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NOT TO BE PUBLISHED

Commonwealth of Kentucky

Court of Appeals

NO. 2007-CA-002282-MR

RACING INVESTMENT FUND 2000, LLC — APPELLANT

v.

APPEAL FROM FAYETTE CIRCUIT COURT
HONORABLE KIMBERLY N. BUNNELL, JUDGE
ACTION NO. 02-CI-00769

CLAY WARD AGENCY, INC. — APPELLEE

OPINION
AFFIRMING

** ** ** ** **

BEFORE: CLAYTON, ACREE, AND KELLER, JUDGES.

CLAYTON, JUDGE: Racing Investment Fund 2000, LLC ("RIF") appeals from a November 1, 2006, order of the Fayette Circuit Court holding it in contempt for its failure to pay the remainder of an agreed judgment to Clay Ward Agency, Inc. ("Clay Ward") for equine insurance. We affirm.

PROCEDURAL AND BACKGROUND FACTS

RIF was an entity created for the purchase, breeding, and racing of thoroughbred horses. It was one of several limited liability companies, which had as the managing member Gaines-Gentry Thoroughbreds, LLC ("Gaines-Gentry"). As manager of RIF, Gaines-Gentry is vested with final decision-making authority. The Gaines-Gentry principals are Olin Gentry, Thomas Gaines, and Gloria Callen. For six years, Gaines-Gentry and its partners (including RIF) did business with Clay Ward, an insurance firm that specializes in equine insurance. Each company, including Gaines-Gentry, had separate accounts with Clay Ward. Hence, RIF purchased separate insurance policies, had its own account, and was billed separately.

In May 2001, because of disputes about the insurance for two horses, the Stormcat/Beautiful Bid foal and Indian Charlie, a stallion, Gaines-Gentry and all related entities, including RIF, terminated Clay Ward as their insurance agent while still owing nearly $500,000 in unpaid policy premiums. At this time, RIF, individually, owed Clay Ward $61,243.30 in insurance premiums, although RIF had no ownership interest in the two horses with the disputed policies.

Eventually, the Gaines-Gentry entities, which included RIF, filed a complaint in this action against Clay Ward alleging tort and other claims on the Stormcat/Beautiful Bid and Indian Charlie insurance policies. Thereupon, Clay Ward asserted counterclaims against the counterclaim-defendants, including RIF, for non-payment of equine insurance premiums.

Clay Ward moved for summary judgment on February 13, 2004, and while RIF did not disagree with the principal amount of the premium, it disputed Clay Ward's claim for prejudgment interest. After the resolution of the interest issue by the parties, the court, on May 27, 2004, entered several agreed judgments against each of the counter-claim defendants. Thereupon, RIF executed an agreed judgment with Clay Ward acknowledging its indebtedness in the amount of $69,858.96, which incorporated the prejudgment interest. One month later, RIF paid Clay Ward $12,719.28 of the judgment. The remaining $57,139.68, upon which post-judgment interest continues to accrue, has not been paid by RIF. RIF insists that after partial payment of the judgment, the entity was no longer actively conducting business, and it had tendered the entirety of its assets when it made the partial payment.

When RIF did not make its full payment on the agreed judgment, Clay Ward filed, on November 30, 2004, an *ex parte* motion for entry of a rule under Fayette Circuit Court Rule 27. Clay Ward contended that RIF should make full payment and is capable of doing so. Judge Mary Noble issued a rule on December 1, 2004, requiring RIF to show cause as to why it should not be held in contempt. After a hearing on December 10, 2004, Judge Noble issued an order on November 1, 2006, which held RIF in technical contempt and ordered that the judgment be paid within 90 days.

RIF asked for the rule to be made final and appealable so that the issue of liability could be appealed, however, for some unknown reason, Judge

Noble's November 1, 2006, order was filed and entered on the record, but never received by the parties. RIF, unaware of the written order, filed an April 10, 2007, motion to reconsider what it thought was the December 10, 2004, bench ruling. Instead, after the court informed the parties of the November 1, 2006, order, RIF, pursuant to Kentucky Rules of Civil Procedures (CR) 59.01 and CR 62.01(f) [*sic*], converted its motion to reconsider the bench ruling into a motion to reconsider the November 1, 2006, written order. Judge Kim Bunnell, who replaced Judge Noble, granted the CR 60.02 motion on the basis of extraordinary relief and ordered that the November 1, 2006, order was effective as of April 23, 2006, the actual date that counsel received the order. Hence, the May 2, 2007, motion to reconsider was timely filed and properly heard on September 6, 2007.

Following the September 6, 2007, hearing, the court on October 9, 2007, denied RIF's motion to reconsider and ruled that "this Court is in complete agreement with the order entered by the previous judge in this matter and finds no basis to alter or amend it." This appeal followed.

ANALYSIS

The issue is whether RIF must pay Clay Ward the remaining balance plus post-judgment interest of the agreed judgment based on the *RIF Operating Agreement*, Section 4.3(a), which provides for routine capital calls of its members "to pay operating, administrative, or other business expenses of the Company, which have been incurred, or which the Manager reasonably anticipates will be

incurred" or whether the dissolution of the RIF forestalls payment of the judgment in light of both the language of the operating agreement and the limited liability statutes of the Commonwealth. Finally, depending on the resolution of the above issues, it must be determined whether the order of contempt is appropriate.

1. LIMITED LIABILITY COMPANIES

Because this case involves the interpretation of RIF's operating agreement and Kentucky Revised Statute (KRS) 275.150, which are issues of law, our standard of review for these issues is *de novo*. *Gosney v. Glenn*, 163 S.W.3d 894, 898 (Ky. App. 2005). While KRS 275.150(1) provides that members and managers are not personally liable for limited liability companies' debts, obligations, and liabilities, pursuant to KRS 275.150(2), members and managers can agree to personal liability in a written operating agreement or another written agreement:

> (2) Notwithstanding the provisions of subsection (1) of this section, under a written operating agreement or under another written agreement, a member or manager may agree to be obligated personally for any of the debts, obligations, and liabilities of the limited liability company.

In the case at hand, when RIF was created, as is common for most limited liability companies, its members (who have not been identified) made initial capital contributions. Somewhat atypical, however, was the fact that RIF's operating agreement in Section 4.3 allows for its member to be regularly billed for

the company's on-going business expenses. Section 4.3(a) of the operating agreement states:

> The Investor Members (including, but not limited to, any Investor Assignees) shall be obligated to contribute to the capital of the Company, on a prorata basis in accordance with their respective Percentage Interests, such amounts as may be reasonably deemed advisable by the Manager from time to time in order to pay operating, administrative, or other business expenses of the Company which have been incurred, or which the Manager reasonably anticipates will be incurred, by the Company.

RIF Operating Agreement, at p. 5, § 4.3(a). In addition, Section 4.4 of the operating agreement states:

> *Except* as otherwise specifically provided in the Act, no Member shall have any personal liability for the obligations of the Company, and, *except* as otherwise provided herein as to Additional Capital Contributions by the Investor Members (*including, but not limited to*, Investor Assignees) and any Default Loans with respect to Deficiencies, no Member shall be obligated to contribute additional funds or loan money to the Company.

Id. at p. 7, § 4.4. To summarize, the unambiguous language in the two cited sections of the operating agreement, clearly, authorizes routine capital calls for operating, administrative or other business expense. In sum, notwithstanding the Act (Limited Liability Statutes), RIF members agreed through the operating agreement to be liable, through capital calls, for payment of operating, administrative and business expenses. That is the situation here – an outstanding debt for insurance premiums. The question of whether unpaid insurance premiums

are a business expense was addressed by Mr. Gentry, the manager, when he testified in his post-judgment deposition that the outstanding equine insurance premiums were a business expense.

While RIF argues that Section 4.4 overrides Section 4.3(a) because of the Limited Liability Statutes, we read it differently. Clearly, the language in Section 4.4 allows for additional capital calls for operating, administrative, and business expenses. RIF's contention that the Limited Liability Act trumps the written agreement is inapposite given the words in KRS 275.150(2). KRS 275.150(2) allows members of a limited liability company, notwithstanding the provisions of KRS 275.150(1), to agree under a written operating agreement to be obligated personally for the debts of the limited liability company. The members of RIF agreed to such liability when they signed the operating agreement.

Moreover, this Court, in making such a determination, is guided by the legislature's intent from the words used in the enacting statutes rather than surmising the intent. *Revenue Cabinet v. O'Daniel*, 153 S.W.3d 815, 819 (Ky. 2005), *quoting Flying J Travel Plaza v. Com., Transp. Cabinet, Dept. of Highways*, 928 S.W.2d 344, 347 (Ky. 1996). KRS 275.150 is unambiguous and plainly allows members of limited liability companies to alter liability under these statutes in an operating agreement. Therefore, the liability is limited to the extent allowed by law except as waived by the parties. Here, the operating agreement as written waived such liability for its members. In general, we "must interpret the statute

according to the plain meaning of the act and in accordance with the legislative intent." *Floyd County Bd. of Educ. v. Ratliff*, 955 S.W.2d 921, 925 (Ky. 1997).

Significantly, contrary to RIF's argument, this case is not about the personal liability of RIF's individual members. Indeed, no judgment has been entered against them individually. Instead, based on the plain meaning of the operating agreement, construed in harmony with the Limited Liability Statutes, the court orders RIF, the separate legal entity, to make a capital call for the purpose of complying with its obligation under the agreed judgment.

In the aforementioned deposition of Gentry, he testified that capital call made to RIF members included itemized amounts for the insurance premiums. Members typically paid these charges through capital calls allowed under Section 4.3(a). Thus, in light of the plain meaning of the statute, the words in the operating agreement, and RIF business practices, we conclude that the members of RIF obligated themselves, from time to time, to pay operating, administrative or other business expenses through capital calls. Therefore, RIF, albeit dissolved, still exists as a legal entity subject to a capital call. We agree with the court that it is reasonable and possible for it to obtain the funds necessary to pay Clay Ward's outstanding debt.

RIF alleges that because the debt to Clay Ward has been reduced to a judgment, this factor changes the character of the liability and the necessity for a capital call. RIF reasons because the debt has become a judgment, the Limited Liability Statutes prevail because the operating agreement does not waive liability

for judgments. Although, the hallmark of a limited liability company is the limitation on the liability of its members, as is noted above, the Limited Liability Statutes permit entities organized under this Act to assume liability in an operating agreement. In fact, RIF did so by allowing capital calls for operating, administrative and business expenses. Certainly, when a debt existed prior to the judgment and became a judgment prior to "dissolution," the mere transformation of an obligation into a judgment will not allow a company to avoid legally obligated payment.

Finally, RIF posits, based upon other sections of its operating agreement and reading it in its entirety, that investor-members are not required to restore deficiencies in their capital accounts either during the operation or dissolution of RIF. RIF construes Section 4.3 narrowly by reference to Section 6.7 of the operating agreement, which it interprets to say that investor-members are not required to restore deficiencies in their capital accounts either during the operation or dissolution of RIF. A reading of a portion of Section 6.7 says:

> *Except* in the case of a deficit in an Investor Member's Capital Account due, directly or indirectly, to any Default Loan with respect to such Investor Member (including, but not limited to, any Investor Assignee), no Member shall be required under any circumstances (either during the period of the Company's operation or upon the Company's dissolution and termination) to restore a deficit in such Member's Capital Account or, except for the Additional Capital contributions required under this Agreement, otherwise make any contribution of cash or property to the Company without such Member's consent, which may be withheld in such Member's sole and absolute discretion. . . .

RIF Operating Agreement, at p. 11, § 6.7. Notably, for us, the key language is "except for the Additional Capital contributions required under this Agreement." Even in this section of the operating agreement, the language refers to the ability to make capital calls for expenses and does not negate it.

As another tactic, RIF uses Section 10.5 of the operating agreement as pertinent and limiting member liability. Despite this contention, it is obvious that Section 10.5 concerns specifically indemnification of "the Manager, the directors and officers of the Manager, the officers of the Company, and, at the discretion of the Manager, any employee or agent of the Manager of the Company[.]" *Id*. at p. 21. It is not relevant to the issue at hand.

Currently, RIF is dissolved but not terminated. And, as we noted, when the debt was incurred and ordered to be paid, RIF could have made a capital call to remedy the lack of funds. Legally, by court order, and equitably for justice, RIF should make a capital call and satisfy the debt. Twisting words and/or ignoring the actual language of the operating agreement does not change RIF's ability, both now, and at the time of the **judgment** to make this capital call. (Emphasis added).

Furthermore, while this entity may be in the process of dissolution, it is not terminated. As stated in Section 11.1 of the operating agreement, "[n]otwithstanding the dissolution of the Company, prior to the liquidation and termination of the Company, the business of the Company and the affairs of the

Members . . . shall continue to be governed by this Agreement." *Id*. at p. 23. In short, as the entity has not been terminated, one way or the other, RIF members or its manager, must meet the mandates of the November 1, 2006, court order.

In conclusion, with regards to the interpretation of the agreement and the statutory liability, we note the following: The interface between the language of RIF's operating agreement and the Limited Liability Statutes does not compromise the public policy behind limited liability provisions. The statutes in KRS 275.150(2) allow incipient companies great latitude in establishing operating agreements. Second, contract interpretation does not permit the creation of ambiguity where there is none. *First Commonwealth Bank of Prestonsburg v. West*, 55 S.W.3d 829, 836 (Ky. App. 2000). The operating agreement is clear. Finally, with regards to contract construal, we do not find the operating agreement to be vague or ambiguous, and thus, the concept of parol evidence will not allow the insinuation of the affidavit of David M. Roth, a drafter of the RIF agreement, into evidence. Under the parol evidence rule, when parties put their agreement in writing, all prior negotiations and oral agreements are merged in the instrument, and a contract as written cannot be modified or changed by parol evidence, except in certain circumstances such as fraud or mistake. *Childers & Venters, Inc. v. Sowards*, 460 S.W.2d 343, 345 (Ky. 1970).

2. CONTEMPT

Civil contempt involves the failure of one to do something under the order of the court. *Grant v. Dortch*, 993 S.W.2d 506 (Ky. App. 1999). The

Supreme Court of Kentucky has defined contempt as the willful disobedience of or the open disrespect for the court's orders or its rules. *Newsome v. Commonwealth*, 35 S.W.3d 836, 839 (Ky. App. 2001).

Contempt falls into two categories: civil and criminal. Civil contempt is distinguished from criminal contempt not by the punishment meted out but by the purpose for imposing the punishment. *A.W. v. Com.*, 163 S.W.3d 4, 10 (Ky. 2005). An individual who has refused to abide by a court's order has committed civil contempt. *Newsome,* 35 S.W.3d at 839. When RIF failed to pay the full amount of the insurance premiums due Clay Ward, it refused to obey one of the circuit court's orders, thus, subjecting it to an order of civil contempt.

We do not agree with RIF's statement that it has not willfully disobeyed a court order but only is unable to pay the judgment. As we have noted, RIF has the ability to make a capital call to garner the funds to pay this debt and its attendant interest. Furthermore, RIF, by its own admission, has not been terminated because of this pending litigation. Finally, if the entity truly had an inability to pay this outstanding debt, it could file for bankruptcy. It has not done so.

When a court exercises its contempt powers, it has nearly unlimited discretion. *Smith v. City of Loyall*, 702 S.W.2d 838, 839 (Ky. App. 1986). Consequently, we will not disturb a court's decision regarding contempt absent an abuse of its discretion. "The test for abuse of discretion is whether the trial

[court's] decision was arbitrary, unreasonable, unfair, or unsupported by sound legal principles." *Com. v. English*, 993 S.W.2d 941, 945 (Ky. 1999).

Indeed, it is appropriate upon a finding of fact that a debtor has the ability to pay to issue an order of contempt for failure to pay. *Blakeman v. Schneider*, 864 S.W.2d 903, 906 (Ky. 1993). The court spent countless hours patiently and carefully reviewing this case. We discern no abuse in its discretion in its order of contempt.

Moreover, RIF's suggestion that satisfaction of the judgment should be sought through KRS Chapter 426 is superfluous. The court, through its contempt powers, has already ordered it to satisfy this judgment.

We affirm the Fayette Circuit Court judgment.

ALL CONCUR.

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