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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of New Jersey, Appellate Division.

Thomas A. LEACH, M.D., Plaintiff–Appellant, Cross–Respondent,
v.
PRINCETON SURGIPLEX, LLC, Leon N. Costa, M.D., and Michael S. Grenis, M.D., Defendants–Respondents/Cross–Appellants,
and
7/49 Solutions, LLC and David J. Shuffler, Defendants–Respondents.

A-6120-11T1
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Argued May 14, 2013.
|
Decided June 6, 2013.

On appeal from the Superior Court of New Jersey, Law Division, Mercer County, Docket No. L–2465–09.

Attorneys and Law Firms

Jeffrey M. Pollock argued the cause for appellant/Cross-respondent (**Fox Rothschild** LLP, attorneys; Mr. **Pollock** and Barry J. Muller, of counsel and on the brief).

David J. Kenny argued the cause for respon-dents/cross-appellants (Hartsough Kenny Chase & Sullivan, attorneys; Mr. Kenny of counsel; Mr. Kenny and Gregory J. Sullivan, on the brief).

Donald R. Chierici argued the cause for respondents (Chierici, Chierici & Smith, attorneys; Mr. Chierici, of counsel and on the brief).

Before Judges FISHER and ST. JOHN.

Opinion

PER CURIAM.

***1** In 2002, three physicians—plaintiff Thomas A. Leach, and defendants Michael S. Grenis and Leon N. Costa—formed a limited liability company, defendant Princeton Surgiplex, L.L.C. (Surgiplex). Pursuant to their operating agreement, Surgiplex was regularly appraised by Physicians Business Advisors, LLC (PBA), which determined Surgiplex's fair market value to be $3,600,000 as of December 31, 2004, and $5,900,000 as of June 30, 2006.

By letter dated September 12, 2008, plaintiff resigned from Surgiplex, effective December 31, 2008. The operating agreement required that Surgiplex purchase a resigning member's interest based on that member's percentage interest in Surgiplex multiplied by its fair market value. At the time plaintiff resigned, other members had joined Surgiplex, resulting in plaintiff possessing a 17.667% interest in the company. And, because plaintiff's resignation occurred more than two years after the most recent biennial appraisal, the operating agreement required that fair market value be fixed "by PBA" or any other appraiser fitting the description contained elsewhere in the agreement.

Surgiplex retained defendant 7/49 Solutions, LLC (7/49) to determine fair market value. Defendant David J. Shuffler, who had been affiliated with PBA, conducted the appraisal for 7/49 and determined the fair market value of Surgiplex to be $2,325,000 as of June 30, 2008. That prompted plaintiff to commence this action against Surgiplex, Grenis and Costa (hereafter "the Surgiplex defendants"), alleging breach of contract, breach of the covenant of good faith and fair dealing, fraud and negligent misrepresentation, civil conspiracy and breach of fiduciary duties. The Surgiplex defendants filed a counterclaim, seeking damages, in the form of attorneys' fees, based on what they alleged was plaintiff's breach of the operating agreement. Plaintiff's complaint also sought relief from 7/49 and Shuffler based on plaintiff's fraud and negligent misrepresentation allegations.

Defendants obtained summary judgment. The judge concluded that the Surgiplex defendants complied with the terms of the operating agreement by retaining 7/49, which fixed the amount due plaintiff for his interest in Surgiplex. Implicit in the judge's brief oral decision was his conclusion that plaintiff had no right to look behind the appraisal's bottom line; he concluded that plaintiff "may be unhappy with the results of [the appraisal] but" his remorse does not support a finding of a breach of contract or any of the other causes of action. The judge also granted summary judgment in favor of plaintiff, dismissing the Surgiplex defendants' counterclaim for damages.

Plaintiff appeals, claiming there are genuine issues of material fact concerning whether defendants breached their contractual and fiduciary duties. Specifically, plaintiff claims he was entitled "to a meaningful review of the 2008 appraisal" in light of the fiduciary duties owed him by the Surgiplex defendants, and because 7/49 "failed to adhere to applicable standards and ignored relevant evidence." Plaintiff also argues, among other things, that the judge mistakenly believed the operating agreement's appraisal process is the equivalent of an arbitration and was insulated from attack in litigation to the same extent. He further asserts there are genuine issues of material fact as to whether the Surgiplex defendants breached their contractual and fiduciary duties by "converting [plaintiff's] membership interest after he had withdrawn his resignation." The Surgiplex defendants cross-appeal, arguing the judge erred in granting summary judgment in favor of plaintiff on their counterclaim.

***2** In reviewing a summary judgment, we adhere to the same standard that bound the trial judge. *Liberty Surplus Ins. Corp. v. Nowell Amoroso, P.A.,* 189 *N.J.* 436, 445–46 (2007); *Voellinger v. Dow,* 420 *N.J.Super.* 480, 486 (App.Div.), *certif. denied,* 208 *N.J.* 599 (2011). That is, we must view the facts in the light most favorable to plaintiff and determine "whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law." *Brill v. Guardian Life Ins. Co. of Am.,* 142 *N.J.* 520, 536 (1995). In determining whether the evidential materials relied upon by plaintiff are sufficient to compel the denial of summary judgment, we must first consider the nature of the dispute.

The Surgiplex defendants' theory, which the judge adopted, is that the operating agreement created a method for fixing the fair market value of the property that no party could thereafter question—that is, whatever the appraiser determined would ultimately be binding, no matter how surprisingly high or low the appraiser might declare fair market value to be. To be sure, the parties no doubt intended that the process outlined in their operating agreement would preclude any lengthy process in the fixing of their rights and liabilities. But, contrary to the import of the judge's decision, such a contractual provision does not eliminate all grounds for attacking the appraiser's methodology or results. In explaining the extent to which such an appraisal may be questioned in litigation, we turn to the implied covenant of good faith and fair dealing.

Every New Jersey contract carries with it an implied covenant of good faith and fair dealing. *Sons of Thunder v. Borden, Inc.,* 148 *N.J.* 396, 420 (1997); *Seidenberg v. Summit Bank,* 348 *N.J.Super.* 243, 253 (App.Div.2002). As described by our Supreme Court, this covenant mandates that "neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract." *Sons of Thunder, supra,* 148 *N.J.* at 420. This principle has been recognized as allowing three particular circumstances: (1) inclusion of terms and conditions not expressed in the written contract; (2) redress for the bad faith performance of a contract; and (3) inquiry into a party's exercise of discretion expressly granted by a contract's terms. *Seidenberg, supra,* 348 *N.J.Super.* at 257. In some respects, the parties' arguments concerning the meaning and scope of the buy-out provisions of the operating agreement invite inquiry into all three of these aspects.

First, we discern from plaintiff's arguments that he contends it would frustrate the purpose of the buy-out provisions to assume those provisions preclude any inquiry into the appraiser's methods, the information considered by the appraiser, the calculations made, or the conclusions drawn by the appraiser, even though the agreement does not contain any provisions for questioning of the appraisal. We agree. The operating agreement expressly designates the appraiser (or its substitute) and directs a determination of Surgiplex's fair market value. It cannot be seriously argued that the appraiser is entitled to determine fair market value by spinning a wheel or flipping a coin, or that the appraiser may consider less than all relevant evidence, or that no party could question a mathematical error in the appraiser's calculations. Implied in the operating agreement must be an understanding that the appraiser will utilize accepted professional norms and that a party to the operating agreement reserves the right to challenge the appraisal's results upon the appraiser's failure to conform to accepted standards. [1]

***3** Second, plaintiff asserts, within the context of his fraud and misrepresentation allegations, that all defendants failed to act in good faith with respect to the appraisal of Surgiplex. In this regard, plaintiff alludes to Grenis's alleged conversations with the appraiser—Shuffler of 7/49—in which Grenis provided financial information to which plaintiff was not privy, and allegedly directed Shuffler to make his appraisal "defensible." Although a trier of fact might interpret this evidence in a multitude of ways, in ruling on defendants' motion for summary judgment the trial judge was required to assume the truth of plaintiff's allegations and adopt the reasonable inference that Grenis suggested to Shuffler that he and Costa were looking for him to produce an appraisal

favorable to them that would also be "defensible." Applying the *Brill* standard, the judge could not properly conclude that plaintiff failed to show that defendants acted in bad faith.

Third, the principles that inform the implied covenant of good faith and fair dealing spring from the law's endeavor to fulfill contracting parties' reasonable expectations. *Seidenberg, supra,* 348 *N.J.Super.* at 257 (recognizing that "the central premise of the implied covenant is the enhanced status of the parties' reasonable expectations"). Here, the provisions of the operating agreement that deal with the ascertaining of fair market value start with the parties' "acknowledge[ment] and agree[ment] that in October, 2005, the fair market value of [Surgiplex] was determined by an independent appraisal performed by [PBA]." As noted earlier, that appraisal valued Surgiplex at $3,600,000 as of December 31, 2004; a later appraisal valued Surgiplex at $5,900,000 as of June 30, 2006. Both appraisals were performed by Shuffler while he was affiliated with PBA, and it was Shuffler who performed the appraisal in question. [2]

In the earlier appraisals, Shuffler applied the same methodology, but he took a different approach in conducting the appraisal in question. Plaintiff acknowledges that in all three appraisals, Shuffler used the "debt-capacity-capitalized-return" method, which determines fair market value by using three key factors: (a) adjusted net cash flow (EBITDA); (2) debt service coverage ratio (DSCR); and (3) amortization rate. In performing the appraisal in question, however, Shuffler made changes in computing the value of EBITDA and DSCR. That is, contrary to his prior practice, Shuffler used only the actual revenue for the twelve months ending on December 31, 2007, rather than annualizing Surgiplex's revenues for the period of January 1, 2008 through September 30, 2008, even though that information was available at the time Shuffler appraised Surgiplex. Plaintiff argues that over the first six months of 2008, Surgiplex's billings and revenues had increased to $903,000, an amount approaching its revenues for all of 2007, i.e., $1,132,000. According to plaintiff, if Shuffler had remained consistent with his earlier methodology, he would have utilized this data, but Shuffler took a different approach in order to reduce Surgiplex's fair market value and provide a benefit to the Surgiplex defendants. Indeed, as support for plaintiff's argument that Shuffler was attempting to underestimate fair market value, plaintiff refers to Shuffler's deposition testimony in which Shuffler offered no reason for his change in approach:

> ***4** Q. Why didn't you adjust the EBIT[D]A to reflect trends for 2008?
>
> A. No reason.
>
> Q. No reason why you didn't do it?
>
> A. No reason. Could have done it, [but I] didn't do it. No reason.

In response to the summary judgment motion, plaintiff provided the report of an expert with experience in appraising surgical centers. The expert opined that Shuffler, without explanation, utilized DSCR—a factor intended to account for "the capital risk peculiar to a specific practice as well as the general economic outlook and the outlook for the health care industry"—of .8102 suggesting a greater capital risk than suggested by the .4365 used by Shuffler in the 2006 appraisal. Observing that the New Jersey Department of Health and Senior Services had imposed a moratorium on new privately-owned ambulatory surgery centers within the State, plaintiff's expert asserted that the DSCR figure should have been at least consistent with the 2006 appraisal if not even further reduced rather than increased.

To be sure, we are dealing with something less than an exact science, and experts in this field will likely disagree as to the precise fair market value for Surgiplex. And we do not mean to suggest there may not be valid reasons for Shuffler's particular methodology. The point is that the judge disposed of this case by way of summary judgment without giving plaintiff the benefit of what his expert opined. The fact that Shuffler appears to have deviated from the methodology employed prior to plaintiff's resignation from Surgiplex supports the contention that plaintiff's reasonable expectations have not been fulfilled. Plaintiff was entitled to the judge's assumption of the truth of plaintiff's claimed expectation that the appraiser would adopt the same approach used for the earlier appraisals. Again, as we noted at the outset of this particular discussion, the operating agreement in this regard alludes to an earlier appraisal and anticipates the use of the same appraiser—a contractual stipulation that strongly suggests the next appraisal would be produced in a similar fashion using the same methodology. The fact that there may have been a departure from what had previously occurred—a circumstance yet to be determined by the trier of fact—presented an adequate ground for the denial of the Surgiplex defendants' motion for summary judgment.

In that same vein, we reject the notion that the parties' consent to a single appraiser to assess the fair market value of Surgiplex foreclosed any litigation about the result derived. In short, we reject the contention that the operating agreement created a form of alternate dispute resolution that precludes litigation. Indeed, we agree with the Court of Appeals for the Tenth Circuit when, in considering a matter governed by New Jersey law, held that an appraisal process designed to fix a purchase price was not akin to arbitration, which, once concluded, offers few grounds for relief for a party aggrieved by the result. *Salt Lake Tribune Publ'g Co., LLC v. Mgmt. Planning, Inc.,* 454 *F.*3d 1128, 1133–35 (10th Cir.2006). The *Salt Lake* court correctly recognized that our standards for setting aside an arbitration award—i.e., fraud, corruption, or similar wrongdoing, *Tretina Printing, Inc. v. Fitzpatrick & Assocs., Inc.,* 135 *N.J.* 349, 358 (1994)—although applicable, are not the only circumstances that may form a challenge to an appraisal designed to fix a contractual term. *Salt Lake, supra,* 454 *F.*3d at 1135. The *Salt Lake* court instead correctly held that our Supreme Court's decision in *Elberon Bathing Co. v. Ambassador Ins. Co.,* 77 *N.J.* 1 (1978) provided the proper framework for consideration of the extent to which such an appraisal may be judicially challenged. *Salt Lake, supra,* 454 *F.*3d at 1134–36. We recognized as much in *Ward v. Merrimack Mut. Fire Ins. Co.,* 332 *N.J.Super.* 515, 527–30 (App.Div.2000).

***5** In short, the law views an appraisal process like that adopted by the parties here differently than the arbitration process. An aggrieved party may challenge an appraisal not only on the grounds recognized in *Tretina* for attacking arbitration awards, but also when the appraiser has made a mistake of law or when the appraiser has misapprehended the facts or issues presented. For example, in *Elberon Bathing,* the Court held that the aggrieved party could challenge the majority appraisers' failure [3] to deduct for depreciation in determining the actual cash value of a loss. 77 *N .J.* at 15. And in *Salt Lake,* the court held that a party could judicially challenge an appraisal on the ground that the appraiser failed to abide by the contract's definition of fair market value. 454 *F.*3d at 1138–39.

Until the record is further developed, we are content to conclude—in giving plaintiff the benefits to which he was entitled in opposing summary judgment—that there is a genuine factual dispute about whether 7/49's apparent departure in methodology from the prior appraisals and whether the other assertions contained in plaintiff's expert's report represent what *Elberon Bathing* referred to as "a mistake of law," 77 *N.J.* at 15, that a court may remedy. [4]

For all these reasons, we reverse the summary judgment entered in favor of the Surgiplex defendants. And, because the judge did not express a separate basis for dismissal in favor of 7/49 and Shuffler, we reverse the summary judgment entered in their favor for the same reasons. Indeed, plaintiff's expert opined that 7/49 and Shuffler departed from acceptable accounting principles in producing the appraisal in question, a contention the judge was required to accept as true in ruling on the summary judgment motion of 7/49 and Shuffler; had the judge adhered to the *Brill* standard, these circumstances required denial of the summary judgment motion of 7/49 and Shuffler.

We lastly turn to two other matters raised in the appeal and cross-appeal.

In his appeal, plaintiff argues that he lawfully rescinded his resignation from Surgiplex. We reject this. Absent the parties' contrary agreement, a member of a limited liability company is dissociated from the company, by operation of law, and unless otherwise agreed or consented to, "on the date the limited liability company receives notice of the member's resignation as a member, or on a later date specified by the member." *N.J.S.A.* 42:2B–24(a)(1). Plaintiff designated December 31, 2008, as the effective date of his resignation. Plaintiff has presented no valid ground to support his argument that he had a right to later rescind his resignation.

We lastly reverse the trial judge's grant of summary judgment in favor of plaintiff on the first count of the counterclaim. In that count, the Surgiplex defendants alleged an entitlement to damages in the form of counsel fees, pursuant to section 7.6(a)(iii)(C) of the operating agreement, claiming plaintiff refused to supply or execute documents necessary to consummate the buy-out of his interest in Surgiplex. Until there is a proper disposition of plaintiff's claims, there can be no clear determination of any liability plaintiff may have, if any, to the Surgiplex defendants based on this provision of the operating agreement.

***6** It is not necessary to consider any of the other arguments posed by the parties in this appeal and cross-appeal to the extent not already discussed.

Reversed and remanded. We do not retain jurisdiction.

All Citations

Not Reported in A.3d, 2013 WL 2436045

Footnotes

1 The operating agreement suggests as much. In describing the attributes of an appropriate replacement for PBA, section 7.8(a)(ii) directs that the "other appraiser" "shall either" be "a member of the American Society of Appraisers" possessing "at a minimum, a designation of 'Accredited Senior Appraiser' ..." or have "national" or other acceptable experience "in appraising or valuing ambulatory surgery centers." In short, the parties intended that the appraisal should have a high reputation and considerable experience in appraising companies like Surgiplex, and it is not reasonable in light of these provisions to assume the parties anticipated that the appraiser could fix Surgiplex's fair market value without resort to principles recognized in the industry.

2 Plaintiff has argued that 7/49's appointment as appraiser was not authorized by Surgiplex. This contention has not been sufficiently developed to permit its summary resolution in the trial court.

3 In *Elberon Bathing,* the process called for each party to appoint an appraiser, who would then select an impartial umpire. 77 *N.J.* at 5. Plaintiff's appraiser and the umpire produced an appraisal with which defendant's appraiser refused to agree. *Ibid .*

4 Our decision in this regard should not be interpreted as a limitation on what other criticisms of the appraisal may also constitute a mistake of law of the type referred to in *Elberon Bathing.* Our decision should also not be viewed as suggesting the outcome of an adjudication of plaintiff's claims. We again emphasize that we are only determining whether the trial court erred in granting summary judgment and not whether, at the end of the day, plaintiff is entitled to relief.