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RECEIVED
COURT OF APPEALS
DIVISION ONE

NO. 64799-7-I

AUG 02 2010

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION I

WORLDWIDE WATER, INC.,
CLEAR WATER COMPLIANCE SERVICES, INC., and
CASCADE ECOSOLUTIONS, INC.,

Appellants,

v.

PLAINFIELD SPECIALTY HOLDINGS II INC.,
a Delaware corporation,
and
TYRELL B. VANCE LLC,
as Receiver for Plainfield Specialty Holdings II Inc.,

Respondents.

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DIVISION ONE

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REPLY BRIEF OF APPELLANTS

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I. INTRODUCTION

At its heart, the issue before the Court is whether a receiver, the fees of whom are being paid by the secured creditor, has the authority to simply transfer, without procedural safeguards, potentially valuable property of the debtor, consisting of claims against the secured creditor to that same secured creditor under the guise of a routine administrative termination of the receivership.

This action is not authorized by the Washington Receivership statute, RCW 7.60.005, *et seq.* (“Receivership Act”). Moreover, it creates a situation where the secured creditor is not obligated to assign any value to the claims against it and reduce its own deficiency claim accordingly and/or provide other parties the opportunity to purchase and pursue the claims against the secured lender. The secured creditor is allowed an end-run around the provisions of Article 9 of the Uniform Commercial Code (“UCC”) and a free

pass with respect to its own actionable conduct, to the detriment of the debtor and other creditors.

Respondent Plainfield's determination to obtain the claims against it so that no one else can pursue them belies its argument that the claims hold no value.

II. STANDARD OF REVIEW

The basis of Appellants' (collectively "Worldwide") argument is that the Receivership Act does not authorize the Receiver to simply give Worldwide's property to Plainfield for no consideration and without due process. As such, Worldwide's argument is one of statutory construction, which the appellate court reviews *de novo*.

Plainfield argues the review to be undertaken relates to termination of a receivership and distribution of estate property. First, while the unauthorized transfer to Plainfield was approved as part of the order terminating the receivership, the transfer was independent of the termination. Second, distribution of receivership property is governed by

RCW 7.60.230, which speaks to “disposition” of a secured creditor’s collateral. This is not what occurred in this case.

Plainfield cites four cases in support of its statement that the court is to review orders terminating receiverships and orders approving distribution of receivership property only for abuse of discretion. None of these cases has any relevance to the issue before this Court. First, each case was decided prior to enactment of the current Receivership Act with its detailed provisions for administration of receivership property.

More importantly, in each case, the appellate court considered an order relating to the sale of property by the receiver. Walton v. Severson, 100 Wn.2d 446, 670 P.2d 639 (1983) (sale of receivership property by auction); Thompson v. Mitchell, 128 Wash. 192, 222 P. 617 (1924) (sale of receivership property was within court's discretion); Boothe v. Summit Coal Min. Co., 63 Wash. 630, 634, 116 P. 269 (1911) (order to sell property was premature under the facts of the case); Ferree v. Fleetham, 7 Wn. App. 767, 502 P.2d 490

(1972) (court did not err in not requiring upset price hearing prior to receiver's sale of property).

There is no dispute here that the Receiver did not seek approval of a sale of assets as part of his termination motion.

None of the cases Plainfield cites stands for the proposition that determination of a receiver's authority under the Receivership Act to simply transfer property to a creditor for no consideration and without any due process is reviewed solely for abuse of discretion.

III. WORLDWIDE DID NOT WAIVE ITS ARGUMENTS ON APPEAL

This Court is authorized to decide the issues on appeal because (1) Worldwide has raised issues of law, which, as stated above, require *de novo* review; (2) RAP 2.5 is discretionary; (3) the issues Worldwide appeals are pertinent to the substantive issues raised below; and (4) there is a sufficient factual record for the issues on appeal.

A. The Issues of Law

Worldwide appeals the trial court's improper interpretation of the Receivership Act and the trial court's failure to properly enforce the procedural requirements of the UCC. "Statutory interpretation is a question of law reviewed *de novo*." Estate of Haselwood v. Bremerton Ice Arena, Inc., 166 Wn.2d 489, 497, 210 P.3d 308 (2009) (citing TCPA Corp. v. Gervin, 163 Wn.2d 645, 650, 185 P.3d 589 (2008)).

B. RAP 2.5(a) Authorizes This Court to Review the Claims of Error on Appeal

Contrary to Plainfield's contention, RAP 2.5(a) is a discretionary rule that allows this Court to review the issues Worldwide appeals. The plain language of RAP 2.5 provides courts with discretion to review claims of error that were not raised at trial. Roberson v. Perez, 156 Wash. 2d 33, 39, 123 P.3d 844 (2005); State v. Ford, 137 Wash. 2d 472, 478, 973 P.2d 454 (1999); RAP 2.5(a) ("appellate court may refuse to review any claim of error which was not raised in the trial

court”) (emphasis added). The operating word in the rule is may; “[t]hus, the rule never operates as an absolute bar to review.” Ford, 137 Wash. 2d at 478.

C. Issues on Appeal are Pertinent to the Substantive Issues Raised Below

Worldwide appeals issues pertinent to the substantive issues raised below, that is, the trial court’s error in allowing the Receiver to neglect the statutory limitations of the Receivership Act and the procedural safeguards of the UCC by simply transferring Worldwide’s claims against Plainfield to Plainfield. Worldwide raised this issue below when it argued before the trial court that it was “inappropriate for [the] court to, in effect, give Plainfield a release for nothing of claims that [Worldwide] may have against it.” RP, December 12, 2009, p. 9.

The entire hearing before the trial court on December 12, 2009, was devoted to the very issue on appeal: whether it was proper for the Receiver to transfer Worlwide’s claims to Plainfield. Despite this fact, Plainfield will have this Court

believe that, somehow, Worldwide waived the opportunity to appeal this sole issue before the trial court.

To determine whether the trial court's ruling was proper, this Court must consider the limitations of the Receivership Act and the procedural safeguards of the UCC. Clearly these two bodies of law are implicated in receivership proceedings. However, even if these statutes were not explicitly recited at the hearing before the trial court, it is nonetheless appropriate for this Court to consider them on appeal: “[A] statute not addressed below but pertinent to the substantive issues which were raised below may be considered for the first time on appeal.” Bennet v. Hardy, 113 Wash. 2d 912, 918, 784 P.2d 1258 (1990) (citing State v. Fagalde, 85 Wash. 2d 730, 732, 539 P.2d 86 (1975)).

An instructive case is Osborn v. Pub. Hosp. Dist. I, Grant County, 80 Wash. 2d 201, 492 P.2d 1025 (1972). In Osborn, the Washington Supreme Court considered a hospital licensing statute raised for the first time on appeal where the statute was

pertinent to the issue at hand: “The issue of hospital’s duty... was squarely before the trial court and the statutes of this state in regard thereto are therefore pertinent to our conversation.” Osborn, 80 Wash. 2d at 206. Just as the hospital licensing statute was pertinent to the issue in Osborn, here, the Receivership Act and the UCC are pertinent to the issue that was squarely before the trial court.

D. Sufficient Factual Record for the Issues on Appeal

Furthermore, the issues raised before this Court are questions of law for which adequate factual record has been developed. Unlike in the cases Plainfield cites, in the present case the Court is not required to engage in any factual analysis. In Brower v. Ackerly, 88 Wn. App. 87, 943 P.2d 1141 (1997), cited by Plainfield, the court refused to hear a new issue raised on appeal regarding an application of a statute which would have required the Court to engage in a close factual analysis of the defendant’s intent to intimidate, use of profanity, and threatening conduct. Brower, 88 Wn. App. at 95 n.18.

Likewise, in Demelabs v. Ross Stores, Inc., 105 Wn. App. 508, 20 P.3d 447 (2001), cited by Plainfield, the court declined to review a theory of negligence raised for the first time on appeal where the issue required a factual determination as to whether the defendant negligently trained and supervised its employees. Demelabs, 105 Wn. App. at 527.

No factual inquiry by this Court is required. This Court is authorized by RAP 2.5 to review the legal issues before it which are pertinent to the substantive issues raised below and for which there is sufficient factual record.

IV. THE RECEIVERSHIP STATUTE DID NOT AUTHORIZE THE OUTRIGHT TRANSFER OF CLAIMS TO PLAINFIELD

The Receivership Act did not authorize the outright transfer of claims to Plainfield. Plainfield works to distract this Court's attention from what did and did not happen below.

A. RCW 7.60.055

First, Plainfield points to the powers of the court to determine all controversies relating to distribution of all the

property under RCW 7.60.055. This appeal is necessary because no determination of any substance was made by either the Receiver or the trial court with respect to the outright transfer to Plainfield of Worldwide's claims against it. The Receiver indicated he was a "neutral" party. He undertook no independent investigation of the claims. Moreover, the trial court admitted it did not know the facts and substance of the claims. Thus, no determination of the value of the claims was made. In fact, no determination was made as to whether the claims even constituted Plainfield's collateral.

Because no controversies were determined, Plainfield's citation to RCW 7.60.055 does not apply.

B. Sale Cases

Plainfield next attempts to find authority for the trial court's order here by citing to receivership sale cases, exactly the type of fair process that did not occur here. In Walton v. Severson, the Court affirmed the trial court's set aside of an earnest money agreement entered into between a receiver and a

party seeking to purchase a receivership asset because the set aside was necessary to “obtain the best possible price for the property.” Walton, 100 Wash. 2d at 453. The Walton court’s concern over the maximization of the value of assets is the heart of the concern here and the purpose of this appeal. With no process in regard to the claims, whether it be a sale, independent investigation, or other valuation of the claims and no determination of whether the claims were Plainfield’s collateral, the trial court departed completely from the purpose of disposition of assets in a receivership.

C. Guaranty Trust

Likewise, Guaranty Trust Co. v. Satterwhite, 2 Wash. 2d 252, 97 P.2d 1055 (1940), cited by Plainfield, wholly supports Worldwide’s contentions here. In Guaranty Trust, an insolvent corporation initially sought to pledge its assets to a trust which would liquidate the assets for the benefit of creditors. Instead, a receiver was appointed. The receiver took significant steps to collect on a claim against a shareholder, including obtaining

court approval for compromise of the claim. Only after the shareholder failed to pay according to the court-approved compromise was the claim, along with the remainder of the receivership assets, transferred to the liquidating trust for the continued liquidation of assets. The Guaranty Trust case provides a prime example of an appropriate use of procedure in a receivership. There, the receiver brought an actual motion for the compromise of a claim which was specifically noted for hearing as such with the associated due process afforded the parties in interest. Again, Guaranty Trust supports Worldwide's position on appeal as to the lack of process in connection with the transfer of claims to Plainfield.

D. RCW 7.60.230

Last, Plainfield points to RCW 7.60.230, the receivership priority statute, but leaves key words out of its citation. The statute contemplates disposition of a secured creditor's collateral: "Creditors with liens on property of the estate, which liens are duly perfected under applicable law, shall

receive the **proceeds from the disposition** of their collateral.” RCW 7.60.230(1)(a) (emphasis added). The statute underscores Worldwide’s argument that a disposition of Plainfield’s collateral (a determination in the first place of whether the claims were Plainfield’s collateral, sale for the highest price after notice and hearing, foreclosure following abandonment) would have required due process. No such disposition occurred.

Moreover, Plainfield admits it holds no security interest in commercial tort claims, which are not its collateral, making the statute inapplicable to those claims.

E. Worldwide’s Claims as in Contract or Tort

Plainfield admits in its Response brief that it does not hold a security interest in commercial tort claims:

Worldwide is correct that, under Washington’s version of UCC Article 9, Plainfield’s security interest in Worldwide’s general intangibles does not reach ‘commercial tort claims.’ See RCW 62A.9A-108(e)(1); RCW 62A.9A-204(b)(2).

Response Brief at 16 (emphasis added).

After this admission, Plainfield proceeds to spend five pages of its brief explaining why the claims transferred to it are in fact not commercial tort claims but instead are claims in contract which do constitute its collateral as general intangibles.

Whether or not Worldwide's claims are Plainfield's collateral is a red-herring. The manner in which Plainfield got ahold of Worldwide's claims against Plainfield violated Worldwide's due process rights whether or not the claims were Plainfield's collateral.

In the event this Court rules that the "transfer" to Plainfield of its collateral was both proper and authorized under the law, at a minimum, the trial court's order should be clarified to exclude any of Worldwide's assets which are not Plainfield's collateral, in particular, Worldwide's commercial tort claims, in which Plainfield admits it holds no security interest.

F. Due Process Protections of the UCC

The UCC as adopted by the State of Washington provides mandatory due process protections to a debtor post-

default. The purpose behind the procedures is of such importance that the drafters made many of the due process requirements nonwaivable:

- (1) right to a response to a request for an accounting, concerning a list of collateral, or concerning a statement of account (Section 9-210);
- (2) the duty to collect collateral in a commercially reasonable manner (Section 9-607);
- (3) the implicit duty to refrain from a breach of the peace in taking possession of collateral (Section 9-609);
- (4) the duty to apply noncash proceeds of collection or disposition in a commercially reasonable manner (Sections 9-608 and 9-615);
- (5) the right to a special method of calculating a surplus or deficiency in certain dispositions to a secured party, a person related to secured party, or a secondary obligor (Section 9-615);
- (6) the duty to give an explanation of the calculation of a surplus or deficiency (Section 9-616);
- (7) the right to limitations on the effectiveness of certain waivers (Section 9-624); and
- (8) the right to hold a secured party liable for failure to comply with this Article (Sections 9-625 and 9-626).

The Official Comment to RCW 62A.9A-602 underscores the great weight the drafters put on the fairness of a creditor's collection and enforcement remedies:

With exceptions relating to good faith, diligence, reasonableness, and care, immediate parties, as between themselves, may vary its provisions by agreement. **However, in the context of rights and duties after default, our legal system traditionally has looked with suspicion on agreements that limit the debtor's rights and free the secured party of its duties.... The context of default offers great opportunity for overreaching.** The suspicious attitudes of the courts have been grounded in common sense. **This section, like former Section 9-501(3), codifies this long-standing and deeply rooted attitude.** The specified rights of the debtor and duties of the secured party may not be waived or varied except as stated.

Official Comment to RCW 62A.9A-602 (emphasis added).

It is undisputed that Worldwide received none of the protections, including the non-waivable protections, provided under the statutory requirements of the UCC.

G. Lack of Due Process under Receivership Act

Even if the Court were to rule that the Receivership Act provided a mechanism for Plainfield to obtain Worldwide's claims against Plainfield, certainly the cursory process that took place in the Receivership afforded Worldwide no process

whatsoever. The ambiguous and rapid path to transfer to Plainfield the very claims against itself developed as follows:

		<u>Pleading</u>	<u>Relief</u>
1.	11/23/09	Receiver's Motion to Terminate Receivership and Discharge Receiver	<u>Relief requested:</u> To terminate the receivership and discharge receiver. CP 5, l. 26. <u>Facts in Support:</u> "All assets of the receivership entities were subject to the security interest of the plaintiff, Plainfield Specialty Holdings, II, Inc." CP 6, ll. 24-25.
2.	12/08/09	Response of Plainfield Specialty Holdings II Inc.	<u>Requested Modification of Proposed Order:</u> Request to add to order: "The Receiver is additionally authorized to assign to Plainfield ... <u>any claims or causes of action possessed by the Receivership Entities.</u> " CP 1192, ll. 13-14.
3.	12/09/09	Response of Defendants	<u>Objection:</u> "While defendant companies have no objection to assignment of other assets of defendant companies to Plainfield, the defendant companies do object to the Receiver's assignment to Plainfield of claims and/or causes of action which the defendant companies may possess against Plainfield." CP 1194, ll. 8-11.
4.	12/10/09	Receiver's Reply	<u>Reply:</u> "Although the Receiver did not do a formal investigation into allegations against Plainfield, the Receiver in the course of fulfilling its [sic] duties, examined the claims and decided not to pursue these." CP 410, ll. 21-23.
5.	12/11/09	Order Granting Receiver's Motion To Terminate Receivership	Contains Language First Requested by Plainfield in Response to Termination Motion: "The Receiver is additionally authorized to assign to Plainfield any assets of the Receivership Entities . . . and any claims or causes of action possessed by the Receivership Entities." CP 1192, ll. 6-10.

As shown above, Worldwide was deprived of its claims against Plainfield in a swift and haphazard fashion by way of a motion by the Receiver to “Terminate Receivership and Discharge Receiver.” No process was provided to allow Worldwide to respond to any issues concerning the potential value of the claims, whether or not the claims were Plainfield’s collateral, or any other questions in connection with the claims. These events resulted in the transfer of Worldwide’s assets to the very party who would make sure to extinguish their value. The events not only contradicted the very meaning of foreclosure under the UCC, they were bereft of basic due process of any kind.

V. THE TRIAL COURT COULD NOT HAVE AND DID NOT MAKE ANY FINDINGS AS TO WORLDWIDE’S CLAIMS AGAINST PLAINFIELD

The trial court could not have and did not make any findings as to Worldwide’s claims against Plainfield.

A. The Receiver as “Neutral” Party Did No Investigation of the Claims

Plainfield argues the Receiver exercised some independent judgment as to Worldwide’s claims and that the trial court deferred to the Receiver’s purported conclusions as to the claims. This is not true. The Receiver admitted to trying to be a “neutral” party who performed no formal investigation into the claims. The entirety of the Receiver’s statements regarding Worldwide’s claims against Plainfield follows:

1. Receiver’s Reply:

Although the Receiver did not do a formal investigation into allegations against Plainfield, the Receiver in the course of fulfilling its [sic] duties, examined the claims and decided not to pursue these.

CP 410, ll. 21-23.

2. Hearing on Receiver’s Termination Motion:

The Court: I don’t know. I don’t feel like Sacajawea today but I guess that’s what I need to do. **It seemed to me by that response the receiver really didn’t take a position.**

Ms. Carey: Well, it’s a difficult one, Your Honor, because the receiver is trying to be a **neutral party** in this case. The receiver did, as I indicated, look

at these briefly, did not determine that it was sufficient allegations to expend the attorneys fees, basically, to explore this any further.

RP, December 12, 2009, p. 6 (emphasis added).

There is no evidence showing the Receiver, as a “neutral” party, conducted any independent review of the claims against Plainfield:

(1) The Receiver decided to not expend attorneys fees to explore the claims or their value--which exploration would have entailed at a minimum interview of Worldwide principals and review of documents;

(2) The Receiver took no steps to engage counsel to pursue the claims on a contingency basis; and

(3) The Receiver had no basis and took no steps to determine the claims’ value.

In fact, the Receiver’s non-committal neutrality was only underscored by the Receiver’s recent letter of May 28, 2010, to

this Court¹ in which his counsel conceded the Receiver's nominal role in this matter:

[Letterhead of Diana K. Carey of Karr Tuttle Campbell]
May 28, 2010

Richard D. Johnson
Court Administrator/Clerk
State of Washington
Court of Appeals, Division 1
600 University Street
Seattle, WA 98101-4170

Re: Case No. 64799-7-1 Plainfield Specialty Holdings,
Respondent v. Worldwide Water, Inc., Appellant

Dear Mr. Johnson

Our firm formerly represented Tyrell B. Vance, LLC, the general receiver of Worldwide Water, Inc., etc. in the Snohomish County Action, 09-2-043934-7. The Receiver has been discharged and is no longer involved in this case. This week we received Appellants' Opening Brief in the above matter and were surprised to see that the Receiver was named as a Respondent, along with Plainfield Specialty Holdings II Inc. The only proper respondent is Plainfield, not the Receiver. **While the Receiver's name appeared on the trial court caption as a nominal party during the pendency of the receivership, the Receiver is not a party in interest, has no stake in the outcome of the appeal and will not be filing a Respondent's Brief. Please remove the Receiver from the caption as a Respondent, and remove my name from the service list.** Thank you.

Very truly yours,
/s/ Diana K. Carey

Emphasis added.

¹ This recent letter is not part of the designated record in this appeal but is part of the Court of Appeals' file in this case.

B. The Trial Court Admitted It Could Not Make Findings on the Claims

The trial court acknowledged it was in no position to make any findings as to the claims themselves:

The Court:

And perhaps **because I don't know enough of the facts in this case**, the rather speculative nature of the potential claim of defendants versus Plainfield for somehow violating the underlying contract itself, and even if there were a recovery it would have to be so substantial to recover the other moneys that were owed. And so at this point I'm going to include any potential causes of action by the defendant corporations against Plainfield as a corporate asset, which they would themselves possess.

RP, December 12, 2009, p. 16 (emphasis added).

C. No "Compromise" Was Before the Trial Court

Moreover, there was certainly no "compromise" being approved by the trial court as Plainfield conjures. No compromise request was made by any party. Had any party sought approval of some sort of compromise, the trial court would have considered instruction from the routinely-cited

Ninth Circuit law applying the standards for approving a compromise in a bankruptcy setting:

In determining fairness, reasonableness and adequacy of a proposed settlement agreement, the court must consider: (a) The probability of success in litigation; (b) the difficulties, if any, to be encountered in the matter of collection; (c) the complexity of the litigation involved, and expense, inconvenience and delay necessarily attending it; (d) the paramount interest of the creditors and a proper deference to their reasonable views in the premises.

In re A & C Properties, 784 F.2d 1377, 1381 (9th Cir. 1986) (quoting In re Flight Transp. Corp. Sec. Litig., 730 F.2d 1128, 1135 (8th Cir. 1984).

The Ninth Circuit, in A & C Properties found no abuse of discretion by a trial court's approval of a compromise "where the evidence on the issue of the compromise **was thorough and comprehensive, the court was familiar with the entire record and touched all material bases of the creditors' objections, and held directly, expressly or by necessary implication, on every substantial point of contention...**". A & C Properties, 784 F.2d at 1383 (emphasis added).

Not only does Plainfield attempt to develop the concept of a compromise out of air where no compromise was in any way before the trial court, Plainfield cites a 1935 Pennsylvania case and a 1939 Florida case with respect to compromise. If compromise had even been a factor in this matter, the stringent Ninth Circuit law on compromise would have instructed the trial court's determination of whether or not any compromise would have been appropriate. Under that standard, the trial court's admission here that it did not know the facts of the case would have precluded approval of any hypothetical compromise.

Moreover, it is abundantly clear that Worldwide's claims against Plainfield continue to exist or there would not be such effort expended by Plainfield at the trial court to capture the claims. The receivership was, of course, still pending at the time of the subject hearing. The claims, although improperly transferred to Plainfield, were never substantively ruled upon or dismissed.

VI. CONCLUSION

Worldwide was stripped of its claims against Plainfield with no due process and lacking a proper mechanism under either the Receivership Act or the UCC. The result turned the law on its head in such a way that Plainfield got ahold of claims against it, thus assuring they would never be pursued.

Worldwide respectfully requests that in the event this Court rules that the “transfer” to Plainfield of its collateral was both proper and authorized under the law, at a minimum, the trial court’s order should be clarified to exclude any of Worldwide’s assets which are not Plainfield’s collateral, in particular, Worldwide’s commercial tort claims, in which Plainfield admits it holds no security interest.

DATED this 2nd day of August, 2010.

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CERTIFICATE OF SERVICE

I certify that on the 2nd day of August, 2010, I caused copies of the Reply Brief of Appellants to be hand-delivered to the following parties:

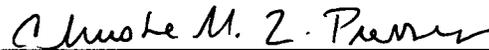
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