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COURT OF APPEALS  
DIVISION II

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STATE OF WASHINGTON

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DEPUTY

No. 42436-3-II

COURT OF APPEALS, DIVISION II  
OF THE STATE OF WASHINGTON

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MERIDIAN PLACE, LLC,  
a Washington limited liability company,

Appellant,

v.

HUMCOR, INC., a Washington corporation d/b/a Callaway Fitness,  
PAWNEE LEASING CORPORATION, a Colorado corporation; KEY  
EQUIPMENT FINANCE, INC., a Michigan corporation, CASCADE  
BANK, a Washington corporation; SMART LENDING, LLC, and  
MICHAEL PETROVIC

Defendants,

JOHN AND JANE DOE HAUGHNEY, and their marital community,  
and JAMES and KRISTI LOVEALL, and their marital community,

Respondents.

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APPEAL FROM THE SUPERIOR COURT  
FOR PIERCE COUNTY  
THE HONORABLE JOHN HICKMAN

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REPLY BRIEF OF APPELLANT

SMITH GOODFRIEND, P.S.

By: Howard M. Goodfriend

WSBA No. 14355

Ian C. Cairns

WSBA No. 43210

1109 First Avenue, Suite 500

Seattle, WA 98101

(206) 624-0974

BUCKNELL STEHLIK SATO

& STUBNER, LLP,

By: Jerry N. Stehlik

WSBA No. 13050

2003 Western Avenue, Suite 400

Seattle WA 98121-2142

(206) 587-0144

Attorneys for Appellant

2/12

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## I. INTRODUCTION

The Uniform Fraudulent Transfer Act does not reward fraudulent actors and neither should this court. Respondents John Haughney and James Loveall concede that they fraudulently transferred the Callaway I fitness club in order to place assets out of reach of Appellant Meridian Place, preventing Meridian from satisfying the lease obligation owed by Callaway I's parent corporation, Humcor Inc. By ignoring the undisputed evidence that the \$750,000 purchase price represented the value of this asset, including the fitness club's equipment, leasehold improvements and membership base, at the time of transfer, the trial court allowed respondents to avoid the consequences of their wrongful conduct, contrary to the Legislature's language and purpose under the UFTA. This court should reverse the trial court's \$75,000 judgment against Haughney and remand with instructions to enter a judgment against Haughney and Loveall of at least \$550,000.

## II. REPLY ARGUMENT

**A. By Imposing On Meridian The Burden Of Proving That The Value Of Callaway I Was More Than Its Stated Purchase Price, The Trial Court Misapplied The UFTA And Its Policies And Ignored Undisputed Evidence Of The Value Of The Asset At The Time Of Its Fraudulent Transfer.**

As respondents concede (Resp. Br. 21), the Uniform Fraudulent Transfer Act's "overriding purpose . . . is to provide relief for creditors whose collection on a debt is frustrated by the actions of a debtor to place the putatively satisfying assets beyond the reach of the creditor." *Thompson v. Hanson*, 168 Wn.2d 738, 750, ¶¶23, 239 P.3d 537 (2009). Here, the trial court made unchallenged findings that Haughney and Loveall engaged in a fraudulent conveyance of Callaway I to place it beyond the reach of Meridian, a Humcor creditor based on its lease deal with the unsuccessful second club, Callaway II. "As the findings of fact are not challenged by a cross-appeal by the defendants, they must be considered verities." *Wine v. Theodoratus*, 19 Wn. App. 700, 707, 577 P.2d 612 (1978).

Having found a fraudulent transfer, the trial court erred in failing to enter judgment “for an amount equal to the value of the asset at the time of the transfer,” under RCW 19.40.081(c). The trial court’s assessment of damages and allocation of the burden of proof allowed the fraudulent actors Haughney and Loveall to benefit from their attempt to place Callaway I beyond the reach of Meridian. This court should adhere to the purpose and letter of the UFTA by reversing the trial court’s \$75,000 judgment and remanding with instructions to enter a judgment of at least \$550,000 against both Haughney and Loveall.

**1. The Trial Court Misapplied The UFTA By Holding That Meridian Did Not Meet Its Burden Of Proving The Value Of Callaway I And By Refusing To Require That Haughney And Loveall Prove That The Asset Was Worth Less Than Its Purchase Price.**

The trial court erred in holding that Meridian failed to meet its burden of proving the value of Callaway I at the January 2008 time of transfer. (CL 7, CP 343) Haughney and Loveall violated the UFTA not because the parties agreed upon inadequate consideration, but because Loveall never actually assumed Haughney’s mortgage. (App. Br. 27-30) Meridian demonstrated below, and the trial court correctly held that the transfer of

Callaway I to Loveall was fraudulent because, contrary to the documents evidencing the purchase and sale, Loveall never assumed Haughney's \$635,000 personal debt obligation, which represented the majority of its \$750,000 purchase price. (FF 17, CP 340; CL 3, CP 342; App. Br. 15, 17-25).

"Washington courts abide by the principle that the wrongdoer shall bear the risk of the uncertainty which [its] own wrong has created." ***Spradlin Rock Products, Inc. v. Pub. Util. Dist. No. 1 of Grays Harbor County***, 164 Wn. App. 641, 664, ¶45, 266 P.3d 229 (2011) (quotations omitted) (App. Br. 25). The trial court's conclusion that Meridian bore the burden of proving that the value of Callaway I was anything other than that established by the undisputed evidence allowed Haughney and Loveall to benefit from their fraud, contrary to Washington law and the purpose of the UFTA. See ***Thompson v. Hanson***, 168 Wn.2d 738, 750, 239 P.3d 537 (2009).

Where, as here, a creditor establishes a fraudulent conveyance, the burden is on the parties perpetrating the fraud to establish that the transfer was harmless or that the value of the asset was different than that stated by the defendants. ***Scholes v. Lehmann***, 56 F.3d 750, 757 (7<sup>th</sup> Cir.), *cert. denied*, 516 U.S. 1028

(1995); *In re Clemons*, 42 B.R. 796, 799 (Bankr. S.D. Ohio 1984) (App Br. 20-26). Haughney's and Loveall's argument that Callaway I was not worth its purchase price is the type of "self-serving" argument rejected by the bankruptcy court in *Clemons* precisely because it would authorize the fraudulent parties to benefit from their wrongful act.

Haughney and Loveall fail to offer any precedent or policy to support the trial court's misallocation of the burden of proof, arguing only that the issue is not preserved for appellate review. Their argument is without merit. In the trial court, Meridian repeatedly argued that once it had sustained its burden of establishing the *fact* of damage, Loveall and Haughney had the burden to refute the undisputed evidence that the purchase price established a reasonable basis for assessing the *amount* of damage.<sup>1</sup> Meridian made the same argument in excepting to the trial court's findings of fact and in its motion for reconsideration after the trial court

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<sup>1</sup> (CP 182 ("By establishing the fact of damage . . . and pointing to evidence sufficient to estimate the value of the property transferred, plaintiff has carried its burden to establish damages with reasonable certainty. On this issue, Washington case law is clear that [t]here is a clear distinction between the measure of proof necessary to establish the fact that the plaintiff has sustained some damage and the measure of proof necessary to enable the jury to fix the amount.") (quotation omitted))

awarded \$75,000 in damages.<sup>2</sup> This court should address the trial court's misallocation of the burden of proof on the merits and reverse the trial court's judgment.<sup>3</sup>

**2. The Trial Court Erred In Requiring Meridian To Establish By Expert Testimony The Value Of Callaway I In The Face Of Undisputed Evidence From The Club's Owners.**

Just as it misallocated the burden of proof, the trial court also committed a legal error in holding that Meridian had to establish by expert testimony the value of an asset that its owners valued at \$750,000. No rule of law required Meridian to produce expert testimony to contradict its owners' testimony that the \$750,000 purchase price accurately reflected its value at the time of transfer. Haughney's and Loveall's attempt to defend this legal error fails. (Resp. Br. 1, 7, 13, 20)

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<sup>2</sup> (CP 220 ("The plaintiff reminds the Court that once the plaintiff proves the fact of damage the burden of proving the actual amount is lessened. The plaintiff is entitled to an award of damages so long as there is evidence which affords a reasonable basis for estimating the loss."); see also CP 304)

<sup>3</sup> The proper allocation of the burden of proof is an important issue under the UFTA and will aid defrauded creditors in obtaining relief in the future, consistent with the purpose of the UFTA. This court can and should address it, even had Meridian failed to adequately preserve the issue. **Home Builders Ass'n of Kitsap County v. City of Bainbridge Island**, 137 Wn. App. 338, 345, ¶¶15-16, 153 P.3d 231 (2007) (reviewing unpreserved issue regarding allocation of burden of proof regarding reasonableness of permit fees; RAP 2.5(a) gives appellate court's discretion to review issues not raised in the trial court).

Haughney, Loveall, and Petrovic were owners of a business who were competent to testify to Callaway I's value. (RP 232, 369, 397, 467, 537, 550) "The decisional law leaves no room for doubt that the owner may testify as to the value of his property because he is familiar enough with it to know its worth." Tegland, 5B Washington Practice: Evidence § 701.18 (5<sup>th</sup> ed. 2007) (quoting **Cunningham v. Town of Tieton**, 60 Wn.2d 434, 374 P.2d 375 (1962) (App. Br. 29)).

Meridian was not required to have an expert corroborate the value that these adverse parties consistently placed on Callaway I. See ER 801(d)(2) (excluding statement by party-opponent from definition of hearsay); **Kurtz v. Fels**, 63 Wn.2d 871, 875, 389 P.2d 659 (1964) ("We take the rule to be that, where a party to an action, in clear and unambiguous terms under oath, asserts the existence or nonexistence of a fact . . . the adverse party may rely on such statements . . ."). Haughney's and Loveall's position on appeal that Callaway I had little or no value stands in stark contrast to their

testimony<sup>4</sup> and the argument of their counsel below<sup>5</sup> in which they repeatedly asserted that the \$750,000 purchase price accurately represented the club's value at the time of its transfer in January 2008.

Because Haughney and Loveall repeatedly asserted to the trial court that Callaway I was worth \$750,000 they should now be estopped from asserting otherwise. See *In re Estates of Smaldino*, 151 Wn. App. 356, 363, ¶20, 212 P.3d 579 (2009) ("Judicial estoppel is an equitable doctrine that precludes a party from asserting one position in a court proceeding and later seeking an advantage by taking a clearly inconsistent position.") (alterations

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<sup>4</sup> (*Compare* Resp. Br. 15 ("not one scintilla" of evidence to support the valuation Meridian asserts on appeal) *with* RP 232 (Loveall: "Q. [D]id you believe that was a fair price for the asset you were buying? A. Yes"), 369 (Haughney: "Q. . . . "Mr. Loveall gave value to Humcor when this deal was done, wasn't it? A. Mr. Loveall paid \$750,000 for the assets, yes, sir."), 397, 467 (Haughney: "Q. That sale satisfies the definition of fair market value as you explained, is that correct? A. In my opinion, yes, sir."), 537 (Haughney: "Q. So he paid \$114,000, assumed a debt. He got assets that you list worth \$743,000, right? A. They actually say \$750,000."); Exs. 5A, 5B)

<sup>5</sup> (RP 37, 47-48 ("the \$750,000 that Mr. Loveall paid for Callaway I, the plaintiff has essentially admitted that was fair consideration"), 706, 715 ("He bought something worth \$750,000."), 720 ("We know that – because the plaintiff has conceded, we know that the \$750,000 paid by Mr. Loveall was fair market value."), 727 ("We know that the value of this business was \$750,000."), 728-29 (Loveall bought Callaway I "for a number that everybody agrees is fair market value"); CP 199 ("Meridian Place simply has no evidence that the consideration received by Humcor ([\$750,000]) was not 'reasonably equivalent to the value' of Callaway 1"))

and quotations omitted), *rev. denied*, 168 Wn.2d 1033. The trial court erred in holding that Meridian was bound to offer expert testimony to refute the undisputed testimony of these adverse owners as to the value of their business.

**3. Undisputed Evidence Established That Callaway I's Purchase Price Accurately Reflected Its Value.**

The trial court's \$75,000 judgment against Haughney is in any event not supported by substantial evidence, regardless of which party had the burden of proof. Haughney and Loveall presented the only evidence of "the value of the asset at the time of the transfer," RCW 19.40.081(c), and there was no evidence from which the trial court could have based its finding that Callaway I had a value of only \$75,000 in January 2008. (RP 232, 369, 397, 467, 537; Exs. 5A, 5B)

While the trial court may under RCW 19.40.081(c)(2) adopt a "value of the asset at the time of the transfer" that falls within the range of competent evidence, the court is not free to completely disregard undisputed evidence in making its findings. See ***North Kitsap School Dist v. K.W.***, 130 Wn. App. 347, 369-70, ¶¶62, 123 P.3d 469 (2005) (finding that ignores undisputed evidence is erroneous), *rev. denied*, 157 Wn.2d 1018 (2006); ***State v. Reite***, 46 Wn.

App. 7, 11, 728 P.2d 625 (1986) (same). Haughney and Loveall cite the trial court's categorical rejection of Callaway I's stated purchase price as "the least reliable evidence" of Callaway I's value (Resp. Br. (quoting RP 759)), but fail to address the undisputed evidence of value that the trial court ignored in allowing the fraudulent actors to benefit from their wrongful conduct.

Loveall understood that he was not just purchasing Callaway I's equipment but that its valuable assets included the club's membership. (RP 232) As Haughney and Loveall concede, the uncontested evidence showed that Callaway I had 1,500 members at the time of the transfer and that other health club companies were willing to pay up to \$300,000 to purchase these memberships. (Resp. Br. 4, citing RP 451-52; *see also* 576) When Haughney purchased stock in Humcor in January 2007, Callaway I's tangible assets, including its exercise equipment and its leasehold improvements, were valued at \$550,000 (Ex. 21 at Schedule B), the same value shown by Haughney's accounting firm's own calculation one year later in January 2008, at the time of sale to Loveall. (Exs. 5A, 5B; RP 378-86)

Haughney and Loveall erroneously assert that Meridian's principal, Gregory Stein, testified that Callaway I's equipment at the

time of transfer was worth \$60,000-\$80,000. (Resp. Br. 15, 18) But the trial court struck this testimony, which related to *Callaway II's equipment*, after Haughney objected to it as hearsay. (RP 98)

In arguing that Callaway I “was operating at a loss” (Resp. Br. 15), Haughney and Loveall fail to mention that Haughney had saddled the profitable Callaway I with the monthly payments required to service the \$630,000 mortgage that he took out to finance Callaway II. (FF 7, CP 338-39; RP 369-70, 395-97; Ex. 1 at 2; *compare* Ex. 5A with Ex. 5B (reflecting transfer of Haughney's \$630,000 mortgage with Callaway I)) The undisputed evidence showed that Callaway I had a history of profitability and had netted a profit of \$100,000 in 2006. (FF 16, CP 340; RP 487-88; Ex. 21 at Schedule B) At the end of 2007, just before the fraudulent transfer, Callaway I was breaking even *despite* being burdened with Callaway II's expenses and despite Humcor's principals' focus on saving Callaway II. (FF 7, CP 338 (unchallenged); RP 346-48, 413-14, 491-92) Loveall's investment of minimal additional funds into Callaway I likewise fails to establish that Callaway I had a negative value, as respondents now claim. (Resp. Br. 6, 15) Loveall invested these funds into Callaway I on Haughney's instruction who

was still using Callaway I's revenue to service his personal mortgage. (CP 251, 395-97)

A trial court's judgment that is not supported by substantial evidence must be reversed. See **Sommer v. Dep't of Soc. & Health Services**, 104 Wn. App. 160, 163, 15 P.3d 664 (2001), *rev. denied*, 144 Wn.2d 1007. The trial court's finding limiting the value of Callaway I to \$75,000 cannot be sustained on this record. This court should reverse with directions to the trial court to enter judgment of at least \$550,000 based on the undisputed evidence presented below.

**B. The Trial Court Erred By Refusing To Enter Judgment Against Loveall, The First Transferee Who Actively Engaged In The Fraudulent Transfer.**

In its opening brief Meridian established that the UFTA by its terms required the court to enter judgment against Loveall as "the first transferee" of Callaway I. RCW 19.40.081(b)(1) (See App. Br. 32-35) Because Loveall makes no argument to support the trial court's refusal to enter judgment against him as the "first transferee" under RCW 19.40.081(b)(1), he has conceded that the trial court erred in limiting its judgment to Haughney, Loveall's transferor. See **State v. Ward**, 125 Wn. App. 138, 144, 104 P.3d 61 (2005) (respondent concedes error by failing to offer argument

in support of challenged decision on appeal) At a minimum, this court should reverse the trial court's refusal to enter judgment against Loveall and direct entry of a joint and several judgment against Loveall and Haughney pursuant to RCW 19.40.081(b)(1).

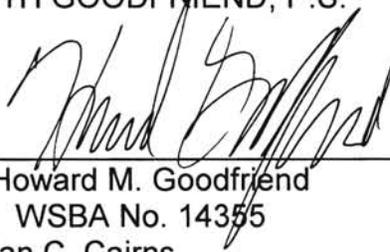
### **III. CONCLUSION**

This court should refuse to allow Haughney and Loveall to benefit from the fraud they concede they perpetrated on Meridian by placing the only valuable asset held by Meridian's tenant beyond the reach of Meridian. The trial court erroneously held that Meridian had not met its "burden" to establish the value of Callaway I when Haughney and Loveall repeatedly asserted that it was worth \$750,000. The trial court's decision is inconsistent with the purpose of the UFTA, which seeks to aid defrauded creditors in obtaining relief. This court should reverse and remand with instructions to enter a judgment for at least \$550,000 against both Haughney and Loveall.

Dated this 4<sup>th</sup> day of September, 2012.

SMITH GOODFRIEND, P.S.

BUCKNELL STEHLIK SATO  
& STUBNER, LLP

By: 

Howard M. Goodfriend  
WSBA No. 14355  
Ian C. Cairns  
WSBA No. 43210

By: 

Jerry N. Stehlik  
WSBA No. 13050

Attorneys for Appellant

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**DECLARATION OF SERVICE**

The undersigned declares under penalty of perjury, under the laws of the State of Washington, that the following is true correct: ~~DEPUTY~~

That on September 4, 2012, I arranged for service of the foregoing Reply Brief of Appellant, to the court and to the parties to this action as follows:

Office of Clerk Court of Appeals - Division II 950 Broadway, Suite 300 Tacoma, WA 98402	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input checked="" type="checkbox"/> U.S. Mail <input type="checkbox"/> E-Mail
William B. Foster Attorney at Law PO Box 69 Lynnwood, WA 98046-0069	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input checked="" type="checkbox"/> U.S. Mail <input checked="" type="checkbox"/> E-Mail
Robert William Novasky Stone Novasky, LLC 1 N Tacoma Ave Ste 201 Tacoma, WA 98403-313	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input checked="" type="checkbox"/> U.S. Mail <input checked="" type="checkbox"/> E-Mail
Jerry N. Stehlik Bucknell Stehlik Sato & Stubner LLP 2003 Western Avenue, Suite 400 Seattle, WA 98121-2142	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input type="checkbox"/> U.S. Mail <input checked="" type="checkbox"/> E-Mail
Michael Petrovic Pro Se mpetrovic@callawayfitness.com	<input type="checkbox"/> Facsimile <input type="checkbox"/> Messenger <input type="checkbox"/> U.S. Mail <input checked="" type="checkbox"/> E-Mail

**DATED** at Seattle, Washington this 4th day of September, 2012.

  
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Victoria K. Isaksen