

**COURT OF APPEALS
DECISION
DATED AND FILED**

September 9, 2010

A. John Voelker
Acting Clerk of Court of Appeals

NOTICE

This opinion is subject to further editing. If published, the official version will appear in the bound volume of the Official Reports.

A party may file with the Supreme Court a petition to review an adverse decision by the Court of Appeals. See WIS. STAT. § 808.10 and RULE 809.62.

**Appeal Nos. 2009AP1825
2009AP2332**

Cir. Ct. No. 2008CV1187

STATE OF WISCONSIN

**IN COURT OF APPEALS
DISTRICT II**

NATIONAL CIVIL LIBERTIES RESEARCH FOUNDATION, INC.,

PLAINTIFF-RESPONDENT,

V.

JOSEPH D. MERKEL,

**DEFENDANT-THIRD-PARTY
PLAINTIFF-APPELLANT,**

**NATIONAL CIVIL LIBERTIES RESEARCH FOUNDATION, INC., BY
BOARD OF DIRECTORS, CRAIG ROYSKE, CHIEKO KNOBLOCK, NELSON
BOON, GARY PLATH, AND JIM HEISER,**

INTERVENOR,

SETH E. DIZARD,

INTERESTED PERSON,

V.

**DAVID C. KANZ, PROVIDENCE SERVICES, LLC, DOUGLAS P. KANZ
AND SCOTT M. McDONOUGH,**

THIRD-PARTY DEFENDANTS.

NATIONAL CIVIL LIBERTIES RESEARCH FOUNDATION, INC.,

PLAINTIFF-RESPONDENT,

V.

JOSEPH D. MERKEL,

DEFENDANT-THIRD-PARTY PLAINTIFF,

**NATIONAL CIVIL LIBERTIES RESEARCH FOUNDATION, INC., BY
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V.

**DAVID C. KANZ, PROVIDENCE SERVICES, LLC, DOUGLAS P.
KANZ AND SCOTT M. McDONOUGH,**

THIRD-PARTY DEFENDANTS.

APPEALS from judgments and orders of the circuit court for
Waukesha County: RALPH M. RAMIREZ, Judge. *Affirmed.*

Before Higginbotham, Sherman and Blanchard, JJ.

¶1 PER CURIAM. Joseph Merkel appeals from judgments and orders granting default judgment to the National Civil Liberties Research Foundation (NCLRF) in this action by David Kanz on behalf of NCLRF.¹ Merkel argues that the orders and judgments must be vacated because: (1) Kanz lacked standing to bring this action on behalf of NCLRF; (2) the circuit court lacked competency to exercise subject matter jurisdiction over this case; (3) Kanz did not present sufficient evidence supporting his cause of action; (4) the court in effect issued an improper contempt penalty; and (5) the default judgment will result in disastrous consequences for NCLRF. We conclude that we have no basis to disturb the circuit court's orders and judgments, and affirm.

Background

¶2 Kanz filed this action on behalf of NCLRF in April 2008. The complaint alleged that Kanz was the president of NCLRF, that Merkel was operating as an officer or director of NCLRF without authority, and that Merkel had wrongfully taken control of NCLRF's bank accounts. Kanz sought an injunction to prevent Merkel from acting on NCLRF's behalf, a constructive trust

¹ A group of individuals who intervened at trial (collectively, the Intervenors) also appeal, and their appeal has been consolidated with this one. Merkel and the Intervenors have filed a joint appellate brief. For ease of reading, we frame the arguments on appeal as Merkel's.

Additionally, Merkel appeals from orders discharging the court-appointed receiver in this action and awarding the receiver attorney fees and costs. The receiver has filed a brief on appeal, pointing out that while Merkel filed a notice of appeal from the orders regarding the receiver, he has not briefed those issues. *See A.O. Smith Corp. v. Allstate Ins. Cos.*, 222 Wis. 2d 475, 491-92, 588 N.W.2d 285 (Ct. App. 1998) (issue must be briefed on appeal to be considered by this court). Merkel replies only that this action was never properly before the circuit court because Kanz lacked standing to sue on NCLRF's behalf, and therefore all orders issued by the circuit court, including the orders regarding the receiver, must be vacated. Because we reject Merkel's underlying contention, we reject his arguments regarding the receiver.

over NCLRF property in Merkel's possession, damages for conversion, and treble damages and attorney fees under WIS. STAT. § 895.446 (2007-08).²

¶3 Merkel answered the complaint, denying that he had acted wrongfully and asserting that he, not Kanz, was the president of NCLRF. He asserted that Kanz did not hold any office within NCLRF and therefore had no standing to bring this action. The circuit court issued a temporary restraining order prohibiting Merkel or Kanz from using or transferring any NCLRF funds. The court also ordered both parties to provide a full disclosure of any information they had regarding NCLRF funds.

¶4 The court set a scheduling order in May 2008, stating that failure to comply with its terms could result in sanctions, including dismissal. Kanz then moved for an order compelling discovery, claiming Merkel had refused to respond to his discovery requests. After a hearing on the motion to compel, the court found that Merkel had failed to comply with its order to disclose information regarding NCLRF assets or respond to Kanz's first set of interrogatories and first requests for production of documents. The court therefore appointed a receiver over NCLRF's assets. The court granted the receiver all necessary powers to control the investigation and management of NCLRF assets. The court also ordered Merkel to provide a written statement of NCLRF's finances to the receiver within ten days of the receiver's request for that information, and ordered the receiver to provide a full statement of NCLRF's finances to the court within sixty days of the order.

² All references to the Wisconsin Statutes are to the 2007-08 version unless otherwise noted.

¶5 In July 2008, Kanz deposed Merkel. Merkel claimed many memory lapses as to the finances of NCLRF. He stated that his wife, Kathy Merkel, had been the other signatory on NCLRF's bank account, and that at some point he was removed as a signatory.

¶6 In August 2008, the circuit court held a hearing on the Intervenors' motion to intervene in this action. The Intervenors claimed to be the lawful members of NCLRF's board of directors. The Intervenors also alleged that Kanz did not represent NCLRF. None of the parties objected to intervention, and the court granted the motion. The Intervenors then filed their own complaint, alleging they were the true board of directors of NCLRF, that Merkel was no longer an officer or director of NCLRF though he had been at one time, and that Kanz had no position within NCLRF. The Intervenors requested a declaration that they, rather than Kanz, lawfully represented NCLRF. Kanz answered, denying the allegations.

¶7 In September 2008, Kanz moved for an order compelling discovery and for sanctions against Kathy Merkel. Kanz asserted that his repeated efforts to depose Kathy Merkel regarding her knowledge of NCLRF bank accounts had been unsuccessful. The court held motion hearings in November and December 2008. At the hearings, the receiver reported that he had encountered difficulties in obtaining financial information from Merkel and the Intervenors. The court issued an order sanctioning Kathy Merkel by prohibiting her from testifying at trial. The court held in abeyance the motion for sanctions against Merkel. The court also warned the parties that failure to comply with discovery or court orders may result in sanctions, including striking of pleadings. The court held another hearing in February 2009, and reiterated that Merkel had not yet complied with the court's orders or discovery.

¶8 In March 2009, Kanz moved to strike the pleadings of Merkel and the Intervenors for failure to comply with court orders and discovery, and for a default judgment. Merkel appeared at the motion hearing, but the Intervenors did not. The receiver and counsel for Kanz stated that hundreds of thousands of dollars of NCLRF funds remained unaccounted for and that Merkel continued to refuse to provide any financial documentation, insisting he did not know what had happened to the funds. Merkel argued that he had complied with discovery to the best of his ability. The court found that Merkel had not complied with the discovery process or court orders.

¶9 The court held an evidentiary hearing on the motion to strike pleadings and for a default judgment. All of the parties appeared at the hearing. The morning of the hearing, the Intervenors provided Kanz with banking records for the NCLRF funds. Merkel argued that although he and the Intervenors had not cooperated with discovery over the course of the year that the case had been pending, they were now willing to cooperate. The receiver testified that Merkel and the Intervenors had not responded to his demands for financial documents for NCLRF, and that funds were withdrawn from the NCLRF accounts without records of where they had gone. He stated that the Intervenors had withdrawn hundreds of thousands of dollars from NCLRF accounts and then refused to turn those funds over to him. He also stated there were multiple withdrawals from NCLRF funds even after he was appointed receiver and after the restraining order prohibiting any use of NCLRF funds was issued. The court found that Merkel and the Intervenors had substantially misrepresented to the receiver that they had no knowledge regarding NCLRF funds, and that they had interfered with those funds contrary to the ongoing restraining order. The court found that Merkel and the Intervenors had failed to comply with discovery or court orders, and that their

behavior was egregious and without justifiable excuse. The court therefore struck their pleadings and entered default judgment in favor of Kanz under WIS. STAT. §§ 804.12, 805.03, and 806.02. Merkel and the Intervenors appeal.

Standard of Review

¶10 A circuit court has discretion to sanction a party by striking pleadings and entering a default judgment. *See Industrial Roofing Servs., Inc. v. Marquardt*, 2007 WI 19, ¶¶39-41, 299 Wis. 2d 81, 726 N.W.2d 898; WIS. STAT. §§ 804.12(2)(a) and 805.03. We uphold a circuit court's exercise of discretion if the court relied on the facts of record and applied the proper standard of law to reach a reasonable determination. *Id.*, ¶41.

Discussion

¶11 Merkel argues that the circuit court erroneously exercised its discretion by striking the defense pleadings and entering a default judgment for Kanz as a sanction for Merkel and the Intervenor's conduct. He argues that the circuit court did not have competency to enter default judgment because Kanz lacked capacity to bring this action on NCLRF's behalf; that the court was required to address its competency to exercise subject matter jurisdiction before entering judgment; that Kanz did not offer evidence sufficient to prove his claim; that the sanction was in effect an improper contempt sanction; and that the default judgment will result in harm to NCLRF. We reject each of these contentions, and affirm.

¶12 Merkel argues first that Kanz lacked standing to bring this action because Kanz was not an officer or director of NCLRF as he claimed in his complaint. *See Norquist v. Zeuske*, 211 Wis. 2d 241, 247, 564 N.W.2d 748

(1997) (“The central standing question is whether a party has a sufficient stake in an otherwise justiciable controversy to obtain judicial resolution of that controversy.” (citation omitted)). Merkel asserts that because Kanz lacked standing, the circuit court lacked competency to enter any rulings or judgment in this action. He also contends that the court was required to address the issue of competency before entering a judgment.

¶13 The problem with Merkel’s argument is that it requires us to resolve a disputed issue of fact: whether Kanz, Merkel, or the Intervenors rightfully controlled NCLRF. The parties’ pleadings made clear that this was one of the issues that would have been litigated at trial. However, the court sanctioned Merkel and the Intervenors by striking their pleadings and entering a default judgment before trial, and therefore the factual dispute was never resolved. The issue in this appeal, then, is not whether Kanz held any office within NCLRF, as he claimed; the issue is whether the circuit court erroneously exercised its discretion in striking the defense pleadings as a sanction and entering default judgment for Kanz.

¶14 Similarly, Merkel’s argument that the circuit court was required to address whether Kanz had standing to bring this action on NCLRF’s behalf before entering a default judgment ignores the procedural posture of this case. The court did not reach the issue of whether Kanz rightfully represented NCLRF because it struck the defense pleadings as a sanction and then entered default judgment. The court was not required to address the disputed issue of Kanz’s standing, which required a trial for resolution. *See Brandon Apparel Grp., Inc. v. Pearson Props. Ltd.*, 2001 WI App 205, ¶11, 247 Wis. 2d 521, 634 N.W.2d 544 (“Default judgment terminates litigation without regard to the merits of the claim.”). Merkel cites no law to support his implied proposition that a court may not sanction a

party by striking pleadings until after a trial to resolve a dispute as to standing, and such a proposition is contrary to Wisconsin case law. *See id.*

¶15 Next, Merkel argues that the default judgment must be reversed because Kanz did not offer evidence as to each element of his claims. Merkel contends that because he appeared and contested issues, Kanz was not entitled to judgment on the pleadings alone, but rather was required to offer affirmative evidence as to each element of his claims. Merkel cites *Paulsen Lumber, Inc. v. Anderson*, 91 Wis. 2d 692, 702, 283 N.W.2d 580 (1979), for the proposition that a default judgment for the plaintiff cannot stand where the plaintiff has not offered sufficient affirmative evidence as to each element of his cause of action.

¶16 At the outset, we note that this is not what *Paulsen* says. Rather, *Paulsen* held that because the circuit court resolved the case on the merits as opposed to entering a default judgment, the fact that the evidence was insufficient required reversal. *Id.* at 701-02. *Paulsen* is therefore inapposite. Moreover, Wisconsin law is clear that when a court strikes a party's pleading as a sanction, the result is that no issues are joined, thus supporting a default judgment. *See Rao v. WMA Sec., Inc.*, 2008 WI 73, ¶37, 310 Wis. 2d 623, 752 N.W.2d 220. We therefore reject Merkel's argument that the court was precluded from entering a default judgment as a sanction after he had appeared in this action.

¶17 Merkel argues next that the sanction in this case was in effect an improper contempt penalty. He contends that the court's orders striking the defense pleadings and entering default judgment for Kanz were based on the court's frustration with Merkel's inappropriate courtroom conduct and voluminous

frivolous filings³ rather than the defense's failure to comply with discovery or court orders. He contends that the sanction was therefore a contempt sanction without a finding of contempt, violating due process. Merkel cites *Hauer v. Christon*, 43 Wis. 2d 147, 168 N.W.2d 81 (1969), in support of this proposition.

¶18 We need not resolve whether a contempt sanction would have been appropriate in this case. While the court acknowledged the inappropriateness of Merkel's actions, it specifically explained that it sanctioned Merkel and the Intervenor for their continuous failure to comply with discovery and court orders under WIS. STAT. §§ 804.12(2)(a) and 805.03. The court also explained that the defense conduct was both egregious and without justifiable excuse, and was the most extreme failure to comply with discovery and court orders that the court had ever seen. See *Industrial Roofing Servs., Inc.*, 299 Wis. 2d 81, ¶43 (circuit court may sanction party for failure to comply with court orders and discovery if conduct was egregious, that is, extreme, substantial and persistent, and without clear and justifiable excuse). We have no basis in the record to conclude that the court's decision was actually a contempt sanction for Merkel's inappropriate courtroom conduct and numerous frivolous filings rather than a sanction for the defense's failure to comply with discovery and court orders under §§ 804.12(2)(a) and 805.03.

¶19 Merkel argues that the information he and the Intervenor refused to provide in discovery related to NCLRF's bank accounts rather than the merits of this action. Merkel contends that it violates due process to deprive a party of the

³ For much of this case, both Merkel and the Intervenor appeared pro se. On appeal, both are represented by counsel, who concede the impropriety of their clients' conduct in the circuit court.

right to present evidence unrelated to the party's discovery violations, citing *Milwaukee Constructors II v. Milwaukee Metro. Sewerage Dist.*, 177 Wis. 2d 523, 537 n.5, 502 N.W.2d 881 (Ct. App. 1993). Merkel also cites federal case law holding that due process requires that discovery violations go to the merits of a case to support a default judgment. See *Hammond Packing Co. v. Arkansas*, 212 U.S. 322, 341-42 (1909); *Estrada v. Speno & Cohen*, 244 F.3d 1050, 1058 (9th Cir. 2001).

¶20 Assuming *arguendo* that only discovery violations that go to the merits of the action are sanctionable with a default judgment, Merkel's argument fails. Merkel relies on the premise that this action is only about who rightfully controls NCLRF. While this is one component of the action, Kanz's complaint alleges conversion of NCLRF funds. Thus, contrary to Merkel's assertion, information about those funds is central to the merits of this action. The refusal to divulge information regarding NCLRF assets, then, supports a default judgment even under the case law Merkel cites.

¶21 Finally, Merkel argues that the default judgment must be reversed because it will lead to disastrous consequences for NCLRF. He outlines his belief that Kanz will destroy NCLRF if he is allowed to control the organization. This appeal, however, is from circuit court orders striking defense pleadings as a sanction for violating discovery and court orders and thus entering default judgment for the plaintiff. We are therefore concerned only with whether the circuit court erroneously exercised its discretion in entering default judgment based on its determination that the discovery and court order violations were egregious and without justifiable excuse. See *Industrial Roofing Servs.*, 299 Wis. 2d 81, ¶¶42-43. Merkel does not contest the circuit court's findings supporting its decision. Accordingly, we have no basis to reverse.

By the Court.—Judgments and orders affirmed.

This opinion will not be published. See WIS. STAT. RULE
809.23(1)(b)5.

