COURT OF APPEALS
DECISION
DATED AND FILED

December 18, 2008

David R. Schanker
Clerk of Court of Appeals

Appeal No. 2008AP185 **Cir. Ct. No. 2004CV933**

STATE OF WISCONSIN **IN COURT OF APPEALS**
DISTRICT IV

JAMES GRAFFT,

PLAINTIFF-RESPONDENT-CROSS-APPELLANT,

V.

DONALD G. JENSEN, JR. D/B/A/ EQUITY MANAGEMENT SERVICES AND EQUITY MANAGEMENT SERVICES, INC.,

DEFENDANTS-APPELLANTS-CROSS-RESPONDENTS.

APPEAL and CROSS-APPEAL from a judgment of the circuit court for Rock County: MICHAEL J. BYRON, Judge. *Affirmed.*

Before Dykman, Vergeront and Bridge, JJ.

¶1 VERGERONT, J. This is a negligence action filed by James Grafft against the accountant who provided services for Injection Technologists, Inc. (ITI), of which Grafft was an investor, lender, and part owner at the time. On Grafft's prior appeal we held that the circuit court had erred in deciding, after a

trial to the court, that his initial investment in ITI and his personal loan to ITI were not recoverable as damages based on public policy grounds. We also held that the circuit court had not erred in offsetting Grafft's damages by the value of the ITI assets he retained. We remanded to the circuit court for additional findings on damages. On remand the circuit court determined that Grafft's total damages were $58,804.61 reduced to $29,402.30 because of Grafft's 50% contributory negligence.

¶2 On this appeal, Grafft's former accountant, Donald Jensen,[1] contends the circuit court erred on remand in two ways. First, the court should have held that, having retained ITI's assets, Grafft is not permitted under WIS. STAT. § 409.505(2)[2] to recover from his accountant damages based on Grafft's payment to the bank on his personal guaranty and the loss on his loan to ITI. Second, according to Jensen, the court erroneously exercised its discretion in not offsetting Grafft's damages by the amount of economic benefit Grafft derived from the new entity he formed with ITI assets. With the correction of these errors, Jensen contends, Grafft is entitled to no damages.

¶3 We conclude that WIS. STAT. § 409.505(2) does not bar Grafft's recovery of damages from his accountant based on Grafft's payment to the bank on his personal guaranty and the loss on his loan to ITI. We also conclude the circuit court did not erroneously exercise its discretion in declining to offset

[1] Donald Jensen owns and operates Equity Management Services, Inc., the other defendant in this action. We refer only to Jensen in this opinion because there is no need to distinguish between the two.

[2] All references to the Wisconsin Statutes are to the 1999-2000 version unless otherwise noted.

Grafft's damages by profits from the new entity. Accordingly, we affirm on the appeal.

¶4 On Grafft's cross-appeal he challenges the circuit court's legal conclusion that his damages should be offset by the amount of his future tax benefit from writing off his loan to ITI. He also challenges the court's finding that a reasonable calculation of the present value of that benefit is $11,211.75. We conclude the court did not err either legally or factually in determining this offset. Accordingly, we affirm on the cross-appeal.

BACKGROUND

¶5 In our decision on the prior appeal, ***Grafft v. Jensen***, No. 2006AP1793, unpublished slip op. ¶¶3-9 (WI App July 12, 2007), we set out the facts leading to Grafft's filing of this action and the testimony at the trial to the court. We do not repeat those here, but begin with the circuit court's ruling after the trial. The court found that Jensen was negligent because he had known that Rusty Schoville, the 50% owner of ITI at the time, had embezzled from the company by taking unauthorized duplicate checks and Jensen had failed to notify Grafft.[3] The court also found that Grafft was 50% negligent. The court found that ITI's insolvency and foreclosure were at least in part due to Schoville's embezzlement.

¶6 At trial, Grafft sought the following damages, which totaled $211,345.86: (1) $10,625 for his initial purchase of 25% of ITI stock; (2) $25,000

[3] These liability determinations were the subject of Jensen's cross-appeal on the prior appeal and were affirmed.

for his purchase of another 25% of ITI stock; (3) $58,444.86, the amount he paid to Johnson Bank pursuant to his personal guaranty of a bank loan to ITI; and (4) $117,276, the balance owed on Grafft's personal loan to ITI. The court determined that Grafft's initial investment and loan to ITI were not recoverable on public policy grounds, but that Grafft's second investment and his payment to the bank were recoverable and were appropriate damages. The court also determined that those damages—$83,444.86—should be offset by the value of ITI's assets, which Grafft retained after being assigned the bank's security interest in the assets. The court valued the assets at $141,329.50, resulting in an award of no damages to Grafft.

¶7 On the first appeal, Grafft contended that (1) the circuit court erred in determining that public policy factors precluded awarding him damages for his initial investment and his loan to ITI, and (2) the circuit court erred in offsetting his damages by the value of the ITI assets he retained. Because Jensen had also argued to the circuit court that any damages should be offset by two additional items—the profits generated by Pro Plastics, the corporation Grafft started with the ITI assets, and the tax savings Grafft realized from his losses in ITI—Grafft asked that we hold that there be no offset for any benefit he derived from the assignment of the bank's security interest in the ITI assets.

¶8 We concluded that policy factors did not preclude damages for Grafft's initial investment or his loan to ITI, just as it did not preclude damages for his second investment and his payment to the bank on his guaranty. ***Id.***, ¶¶15-17.

¶9 With respect to the offset made by the circuit court for the ITI assets, we rejected Grafft's arguments that the court had erred in this regard. ***Id.***, ¶¶25, 29. With respect to an offset for Pro Plastics' profits, we explained that we were

not considering it because the circuit court had not done so. ***Id.***, ¶30. With respect to the tax benefit, we noted that the court had found Grafft did enjoy a tax benefit by writing off his loan to ITI but did not make a finding on the amount and the testimony of Jensen's expert presented a range on this value. ***Id.*** Because of this, we said, "[w]e are unable to determine the actual benefit Grafft accrued or whether that amount offsets Grafft's damages. We therefore remand to the circuit court for its factual determination as to Grafft's total damages." ***Id.*** (Footnote omitted in which we recognized that, given the lower amount of damages the circuit court had arrived at as a result of excluding two items based on the public policy factors, the amount of the tax benefit had not been relevant.)

¶10 In the summary of our holdings, after stating that we reversed the circuit court's ruling on the public policy factors and affirmed its ruling on the offset for the ITI assets, we stated:

> Because the circuit court did not make a finding as to the amount Grafft would reasonably benefit from the lost loan as a bad debt on his taxes, and whether that or any other amount should also be considered in calculating Grafft's damages, we remand for proceedings consistent with this opinion.

Id., ¶31 (footnote omitted).

¶11 In briefing on remand, Jensen argued that Grafft was not entitled to recover for the amount he paid the bank on his personal guaranty of ITI's loan nor for the amount he lost on his loan to ITI because under WIS. STAT. § 409.505(2) Grafft's retention of ITI assets constituted a full satisfaction of ITI's secured debt to the bank and to Grafft personally.[4] Jensen also argued that the court should

[4] WISCONSIN STAT. § 409.505(2) provided:

(continued)

make findings on offsets against damages for the tax benefit and for the full economic gain Grafft realized by using ITI's assets in the "conversion" of that business to Pro Plastics.

¶12 Grafft's position on remand was that our decision had limited the circuit court on remand to making findings regarding whether the tax benefit should be an offset and, if so, how much. Grafft argued that as a matter of law there could be no offset for any tax benefit, but, even if an offset was permissible, Jensen had not carried his burden to prove the amount.

¶13 The circuit court issued a written decision and order as well as findings of fact and conclusions of law. It rejected Grafft's argument that it should not allow an offset for the tax benefit from the capitol loss on Grafft's personal loan to ITI and determined the present value of the tax benefit from the loss to be $11,211.75. The court also found that, besides the value of the ITI

> In any other case involving consumer goods or any other collateral a secured party in possession may, after default, propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if the debtor has not signed after default a statement renouncing or modifying the debtor's rights under this subsection and except in the case of consumer goods to any other secured party who has a security interest in the collateral and who has duly filed a financing statement indexed in the name of the debtor in this state. If the debtor or other person entitled to receive notification objects in writing within 21 days from the receipt of the notification or if any other secured party objects in writing within 21 days after the secured party obtains possession the secured party must dispose of the collateral under s. 409.504. In the absence of such written objection the secured party may retain the collateral in satisfaction of the debtor's obligation.

WISCONSIN STAT. § 409.620 (2005-06) replaced WIS. STAT. § 409.505(2) (1999-2000) effective July 1, 2001. 2001 Wis. Act 10, § 78.

assets and the tax benefit, "no other amounts have been proven which should be off-set in calculating Grafft's damages." The court found that Grafft suffered damages in the amount of $211,345.86 as a result of Jensen's negligent conduct. Reducing that amount by the offsets for the ITI assets and the tax benefit and by the 50% reduction for Grafft's contributory negligence, the court awarded Grafft $29,402.30 in damages.

DICUSSION

I. Jensen's Appeal

A. Effect of WIS. STAT. § 409.505(2) on Grafft's Damages

¶14 Jensen contends the circuit court erred in considering Grafft's payment to the bank on his personal guaranty and the loss on his loan to ITI as damages because, under WIS. STAT. § 409.505(2), Grafft's retention of ITI assets constituted a full satisfaction of those secured debts. Grafft responds that Jensen has waived this issue by not sufficiently raising it in the circuit court at trial and not presenting a developed argument on this point on the prior appeal. On the merits, Grafft responds that neither § 409.505(2) nor any case law Jensen presents supports his contention that a satisfaction of ITI's debt to him under the statute precludes him from recovering the deficiency from Jensen.

¶15 We first address waiver. We agree with Jensen that he did argue in his post-trial brief in the circuit court that Grafft's taking of ITI's assets constituted a satisfaction in full of ITI's debt to him under WIS. STAT. § 409.505(2) and therefore Grafft could not recover from Jensen for the amounts Grafft paid to the bank on his personal guaranty or the loss on his loan to ITI. The circuit court found that Grafft "seized and held the assets in full satisfaction of the

debts owed by ITI to Johnson Bank … and Grafft." However, the circuit court did not conclude that, as a result, Grafft could not recover those items of damages from Jensen. While the court apparently did not discuss its reasons for rejecting Jensen's position on this point, it implicitly rejected it in deciding that Grafft was entitled to recover the $58,444.86 he paid to the bank on his personal guaranty. As noted above, the court's decision that Grafft could not recover for the loss of his loan to ITI was based on public policy grounds, not on Jensen's theory under § 409.505(2).

¶16 Because the circuit court rejected Jensen's argument, Jensen could have argued, as the respondent on the prior appeal, that the circuit court erred in doing so. Such an argument would have been a ground for reversing the court's decision that Grafft's payment on his guaranty was an appropriate item of damages and it would have been an alternative ground for affirming the circuit court's decision that the loss on Grafft's loan to ITI was not an appropriate item of damages. Although Jensen did assert in his brief on the prior appeal that Grafft's acquisition of the assets was a full satisfaction of ITI's debt to him, he did so briefly and only in the context of refuting Grafft's challenges to the court's public policy determination and to the offset for the ITI assets.

¶17 Had Jensen developed a separate argument that the full satisfaction of ITI's debt was a reason the circuit court erred in awarding damages for Grafft's payment on his personal guaranty and also was an alternative ground for affirming the circuit's decision not to award damages for Grafft's loss on his loan to ITI, we would have decided this issue in our prior opinion. Instead, we did not address it. As Jensen points out, the construction and application of the statute to undisputed facts is a question of law, which we review de novo. ***Guertin v. Harbour Assur. Co.***, 141 Wis. 2d 622, 627-28, 415 N.W.2d 831 (1987). Our remand, as the circuit

court correctly understood, was for the purpose of making findings of fact regarding offsets for damages. Nothing in our opinion required the circuit court to decide this question of law, which it had already implicitly rejected.

¶18 Even though Jensen may have waived the right to raise this issue on this second appeal by not presenting it on the prior appeal in a sufficiently developed and prominent manner, we choose to address the issue on its merits now.

¶19 WISCONSIN STAT. § 409.505(2) provides a procedure for a secured party to "retain the collateral in satisfaction of the debtor's obligation." It plainly does not address the issue here—whether Grafft may recover the difference between the value of the collateral and the amount of ITI's obligation from a third party whose negligence, the court found, caused ITI to be unable to fulfill its obligations. Jensen does not provide any case law authority for the application of the statute to bar recovery on a negligence theory from a third party, as distinguished from recovery from the debtor on the note.

¶20 We conclude the circuit court did not err in awarding damages for Grafft's payment to the bank on his personal guaranty and for the loss on his loan to ITI.

B. Offset of Economic Benefits from Pro Plastics

¶21 Jensen contends the circuit court erroneously exercised its discretion by failing to make an express ruling on whether all or some portion of Pro Plastics' profits should be applied as an offset to Grafft's damages. According to Jensen, this is contrary to our directions on remand. We disagree.

¶22 In rendering its decision after the trial, the circuit court considered Jensen's argument that Grafft's damages should be offset by the economic gain Grafft realized from using the ITI assets in his new company. The court stated its decision as follows:

> Now, the question of the amount—as I said, if someone were evaluating a going business, which this was, it never stopped being a going business until it was just let go by Mr. Grafft. A new corporation was founded. The first year profits, I agree, shouldn't dollar for dollar be put into this. It probably should have been put into an analysis of what the going business was worth before it was started, but that hasn't been done. I don't have any figures. So the best figures I got are what the book value of the equipment was and what was come up with by Mr. Bagley.
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> ….
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> The accounts receivable, he's [Mr. Bagley] got low and high valued and the accounts receivable at 32,495 or 35. And everybody's testimony was they were quality accounts receivable. The inventory, 40,000, minimum of 53,794. The fixed assets, which admittedly are the most difficult to try to ascertain, but when you're—when you continue to run a growing business or if you sell something as a going business, you don't take the scrap value. You take the value as it sits, and Mr. Grafft already had the lease for the building.
>
> So I'm going to find that the—whatever damages I found that Mr. Grafft has suffered is mitigated by the sum of the average of 122,495 and 160,164. [$141,329.50] I think all of those assets are attributable to his realizing on his security interest.

¶23 On the prior appeal, as noted above, Grafft asked that we rule that the circuit court could not offset against damages *any* benefit he derived from the ITI assets, even though the court had offset only the value of the assets and had rejected a greater offset based on the profits of Pro Plastics. In response, Jensen argued that the court properly considered the value of the assets as an offset and in that context referred to other financial benefits Grafft realized from the profits of

Pro Plastics. However, Jensen did not argue that the circuit court erred in not applying the profits as an offset in addition to the offset for the value of the ITI assets. Such an argument would have brought to our attention the trial court's above-cited rejection of Jensen's proposal to include Pro Plastics' profits in the offset and would have explained why that decision was in error. Reflecting the argument Jensen made to us, we did not rule in our prior opinion on whether the court's decision not to allow an offset for profits from Pro Plastics was in error.

¶24 On remand the circuit court found that, besides the value of the ITI assets and the tax benefit, "no other amounts have been proven which should be off-set in calculating Grafft's damages." We are satisfied from this finding that the circuit court understood that on remand it could consider offsets in addition to the ITI assets it had already allowed and in addition to the tax benefit, which was the focus of our remand. We also observe that the circuit court specifically cited in its decision our directions that,

> because the circuit court did not make a finding as to the amount Grafft would reasonably benefit from the lost loan as a bad debt on his taxes, and *whether that or any other amount* should also be considered in calculating Grafft's damages, we remand for proceedings consistent with this opinion.

(Footnote omitted, emphasis added.) Having already determined that it was not appropriate to offset the profits of Pro Plastics against Grafft's damages, the court was not obligated to reconsider that on remand and its finding—that no amounts other than the value of ITI assets and the tax benefit should be offsets—makes clear that the court was affirming its earlier ruling on Pro Plastics' profits.

¶25 Thus, the only issue before us is whether the circuit court's decision not to allow an offset for Pro Plastics' profits has a reasonable basis in the

evidence viewed most favorably to the award.[5] *See* ***Cords v. Anderson***, 80 Wis. 2d 525, 552-53, 259 N.W.2d 672 (1977). While Jensen's expert presented evidence of the profits of Pro Plastics, the court could reasonably decide it would be unfair to Grafft to reduce his damages by those amounts. The success Grafft achieved in using the assets of ITI in a new company can reasonably be seen as the result of Grafft's efforts, talents, perhaps luck, and other factors that are either unrelated to the assets from ITI or are too tenuously connected to them. Undoubtedly, had Grafft lost money on Pro Plastics, Jensen would not concede that this should *increase* Grafft's damages.

¶26 We conclude the circuit court did not erroneously exercise its discretion in declining to offset Grafft's damages by profits from Pro Plastics.

II. Grafft's Cross-Appeal.

¶27 On his cross-appeal, Grafft challenges on two grounds the court's offset for the tax benefit. First, citing ***Behringer v. State Farm Mutual Automobile Insurance Co.***, 6 Wis. 2d 595, 604, 95 N.W.2d 249 (1959), Grafft contends the circuit court erred in considering any tax benefit because under established law, tax ramifications are ignored in setting damages in personal injury actions. In ***Behringer*** the court held it was not error for the circuit court to decline to instruct the jury in a personal injury action that, because a personal injury award is not subject to state or federal income tax, it should not include in the damage award any amount to compensate for income tax. The court held that if an instruction on the nonliability for taxes *is* given, the instruction should state "not

[5] Jensen does not articulate a legal standard that the circuit court erred in applying or not applying.

only that the jury is to add nothing to the award of damages because of non-liability for income tax but also that nothing is to be deducted from the award because of such factor." ***Id.*** We do not see how the nonliability under state and federal tax law for income taxes on personal injury awards has any bearing on the issue here. In the absence of any authority supporting Grafft's position, we conclude the circuit court was not precluded from considering the tax benefit resulting from a business loss for which Grafft seeks to recover damages.

¶28 Second, Grafft contends the evidence is insufficient to support the circuit court's finding that the present value of the tax benefit was $11,211.75. Again, we disagree.

¶29 Jensen's expert testified that the value of the tax benefit was between $17,591 and $41,047, based on Grafft's tax bracket and depending on the type of income that is being offset. Grafft's expert did not offer any alternative method of valuing the benefit. He testified instead that the tax benefit was not a legitimate offset to Grafft's damages, but we have already rejected this proposition.

¶30 The circuit court did not accept Jensen's expert's testimony as it could have done, but made its own calculations. It considered the amount of the capitol loss Grafft claimed on schedule D of his 1999 tax return from his uncollectible loan to ITI and the benefit Grafft realized for 1999 from the claimed loss. It took the judicial notice of the instructions for schedule D and determined that thirty-nine years was the maximum period of time Grafft would have to wait to realize the full tax benefit from the claimed loss. This assumption benefited Grafft, as the court recognized. Based on the amount of Grafft's capitol gains in 1999 and the corresponding tax benefit he realized from the capitol loss for 1999, as well as his banker's testimony of his financial situation, it is likely that Grafft

will enjoy the full benefit of the capitol loss long before the expiration of thirty-nine years. The court also decided that it was reasonable to average the tax rates identified by Jensen's expert based on the 1999 return, another assumption that benefited Grafft. As the court noted, it was probable, based on the testimony of Grafft's banker, that Grafft's tax bracket was higher than that on the 1999 return. The result of the court's calculation was a present value of the tax benefit that was significantly lower than that presented by Jensen's expert.

¶31 We are satisfied that there was credible evidence from which the court could reasonably find that Grafft had received a tax benefit from the capitol loss and would in the future receive it. We are also satisfied that the court's determination of $11,211.75 is based on credible evidence and is reasonable. *See* ***Cords***, 80 Wis. 2d at 552-53. Accordingly, we affirm the court's offset in this amount.

CONCLUSION

¶32 We affirm the circuit court's rulings on Grafft's damages that Jensen challenges on his appeal. On Grafft's cross-appeal, we affirm the court's offset against his damages for a tax benefit in the amount of $11,211.75. The effect of these holdings is that we affirm the court's award to Grafft of $29,402.30 in damages.

By the Court.—Judgment affirmed.

Not recommended for publication in the official reports.