IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

Supreme Court Docket No. 34866
Civil Action No.: 07-C-76 (Circuit Court of Braxton County, West Virginia)

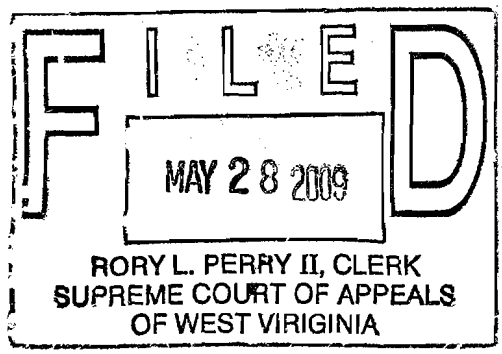
LLOYD'S, INC., a West Virginia Business corporation,

Appellant,

v.

CHARLES R. LLOYD,

Appellee.



BRIEF ON BEHALF OF APPELLANT

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KIND OF PROCEEDING AND NATURE OF RULING BELOW

This action is an appeal by Lloyd's, Inc. ("Lloyd's"), a West Virginia business corporation owned and operated by William G. "Greg" Lloyd, which operates a hardware store in Flatwoods, Braxton County, West Virginia. Lloyd's appeals an Order entered February 11, 2009 by Judge Facemire of the Circuit Court of Braxton County which denied Lloyd's motion to amend its Complaint and then dismissed Civil Action No.: 07-C-76. In the Civil Action, Lloyd's brought an action for unjust enrichment and conversion against Charles R. Lloyd (Appellee) who is the estranged father of Greg Lloyd and who performed bookwork for Lloyd's in the late 1990s and into the early 2000s. The Civil Action is based upon accounting entries in the books of Lloyd's made by the Appellee that conclusively show that the Appellee, or a company the Appellee owns or controls – Lloyd Stave Company – was overpaid on a debt by at least $84,000.00.

This misapplication/overpayment came to light during the prosecution of an earlier civil action which included, *inter alia*, an action by the Appellee against Lloyd's to collect a $132,000.00 Promissory Note. At the trial on the Promissory Note, Lloyd's sought to introduce evidence about the misapplication/overpayment in defense of the note obligation. Counsel for Appellee objected and claimed that the alleged overpayment went to Lloyd Stave Company – who was not a party to the earlier civil action – so that the misapplication/overpayment was not properly a part of the earlier civil action. Counsel for Lloyd's argued that the misapplication/overpayment issue was a proper defense and, in the alternative, asked that the pleadings be amended to conform to the evidence so that Lloyd's could present the misapplication/overpayment issue as a defense to the $132,000.00 note obligation. The trial court – also Judge Facemire and the Circuit Court of Braxton County –

sustained the Appellee's objection and denied Lloyd's motion to amend the pleadings in the earlier civil action to conform the case to the evidence. Importantly, Judge Facemire ruled that the misapplication/overpayment would have to be pursued in another action. Accordingly, Lloyd's filed the proceeding below at the conclusion of the earlier action.

In response to the proceeding below, Appellee, by counsel, changed course entirely and argued that the misapplication/overpayment should have been asserted in the earlier civil action. Appellee's contention in the earlier civil action notwithstanding – that the misapplication/overpayment could not properly be considered in the earlier civil action – Appellee moved to dismiss the proceeding below on *res judicata* grounds. In the February 11, 2009 Order that Lloyd's seek relief from herein, Judge Facemire likewise changed course and now holds that Lloyd's should have raised the misapplication/overpayment issue in the earlier civil action even though Judge Facemire acknowledges that Lloyd's attempted to do so and that the trial court refused to allow Lloyd's to raise the misapplication/overpayment issue. *See* February 11, 2009 Order at ¶ 3 and 4.

Under the facts and law involved in the proceeding below and the earlier civil action, the trial court committed reversible error when it dismissed the proceeding below and refused to allow amendment of the proceeding to join Lloyd Stave Company as a party-defendant. The trial court misapplied the doctrine of *res judicata* and improperly held that the misapplication/overpayment issue was a compulsory claim under the facts and circumstances of the earlier case. Where, as in the earlier case, a party is prevented from presenting an issue on the merits, *res judicata* should not apply. Additionally, because the misapplication/overpayment issue was being offered as a defense to the note obligation and was discovered well after the

pleading stage of the earlier case, the lower court improperly held that misapplication/overpayment issue was a compulsory claim in the earlier case.

STATEMENT OF FACTS

Lloyd's is a West Virginia Corporation with its principal place of business in Braxton County, West Virginia. *Complaint.* Lloyd's is wholly owned by Greg Lloyd and is the corporation through which Greg Lloyd owns and operates a hardware store in Braxton County, West Virginia. *Trial Transcript,* Civil Action No. 04-C-39 at 122-23 (hereinafter *Tr.*).[1] Appellee, Charles R. Lloyd (Charles or Charles Lloyd), is an individual residing in Braxton County, West Virginia. *Complaint.* Lloyd Stave Company, Inc. (Lloyd Stave) is a West Virginia Corporation with its principal place of business in Braxton County, West Virginia. *Complaint.* Lloyd Stave is owned by Charles Lloyd, and is the company through which he operates a convenience store and motel in Braxton County, West Virginia. *Tr.* at 239, 639. Braxton Lumber Company (Braxton Lumber) is a business jointly owned by Greg Lloyd and his brother, Charles R. Lloyd II (Chuck Lloyd). *Tr.* at 121. Charles, Chuck, and Greg Lloyd are involved in several businesses in Braxton County, West Virginia (Lloyd businesses).

Charles Lloyd assisted with the bookkeeping of Lloyd's beginning in approximately 1996, and kept the general journal, which tracked the credits and debits of Lloyd's. *Complaint, Tr.* at 647, 810; *Pl. Ex.* 158, Civil Action No. 04-C-39. Part of Charles Lloyd's responsibility in assisting with Lloyd's bookkeeping was keeping track of inter-company loans and officer accounts receivable. *Tr.* at 810. Account 2013 was a $290,000.00 notes payable account on Lloyd's books credited to Appellee, Charles Lloyd. *Tr.* at 648; *Pl. Ex.* 158.

[1] Relevant portions of Civil Action No. 04-C-39's trial transcript are attached hereto as Exhibit A.

Beginning on June 23, 1997, Braxton Lumber purchased the entire $290,000.00 balance of Account 2013 in successive payments. *Tr.* at 649-52; *Pl. Ex.* 160.

In June 1997, Braxton Lumber purchased $150,000.00 of the $290,000.00 balance of Account 2013. *Pl. Ex.* 160. In July 1997, Braxton Lumber purchased the remaining balance of Account 2013 in three successive purchases, completing the entire purchase of Account 2013 on July 23, 1997. *Pl. Ex.* 160. Because Braxton Lumber purchased the entire $290,000.00 balance of Account 2013, Lloyd's debt to Appellee Charles Lloyd and/or Lloyd Stave Company on Account 2013 was extinguished, and the balance was zero. *Pl. Ex.* 160. Also in 1997, Appellee Charles Lloyd purportedly loaned Lloyd's $132,000.00 to assist in the startup of the hardware store. *Tr.* at 382.

In December 1999, Greg Lloyd paid Charles Lloyd $100,000.00 to be applied to debt owed by Greg Lloyd or Lloyd's to Charles Lloyd. *Tr.* at 653; *Pl. Ex.* 161. The accounting records of Lloyd's maintained at the time by Charles Lloyd show that Charles Lloyd applied $84,000.00 of this $100,000.00 payment to Account 2013, which had previously been settled in 1997. *Tr.* at 658; *Pl. Ex. 161*. This is the evidence of misapplication/overpayment that Lloyd's sought to use defensively against the $132,000.00 note obligation sued on by Charles Lloyd in the earlier action.

On April 20, 2004, Greg Lloyd filed Civil Action No. 04-C-39 (hereinafter referred to as "earlier or previous civil action") against Chuck Lloyd and Braxton Lumber because he had been shut out of Braxton Lumber and his brother and father failed to keep him informed about what was happening in the business. In the previous civil action, Greg Lloyd sought judicial dissolution of Braxton Lumber; shareholder damages for waste, self dealing, and

insider lending; and partition of real estate situated in Salt Lick, West Virginia. In 2005, Greg filed an amended complaint against Chuck Lloyd and Charles Lloyd for fraud and/or forgery regarding the fabrication of false board meeting minutes and civil conspiracy.

Charles Lloyd answered and counterclaimed against Greg for unpaid rent on a parcel of land where Greg operated his hardware store. Charles also included a third party claim against Lloyd's, Inc. for the unpaid rent as well as a claim against Greg Lloyd and/or Lloyd's, Inc. for payment of the $132,000.00 loaned to Lloyd's, Inc. in 1997. Lloyd Stave was not a party in the previous civil action. Before trial and after pouring over the book work of Charles Lloyd, Greg Lloyd, Lloyd's and counsel discovered that Charles Lloyd misapplied $84,000.00 of Greg Lloyd's December 1999 payment to Charles Lloyd by applying the payment to Account 2013, which had previously been settled in 1997. *Tr.* at 1015-20.

In their response to Charles Lloyd's motion for summary judgment on his rent and note claims, Greg Lloyd and Lloyd's raised Charles Lloyd's misapplication of the $84,000.00 and argued that, if Charles had correctly applied the $84,000.00, then the amount owed to him by Lloyd's would be far less than $132,000.00. Charles Lloyd did not address this argument in his reply to Greg Lloyd and Lloyd's response to his motion for summary judgment, and he did not argue at the summary judgment stage or prior to trial that Lloyd Stave was a separate entity and must be sued in a separate action for unjust enrichment. The trial court denied Charles Lloyd's motion for summary judgment on October 4, 2006.

Again at trial, Lloyd's asserted the defense of payment or setoff in order to persuade that the trial court and the jury that the $84,000.00 did not actually go to pay off Account 2013 because the debt had been extinguished in 1997. *Tr.* at 1015-20. While neither

Lloyd's nor its counsel knew what happened to the $84,000.00 when Charles Lloyd misapplied it, these funds were paid to either Charles Lloyd, Lloyd Stave, or an unknown third-party. *Tr.* at 1015-20. At trial in the previous civil action, Greg Lloyd and Lloyd's presented evidence, testimony and argument to the lower court and the jury that Lloyd's was entitled to a correct application of the $84,000.00, which would have reduced the $132,000.00 debt allegedly owed by Lloyd's to Charles Lloyd. *Tr.* at 1015-20.

At trial, counsel for Charles Lloyd argued to the trial court for the first time that if the $84,000.00 payment was misapplied and went to Lloyd Stave, then Lloyd's should pursue a separate action against Lloyd Stave. *Tr.* At 1016, 1019. The trial court did not entertain Lloyd's misapplication/overpayment argument, but stated that if the facts were that the $84,000.00 was misapplied and received by Lloyd Stave, then Lloyd's may have an unjust enrichment claim which should be filed as a separate civil action. *Tr.* at 1022 , 1077-78. Accordingly, Lloyd's filed the civil action below on August 17, 2007 in order to determine where Charles Lloyd applied the $84,000.00 payment and whether Charles Lloyd converted and/or was unjustly enriched by the misapplication of the $84,000 payment. Moreover, based upon the representations of Appellee's counsel that the money may have gone to Lloyd Stave, Lloyd's filed a Motion for Leave to File an Amended Complaint to add Lloyd Stave as a party-defendant to the action below. By Order entered February 11, 2009, the trial court denied Lloyd's motion to amend and dismissed the proceeding below. Lloyd's now seeks a reversal of the February 11, 2009 Order.

ASSIGNMENTS OF ERROR

1. The trial court incorrectly applied the doctrine of *res judicata* and erred by denying Lloyd's motion to amend and dismissing the proceeding below.

2. The trial court incorrectly concluded that the misapplication / overpayment issue was a compulsory claim and erred by denying Lloyd's motion to amend and dismissing the proceeding below.

POINTS AND AUTHORITIES AND DISCUSSION OF LAW

I. Standard of Review

Appellate review of a circuit court's order granting a motion to dismiss a complaint is *de novo*. *McGraw v. Scott Runyan Pontiac-Buick, Inc.*, 194 W.Va. 770, 461 S.E.2d 516 (1995).

II. Appellee has not satisfied the third element of *res judicata* because the trial court previously ruled that Lloyd's, Inc.'s claims could not be resolved in the previous civil action.

Lloyd's unjust enrichment and conversion claims are not barred by the doctrine of *res judicata* because the requisite elements are not satisfied in the present action. For a claim to be barred by *res judicata*, three elements must be satisfied:

> First, there must have been a final adjudication on the merits in the prior action by a court having jurisdiction of the proceedings. Second, the two actions must involve either the same parties or persons in privity with those same parties. Third, the cause of action identified for resolution in the subsequent proceeding either must be identical to the cause of action determined in the prior action or must be such that it could have been resolved, had it been presented, in the prior action.

Syl. Pt. 4, *Blake v. Charleston Area Medical Center, Inc.*, 201 W. Va. 469, 498 S.E.2d 41 (1997). *Res judicata* may bar a subsequent proceeding even if the precise cause of action was not actually litigated in the former proceeding so long as the claim could have been raised and determined. *Id.* at 477, 498 S.E.2d at 49. Nonetheless, even if the requirements of *res judicata* were satisfied, the doctrine is not rigidly enforced where doing so would plainly defeat the ends of justice. *Id.* at 478, 498 S.E.2d at 50 (quoting *Gentry v. Farruggia*, 132 W. Va. 809, 811, 53 S.E.2d 741, 742 (1949)).

In the present matter, application of *res judicata* would plainly defeat the ends of justice. Petitioner agrees with Appellee that the first two elements of the doctrine are met. There was a final adjudication on the merits in the previous civil action.[2] Moreover, the previous civil action and the present action involve the same parties -- both Lloyd's, Inc. and Charles R. Lloyd were parties to the previous civil action.[3] The third element, however, is not met. The present cause of action is not identical to the cause of action determined in the previous civil action. Furthermore, while Appellee asserted below that Lloyd's did not present its unjust enrichment and conversion claims in the previous civil action, the trial transcript evidences Lloyd's attempt to do just that as a defense to Appellee's $132,000 note claim.

At the trial of the previous civil action, Appellee asserted a claim against Lloyd's for payment of a $132,000 Note which the trial court ruled was owed Appellee as a matter of law in the earlier civil action. In earlier civil action, counsel for Lloyd's clearly argued that Appellee

[2] The term "previous civil action" as used in this response refers to Civil Action No. 04-C-39, tried in the Circuit Court of Braxton County in March 2007, and involving Charles R. Lloyd, Charles R. Lloyd, II, Greg Lloyd, Braxton Lumber Company, and Lloyd's, Inc. The trial court entered orders in the previous civil action on February 22, 2008 and March 5, 2008, and an order certifying those orders as final on July 12, 2008.

[3] Petitioner filed a Motion for Leave to File an Amended Complaint to add Lloyd Stave Co., Inc. as a party defendant in this matter.

misapplied a $84,000.00 payment from Lloyd's to a debt allegedly owed by Lloyd's to Lloyd Stave which is solely owned by Appellee, when that debt had previously been satisfied and the balance was zero.[4] Lloyd's counsel argued in the previous civil action that, when Appellee misapplied this $84,000.00, the money did not actually go to pay off the debt to Lloyd Stave because that debt had been paid in 1997.[5] Instead, Appellee paid himself and/or Lloyd Stave the $84,000. Accordingly, Lloyd's argued in the previous civil action it was entitled to a correct application of the $84,000.00, which would have reduced the $132,000 debt allegedly owed by Lloyd's to Appellee. As such, Appellee and/or Lloyd Stave Company has been unjustly enriched by Appellee's misapplication of funds. *Id.* The trial court, however, did not entertain this argument, but indicated that if the facts were as Petitioner presented, then an unjust enrichment claim may exist and should be filed as a separate civil action. *Id.* at 1022, 1077-78. Because Lloyd's attempted to address these claims in the previous civil action and because it was not permitted to do so, Petitioner was forced to bring a subsequent action to address these claims.

For a claim to be barred by the doctrine of *res judicata*, all three elements of the doctrine must be satisfied. Here, element three is not satisfied because Appellant's unjust enrichment and conversion claims were not resolved in the previous civil action, despite Appellant's attempt to address them. Because all the elements of *res judicata* are not satisfied, the doctrine does not bar the action below and the trial court erred in dismissing the action.

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[4] *See* Exhibit A at pp. 1016-18.

[5] *Id.* at 1015-16.

III. Lloyd's misapplication/overpayment claims should not be dismissed pursuant to Rule 13 because, in the previous civil action, Lloyd's attempted to use this claim as a defense against Appellee's $132,000 note claim and because Lloyd Stave Company was not a party in the previous civil action.

Lloyd's claims for unjust enrichment and conversion were not compulsory counterclaims to the previous civil action and Lloyd's attempt to address them at trial was met with the lower court's opinion that such claims were more properly suited for a separate civil action.

Rule 13 of the West Virginia Rules of Civil Procedure provides as follows:

> A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction.

By its plain terms, Rule 13 applies only to those counterclaims that a party has "at the time of serving" its pleading. A counterclaim is compulsory only if it exists at the time the pleading is served. *Country Club, Inc. v. U. S. Fid. & Guar. Co.*, 563 S.E.2d 269, 276 (N.C. Ct. App. 2002).[6] If a party does not know that its claim exists at the time it serves its pleading, it is not required to supplement its pleading when the claim becomes known to the party, and the failure to bring the counterclaim does not bar subsequent litigation on the claim. *Id.* A party cannot be expected to plead what it does not know. *Id.*

At the time, Lloyd's answered Appellee's note claim in the previous civil action, Lloyd's was not aware of the underlying facts that support its claims for unjust enrichment and

[6] *Country Club, Inc. v. U. S. Fid. & Guar. Co., infra.* addressed the application of Rule 13(a) of the North Carolina Rules of Civil Procedure to claims between a North Carolina country club and its insurer. North Carolina's Rule 13(a) is identical to Rule 13(a) of the West Virginia Rules of Civil Procedure.

conversion against Appellee. While Greg Lloyd may have known of certain transgressions committed by the defendants in the earlier civil action against Greg Lloyd and Lloyd's, the details and gravity of those transgressions did not come to light until a significant amount of discovery took place in the previous civil action. Until the books of the family businesses were carefully examined, it was not evident that Appellee took money belonging to Greg Lloyd or Lloyd's and misapplied it to a debt which had already been paid. For many years, Appellee was in the unique position of managing all the businesses' books, and he did so in such a haphazard manner that it made very difficult the task of sorting through the various transactions. Determining what causes of action may have flowed from Appellee's actions was even more difficult, and Lloyd's certainly was not aware of the unjust enrichment and conversion claims until late in the previous civil action. Moreover, Lloyd Stave, which was not a party to the previous civil action, may be the beneficiary of the $84,000 which is the subject of Lloyd's unjust enrichment and conversion claims. As such, Lloyd's additionally sought leave from the lower court to amend its complaint in the proceeding below to add Lloyd Stave as a party-defendant to this civil action.

Because the misapplication/overpayment claims and the involvement therein of Appellee and Lloyd Stave were not known at the time Lloyd's filed its answer to Appellee's note claim in the earlier civil action, the misapplication/overpayment claims were not compulsory counterclaims to the previous civil action. Further, the trial court's discussion in the previous civil action regarding the possibility and subsequent treatment of Lloyd's unjust enrichment claim provides further support that this claim was not a compulsory counterclaim to the previous civil action. As discussed above, Lloyd's counsel attempted to argue that Appellee or Lloyd Stave was unjustly enriched by Appellee's poor bookkeeping, but rather than address it in the

previous civil action, the trial court – at the urging of Appellee's counsel – determined that such claims should be dealt with in a separate civil action.[7] Lloyd's obeyed the trial court's directive and brought the misapplication/overpayment claims subsequently in the proceeding below only to have – again at counsel for Appellee's urging – the proceeding below dismissed because the trial court and Appellee's counsel now have an opposite view about how the misapplication/overpayment claims should have been handled. Under the facts and circumstances of the earlier civil action and the proceeding below, the misapplication/overpayment claims were not compulsory claims and the trial court erred by dismissing the claims.

RELIEF REQUESTED

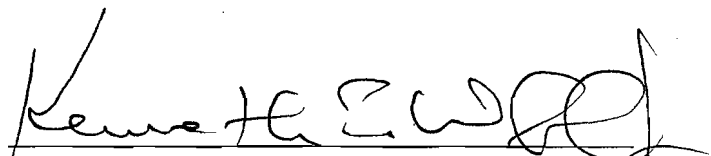
The trial court erred when it determined that the doctrine of *res judicata* barred Lloyd's misapplication/overpayment claims in the proceeding below because Lloyd's unjust enrichment and conversion claims were neither presented nor resolved in the previous civil action, despite Lloyd's attempt to address them. The trial court also erred when it determined that Lloyd's misapplication/overpayment claims in the proceeding below were compulsory claims because Lloyd's did not know that the claims existed when it answered Appellee's note claim.

[7] *See* Exhibit A at p. 1078.

WHEREFORE, Appellant, Lloyd's, Inc., respectfully requests that this Honorable Court reverse the decisions of Judge Facemire of the Circuit Court of Braxton County and remand the matter to the trial court for further proceedings.

LLOYD'S, INC.

By Counsel



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CERTIFICATE OF SERVICE

I, Kenneth E. Webb, Jr., hereby certify that a true and correct copy of the foregoing ***Brief on Behalf of Appellant*** was forwarded via U.S. Mail upon counsel of record, addressed as indicated, **on the 28th day of May, 2009:**

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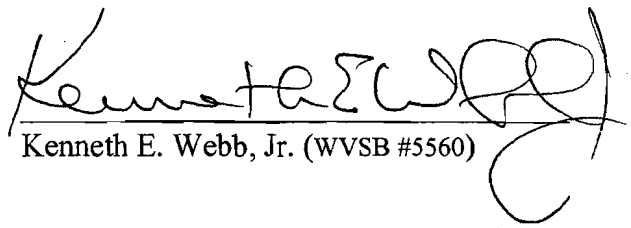

Kenneth E. Webb, Jr. (WVSB #5560)

EXHIBITS

ON

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