

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

HON. RANDALL H. WARNER

CLERK OF THE COURT

K. Ballard

Deputy

ANDREW PROVENCIO

SAL J RIVERA

v.

TIFFANY YOUNG, et al.

JEFFREY C MATURA

JON S MUSIAL
MATT YOUNG
4911 E HILLERY DR
SCOTTSDALE AZ 85254
GILBERT B BLUMENTHAL CPA
12174 E IRONWOOD DR
SCOTTSDALE AZ 85259-5122

UNDER ADVISEMENT RULING

Plaintiff's Application for Preliminary Injunction is under advisement following an evidentiary hearing and submission of post-hearing briefs. Based on the evidence presented, the court makes the following findings, conclusions and orders. The court finds that Desert Medical Center, Inc. has no shareholders; that Plaintiff Andrew Provencio and Defendant Tiffany Young are its only two directors; that Defendant Matthew Young is neither a shareholder nor a director; and that Mr. Provencio remains its president. The court grants the Application in part.

I. BACKGROUND.

Mr. Provencio and Ms. Young were doing real estate business together when they decided to get into the medical marijuana business. On May 25, 2011, Desert Medical Center, Inc. ("DMC") was formed as an Arizona corporation. Its Articles of Incorporation list Marc

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

Jacott, Sr. and Steve Langston as initial directors, list attorney Joseph Parker as organizer, and state that 1,000 shares of stock are authorized. The Articles were amended on May 10, 2012 to establish a two-person board of directors and to make Mr. Provencio and Ms. Young the directors.

Mr. Provencio and Ms. Young set up DMC to operate on a not-for-profit basis as required by the Medical Marijuana Act. But they intended to make money a number of ways. One was by loaning money to DMC at interest. Another was by causing DMC to contract for management services with A & T Management, LLC, which they both owned. And at some point, Mr. Provencio testified, they hoped the law regarding marijuana would change so that their interests in DMC could be sold at a profit.

Mr. Provencio and Ms. Young did not formalize these arrangements in any clear way. This litigation results from their failure to clearly define their relationship in writing at the outset.

The parties dispute who owns what percentage of DMC. Mr. Provencio testified that he owns 80% of DMC and Ms. Young owns 20%. Ms. Young testified that each of them initially owned 50% of DMC, but that Mr. Provencio gave part of his interest to Matthew Young, who now owns 20%.

DMC obtained a certificate to open a medical marijuana dispensary and the company started operating. For most of its existence, Ms. Young worked full time for DMC. She did not take a salary, but anticipated that her "sweat equity" would result in compensation in some manner in the future. Her husband, Defendant Matthew Young, worked as DMC's chief marijuana grower. Mr. Provencio did not work full time for DMC and was not compensated.

The parties dispute how DMC was financed. Mr. Provencio testified that he provided between \$1.2 and \$1.4 million in loans to the venture. Ms. Young testified that most of the money provided was hers.

In late 2014, disputes arose between the parties, which came to a head on December 22. On that date, a board meeting was noticed. Mr. Provencio showed up and, when Ms. Young and Mr. Young were not there, he departed, leaving a note saying the board meeting was cancelled. When Ms. Young and Mr. Young arrived a short time later, they held a meeting without Mr. Provencio. In that meeting, they voted to remove Mr. Provencio as an officer and director.

After December 22, 2014, Ms. Young made the unilateral decision to pay herself a \$150,000 per year salary from DMC.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

Mr. Provencio's Application for Preliminary Injunction asks that he be declared DMC's president and controlling shareholder.

II. LEGAL STANDARD.

To obtain a preliminary injunction, Mr. Provencio must show:

1. A strong likelihood of success at trial on the merits;
2. The possibility of irreparable injury not remediable by damages if a preliminary injunction is not granted;
3. The balance of hardships favors a preliminary injunction; and
4. Public policy favors an injunction.

IB Property Holdings, LLC v. Rancho Del Mar Apartments Ltd. Partnership, 228 Ariz. 61, 64-65, 263 P.3d 69, 72-73 (App. 2011). Application of these factors may be on a "sliding scale." That is, a preliminary injunction may issue if there is either probable success on the merits and the possibility of irreparable injury, or the presence of serious questions on the merits and the balance of hardships tips sharply in favor of relief. *Arizona Citizens Clean Elections Com'n v. Brain*, 233 Ariz. 280, 288-89, 311 P.3d 1093, 1101-02 (App. 2013).

III. IRREPARABLE HARM.

The parties have many disputes, but only one as to which there is a possibility of irreparable harm. If, as Mr. Provencio alleges, he was wrongfully ousted as president and has the right to control DMC as its majority shareholder, then permitting Ms. Young to run DMC unilaterally pending the outcome of this litigation will likely result in irreparable harm.

The court need not decide at this stage who is entitled to what money out of DMC. There are many issues: Who contributed what amount of money to the venture? Were the payments loans or capital contributions? At what rate do they bear interest? Did anyone improperly take money out of DMC? Is anyone entitled to additional compensation for services provided to DMC? The court finds no possibility of irreparable harm if these issues are not decided at this stage. Rather, they can be decided at trial on the merits. Thus, the only issues to decide are who owns and/or controls DMC, and how the company is to operate pending the outcome of this litigation.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

IV. THE MERITS.

A. Does Andrew Provencio Own An 80% Interest In DMC?

Mr. Provencio testified that he and Ms. Young agreed he would have an 80% interest in DMC and she would have a 20% interest. He offers documentary evidence to support this testimony. Most significantly, DMC's application for a medical marijuana certificate, which both he and Ms. Young signed, says their respective interests are 80% and 20%.

The court finds that Mr. Provencio does not own 80% of DMC for two reasons. First, the court does not believe that Mr. Provencio and Ms. Young reached agreement on this. To the contrary, they never reached any agreement regarding what their respective ownership interests would be. They discussed several different numbers, but never had a meeting of the minds. The court believes Ms. Young's testimony that they listed themselves as 80/20 owners on the application to avoid any inquiry into Ms. Young's personal bankruptcy.

Second, and more significantly, the Board of Directors of DMC never took any official act to issue 80% of the company's stock to Mr. Provencio. A basic premise of Mr. Provencio's argument is that he and Ms. Young could determine their respective interests in DMC by oral agreement reflected in communications to the State. Such informal dealings might be appropriate for an LLC, but DMC is a corporation. Formality was required to issue stock.

A.R.S. § 10-621 governs issuance of stock by a corporation and it requires formal board action. Subsection C says, in pertinent part: "Before the corporation issues shares, the board of directors must determine that the consideration received or to be received for shares to be issued is adequate." There is good reason for this. As a Delaware court explained when construing that state's statute on the same subject:

"[I]ssuance of corporate stock is an act of fundamental legal significance having a direct bearing upon questions of corporate governance, control and the capital structure of the enterprise. The law properly requires certainty in such matters." Delaware's statutory structure implements these policies through a "clear and easily followed legal roadmap" of statutory provisions. This statutory scheme consistently requires board approval and a writing.

Grimes v. Alteon, Inc., 804 A.2d 256, 260 (Del. Supr. 2002), *quoting STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136 (Del. 1991).

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

Even if the parties had agreed to an 80/20 stock split, neither would own stock in DMC without formal Board action, reflected either in the minutes of a Board meeting or in a consent in lieu of a meeting.

B. Is The May 25, 2011 Consent Regarding Tiffany Young's And Andrew Provencio's Interests Valid?

Ms. Young points to a May 25, 2011 consent purportedly signed by her and Mr. Provencio, as the required formal action issuing stock. That consent, which was trial exhibit 11, meets the requirements of Arizona law if it was validly signed. Mr. Provencio, however, claims he did not sign it; rather, Ms. Young forged his signature. To bolster his testimony, he offers the report of a handwriting expert.

The court finds that Ms. Young's testimony on this issue is not believable. Mr. Provencio did not sign the May 25, 2011 consent, so it is not valid.

C. Is Matthew Young A Director Or Shareholder?

Mr. Young claims he has a 20% interest in DMC, and that his 20% came out of Mr. Provencio's 50%. He argues that Mr. Provencio orally agreed to give him a 20% interest. This argument fails for two reasons. First, the court does not believe Mr. Provencio did or would agree to having less than a 50% interest in DMC. Doing that would give him no ability to control the company and would leave his investment at the whim of Mr. and Ms. Young. Moreover, there is no written documentation of any stock transfer from Mr. Provencio to Mr. Young.

More fundamentally, as discussed above, DMC has never issued any stock. Consequently, Mr. Provencio had no shares to transfer to Mr. Young.

Nor is Mr. Young a director. The Board took no official action whereby it named Mr. Young a director.

D. Was The Ouster Of Mr. Provencio Valid?

Because Mr. Young is not a director, he and Ms. Young could not agree to oust Mr. Provencio as president and as a director. The only directors were Ms. Young and Mr. Provencio. Under DMC's bylaws, a quorum is 51% of the directors, so neither acting alone could constitute a quorum. Neither acting alone has the power to get rid of the other. This is consistent with how Mr. Provencio and Ms. Young envisioned their venture, as neither intended that the other could control the medical marijuana business without the other.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

Ms. Young claims Mr. Provencio forfeited his right to be a director by failing to attend three consecutive meetings. There is no factual basis for this claim.

E. Who Controls DMC?

Because DMC has not issued any stock, its legal status is unclear. But control remains in the hands of the two directors named in the Articles of Incorporation: Mr. Provencio and Ms. Young. Each has one vote. And because the company cannot act except by a majority vote of the directors, agreement between the two of them is necessary for the company to do anything.

This result may be unwanted by both Mr. Provencio and Ms. Young. Each claims a right to control the company, and each appears unwilling or unable to cooperate with the other. But this result is required by the structure they established. It is also consistent with what they always understood, which is that this medical marijuana venture would be theirs together.

V. BALANCE OF HARDSHIPS.

Mr. Provencio will suffer substantial hardship if he continues to be locked out of the management of DMC. He has invested substantial money in DMC and has a right to an equal say in its operation.

Ms. Young will suffer some hardship if she is not able to run DMC the way she wants. She will also suffer hardship if she is not paid a salary for her work. But the latter is mitigated by the fact that she is not required to work for DMC. Who gets paid for working for DMC must be a matter of agreement between Mr. Provencio and Ms. Young.

Balancing these hardships, the court finds that a preliminary injunction is warranted reinstating Mr. Provencio as president and a director, and ordering that DMC can do nothing without the written concurrence of Mr. Provencio and Ms. Young. This is the only way to preserve the structure of the business that the parties intended.

This creates a potential additional hardship. DMC owns a medical marijuana certificate, which is a valuable asset, but cannot make use of that asset unless its presently-fighting directors are in agreement. If DMC's directors are deadlocked and, as a consequence, the company's operations come to a halt, both its customers and its employees (including Mr. Young) may suffer. But any other result would give one party control over DMC, which is not warranted by the facts or the law.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

VI. PUBLIC POLICY.

There are public policy considerations. Mr. and Ms. Young argue in their brief that the court should not appoint a receiver, but should make specific orders regarding how DMC is operated. It is not in the public interest for the court to run this business.

Nor is it in the public interest for the sole medical marijuana certificate in this CHAA to be held by a company that is deadlocked. Ms. Young and Mr. Provencio obtained a medical marijuana certificate together. Either they can run DMC together, or the company's affairs should be wound up.

VII. CONCLUSION.

Based on the foregoing, the court issues the preliminary injunction set forth below. The main effect of the order is that agreement of both directors is required for DMC to operate. If they cannot reach agreement, Arizona law provides remedies for deadlocked corporations, which may include appointment of a receiver and/or dissolution.

There remains the issue of whether a Special Master is necessary. The court appointed Mr. Blumenthal to assist in implementing the temporary restraining order issued on February 9, 2015. There should be less of a need for the Special Master now that the court's order no longer specifies how DMC is to be operated on a day-to-day basis. Nonetheless, there may still be a need for a Special Master in two respects. First, the parties may wish to use Mr. Blumenthal to assist them in reaching agreements regarding management of the company. Second, to the extent there is disagreement about whether a party has complied with the preliminary injunction (including its provisions regarding the sharing of information), such dispute should first be submitted to Mr. Blumenthal for resolution.

There is no need for the Special Master to undertake a forensic accounting or to hire someone to do so without the parties' consent.

VIII. ORDERS.

IT IS ORDERED granting a preliminary injunction as follows:

1. Andrew Provencio is reinstated as president of DMC and a director.
2. Neither Andrew Provencio nor Tiffany Young shall act on behalf of DMC or cause DMC to do anything except with both Mr. Provencio's and Ms. Young's written consent.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

This includes everything DMC does. By way of illustration only, none of the following acts may be done unless Mr. Provencio and Ms. Young agree in writing:

- a. No employee may be paid.
- b. No product or material may be ordered or manufactured.
- c. No wholesale or retail products may be sold.
- d. No bill, debt or other obligation may be paid.
- e. No contract may be entered into with any entity.
- f. No attorney may be retained to represent DMC in this litigation.

3. Both Andrew Provencio and Tiffany Young shall have full access to all books, records and facilities of DMC.

4. Neither Andrew Provencio, Tiffany Young nor Matthew Young is obligated to perform any work for DMC or its affiliated entities.

IT IS FURTHER ORDERED that this preliminary injunction is effective at 8:00 a.m. on April 6, 2015 and until final judgment is entered in this action. Before 8:00 a.m. on April 6, 2015, the temporary restraining order issued on February 9, 2015 remains in effect. After that time, the temporary restraining order is superseded and, therefore, vacated.

IT IS FURTHER ORDERED affirming the appointment of Gilbert Blumenthal as Special Master on the following terms:

1. Any party may submit to the Special Master a dispute concerning compliance with this preliminary injunction. He or she shall do so by written request sent electronically to the Special Master with a copy to all parties.

2. The Special Master may conduct such formal or informal proceedings as he deems appropriate to resolve the dispute.

3. The Special Master shall issue a written decision and shall submit it electronically to the parties.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-002274

03/24/2015

4. Any party wishing to appeal the decision shall submit a written request for review to the court within five business days of its issuance and serve it electronically on all other parties. Any other party may respond to the request by filing a written response with the court within five business days and serving it electronically on all other parties.

5. Upon receiving a request for review, the court will determine whether a hearing on the issue is appropriate.

6. The Special Master is not authorized to hire others without the parties' consent or a court order.

IT IS FURTHER ORDERED that the parties jointly or separately lodge a formal order of appointment that complies with Ariz. R. Civ. P. 53(b).

IT IS FURTHER ORDERED that the parties lodge a proposed scheduling order no later than **May 15, 2015**.

FILED: Exhibit Worksheet

/ s / RANDALL H. WARNER

JUDGE OF THE SUPERIOR COURT