STATE OF MICHIGAN

IN THE CIRCUIT COURT FOR THE COUNTY OF GRAND TRAVERSE

WILLIAM J. STRICKLER, THOMAS G. McINTYRE, WILLIAM D. McINTYRE, JR., E. DAVID ROLLERT and JOHN A. MACNEAL,

Plaintiffs,

v

File No. 97-15735-CK
HON. PHILIP E. RODGERS, JR.

THE RAO GROUP, INC. (formerly known as ELLIS TIRE CENTERS, INC., and/or RAO WHOLESALE TIRE CENTERS, INC.), jointly and severally,

Defendants.
______________________________/

John A. MacNeal (P24098)
Attorney for Plaintiffs

Thomas L. Phillips (P23106)
Co-Counsel for Plaintiffs

Mark M. Snitchler (P41117)
Attorney for Defendants

Joseph C. Fisher (P24061)
Co-Counsel for Defendants

DECISION AND ORDER

Plaintiffs' Complaint alleges a breach of contract by the Defendants regarding payment for stock sold pursuant to a written Stock Purchase Agreement ("Agreement"). The Court first substantively addressed the parties' competing claims in their cross-motions for summary disposition. In an oral bench opinion provided on March 5, 1998, the Court ruled in Plaintiffs' favor and held that a disputed $20,000 payment was the price of deferring further payments under the

terms of the parties' Agreement. However, the Court also held that a judgment for the deferred purchase price could not enter at that time as there were outstanding factual issues regarding whether the remaining portion of this initial payment had been forgiven or waived and there were questions of law regarding the application of the equitable doctrines of waiver, estoppel or laches and an ostensible parol modification of the parties' Agreement. These issues had been partially briefed but were not before the Court for decision as a part of the parties' dispositive motions.

The case was then tried to the Court as a bench trial on March 10, 11 and 24, 1998. The Court then took the matter under advisement. Having now had the opportunity to review the evidence introduced at the trial, the parties' written and oral presentations and being fully advised in the premises, the Court will now make its findings of fact and present its conclusions of law. MCR 2.517.

The Plaintiffs were the original shareholders in American Tire Reclamation, Inc. ("ATR"). Simply stated, ATR was a thinly capitalized, closely held corporation whose business was to develop a profitable process for collecting, shredding and recycling scrap tires. This specific process for recycling is described as pyrolysis and involves "cracking" tires in a fashion analogous to the "cracking" of crude oil at refinery into component parts. If ATR was to be successful, it had to profitably market the by-products of tire pyrolysis. The most significant of these by-products was carbon black.

Plaintiffs were aware of others' unsuccessful efforts to address the significant environmental issue posed by the millions of scrap tires located in this country, but believed they had a unique method to further process the carbon black into a commercially saleable product. The inventor of this process was Jack Fader. ATR applied for and obtained patents relating to Mr. Fader's processes. Plaintiffs ultimately invested hours of time and approximately $362,500 in cash when they determined that they had neither the energy nor the finances to move the venture to the point of commercial success. Plaintiffs sought an equity partner.

The Defendants are tire wholesalers and distributors with significant expertise in the collection and disposal of scrap tires. The Defendants (collectively referred to as "RAO") purchased a 50 percent interest in ATR in 1988. Over the next two years, RAO ran ATR and invested time, energy

and funds substantially equivalent to Plaintiffs' capital investment. Mr. Fader continued to hold five percent of ATR's outstanding shares.

After two years of operating and thoroughly examining ATR, Defendants offered to buy the remaining shares of ATR, with the exception of Mr. Fader's five percent. The parties' Agreement was reduced to writing and is memorialized as a Stock Purchase Agreement dated July 1, 1990. It was received into evidence as Defendants' Exhibit A.

It is acknowledged that the terms of payment were extremely favorable to the RAO Defendants. The Plaintiffs had made a substantial initial investment but were incapable of pursuing the technology to the point of financial success. Recovery of their capital investment was doubtful. Accordingly, the sale price was approximately equal to Plaintiffs' capital investment. Further, so long as the Defendants pursued the technology in good faith and made a timely $20,000 down payment, the balance of the purchase price would be deferred until the technology became commercially viable and, if that never occurred, the price would be deferred forever. The purchase price was $362,500. RAO also had the option to obtain a prompt discount for cash and could have purchased the remaining shares for $275,000. This option was not exercised.

As previously discussed, this Court interpreted the parties' contract as a matter of law in the context of the cross-motions for summary disposition. The individual businessmen on each side of this transaction are bright and commercially sophisticated. Each was well represented by independent counsel at all relevant times.

The parties agreed that it was the Court's obligation to interpret the Agreement consistent with its clear and unambiguous terms. Each side agreed that the contract had to be given its plain and ordinary meaning, that constrained constructions should be avoided and, where possible, the intent of the parties had to be ascertained within the four corners of the instrument.

In recognition of these hornbook principles, the Court rather quickly determined that the alternate payment provisions of section 8.2 required that $20,000 be paid prior to March 31, 1991, with the balance of $342,500 to be paid by February 1, 1995, unless, despite Defendants' good faith efforts, the commencement of operations of a commercially viable enterprise had not begun. In these latter circumstances, the remaining payment might be deferred forever.

A successful commercial venture has not commenced, and RAO exercised good faith in its efforts to pursue the technology. It is undisputed that no portion of the $20,000 down payment was tendered by March 31, 1991. Plaintiffs filed a lawsuit to secure the initial payment in April of 1991, which suit did not accelerate the balance. However, Plaintiffs chose not to serve the complaint and the lawsuit was dismissed without prejudice for the failure to serve the process within the time period allowed by the summons.

After forebearing for approximately one year, the Plaintiffs elected to accelerate the entire $362,500 payment and communicated their intent in written correspondence. See, Defendants' Exhibit B. Not surprisingly, this letter led to a discussion between Plaintiffs and Defendants. The parties agreed that the $20,000 would be paid in two installments. The first was due on or before August 11, 1992 and the second no later than October 11, 1992. This agreement is memorialized in a writing signed by the parties which was received as Defendants' Exhibit C. The first $10,000 payment was timely made consistent with the August 4, 1992 letter agreement. The remaining $10,000 was not paid by October 11, 1992. Defendants alternatively argue that it was paid in a different form or that its payment was forgiven or that Plaintiffs may not accelerate the deferred sums for equitable reasons.

The Court finds as a matter of fact that the payment was not made in an alternative form. The two alternatives provided to the Court both involve the inventor, Jack Fader. Mr. Fader was apparently bright and motivated, but financially irresponsible. The first alternative offered was a payment that satisfied a Jack Fader mortgage issue and the second involved the resolution of litigation between Mr. Fader and the Pebble Creek Condominium Association. The mortgage issue was satisfied prior to the 1990 Stock Purchase Agreement and is referred to in the Agreement. See, Defendants' Exhibit A, p 4. Resolution of this mortgage issue cannot constitute legal consideration for the forgiveness of a debt first recognized in the Stock Purchase Agreement and later ratified in the August 4, 1992 letter agreement.

The second alternative relates to the resolution of the Pebble Creek Condominium Association lawsuit. In his affidavit, Mr. Rao referred to his settlement of this 1991 litigation as the mechanism by which he made the second $10,000 payment called for in the August 4, 1992 letter agreement. Yet, the Pebble Creek Condominium Association litigation was not even filed until after

Plaintiffs had forwarded and Mr. Rao had accepted the forbearance terms on our about August 4, 1992. Nor is there any written documentation which would suggest that the resolution of the Pebble Creek litigation was intended to constitute payment of the final $10,000.

Next, RAO argues that one of the Plaintiffs, Thomas McIntyre, met with the principal of the Defendants, Duane Rao, in his office in Detroit and orally promised to forgive the $10,000 in consideration for continued investment by Mr. Rao. There is no documentation to support the communication, and Mr. McIntyre denies making the promise. An employee of Mr. Rao's, Mr. Jung, confirms the agreement although he recalls nothing else that occurred in 1992 and although he had no involvement whatsoever with the ATR project in 1992. In resolving this dispute, the Court must return to the agreement and its provision for amendments, review the course of conduct between the parties and then determine whether Defendants have proven an oral modification by a preponderance of the evidence.

Each party was independently represented by a competent counsel when the 1990 Agreement was drafted and executed. Not surprisingly, the Agreement clearly provides that it may not be amended orally but only in a writing signed by the parties. Consistent with this agreement, the course of conduct between the parties was to have their one contractual modification reduced to a writing signed by the parties. This is the agreement to forbear from accelerating the balance due and provide RAO with an opportunity to cure that is reflected in the August 4, 1992 letter agreement. Defendants' Exhibit C.

Further, since the Agreement was one for the purchase and sale of stock certificates, it was subject to the Statute of Frauds. MCL 440.8319; MSA 19.8319. Michigan appellate decisions have refused to recognize oral modifications of written agreements as violative of the Statute of Frauds. *Schultz v Silver*, 323 Mich 454, 460; 35 NW2d 383 (1949); *Windorf v Ferris,* 154 Mich App 201, p 203-204; 397 NW2d 268 (1986).

Parol modifications of written agreements is also the subject of a Michigan statute. MCL 566.1; MSA 26.978(1) requires written modifications of written agreements. It provides as follows:

> An agreement hereafter made to change or modify, or to discharge in whole or in part, any contract, obligation, or lease, or any mortgage or other security interest in personal or real property, shall not be invalid because of the absence of the consideration: Provided That the agreement changing, modifying, or discharging such

contract, obligation, lease, mortgage or security interest shall not be valid or binding unless it shall be in writing and signed by the party against whom it is sought to enforce the change, modification or discharge.

While there are exceptions to this statute which have been recognized for subsequent oral modifications supported by independent consideration, explicit contract language generally prevails over inconclusive oral assurances. See, *Evans v F J Boutell Driveaway Co*, 48 Mich App 411, 421; 210 NW2d 489 (1973). Here, RAO had an independent obligation to exercise good faith in the development of the technology. RAO's continued investment in ATR technology could not constitute an enforceable promise to support the deferral of a payment obligation arising from the Agreement since RAO was under a pre-existing contractual obligation to do just that. In other words, RAO could not make a new promise to invest in ATR technology as it already had the obligation to do so. The attempt to bootstrap a pre-existing promise into consideration for forgiveness of its obligation to make the modest $20,000 payment must fail. See, *Green v Millman Bros Inc*, 7 Mich App 450, 455; 151 NW2d 860 (1967).

Without question, RAO negotiated an advantageous purchase agreement with Plaintiffs. Indeed, Plaintiffs were over a barrel. Plaintiffs had invested in excess of $360,000 of their money and countless hours of their time and were in no position to pursue the technology further. RAO negotiated a contract which gave it a choice between a substantial discount for a prompt cash payment or with an exceedingly modest down payment the opportunity to defer paying Plaintiffs forever should its good faith efforts to pursue ATR technology not be successful. Alternatively, if RAO was successful, Plaintiffs would receive their original investment and nothing more and RAO would reap the benefit of substantial profits.

It was illogical not to pay the $20,000 in a timely fashion and then not to take full advantage of the forbearance agreement negotiated in August of 1992. The question, however, is not whether RAO acted logically, but whether RAO's poor decision is attributable to inappropriate behavior on the part of the Plaintiffs which led to justifiable reliance of the type recognized in equity. Here, RAO argues from an undocumented oral conversation between Thomas McIntyre and Duane Rao, which conversation ostensibly occurred in the RAO offices subsequent to August of 1992. RAO states that Thomas McIntyre waived the final $10,000 payment for all Plaintiffs in exchange for Mr. Rao's

continued pursuit of ATR technology. Despite the fact that Mr. Rao had signed two separate written agreements promising to pay this sum, he did not confirm this conversation with a letter or memorandum in any form. Yet, RAO would have this Court invoke its equitable powers to preclude the Plaintiffs' reliance on clear written agreements and a course of conduct consistent with those written agreements in deference to this alleged oral promise.

It is precisely this type of swearing contest that the Statute of Frauds, Parol Evidence Rule and the legion of cases interpreting each attempt to avoid. Did such a conversation occur and was Mr. Rao justified in relying upon it? What value do we provide to the certainty of precise written instruments in the face of such oral modification claims? Given the precision with which the Agreement was drafted and the course conduct leading up to the execution of the August 4, 1992 forbearance agreement, the Court cannot find justifiable reliance even if it were to assume the conversation did occur. Mr. Rao was not mislead.

A simple letter to the other parties confirming his understanding with Mr. McIntyre and requesting a signature in a fashion similar to that in August of 1992 would have allowed Mr. Rao to determine whether Mr. McIntyre was making an agreement on behalf of his partners or whether there was some misunderstanding regarding the Plaintiffs' position. Mr. Rao chose not to do this but to continue to abide by his original agreement; i.e., he continued to pursue the ATR technology. Without written confirmation, the parties' course of conduct gave Mr. Rao no justifiable reason to rely on what he claims to have perceived as an oral waiver. Given the paucity of evidence provided to the Court and recognizing that waiver, estoppel and laches are affirmative defenses, the burden of persuasion for which lies with the RAO Defendants, the Court cannot find a knowing and intentional relinquishment of a known right by the Plaintiffs, nor can it find justifiable reliance or conduct abhorrent to equitable principles.

Rather, whether born out of frustration at the monies he was investing and the absence of light at the end of a long financial tunnel or for other unarticulated reasons, Mr. Rao exercised poor judgment and failed to make the final $10,000 payment necessary to purchase potentially indefinite forgiveness of the remaining purchase price. Accordingly, it is the determination of this Court that Plaintiffs are entitled to a judgment in the principal amount of $352,500 together with interest at the

rate of 6 percent per annum from October 11, 1992 through the date the complaint was filed and thereafter at the statutory rate of 12 percent. Plaintiffs are also entitled to an award of taxable costs.

Plaintiffs are directed to submit a proposed judgment consistent with this Decision and Order pursuant to one of the alternative provisions described in MCR 2.602(B). Plaintiffs should also set forth their calculation of interest, including a per diem figure and statutory costs. Timely filed objections to the Plaintiffs' calculations or requests for costs will either be resolved pursuant to written arguments on a pre-hearing order or the Court will schedule unresolved issues for oral argument after the written submissions are received.

IT IS SO ORDERED.

____
HONORABLE PHILIP E. RODGERS, JR.
Circuit Court Judge

Dated: __________________________