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No. 64518-8-1

IN THE COURT OF APPEALS
STATE OF WASHINGTON
DIVISION I

ALASKA DISTRIBUTORS CO.,

Claimant/Respondent,

v.

ALASKAN BREWING COMPANY,

Respondent/Appellant.

APPELLANT'S OPENING BRIEF

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ORIGINAL

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I. INTRODUCTION

Appellant Alaskan Brewing Company (“Alaskan”) and Respondent Alaskan Distributing Company (“ADCO”) were parties to an agreement entitled Wholesale Malt Beverage Distribution Agreement (Washington) (the “Agreement”). Washington’s Wholesale Distributors and Suppliers of Malt Beverages Act, RCW 19.126, *et seq.* (the “Act”) governs the parties’ relationships and mandates certain contractual terms.

In the late summer of 2008, Alaskan terminated ADCO as its distributor because of the pending sale of ADCO’s business to another distributor with whom Alaskan did not want to do business. In terminating ADCO, Alaskan invoked paragraph III(I) of the parties’ contract. In accordance with RCW 19.126.040(3), paragraph III(I) provided for liquidated damages in cases of termination without cause, which is defined as “Fair Market Price” (“FMP”). Under the valuation matrix set forth in paragraph III(I), FMP amounted to approximately \$1.4 million.

In addition to defining how to calculate FMP in cases of termination without cause, paragraph III(I) provides that Alaskan “may” give 90-days notice of termination. Alaskan chose not to give 90-days’ notice, but instead gave four days’ notice because of concerns it had over potential damage to its brand should it remain with ADCO an additional 90 days.

Within four days of receiving Alaskan's notice of termination, ADCO filed an arbitration demand, arguing that paragraph III(I) could not be invoked because of Alaskan's failure to give notice. ADCO sought over \$5 million in damages.

In his final award, the arbitrator made an error of law on the face of the award, as he concluded that the 90-day notice provision was a condition precedent to invoking termination under paragraph III(I). The arbitrator then threw out paragraph III(I) altogether and awarded ADCO over \$5 million in damages. The arbitrator committed legal error by holding that the 90-day notice requirement constituted a condition precedent to invoking the paragraph rather than a broken promise that could be compensated by damages.

Further, while ADCO may be entitled to damages for profits lost during the notice period of 90 days, based on Alaskan's failure to give notice, it was not entitled to have paragraph III(I) thrown out completely. Paragraph III(I) not only contains the notice provision, it also contains the definition of FMP for termination without cause. Under the Act, the parties are required to define FMP in their Agreement. But the arbitrator threw out that definition and applied a current FMP calculation, which he held was required by the Act. But the Act does not define FMP. The arbitrator committed error by awarding an FMP that differs from the parties' definition of FMP in the Agreement.

Alaskan also asserts that the arbitrator committed legal error by awarding attorneys' fees to ADCO in direct contradiction to the parties written Agreement. Alaskan respectfully moves this Court to correct that error.

II. ASSIGNMENTS OF ERRORS

A. Assignments of Error

1. Whether the arbitration award issued in this matter on October 14, 2009 should be vacated, reversed and remanded for further proceedings on the grounds that the arbitrator exceeded his powers and made a mistake of law that is apparent from the face of the award by failing to honor the parties' definition of FMP. RCW 7.04A.230(1)(d).

2. Whether the arbitration award issued in this matter on October 14, 2009 should be vacated, reversed and remanded for further proceedings on the grounds that the arbitrator exceeded his powers and made a mistake of law that is apparent from the face of the award by failing to hold the term "may" as used in paragraph III(I) constituted a promise rather than a condition precedent. RCW 7.04A.230(1)(d).

3. In the event that the arbitrator's award is upheld, whether the arbitrator's award of award of attorneys' fees and costs should be reversed as an error of law apparent on the face of the award. RCW 7.04A.230(1)(d).

B. Issues Related to Assignments of Error

1. Whether the arbitrator committed an error of law that is apparent on the face of the award when he failed to consider that RCW 19.126.040 requires parties to define FMP in their contracts. (Issue No. 1).

2. Whether the arbitrator committed an error of law by failing to apply the definition of FMP in the parties' Agreement. (Issue No. 1).

3. Whether the arbitrator committed an error of law by finding that the use of the word "may" in paragraph III(I) constitutes a condition precedent rather than a promise. (Issue No. 2).

4. Whether attorneys' fees and costs are permitted under the Agreement. (Issue No. 3).

III. STATEMENT OF THE CASE

In 1992, ADCO (then Western Washington Beverage) took over the distribution of Alaskan's malt beverage products. On March 1, 1996, Alaskan renewed its Agreement with ADCO. In mid-July 2008, ADCO informed Alaskan that it was selling its business to Columbia – another malt beverage distributor. On August 26, 2008, Alaskan terminated its Agreement with ADCO and entered into a distributorship agreement with K & L Distributors. In terminating ADCO, Alaskan invoked paragraph III(I) of the parties' contract that, in accordance with RCW 19.126.040(3),

provides for liquidated damages in cases of termination without cause.

See Clerk's Papers ("CP") 11-19.

The liquidated damages provision in the Agreement specifically references RCW 19.126.040(3)¹, its requirement that FMP be paid if the distributor were terminated without cause, and defines how FMP would be calculated.

Paragraph III(I) provides:

1. Distributor acknowledges and agrees that, anything herein to the contrary notwithstanding, Alaskan may, upon ninety (90) days' written notice cancel this Agreement, but that during said period of notice Alaskan will continue to provide Distributor with Alaskan Product.

2. Upon termination pursuant to this Section III(I) Alaskan will reimburse Distributor in the manner set forth at Section III(F) hereof plus the fair market price of the "Distributor's business of selling Alaskan's Product," pursuant to RCW 19.126.040(3), which it is mutually agreed shall be determined as follows:

¹ RCW 19.126.040 was recently amended by the Legislature. The version of the statute in effect at the time of contracting provided in pertinent part:

(3) The wholesale distributor is entitled to compensation for the laid-in cost of inventory and liquidated damages measured on the fair market price of the business as provided for in the agreement for any termination of the agreement by the supplier other than termination for cause, for failure to live up to the terms and conditions of the agreement, or any reason set forth in RCW 19.126.030(5).

(Emphasis added.)

....

Over 3000 barrels: Gross sales – (Gross Costs)

CP 12-13. Under the Agreement’s definition of FMP ADCO would receive approximately \$1.4 million upon termination. *Id.* This amount was not contested at the hearing. *Id.*

Immediately upon receiving Alaskan’s notice of termination, ADCO filed an arbitration demand, arguing that the Agreement should be thrown out. ADCO argued that paragraph III(I) did not apply to Alaskan’s termination of the contract because Alaskan failed to give 90-days’ notice. ADCO sought damages of \$5,537,520, which represented “three times ADCO’s trailing 12-month gross profit on sales of Alaskan product at the time of termination.” CP 12. This amount was not contested at the hearing. *Id.*

The arbitrator held that RCW 19.126.040(3) provided the basis for the damage award. CP 19. However, RCW 19.126.040(3) requires that FMP be defined “as provided for in the agreement.” And the Agreement does not define FMP as three times the distributor’s trailing 12-month gross profit. CP 12-13.

At the arbitration hearing, Alaskan admitted it failed to give the required notice, but argued that it was liable to ADCO for damages incurred during the notice period for breach of that promise. That is, the failure to give 90-days’ notice constituted a promise, not a condition

precedent. Alaskan argued that it was an error of law to throw out paragraph III(I) altogether – particularly since the Act requires the parties to define FMP in their contracts. CP 13-14.

The arbitrator awarded ADCO \$5,537,520. CP 19. To reach this decision, the arbitrator committed legal error by finding that the notice provision in paragraph III(I) constituted a condition precedent to invoking its liquidated damages provision. CP 16-17. And in making his award, the arbitrator committed further legal error by throwing out paragraph III(I) altogether.

The arbitrator did not decide “whether RCW 19.126.040(3) requires parties to enter into enforceable agreements defining [FMP] and/or implementing that provision’s [FMP] requirement through adoption of an agreed contractual liquidated damages provision.” CP 19. The failure to apply the definition of FMP in the parties’ Agreement when making his award constituted legal error because the statute requires FMP to be contractually defined. Had the arbitrator applied the contractual language, he would have awarded \$1.4 million, not the over \$5 million that is stated on the face of the award. CP 13, 20.

Finally, the arbitrator awarded attorneys’ fees and costs in the amount of \$73,742.94. CP 21. But the Agreement provides that either party shall bear its own fees and costs. CP 104. Had the arbitrator

correctly applied the Agreement's contractual language, no attorneys' fees and costs would be reflected on the face of the award.

These errors of law are apparent on the face of the award as the arbitrator could not have reached the award he did without making such errors. As discussed below, based on these errors of law, the award should be vacated and remanded with directions for a new hearing.

IV. ARGUMENT

A. Standard of Review

The Legislature did not change the scope of review of arbitration awards when it amended the Arbitration Act in 2006. RCW 7.04A.230 provides in pertinent part:

- (1) Upon motion of a party to the arbitration proceeding, the court shall vacate an award if: ...
 - (d) An arbitrator exceeded the arbitrator's powers.

An arbitrator exceeds his powers when he commits an error of law on the face of the award. Boyd v. Davis, 127 Wn.2d 256, 259-60, 897 P.2d 1239 (1995). Courts have applied this standard to both pre-2006 and post-2006 motions to vacate. See Morrell v. Wedbush Morgan Sec., Inc., 143 Wn. App. 473, 485, 178 P.3d (2008) (discussing Washington's 2006 Arbitration Act in the context of similar California law).

For example, in Lindon Commodities, Inc. v. Bambino Bean Co., Inc., 57 Wn. App. 813, 790 P.2d 228 (1990), the appellate court vacated

an award in favor the defendant on the grounds that arbitrator exceeded his powers by committing an error of law that was apparent on the face of the award. The parties disputed whether a modification had been made to a contract for goods under Washington's U.C.C. Id. at 814-15.

Washington's U.C.C. does not require additional consideration to be paid to support a modification. Id. at 816. Yet the arbitrator found that no modification had taken place because of a lack of consideration. Id. at 814. Because of the conflict between the arbitrator's decision and the U.C.C., the appellate court vacated the award and remanded to the arbitrator for rehearing. Id. at 816.

Lindon stands for the proposition that when an arbitrator ignores or misconstrues a statute, then judicial review is available to correct that error. Here, the arbitrator erred in two instances. First, he erred by finding that "may" equated to "shall." Second he erred by ignoring the parties' contractual definition of FMP as required by RCW 19.126.040. The arbitrator erred by ignoring altogether the interplay of the statutory scheme and the Agreement.

Further, in Federated Serv. Ins. Co. v. Pers. Representative of Estate of Norberg, 101 Wn. App. 119, 4 P.3d 844 (2000), the appellate court vacated a damages award for future lost inheritance because such damages are not available in personal injury actions. In awarding such damages, the arbitrator committed an error of law, and such error appeared

on the face of the award. *Id.* at 121. In so holding, the appellate court found that “[t]he dispute is about law, not about evidence. It can be decided by reference to existing law without resort to the evidence that was before the arbitrators and without second-guessing their application of the law to the fact.” *Id.* at 125. The same standard may be applied here. Both the failure to consult the statutory requirements when construing the parties’ contract and the categorization of the notice period called for in paragraph III(I) as a condition precedent may be decided as a matter of law based on the face of the final award. Indeed, if the arbitrator had not made one or both of these errors, then the Agreement’s definition of FMP would have applied and approximately \$1.4 million awarded.

B. RCW 19.126, *et seq.*, Contemplates That FMP Will be Defined in the Parties’ Contract

RCW Chapter 19.126 generally governs the relationship between malt beverage suppliers (i.e., Alaskan) and distributors (i.e., ADCO). The Act provides that agreements by and between the suppliers and distributors be in writing. RCW 19.126.040(1). Under the Act, a distribution agreement may be terminated for cause, in which case notice and an opportunity to cure must be provided. RCW 19.126.040(2). A distribution agreement may also be terminated for convenience (i.e., without cause) in which case the distributor is entitled to the FMP of the

business being terminated “as provided for in the agreement.”

RCW 19.126.040(3). Alaskan terminated ADCO for convenience.

Again, the Act provides that:

The wholesale distributor is entitled to compensation for the laid-in cost of inventory and liquidated damages measured on the fair market price of the business as provided for in the agreement for any termination of the agreement by the supplier other than termination for cause

RCW 19.126.040(3) (emphasis added).

The Act does not itself provide a formula for FMP that binds the parties as a statement of Washington public policy. Compare Kelso Educ. Ass’n v. Kelso Sch. Dist. No. 43, 48 Wn. App. 743, 749, 740 P.2d 889 (1987) (“Where a statutorily created private right serves a public policy purpose, the persons or entities protected by the statute cannot waive the right.”); with Birkenwald Dist. Co. v. Heublein, Inc., 55 Wn. App. 1, 9, 776 P.2d 721 (1989) (finding that the Act constitutes “special interest legislation” rather than serving a public policy interest). Nor does the Act prohibit the parties from contracting to apply a specific formula to determine FMP. Indeed, the Act mandates that a formula for calculating FMP be “provided for in the agreement.”

The arbitrator held that “ADCO is entitled by RCW 19.126.040(3) to the full [FMP] of its terminated distribution rights.” But RCW 19.126.040(3) does not contain language entitling ADCO to “full [FMP].”

It entitles ADCO to “[FMP] of the business as provided for in the agreement.” See RCW 19,126,040(3), supra. The arbitrator never reached the issue of “whether RCW 19.126.040(3) requires parties to enter into enforceable agreements defining [FMP] and/or implementing that provision’s [FMP] requirement through adoption of an agreed contractual liquidated damages provision.” CP 19. Hence, holding that ADCO was entitled to current FMP (defined as ADCO’s three months’ trailing gross profit) and ignoring the definition set forth in the Agreement contradicts the Act and constitutes legal error apparent on the face of the award.

C. The 90-Day Notice Clause is a Promise, Not a Condition Precedent

A promise is “a manifestation of intention to act or refrain from acting in a specified way” rather than something that must occur before performance on the part of the other party is due. Colorado Structures, Inc. v. Ins. Co. of the West, 161 Wn.2d 577, 588, 167 P.3d 1125 (2007). “If there is doubt as to whether a promise or an express condition has been created, courts will interpret words in a contract as creating a promise.” 25 Wash. Practice, Contract Law and Practice § 8.3; see also Aesco Steel, Inc. v. J.A. Jones Constr. Co., 621 F. Supp. 1576, 1579 (E.D. La. 1985) (recognizing the “modern trend” is to construe contractual terms as promises rather than conditions).

1. Use of the Word “May” Does Not Denote a Condition Precedent

Words such as “provided that,” “on condition,” “when,” “so that,” “while,” “as soon as,” and “after” denote the intent to create a condition rather than a promise. Jones Assoc. v. Eastside Prop., Inc., 41 Wn. App. 462, 467, 704 P.2d 681 (1985). The use of the word “may” as in “Alaskan *may*, upon ninety (90) days’ written notice cancel this Agreement,” does not denote a condition. See CP 12-13. Rather, it denotes action that Alaskan may (or may not) take when terminating the Agreement. Merriam Webster’s Online Dictionary defines “may” as: “have the ability to,” “have permission to,” “be free to.” Merriam Webster Online Dictionary available at <http://www.merriam-webster.com/dictionary/may>. Under this definition “may” does not denote a mandatory duty to act. The arbitrator erroneously construed paragraph III(I) as mandatory rather than permissive.

2. Failure to Give Notice is Breach of Promise, not Breach of a Condition

The failure of a condition precedent is not a breach of contract because the accompanying obligations never come into effect. Howard O. Hunter, Modern Law of Contracts § 10:1 (Supp. 2009). This rule may be illustrated by the case of Lewis-Pac. Dairymen’s Ass’n v. Frame, 126 Wash. 493, 218 P.2d 385 (1923). In Lewis-Pac., the Washington Supreme Court held that a contract could be terminated despite a clause requiring

the obligee to pay off all debt prior to termination. The Court found that “[i]t was the duty of the appellant, under the contract, to make the payment prior to March 1st; but it should not be held to be a condition precedent.” Id. at 495. That is, the failure to pay the debt breached the contract regardless of whether it was terminated. If payment of the debt were categorized as a condition to termination, the obligee could avoid payment by never terminating the contract – an absurd result.

Likewise, here paragraph III(I) is a promise by Alaskan to give 90-days’ notice and supply product for that period of time. The failure to give notice subjects Alaskan to damages for the profits ADCO would have earned during the notice period. The arbitrator erred by holding notice to be condition. Notice cannot be a condition to invoking paragraph III(I) because Alaskan must still compensate ADCO upon termination for FMP “as provided for in the agreement.” RCW 19.126.030(4). Had the arbitrator not erred, his award would not have been for ADCO’s three month trailing gross profit as is shown on the face of the award. CP 20.

3. Lapse of Time Does Not Constitute a Condition Precedent

“A condition precedent is an act or event, other than a lapse of time, which must exist or occur before a duty to perform a promised performance arises.” 25 Wash. Practice, Contract Law and Practice § 8.3 (Supp. 2008-09) (emphasis added). Inherent in a “condition” is the risk that the condition will not occur. Restatement (Second) of Contracts §

224 cmt. b (1981). As the Restatement explains: “[T]he mere passage of time, as to which there is no uncertainty, is not a condition and a duty is unconditional if nothing but the mere passage of time is necessary to give rise to the duty of performance.” Id. The Restatement goes on to provide that “an event is not a condition, even though its occurrence is uncertain, if it is referred to merely to measure the passage of time after which an obligor is to perform.” Id.; see also Howard O. Hunter, Modern Law of Contracts § 10:1 (Supp. 2009) (“The passage of time is not a condition, because it is certain to occur. Weather, health and the actions of third parties are examples of common conditions.”); Aesco Steel, Inc., 621 F. Supp. at 1578-80 (construing contractual provision that payment would not be made by contractor to subcontractor until payment was received by contractor from owner as a promise to pay within a reasonable time and rejecting argument that payment clause was a condition precedent)

Here, the passage of 90 days measured the time that may pass between the date of notice and the date of termination. Under the Restatement’s definition, this passage of time is not a condition, but merely the measurement of time before Alaskan became obligated to pay ADCO FMP under the Agreement. And the breach of the promise to provide ADCO with Alaskan product during that time period subjects Alaskan to damages for the profit ADCO would have earned from sales. The arbitrator committed legal error by finding that lapse of time – 90

days' notice – constituted a condition precedent to termination without cause.

D. The Arbitrator Erred in Awarding Attorneys' Fees and Costs

Parties are presumed to contract with reference to existing statutes. In re Clise Estates, 64 Wn.2d 320, 322, 391 P.2d 547 (1964). Here, RCW 19.126.060 provides for an award of attorneys' fees and costs in case of a dispute under the statute. In contrast, the Agreement provides that either side will bear its own fees and costs. CP 104.

The arbitrator found that this dispute arose under the statute, not the Agreement, hence he awarded fees pursuant to RCW 19.126.060. But at the hearing, the “principal issues presented for decision ... [were] whether the Agreement’s contractual liquidated damages provision [was] applicable, and, if so, enforceable.” CP 12. That is, this dispute arose because of a disagreement over the application of contractual provisions. The arbitrator’s decision did not address whether the parties had incorporated a definition of FMP into the contract. Neither did the decision address the preemption of the contract by Washington law as ADCO argued. CP 19. Because the decision addressed the applicability and enforceability of the Agreement, and because the Agreement provides each party to bear its own attorneys’ fees and costs, a statutory award of attorneys’ fees and costs is not available to ADCO.

As an example, in CPL (Delaware), LLC v. Conley, 110 Wn. App. 786, 40 P.3d 679 (2002), two contracts were at issue. The first was a purchase and sale agreement providing that attorneys' fees and costs were available to the prevailing party seeking to enforce or interpret the agreement. The second was a "Memorandum Agreement" which provided a valuation matrix but did not provide any attorneys' fees or costs in case of a dispute. Id. at 797. The court of appeals concluded that because the action was brought "asserting mutual mistake in the formation of the Memorandum Agreement" and because it was resolved on those grounds, the application of the attorneys' fees and costs provision in the purchase agreement was inappropriate. Id. at 797-98. Thus, the prevailing party was not entitled to any award – the Memorandum Agreement 'trumped' the purchase and sale agreement." Id. at 797. The same analysis applies here.

ADCO sought attorneys' fees and costs under the statute because it could not do so under the contract. Yet the dispute centers on that contract's interpretation, not the statute. As the arbitrator resolved the matter based on contractual language, that same contractual language should be applied. As the contract provides, each party should bear its own attorneys' fees and costs the arbitrator's award of those fees and costs constitutes legal error.

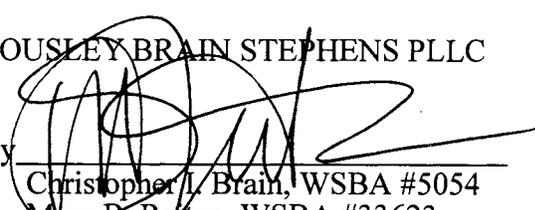
V. CONCLUSION

The arbitrator committed errors of law that are apparent on the face of the award. Had the arbitrator not committed error by relying on statutory language that does not exist, his award would not have equaled the over \$5 million that ADCO sought. That is, the statute does not provide that in the absence of an agreement a terminated distributor is entitled to current FMP. Rather it provides that the terminated distributor is entitled to FMP “as provided for in the agreement.” The arbitrator further erred by holding that “may” equated to “shall.” As a matter of law, the use of the word “may” is permissive, not mandatory. Finally, the arbitrator erred by awarding attorneys’ fees and costs, an award that directly contradicts the language of the parties’ Agreement.

For these reasons and those stated above, Alaskan moves this Court to vacate the arbitration award and remand for further hearing with instructions on the interpretation of the law.

DATED this 5th day of February, 2010.

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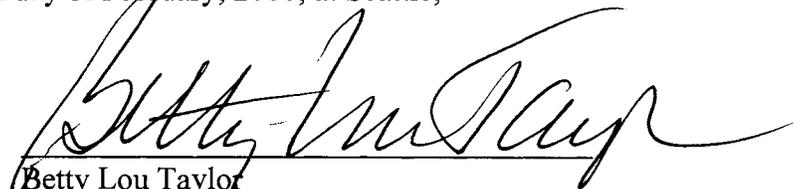
CERTIFICATE OF SERVICE

I, Betty Lou Taylor, hereby certify that on the 5th day of February, 2010, I caused to be served true and correct copies of the foregoing to the following person(s) in the manner indicated below:

Paul Taylor, WSBA #14851	<input type="checkbox"/>	U.S. Mail, postage prepaid
Joshua B. Selig, WSBA #39628	<input checked="" type="checkbox"/>	Hand Delivered via Messenger Service
BYRNES & KELLER LLP	<input type="checkbox"/>	Overnight Courier
1000 Second Street, Suite 3800	<input type="checkbox"/>	Facsimile
Seattle, WA 98104	<input type="checkbox"/>	Electronic Mail

I certify under penalty of perjury under the laws of the United States and the state of Washington that the foregoing is true and correct.

EXECUTED this 5th day of February, 2010, at Seattle, Washington.


Betty Lou Taylor