaim, Sam seeks:

> (1) a decree that the partnership was dissolved in March 2009;
> (2) a decree that the parties voluntarily agreed to dissolve the partnership, with Nelson taking benefits as may be proven, and Sam undertaking liabilities and benefits as may be proven;
> (3) an accounting of the partnership assets and liabilities;
> (4) an accounting of partnership assets wrongfully converted by Nelson and restoration of such property;
> (5) an accounting of the contributions made to the partnership by Sam Masang and judgment that Nelson owes Sam for such contributions;
> (6) an accounting of all partnership losses and entry of judgment against Nelson; and

(7) general damages, punitive damages, costs, and attorneys' fees.

B. Dissolution

[1] The parties were each half-owners of the business, and the partnership maintained no fixed term of operation or aimed at completing a particular undertaking (other than perpetually selling auto parts). The partnership was therefore "at will," and either partner could dissolve it as long as the dissolving partner gave "notice to the copartner of the intent to dissolve the partnership." *See* 59A Am. Jur. Partnership § 82.

Sam unambiguously gave notice of his intent to dissolve the partnership on March 27, 2009. By locking Nelson out of the business on that same date, Sam caused the dissolution of the partnership. *See id.* § 569 ("Dissolution is ... available on grounds of the wrongful or forcible exclusion of one partner from the place of business of the firm."). *Cf. Platt v. Henderson,* 361 P.2d 73, 80 (Or. 1961) (partnership was dissolved when defendant left the firm's offices and moved to his new quarters). Sam then entered into a new agreement to distribute NAPA auto parts in May 2009; NS Auto Parts –Sam and Nelson's partnership– was no longer operational as of May 2009.[3]

[3] Sam points to 59A Am. Jur. Partnership § 569 as grounds for judicial dissolution based on the expulsion of a partner. However, the provision assumes that the partnership continued in the absence of the excluded partner. Here, though Sam assumed the assets and liabilities of the business, NS Auto Parts no longer existed as a business entity by the time Sam filed his counterclaims.

[2] Sam's dissolution of the partnership on March 27, 2009, vitiates any need for judicial dissolution, as requested by Nelson. *See* 59A Am. Jur. Partnership § 561 ("A prerequisite to the judicial dissolution of a partnership is its actual existence at the time dissolution is sought.").

C. Wind-Up

[3, 4] Inasmuch as Sam expelled Nelson from the business in March 2009, he violated Nelson's right to participate in the wind-up and termination of NS Auto Parts. *Id.* § 704 (All partners have a right to wind up the partnership's affairs.). "Dissolution does not end the partnership, but instead commences a period of winding up." *Id.* § 584. Typically, the wind-up involves "selling [the business's] assets, paying its debts, and distributing the net balance, if any, to the partners in cash according to their interests." *Id.* § 550; *see also id.* § 702 (discussing the wind-up process). What distinguishes the facts in this case from those cited in every other partnership wind-up case is that the partnership here was not profitable, and therefore the main reason for a wind-up, namely the disgorging of profits to the partners in equitable shares, does not hold true here.

Nelson's inability to participate in the wind-up would normally entitle him to a share of any profits received during the wind-up process. Accordingly, Nelson seeks an accounting of the business after March 27, 2009. However, NS Auto Parts was never a profitable business. Though Nelson received a salary for his work as manager, and Sam received rent for the business's use of his property, no actual profits were ever split

amongst the partners. Moreover, there is nothing in the record indicating that NS Auto Parts was on the verge of becoming a profitable business after March 27, 2009. To the contrary, the income statements for March, April and May 2009 show the business repeatedly losing money.

As the partner in control of the business after dissolution, Sam is the only one who could have supervised the wind-up process, but he failed to initiate a proper wind-up of NS Auto Parts—though he indicated in his letters to Nelson that he intended to do so. Instead, he just converted the assets of NS Auto Parts into his new business. Had Sam properly performed a wind-up by liquidating the assets of NS Auto Parts, the Court would have a basis for determining the amount due, or owing, to each partner. Such a determination is impossible at this juncture –two years after the dissolution of the business. Further, the parties have offered no analysis of the March 2009 business records, which both parties apparently had access to prior to trial, to support a proposed division.

D. Accounting

[5-6] An accounting typically runs hand-in-hand with dissolution and winding up. *See, generally,* 59A Am. Jur. Partnership § 667. It is "an action to determine the rights and liabilities of the partners. The goal of an accounting is to ascertain the value of the partners' interest in the partnership as of a particular date, typically the date of dissolution, and to determine the existence of any profits or losses." *Id*. Actions for accounting of partnership assets and liabilities lie in equity. *See id.* § 669. Because an accounting would be impossible based on the numbers tendered, and a dissolution would be financially disadvantageous for both parties, there is no good reason to order an accounting, liquidation and distribution of assets and losses under the circumstances.

[7] First, because neither party established that he was denied access to the March 2009 business records and an accounting prior to trial, there is no right to a court-ordered accounting. 59A Am. Jur. Partnership § 379 ("In order to enlist the aid of a court of equity in vindicating a right to accounting, the [movant] must show (1) a [timely] demand for the accounting; and (2) the failure or refusal by the partner with the books, records, or other assets of the partnership in his or her possession to account to the other partner or partners."); *see also id.* § 676 ("[A]n essential element of an action for accounting on the dissolution or termination of a partnership is a prior demand for an accounting and a failure or refusal to account by the partner with the books, records, profits or other assets of the partnership in his or her possession."). Obviously, Sam had access to the documents and could "determine the existence of any profits or losses" without the aid of a court order. As for Nelson, it appears that he declined to play a role in the "assessment," which Sam proposed in his March 20 letter, and nothing in the record reflects that he demanded an accounting thereafter.

Moreover, the records submitted to the Court provide only a speculative basis for an accounting (and subsequent division of assets and liabilities), which is insufficient. For instance, the NS Auto Parts' balance sheets submitted by the parties indicate values for the business's assets, inventories and liabilities, but Sam testified credibly that these numbers

are not accurate. Sam provided alternative, significantly lower numbers based on a third party's assessment, but Nelson rightly pointed out the difficulty of reliance upon these numbers when the third party was not available for testimony or cross-examination at trial. In sum, neither side provided viable numbers upon which the Court, or even better an accountant, could rely to reach a proper accounting of the assets and liabilities of this partnership in March 2009.

[8] Finally, even if the Court were provided a basis to distribute assets and liabilities based on each party's interest, it is unlikely that either party would benefit financially. The liabilities of the partnership are to be resolved prior to any partner receiving part of the firm's assets. 59A Am. Jur. Partnership § 764. Therefore, if liquidation of the assets and inventory was ordered (which would likely result in a substantial loss on investment), creditors such as NDBP would be repaid first. It appears that the liabilities of NS Auto Parts as of March 2009 matched or exceeded outstanding liabilities, and no one presented evidence to prove otherwise.[4]

Nelson's request for an accounting of business assets and liabilities after March 27, 2009, is therefore denied as he would receive no benefit from such an accounting. Sam's requests for an accounting is also denied because he has presented no evidence that such a court order is necessary. Importantly, he has cited no authority requiring the Court to order an accounting under circumstances where he already has unfettered access to the relevant documents.

Despite being excised from the partnership, Nelson may remain liable to NDBP for the remainder of the 2006 loan. Sam has since taken control of the assets and inventory however, and it would be inequitable for Nelson to be liable to NDBP when he is deprived of access to any potential profits or salary from the partnership. Therefore, though accounting, liquidation and division of assets and liabilities is not justified for the reasons discussed above, it would be equitable to order Sam to indemnify Nelson for any personal losses that Nelson may incur should NDBP foreclose upon its loan. This

[4] Of note, no one testified as to the proper basis for determining a division of debts and assets based on a calculation of each partner's interest. Such a calculation would take into consideration the capital contributions by each partner. Here, by mortgaging his properties in order to secure the loan, Sam's capital contributions far exceed those of Nelson. *See generally* 59A Am. Jur. Partnership §§ 631-633. Conversely, Nelson cites the difficult-to-quantify, but very real, asset which he brought to the partnership, namely his long term relationship with NAPA and Bisnes-Mami. Again, although such an asset may be included in an accounting, no one testified as to its value.

Even if the Court were to order a third-party accounting of the assets and liabilities of NS Auto Parts as of March 27, 2009, along with a determination of each partner's interest in the partnership in light of capital investments and services, to be paid for by the parties (such an accounting would be a cost of the partnership and borne by the parties as partners), the results would be the same. Following the accounting, the Court would resolve any disputes regarding the accounting process and ultimately order liquidation of any assets and inventory that may be attributable to NS Auto Parts. Given the liabilities of NS Auto Parts, the likely outcome of such an accounting would be that both partners would see no gains and instead be saddled with the losses not resolved by liquidation of the assets.

solution provides reasonable protection for Nelson in light of the status of the inventory and assets, and permits a means to pay off the loan—through Sam's ongoing business—without the likely losses that would be incurred in a court-ordered liquidation of inventory.[5] Moreover, because Sam unilaterally took it upon himself to assume the assets and liabilities of the partnership, the Court finds it equitable to relieve Nelson of liability for his share of any losses suffered by the partnership prior to March 27, 2009. In other words, Sam maintains possession of the assets and inventory that may be attributable to NS Auto Parts, but he has no claim against Nelson for contribution as to the losses of NS Auto Parts and must indemnify Nelson against personal liability for NS Auto Parts loans, including any liability to NDBP.

E. Compensatory or Actual Damages

[9] To the extent that Sam seeks damages based on Nelson's alleged misappropriation of partnership funds, his claim must be denied. "One partner cannot generally maintain an action at law against a copartner for a misappropriation of partnership moneys." *Id.* § 369 Thus, Sam's allegations that Nelson charged fuel to the partnership for his personal use, converted partnership cash to his own benefit, and used partnership assets for his personal benefit cannot form a basis for compensatory damages (though such actions might be relevant in an accounting and equitable division).[6]

Similarly, Nelson cannot maintain an action for compensatory damages based on Sam's alleged conversion of NS Auto Parts assets and inventory, because the assets and inventory were partnership property (although, again, such "conversion" might be relevant in an accounting and equitable division of assets).[7] *Id.* § 364 ("Generally, a partner cannot maintain an action for trover or conversion against a copartner in respect to partnership property ...."). Nelson's reliance on 59A Am Jur Partnership § 366, is misplaced since that section speaks only to the conversion by one partner of the other partner's *separate* property.

[10] Nelson has not otherwise established an entitlement to compensatory damages for wrongful dissolution or loss of wages. Inasmuch as the partnership was one "at will" that either partner could dissolve, Nelson cannot maintain a claim for "wrongful dissolution." *See id.* § 357 ("The right of action for damages from a partnership dissolution depends on the fact that the

[5] This solution appears in line with one of Nelson's concerns, that he remains personally liable for part of the NDBP loan.

[6] Sam contends that Nelson wrongly took $1,600 out of the partnership bank account in June and July 2009 after the partnership was dissolved. However, in his letter dated March 20, 2009, Sam told Nelson that he was on paid leave, and the subsequent communication (or lack thereof) between the parties leaves an open question as to whether Nelson paying himself what he believed to be his rightful salary is a valid basis for damages.

[7] This analysis also refutes Nelson's argument that he should get some type of credit for his payments toward the van. The record reflects that Nelson borrowed money from the partnership to purchase the van and later the van was used for partnership business. Though Nelson voluntarily paid money back to the partnership for the purchase of the van, the funds are partnership funds and cannot form the basis for a damages claim.

dissolution is brought about in violation of the contract between the partners. If a firm is one dissolvable at will, a partner's election to dissolve the partnership is not a breach of the partnership contract and there is no right to recover damages resulting from the dissolution, in the absence of a partnership agreement to the contrary."). Moreover, as a partner, Nelson cannot maintain an action for damages based on discontinuation of his salary. *See generally id.* § 310 (under common law, a partner is not entitled to compensation for services to the partnership, but compensation for management may be taken into consideration in an accounting).

F. Punitive Damages

[11, 12] Finally, neither party has presented sufficient evidence to support a claim for punitive damages, costs or attorneys' fees. The award of punitive damages and attorneys' fees is a discretionary matter. *W. Caroline Trading Co. v. Kloulechad*, 15 ROP 127, 128 (2008). Punitive damages are defined as "damages, other than compensatory or nominal damages, awarded against a person to punish him for his outrageous conduct and to deter him and others like him from similar conduct in the future." Restatement (Second) of Torts§ 908(1). "Factors to be considered in assessing punitive damages include 'the character of the defendant's act, the nature and extent of the harm to the plaintiff that the defendant caused or intended to cause and the wealth of the defendant.'" *Kloulechad*, 15 ROP at 129 (quoting Restatement (Second) of Torts § 908(2)). The burden is on the party claiming punitive damages. *See* 59A Am. Jur. Partnership § 355.

[13] Punitive damages in a partnership context are awarded based on "malice or acts undertaken with wanton and reckless disregard to the rights of others." *Id.* Sam no doubt treated Nelson shabbily, and Nelson was understandably hurt by his brother Sam's actions, but such actions were not sufficiently outrageous or malicious to justify punitive damages. *See Johnson v. Gibbons*, 11 ROP 271, 276 (Tr. Div. 2004) (Defendant's beating "an unarmed person with a baseball bat [so badly that he broke his arm] in a public place and in the absence of any threat of injury to himself or any other persons" justified punitive damages); *Arugay v. Wolff,* 7 ROP Intrm. 226, 232 (Tr. Div. 1997) (trial court awarded punitive damages where Defendant raped one of the Plaintiffs and forced both Plaintiffs to walk naked down the main street of a village); *Robert v. Ikesakes*, 6 ROP 234, 239, 244 (1997) (trial court properly awarded punitive damages of attorney fees where defendants bulldozed plaintiffs' partially-constructed home). Further, in the context of a partnership, "actual damages usually must be established first," 59A Am. Jur. *Partnership* § 355, and Nelson has proven no actual damages.

As for Sam's claim of punitive damages, he introduced no evidence to support a claim that Nelson acted outrageously or maliciously to warrant punitive damages. Sam blind-sided his brother, and summarily removed his livelihood. In response, Nelson sought the advice of counsel, and continued to draw his salary from the partnership's bank account, consistent with Sam's decree in his March 20 letter. Where is Nelson's "outrageous" or "malicious" conduct?

As for attorneys' fees and costs,

neither party has established a right to attorneys' fees or costs based on contract, statute or punitive damages and in the absence of such, each party is responsible for his own fees and costs. *See Kloulechad*, 15 ROP at 128-29 (citing *Rdialul v. Kirk & Shadel*, 12 ROP 89, 94 (2005)).

III. Conclusion

The Court holds that the partnership between Sam and Nelson Masang was "at will," and was dissolved on March 27, 2009 by the actions of Sam Masang. The partnership was not a profitable enterprise and neither party has shown that he would receive a financial benefit were the Court to order an accounting and liquidation of partnership assets. Accordingly, both requests for a Court-ordered accounting of partnership assets and liabilities and subsequent distribution of profits and losses is **DENIED**. Sam is responsible for the resolution of all NS Auto Part's liabilities that may remain outstanding, and will indemnify Nelson from future liability for any NS Auto Part losses, including any personal liability that Nelson may incur should NDBP foreclose on the 2006 loan. Finally, neither party has shown that he is entitled to compensatory or punitive damages, and the parties' requests for costs and attorney fees are also **DENIED.**