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September 28, 2016

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You are hereby notified that the Court has entered the following opinion and order:

2015AP2583	Donald F. Nitschke v. John C. Spitz
2015AP2644	(L.C. # 2014CV1616)

Before Neubauer, C.J., Reilly, P.J., and Hagedorn, J.

Timothy Zignego and John C. Spitz separately appeal from an order denying their motions to stay this litigation and proceed to arbitration.¹ Based on our review of the briefs and the record, we conclude that this case is appropriate for summary disposition. *See* WIS. STAT. RULE 809.21 (2013-14).² We reverse the order denying the motions of Zignego and Spitz to stay this litigation and proceed to arbitration and remand to the circuit court for reconsideration.

¹ Zignego and Spitz filed a joint brief.

² All references to the Wisconsin Statutes are to the 2013-14 version unless otherwise noted.

According to the amended complaint, Nitschke, Spitz, and Zignego entered into a business venture with the intent of acquiring three apartment buildings, converting them to condominiums, and selling them to the public. They established three limited liability companies for that purpose: Oak Leaf 130, LLC, Oak Leaf 135, LLC, and Oak Leaf 155, LLC. Nitschke, Spitz, and Zignego each initially contributed \$200,000, and each took a one-third interest in the Oak Leaf LLCs. The balance of the money needed to purchase the buildings was borrowed from Park Bank of Milwaukee, which secured the loans by a first mortgage on each of the buildings and by a personal guaranty of the three members of the Oak Leaf LLCs. Subsequently, Park Bank provided an additional loan to the Oak Leaf LLCs, and in exchange required that the three members provide additional collateral. Nitschke pledged real estate he owned with his wife in Shawano County (the Aniwa Property).

On January 15, 2014, a special meeting of the members of the Oak Leaf LLCs was called because the loans from Park Bank were coming due at the end of the month, and Park Bank was refusing to renew the loans unless the Oak Leaf LLCs made a substantial payment to reduce the principal balances on those loans. Spitz and Zignego voted, with Nitschke abstaining, to borrow up to \$700,000 from its members, even though the Oak Leaf LLC operating agreement did not require any additional capital contributions or loans after the initial contribution. Spitz and Zignego also voted, with Nitschke abstaining, to authorize the Oak Leaf LLCs to sell all of their assets to an unaffiliated third-party or to an affiliated party if two of the three members agreed. Spitz and Zignego also voted to authorize the Oak Leaf LLCs to merge into an unaffiliated third-party or with an affiliated third-party if two of the members agreed. Nitschke voted against the motion. Spitz and Zignego also voted to require only the written consent of two of the three

members for all future acts of the Oak Leaf LLCs. Nitschke voted against the motion. Thus, Nitschke alleged, Spitz and Zignego were trying to “squeeze” him out as a member.³

In order to refinance the Park Bank loans, Spitz and Zignego formed a new entity, J & T Lending, LLC. J & T loaned the Oak Leaf LLCs approximately \$660,000 to help pay off the Park Bank loans. In addition, the Oak Leaf LLCs obtained loans of \$4,182,000 from Home Federal Savings. About the same time, J & T purchased the loans Park Bank had made to the Oak Leaf LLCs, totaling \$4,795,797.91, and Park Bank assigned to J & T all of the notes, mortgages, guarantees, and collateral that the Oak Leaf LLCs and its members had pledged to Park Bank, which included the Aniwa Property. J & T agreed with the Oak Leaf LLCs to subordinate the loans it had purchased from Park Bank to the first and second mortgages that the Oak Leaf LLCs now had with Home Federal Savings. The purpose of “this scheme,” Nitschke alleged, was to take ownership of the Park Bank notes and collateral so that J & T could collect \$5,000,000 from Nitschke, including in a foreclosure action J & T had commenced against the Aniwa Property.⁴ All of this was done without the knowledge, consent, or approval of Nitschke.

Based on the foregoing, Nitschke alleged that Spitz and Zignego, as members of the Oak Leaf LLCs, had violated the rights of Nitschke under the operating agreements of the Oak Leaf LLCs, breached the fiduciary duty they owed to him, and violated WIS. STAT. § 183.0402, and that Zignego, as the managing member of the Oak Leaf LLCs, had breached the operating agreements of the Oak Leaf LLCs. Nitschke named Spitz, Zignego, the Oak Leaf LLCs, and J & T as defendants, and he sought damages and a judgment declaring, among other things, that

³ Shortly thereafter, Nitschke and his wife filed for bankruptcy, but his interest in the Oak Leaf LLCs was deemed abandoned and, thus, not subject to bankruptcy.

⁴ *J & T Lending, LLC v. Nitschke*, Shawano County Case No. 2014CV215. J & T was granted a judgment of foreclosure against Nitschke and his wife.

the assignment Park Bank made to J & T was null and void and that all personal guarantees, collateral pledges, and mortgages that Nitschke made were null and void.

Zignego moved to stay the action pending arbitration.⁵ In an affidavit, Zignego stated that each of the Oak Leaf LLC operating agreements contained a mandatory arbitration clause stating as follows:

12.8(b) Disputes. Any dispute arising with respect to this agreement, its making or validity, its interpretation, or its breach shall be settled by arbitration in Waukesha or Milwaukee Counties, Wisconsin, pursuant to the then-obtaining rules of the American Arbitration Association. Such arbitration shall be the sole and exclusive remedy for such disputes except as otherwise provided in this agreement. Any award rendered shall be final and conclusive upon the parties, and a judgment may be entered in any court having jurisdiction.

Nitschke opposed the motion, arguing that the arbitration clause did not cover the allegations, that Spitz and Zignego had waived the arbitration clause, and that the arbitration clause was unconscionable.⁶

The court granted the stay and directed the parties to proceed to arbitration, finding that the members of the Oak Leaf LLCs willingly entered into the arbitration clause when they formed the Oak Leaf LLCs, that the arbitration clause applied, and that it was appropriate to proceed to arbitration. The court directed Nitschke's attorney to submit a proposed order. The parties stipulated to dismiss J & T from the case.

⁵ Spitz joined in the motion. In the answer of the Oak Leaf LLCs, they asserted that all of Nitschke's claims were subject to arbitration.

⁶ Nitschke claimed that Spitz and Zignego were trying to slow down this action while aggressively pursuing the foreclosure action.

Nitschke's proposed order stayed the action "pending the outcome of arbitration of the issues raised by the parties remaining in the action." Zignego's attorney objected to the proposed order and submitted his own proposed order, which directed arbitration "between and among the parties to the operating agreements" of the Oak Leaf LLCs. In other words, Zignego's position was that arbitration would not include the Oak Leaf LLCs. Nitschke's counsel in a letter objecting to that proposed order stated that the Oak Leaf LLCs "are not parties to the [o]perating [a]greements."

At a subsequent hearing to resolve what order should be issued, the circuit court reversed itself and refused to stay the litigation pending arbitration. The court, citing WIS. STAT. § 183.02,⁷ stated that "the LLC is not a member, not a party to the operating agreement, that these LLCs here are not parties to the operating agreements and there's no basis to forcing [sic] the LLCs into arbitration." The court refused to send some of the parties to arbitration and some to litigation. The court signed a written order to this effect, and Zignego and Spitz appeal.

The circuit court determined that the Oak Leaf LLCs are not parties to their own operating agreements. We fail to understand how this analysis precludes enforcement of the arbitration clause.

We begin by noting that the record does not contain copies of the operating agreements. That said, the circuit court's reasoning is inconsistent with Wisconsin's statutes governing LLCs as well as the basic principles governing LLCs. The issue is not whether the LLCs are parties to the operating agreement, but rather, whether the operating agreements, with the arbitration clauses, govern the LLCs.

⁷ This appears to be a misstatement or error of transcription because WIS. STAT. § 183.02 was repealed by 1963 Wis. Laws, ch. 158, § 16, and did not address limited liability companies.

First, typically the LLC operates through its members (or managers) who, as agents, have the ability to bind the LLC. *See* WIS. STAT. § 183.0301(1)(a), (b) (“Each member is an agent of the limited liability company ... for the purpose of its business,” and “[t]he act of any member ... binds the limited liability company unless the member has, in fact, no authority to act for the limited liability company in the particular matter, and the person with whom the member is dealing has knowledge that the member has no authority to act in the matter.”).

The management of the LLC is vested in the members, or, managers, subject to the terms of the operating agreement and WIS. STAT. Ch. 183. *See* WIS. STAT. § 183.0401. The operating agreement established by the members governs “the business of a limited liability company and its *relationships* with its members.” WIS. STAT. § 183.0102(16) (emphasis added). Here, although we do not have copies of the entire operating agreements, each included an arbitration clause governing the members of the Oak Leaf LLCs and, presumably, the LLCs themselves. Thus, unless the governing documents provide otherwise, the arbitration clauses would apply to the Oak Leaf LLCs themselves.

Indeed, Nitschke’s claims against the other members for violation of the operating agreement or breach of fiduciary duty seek to enforce his rights against the LLCs. *See* WIS. STAT. § 183.0305 (“A member of a limited liability company is not a proper party to a proceeding ... against a limited liability company, solely by reason of being a member of the limited liability company, except if ... (1) The object of the proceeding is to enforce a member’s right against or liability to the limited liability company.”). Thus, it would make no sense to bind only the members to the arbitration clause when the claims alleging breach of the agreement by a member seek to enforce rights against, and liability of, the LLC.

In sum, the members of the limited liability company have the authority to enter into an operating agreement, which they did; the operating agreement governs the relationship between the limited liability company and its members, and those operating agreements called for

arbitration when there was “[a]ny dispute arising with respect to this agreement, its making or validity, its interpretation, or its breach.” Since we do not have the operating agreements before us, and apparently neither did the circuit court, we remand to the circuit court to reconsider this issue.

While Nitschke argues that the arbitration clause does not cover the claims at issue, we disagree. As the circuit court initially found, each of the five claims either explicitly or implicitly arises with respect to the operating agreement and alleges a violation of the operating agreements. *See Cirilli v. Country Ins. & Fin. Servs.*, 2009 WI App 167, ¶14, 322 Wis. 2d 238, 776 N.W.2d 272. WISCONSIN STAT. § 788.02 requires a stay of the litigation between all of the parties subject to arbitration.

Although Nitschke raises other reasons, waiver and unconscionability, as to why this matter should not proceed to arbitration, the circuit court should address these other reasons in the first instance on remand. *See Flooring Brokers, Inc. v. Florstar Sales, Inc.*, 2010 WI App 40, ¶15, 324 Wis. 2d 196, 781 N.W.2d 248.

Upon the foregoing reasons,

IT IS ORDERED that the order denying the motions of Zignego and Spitz to stay this litigation and proceed to arbitration is reversed and the matter is remanded to the circuit court for reconsideration. WIS. STAT. RULE 809.21.

Diane M. Fremgen
Clerk of Court of Appeals