NORTH CAROLINA

GASTON COUNTY

IN THE GENERAL COURT OF JUSTICE
SUPERIOR COURT DIVISION
06 CVS 4626

JERRY W. WEBB, DARLEEN WEBB, LLOYD ALWRAN, DOROTHY ALWRAN, AMERICAN CORD & TWINE, INC., & ROYAL CORDAGE CORPORATION, Plaintiffs, v. ROYAL AMERICAN COMPANY, LLC, WALL INDUSTRIES, INC., ROYAL ACQUISITION CORPORATION, FCC, L.L.C. D/B/A FIRST CAPITAL, STANLEY J. SWIDER, & SAMUEL B. FORTENBAUGH III, YALE CORDAGE, INC., & YALE ROPE TECHNOLOGIES, INC., Defendants.	**REPLY BRIEF OF FCC, LLC, D/B/A FIRST CAPITAL IN SUPPORT OF ITS MOTION TO DISMISS OR IN THE ALTERNATIVE MOTION FOR JUDGMENT ON THE PLEADINGS**

Defendant, FCC, LLC d/b/a First Capital ("FCC"), through counsel, pursuant to BCR 15.7 and Rule 12(b)(6) of the North Carolina Rules of Civil Procedure or alternatively Rule 12(c), respectfully submits this Reply in support of FCC's motion to dismiss or in the alternative motion for judgment on the pleadings.

INTRODUCTION

As an initial matter, FCC emphasizes again that its limited involvement in the circumstances surrounding this lawsuit merely amounts to conducting business as a commercial lender and that the underlying transaction involved in this lawsuit was an arm's length commercial transaction conducted everyday by banks and other lending institutions. The transaction was not between FCC and Plaintiffs, but between FCC and Defendants Wall, Royal Acquisition, and Royal American. Considering the significant pleading deficiencies that FCC has noted for the Court and FCC's very limited role as lender to parties other than Plaintiffs, this case should not be allowed to proceed against FCC or else traditional lending practices used everyday by commercial lending institutions could be negatively impacted.

On February 15, 2007, after receiving notification that the FCC's Brief in Support of Its Motion to Dismiss or in the Alternative Motion for Judgment on the Pleadings (the "Opening Brief") contained a minor formatting error and lacked a Rule 15.8 certification, FCC resubmitted a brief to the Court that was double spaced, but otherwise identical to the Opening Brief, with an accompanying letter and appropriate certification. FCC respectfully submits that the remedy requested by Plaintiffs for this error is not proper under Local Rule 15.11.

Addressing Plaintiffs' request that this Court deny FCC's motion for judgment on the pleadings, FCC notes that Rule 12(c) is pled in the alternative only. The law, arguments, and evidence presented in FCC's Opening Brief are directed at the factual allegations, causes of action, and underlying agreements referenced in Plaintiffs' Amended Complaint, and therefore this motion should be treated as a Motion to Dismiss based on Rule 12(b)(6) of the North Carolina Rules of Civil Procedure. Should, however, the Court deny the alternatively pled motion for judgment on the pleadings, FCC requests that the motion be denied without prejudice to FCC's right to file a motion under Rule 12(c) after Plaintiffs file their reply to FCC's counterclaim.

ARGUMENT

I. GENERAL DEFICIENCIES IN PLAINTIFFS' RESPONSE

At the outset of Plaintiffs' Reply and Brief in Opposition to FCC's Motion to Dismiss (the "Response"), Plaintiffs recite several paragraphs from the Amended Complaint and state, "[t]he following specific facts demonstrate that plaintiffs have properly stated claims upon which relief can be granted . . ." After such a statement, one might expect Plaintiffs to attempt to establish how the "specific facts" support their position; however, Plaintiffs failed to do this in their argument. Rather than denote which and explain how the allegations in the Amended Complaint state the claims made therein, Plaintiffs attempt to obscure FCC's 12(b)(6) position by offering predominantly merit-based argument and legal theory in response. For example, in the section relating to Plaintiffs' claim of fraud, Plaintiffs fail to cite a single paragraph in the Amended Complaint that alone or in combination with other paragraphs satisfies the particularity pleading requirement of fraud. (Response 18.) Instead, much as they did in the Amended Complaint, Plaintiffs allege, in very general terms, that FCC made broad misrepresentations and then propose theoretical arguments for why the alleged misrepresentations were made with the necessary intent, why Plaintiffs were deceived, and how Plaintiffs have been damaged.[1]

Several notable contradictions pervade Plaintiffs' Response. The most notable example occurs in the section relating to the Exculpatory Clause. (Response 8-11.) In that section, Plaintiffs argue that the Debt Subordination Agreement has been terminated due to the alleged satisfaction of the loan, is void for fraudulent inducement, may not be a valid or enforceable contract for lack of consideration, and that it violates public policy. Yet Plaintiffs, in large part, base their breach of contract claim against FCC on FCC's alleged breach that agreement. Any argument that a single agreement is both *invalid and breached* is inherently flawed.

On a number of occasions, Plaintiffs make unsubstantiated self-serving statements which find no support at all in the Amended Complaint. For instance, in the section relating to Plaintiffs' claim of breach of fiduciary duty, Plaintiffs postulate for the first time their theory that

[1] Additional examples include the following: (1) Plaintiffs argue their new legal theory for why FCC should be considered a "debtor" in the context of the fraudulent conveyance claim rather than direct the Court to supporting allegations in the Amended Complaint (Response 15-16); and (2) Plaintiffs argue that FCC "claims a lien over several funds of Royal American, Wall Industries, and Royal Acquisition" in the section on Marshalling of the Assets (Response 17) and that their own "claims are in peril", but they do not provide support for this argument in the Amended Complaint (Response 17-18).

FCC acquired a fiduciary duty by allegedly "stepping into the shoes of the majority members, officers and directors of the companies . . ." *via* the Debt Subordination Agreement and "after FCC took over and controlled Royal, Royal Acquisition, and its parent Wall." (Response 22.) These allegations are not present in the Amended Complaint, and Plaintiffs failed to cite support within its pleading for this contention.

II. FCC'S REPLY TO SPECIFIC ARGUMENTS

A. The Exculpatory Clause

FCC first notes that Plaintiffs argument focuses exclusively on trying to invalidate the underlying Debt Subordination Agreement rather than the ultimate preclusive affect of the Exculpatory Clause. FCC also notes the lack of controlling legal support cited by Plaintiffs in support of its contention that the provisions of the Debt Subordination Agreement that "forbid them from bringing any suit or claim against FCC, including claims of fraud and bad faith . . . are also void as against public policy."

As mentioned previously, Plaintiffs talk out of both sides of their mouth in the context of the Debt Subordination Agreement; arguing that it is invalid and/or unenforceable on the one hand and that it serves as the basis for its claim of breach of contract on the other. These obvious contradictions demonstrate the dilemma that Plaintiffs find themselves in, and if the allegations in the Amended Complaint are to be taken as true for the purposes of this motion, Plaintiffs' cause of action against FCC for breach of the Debt Subordination Agreement should serve as an implied admission of the validity and enforceability of the agreement. Therefore all of Plaintiffs' arguments to the contrary should be ignored.

In support of their arguments against the validity and/or enforceability of the Debt Subordination Agreement, Plaintiffs cite North Carolina case law and statutes. However, as FCC pointed out in its Opening Brief, Georgia law governs by the contract's terms; thus the law proffered by Plaintiffs in support of their arguments should be given little consideration. FCC additionally notes that the Debt Subordination Agreement contains a Severability Provision (§ 3.6), which states that unenforceable provisions do not render the rest of the agreement unenforceable.

As to Plaintiffs' assertion that the Debt Subordination Agreement is void due to FCC's alleged fraud in the inducement, FCC directs the Court's attention to its arguments noting the inherent deficiencies associated with Plaintiffs' claim of fraud. As discussed in the Opening Brief and as further discussed below, Plaintiffs failed to satisfy the particularity pleading requirement associated with common law fraud and therefore failed to state a claim upon which relief can be granted.

Plaintiffs blatantly reach beyond the scope of the allegations contained in the Amended Complaint in an effort to defend against the preclusive affect of the exculpatory clause on its causes of action. The arguments relating to (1) the termination of the Debt Subordination Agreement due to the alleged loan repayment, and (2) the unenforceability and/or invalidity of the Debt Subordination Agreement due to lack of consideration and public policy considerations were not pled and should not be considered by the Court for the purposes of this motion.

Finally, Plaintiffs' assertion that Mrs. Webb and Mrs. Alwran's claims in the Amended Complaint are unaffected by the exculpatory clause because they are not parties to the Debt Subordination Agreement is incorrect. Without an agreement upon which to hinge their claims, it is difficult to imagine what claims Mrs. Webb and Mrs. Alwran have standing to assert. As the wives of Jerry Webb and Lloyd Alwran, the shareholders of Plaintiffs Royal Cordage and American Cord, they do not have standing to recover derivatively on behalf of either corporation.

They were not parties to any of the agreements upon which Plaintiffs base most of their claims. The only connection to the causes of action asserted in the Amended Complaint, which is extremely tenuous, are their personal guarantees to various creditors of Royal American, Royal Cordage, and American Cord.[2] This remote connection does not give them standing to sue, and all claims to the extent they are asserted by Mrs. Webb and Mrs. Alwran should be dismissed.

B. Breach of Contract

First, Plaintiffs acknowledged in their Response that their breach of contract claims extend to FCC's alleged breach of the Debt Subordination Agreement and the Loan Agreement only and not to the various other agreements referenced in the Amended Complaint. Second, Plaintiffs fail to point to a specific provision of the Debt Subordination Agreement in their Amended Complaint or their Response that has been breached by FCC.

As to the Loan Agreement, Plaintiffs', as the sellers, are not third-party beneficiaries to the Loan Agreement between FCC, Wall, Royal Acquisition, and Royal American.[3] Other courts have addressed this issue.

> [W]here a loan commitment is relied upon by persons dealing with the borrower, no third-party rights are recognized, even if the lender knew the identity of the third party such as a home seller, or the lender directly communicated with the third party regarding the loan commitment.

Corrugated Paper Products, Inc. v. Longview Fibre Co., 868 F.2d 908, 911-12 (7th Cir. 1989). *See also Dale v. Groebe & Co.*, 103 Ill. App. 3d 649, 653, 431 N.E.2d 1107, 1111 (1981) (seller

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[2] The Amended Complaint also refers to group health insurance coverage for Mrs. Webb under Section 19.5 of the Limited Liability Company Membership Interest Purchase Agreement, but FCC was not a party to this agreement and is not accused of breaching this agreement as acknowledge by Plaintiffs. Furthermore, Count 10 of the Amended Complaint for "Failure to Provide Health Insurance" (pg. 20) is specifically directed at Royal Acquisition, Wall, and Royal American.

[3] The language in the Loan Agreement noted in paragraph 4, pg. 4 of the Response in fact reads as follows: "[E]ach borrower acknowledges *that it* will receive substantial direct and indirect benefits by reasons of the making of the loans and other financial accommodations to Borrowers . . ." (Opening Brief, Exh. 1, pg. 1.) The Loan Agreement further states that "the Lender's willingness to extend financial accommodations *to Borrowers* . . . is done solely as *an accommodation to Borrowers* and *at Borrowers' request* and *in furtherance of Borrowers' mutual and collective enterprise*." (*Id.*)

not third-party beneficiary of loan commitment between lender and home buyer, even though seller relied on lender's confirmation of loan commitment to enter into a further home purchase contract).

Even if Plaintiffs somehow are found to be proper third-party beneficiaries, the Loan Agreement, Borrowing Base Certificate, and multiple allegations in the Amended Complaint, show that FCC performed its obligations to the Borrowers by providing the credit facility to the Borrowers for their use, including the $500,000 in borrowing availability as certified by the borrowers. The allegations relating to the other defendants' alleged misuse and misappropriation of the $500,000 working capital directly contradict Plaintiffs' contention that FCC failed to provide the $500,000 in working capital. (Am. Compl. ¶¶ 53, 67(g), 87, 109(a), 157.) Something cannot be misappropriated unless it is made available for misappropriation. Finally, the fact that the transaction between FCC and the borrowers for the loan and the transaction between borrowers and Plaintiffs for Royal American's purchase closed further contradicts Plaintiffs' claims that the financing was not in place and FCC somehow did not satisfy its obligations to borrowers. (*Id*. ¶ 43.) Plaintiffs cannot point to a specific provision in the Loan Agreement wherein FCC required that borrowers use the credit facility for any specific purpose.

C. <u>Conspiracy and Facilitating Fraud</u>

As explained in FCC's Opening Brief, the Amended Complaint does not contain allegations denoting *specific tortious or unlawful acts committed in furtherance* of any agreement between the parties. *Kirby v. Reynolds*, 193 S.E. 412 (N.C. 1937); *Shope v. Boyer*, 268 N.C. 401, 405, 150 S.E.2d 771, 773-74 (1966). Stating generally that "<u>Upon information and belief</u>, Defendants committed overt acts in furtherance of their unlawful agreement . . ." or that "<u>[u]pon information and belief</u>, Defendants, in some way or manner, or through some contrivance, came to an agreement . . ." is not sufficient. (Am. Compl. ¶¶ 152-153.) Plaintiffs' Response also fails in this respect.

D. Tortious Interference with Contract

Plaintiffs attempt to distinguish *Filmar Racing* from the current set of facts is filled with inaccuracies; therefore, FCC will clarify *Filmar Racing*'s application. *Filmar Racing* involved two simultaneously pending lawsuits in North Carolina and Tennessee. *Filmar Racing, Inc. v. Stewart*, 141 N.C. App. 668, 669-70 (2001). In the Tennessee action, Gilford Martin sued Filmar Racing as a minority shareholder, a creditor and employee of Filmar Racing. *Id*. Filmar Racing had entered into a contract with Pinnacle Motorsports Group to purchase all of its assets, and Martin asked the Tennessee court to enjoin the sale and sequester the assets pending the outcome of the Tennessee litigation. *Id*. The Tennessee court denied Martin's request, and Martin moved the court for reconsideration. Before the Tennessee Court ruled on Martin's motion to reconsider, Martin's attorney, Donald Stewart, wrote a letter to Pinnacle informing them about the status of the Tennessee litigation and warning Pinnacle that Martin would hold them liable for his lawful share of the corporate proceeds if the deal was consummated. *Id.* Pinnacle backed out of the transaction. Filmar Racing then brought an action in North Carolina alleging tortious interference against Donald Stewart, Stewart & Smith, P.A., and Martin for the letter to Pinnacle. *Id.* According to the Court,

> Filmar's complaint alleges that [defendants] 'lacked justification' for their acts . . . However, the complaint also describes the litigation pending in Tennessee. Thus, on the face of the complaint, Filmar alleges that defendants have a legitimate business interest in both Filmar's contract with Pinnacle, as well as for mailing the 25 January letter. Because the face of the complaint admits of "motive for interference other than malice," the trial court did not err in granting the Rule 12(b)(6) motion to dismiss."

Id. at 674-675.

The complaint in *Filmar Racing* merely described the litigation pending in Tennessee which, according to the court, was a sufficient admission of a "motive for interference other than malice." Similarly, as explained in FCC's Opening Brief, Plaintiffs' Amended Complaint contains allegations that admit of a "motive for interference other than malice" on the part of FCC, namely its contractual right to institute remedial action with respect to its collateral following defaults under a Loan Agreement. (Opening Brief 15.)

E. Royal Cordage and American Cord Do Not Have Standing to Bring Their Derivative Claims

Plaintiffs have not sufficiently pled the exhaustion of intracorporate remedies as required to bringing suit on their derivative claims. Under N.C. Gen. Stat. § 55-7-42, a shareholder may not initiate a derivative suit unless he has made written demand on the corporation and 90 days have passed since making demand (or the demand has been rejected). Plaintiff have neither specifically pled each of these requirements nor alleged generally that all conditions precedent to bringing their derivative claims have been met. *See Norman v. Nash Johnson & Sons' Farms, Inc*., 140 N.C. App. 390, 411-12, 537 S.E.2d 248, 263 (2000). Therefore, to the extent Plaintiffs claims are based on damages stemming from diminution of the value of their shares in the company, their claims should be dismissed.

F. Fraudulent Transfers

It is too late for Plaintiffs to cure patent deficiencies in their complaint, and Plaintiffs' invented theory as to why FCC should be considered a debtor for the purposes of this claim should be rejected. The Amended Complaint clearly states, "Royal America, Wall, Royal Acquisition, Yale Cordage, and Yale Rope are debtors of Plaintiffs pursuant to the Purchase Agreement, Lease, Subordinated Promissory Note, and Amended LLC Agreement." FCC is not included. (Am. Compl. ¶ 107.) The Amended Complaint further states "[u]pon information and belief, Royal American, Royal Acquisition and Wall were insolvent at the time of the above-mentioned transfers." (*Id.* at ¶ 110.) FCC is not included.

G. Marshalling of the Assets

Again, Plaintiffs allege facts not contained in their Amended Complaint, including a reference to alleged liens over "several funds" of Royal American, Wall Industries, and Royal Acquisition. (Response 17.) FCC stands by the arguments made in its Opening Brief. (Opening Brief 17-18.)

H. Fraud

Plaintiffs fail to cite support from the Amended Complaint to show how the allegations contained therein satisfy the particularity pleading requirement of actual fraud. FCC and the Court are left with broad allegations of misrepresentations, legal theories, and merit-based arguments.

As to the Loan Agreement, Plaintiffs were not parties to this agreement and therefore could not have reasonably relied on any of the representations made therein. That said, even if Plaintiffs could rely on statements made in the agreement, Plaintiffs have not identified any provision wherein FCC made a representation regarding specific "permissible uses" of the "money advanced to Wall" or a promise by FCC "to finance the continuation of the normal manufacturing business of the company, such that Royal could fulfill its commitments under a 7 year lease and the 'Earnout Case Payments." (Response 18-19.) Furthermore, FCC cannot find a single reference in the Amended Complaint to the sweeping allegations proposed for the first time in Plaintiffs' Response including: (1) a promise by FCC "to finance the acquisition of Royal by Wall, conditioned upon FCC's approval of the 'Acquisition Documents,' Articles of Organization and new Limited Liability Company Agreement for Royal . . ."; and (2) an obligation to disclose the unavailability of operating funds . . ." (Response 19.) The list of alleged representations are confined to those set forth in Paragraph 135 of the Amended Complaint which begins "[s]pecifically, said Defendants represented the following . . .", and these are not included. FCC stands by the arguments made in its Opening Brief.[4] (Opening Brief 11-12.)

I. Breach of Fiduciary Duty and Constructive Fraud

FCC relies on the arguments made in its Opening Brief for each of these causes of action. FCC also notes that Plaintiffs fail to cite to any support (law or pleadings) for its new theory on why FCC, a lender, owed a fiduciary duty to Plaintiffs. (Opening Brief 18.) Finally FCC notes that the allegations associated to these claims are explicitly directed at defendants other than FCC, namely Royal Acquisition, Wall, Swider, and Fortenbaugh and thus fail as a matter of law to provide FCC with sufficient notice of transactions intended to be proved in accordance with Rule 8 of the North Carolina Rules of Civil Procedure. (Am. Compl., ¶¶ 66, 173-174.)

J. Negligent Misrepresentation

FCC relies on the arguments made in its Opening Brief. (Opening Brief 13.) Plaintiffs fail to cite to any support in the Amended Complaint for its theory regarding why FCC, as a lender to parties other than Plaintiffs, owed them a duty of care.

K. Remaining Causes of Action

For the remaining causes of action that are directed at FCC, FCC relies on the arguments made in its Opening Brief. With respect to the causes of action that are left over, FCC asserts

[4]Plaintiffs contention regarding its purported reasonable "reliance on future payments for the execution of the Acquisition Documents and the Subordination Agreement" is worthy of comment. (Response 20.) FCC notes that in the event of Borrowers' default, the Debt Subordination Agreement contemplates FCC repayment before any junior creditor including Plaintiffs. They are charged with knowledge of this provision. (Opening Brief, Exh. 2, Section 2.1(a),(c)).

that they are either moot, as with Receivership (Am. Compl., ¶ 126-132) and Preliminary Injunction (*Id*. ¶¶ 116-125), or explicitly involve defendants other than FCC.

III. CONCLUSION

For the foregoing reasons, Defendant FCC respectfully requests that the Court grant its motion to dismiss.

This the 27th day of February 2007.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and accurate copy of the foregoing **REPLY BRIEF OF FCC, LLC, D/B/A FIRST CAPITAL IN SUPPORT OF ITS MOTION TO DISMISS OR IN THE ALTERNATIVE MOTION FOR JUDGMENT ON THE PLEADINGS** has been served upon counsel of record by depositing a copy thereof in the United States mail, postage prepaid and addressed as follows:

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This the 27th day of February 2007.

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CERTIFICATION OF ATTORNEY UNDER BCR 15.8

The undersigned attorney hereby certifies that the foregoing **REPLY BRIEF OF FCC, LLC, D/B/A FIRST CAPITAL IN SUPPORT OF ITS MOTION TO DISMISS OR IN THE ALTERNATIVE MOTION FOR JUDGMENT ON THE PLEADINGS** complies with BCR 15.8.

This the 27th day of February 2007.

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