FILED

AUG 05 2013

COURT OF APPEALS
DIVISION III
STATE OF WASHINGTON
By_____

No. 90891-5

No. 314910-III

COURT OF APPEALS, DIVISION III
OF THE STATE OF WASHINGTON

NORTHWEST WHOLESALE, INC., a Washington corporation,

Plaintiff,

vs.

PAC-O FRUIT, LLC a Washington limited liability company; GREG HOLZMAN, INC., a foreign corporation authorized to do business in the State of Washington; and HAROLD OSTENSON and SHIRLEY OSTENSON,

Defendants.

HAROLD OSTENSON and SHIRLEY OSTENSON, as members of PAC-O FRUIT, LLC a Washington limited liability company,

Appellants,

vs.

GREG HOLZMAN, an individual, TOTAL ORGANIC LLC, a Washington limited liability company, and GREG HOLZMAN, INC., a foreign corporation doing business in the State of Washington,

Respondents.

APPELLANTS' OPENING BRIEF

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I. INTRODUCTION.

The instant appeal is taken from two Orders entered by the trial court in *Northwest Wholesale, Inc. v. Pac Organic Fruit, LLC*, et al., Chelan County Superior Court Cause No. 07-2-00514-0:

1. Findings of Fact, Conclusions of Law, and Order Granting Motion to Dismiss Count VIII of Ostensons' Amended Crossclaims and Third Party Complaint, entered on October 3, 2012; and

2. Order Denying Ostensons' Motion for Reconsideration, entered on February 14, 2013.

The litigation stems from the deliberate and improper dismantling of a limited liability company, Pac Organic Fruit, LLC ("Pac-O"), by Respondents Greg Holzman, Inc. ("GHI")[1], Greg Holzman and Total Organic LLC ("Total Organic"). Appellants Harold Ostenson and Shirley Ostenson held a 49% membership interest in Pac-O while GHI held a 51% membership interest. GHI, in turn was owned by Mr. Holzman.

Mr. Holzman was a fruit broker from San Francisco, California who was doing business in Washington State. In 1997, he was introduced to Mr. and Mrs. Ostenson who were owners of a small Washington State orchard and packing plant. Mr. Holzman approached the Ostensons to start a joint venture packing business in Washington State. Pac-O was

[1] Now known as Purity Organic Products.

formed on June 1, 1998 to operate a facility owned by the Ostensons to pack and store organic fruit. Mr. Ostenson ran the day to day operations of the facility. Mrs. Ostenson was the bookkeeper. The organic fruit packed and stored by Pac-O was sold primarily through GHI, a San Francisco company owned by Mr. Holzman.

In 2004, GHI was experiencing substantial business setbacks which resulted in serious cash flow problems. As a result, GHI began withholding proceeds from sales of organic fruit which rightfully belonged to Pac-O. This, in turn, caused cash flow problems for Pac-O, causing it to default on its operating line of credit and the Ostensons to default on their mortgage for the facility in January 2005.

On March 8, 2005, Mr. Holzman, through GHI as the controlling and managing member fired the Ostensons from their positions with Pac-O. On July 27, 2005 Mr. Holzman, as the controlling and managing member of Pac-O, executed a fraudulent Demand Promissory Note ("Note") in favor of GHI in the amount of $1,023,009.38. The Note was also signed by Mr. Holzman on behalf of GHI as holder of the Note. The amount of the Note was based in part on a series of itemized transactions totaling $978,009.38. Mr. Holzman subsequently executed three agreements which seized all assets of Pac-O to satisfy the Note, leaving Pac-O an empty shell.

Due to the financial crippling of Pac-O by GHI and on-going foreclosure proceedings against them, the Ostensons, on January 7, 2007, filed a Voluntary Petition for Bankruptcy in the United States Bankruptcy Court for the Eastern District of Washington under Chapter 11 of the Bankruptcy Code.

During the course of the Ostenson Bankruptcy, the Ostensons identified assets of their bankruptcy estate to include unliquidated claims against Holzman, GHI, and Total Organic LLC. In order to resolve these claims, all parties entered into a Stipulation, signed by the Ostensons, and Mr. Holzman, on behalf of himself as well as his entities GHI, Pac-O, Pacific Organic Produce, Inc. and Total Organic. The Stipulation was approved by the Bankruptcy Court.

Pursuant to the Stipulation, the Ostensons filed their Amended Crossclaims and Third Party Complaint ("Complaint"). The Complaint asserts eight causes of action. The first seven causes of action are crossclaims by the Ostensons directly against Pac-O, including four claims for breach of contract, as well as three claims for recovery of unpaid compensation, failure to make distributions and breach of fiduciary duties. None of the seven causes of action name Mr. Holzman, GHI and Total Organic LLC as cross-defendants. The eighth cause of action ("Count VIII") is a derivative claim brought by the Ostensons, as minority

members of Pac-O against Mr. Holzman, GHI and Total Organic LLC. Pac-O is not named as third party defendant in Count VIII.

Trial in this matter commenced on July 11, 2011 in Chelan County Superior Court before the Honorable Lesley A. Allan. After the Ostensons had presented their case in chief, Mr. Holzman and GHI moved for dismissal pursuant to CR 41(b)(3), alleging, with respect to the derivative claim asserted in Count VIII, that the Ostensons lacked standing to bring the claim due to their bankruptcy filing.

The trial court took the matter under advisement and Mr. Holzman began to introduce witnesses and evidence in defense.

After a several month break in the trial due to the trial court's calendar, Mr. Holzman again renoted his motion to dismiss and on October 3, 2012, the trial court dismissed Count VIII, concluding that because of their bankruptcy filing, the Ostensons lacked standing to bring a derivative claim. The Ostensons subsequently moved for reconsideration, which was denied on February 14, 2013.

This appeal, seeking review of the dismissal of Count VIII, followed.

II. ASSIGNMENTS OF ERROR.

1. The trial court erred in granting Respondents' motion to dismiss Count VIII pursuant to CR 41(b)(3).

2. The trial court erred in concluding that by filing their Bankruptcy Petition the Ostensons relinquished their membership in Pac-O.

3. The trial court erred in enforcing the dissociation provisions of RCW 25.15.130(1)(d)(ii) against the Ostensons.

4. The trial court erred in concluding that the Ostensons lacked authority to assert the derivative claims set forth in Count VIII.

5. The trial court erred in concluding that the Stipulation did not constitute the consent of the members of Pac-O to continue as members allowing them to assert the derivative claims set forth in Count VIII.

6. The trial court erred in concluding that Respondents' motion to dismiss pursuant to CR 41(b)(3) was not barred by the doctrine of judicial estoppel.

7. The trial court erred in concluding that Respondents' motion to dismiss pursuant to CR 41(b)(3) was not barred by the doctrine of collateral estoppel.

8. The trial court erred in concluding that Respondents' motion to dismiss pursuant to CR 41(b)(3) was not barred by the doctrine of res judicata.

III. ISSUES PRESENTED FOR REVIEW.

Whether Respondents waived their motion to dismiss pursuant to CR 41(b)(3) by presenting evidence on their behalf.

Whether Appellants became dissociated from Pac-O as a result of their bankruptcy filing.

Whether Appellants have standing as members of Pac-O to prosecute the derivative claim set forth in Count VIII.

Whether the dissociation provision under RCW 25.15.130 is unenforceable under the Supremacy Clause of the United States Constitution and provisions of the Bankruptcy Code, 11 U.S.C. § 541, *et seq.*

Whether Respondents, by stipulating that claims held by Pac-O could be brought against them, consented to the Ostensons' continued membership in Pac-O notwithstanding their bankruptcy filing.

Whether Respondents are barred by the doctrine of judicial estoppel from contesting Appellants' standing to prosecute Count VIII.

Whether Respondents are barred by the doctrine of collateral estoppel from contesting Appellants' standing to prosecute Count VIII.

Whether Respondents are barred by the doctrine of res judicata from contesting Appellants' standing to prosecute Count VIII.

IV. STATEMENT OF THE CASE.

This lawsuit, *Northwest Wholesale, Inc. v. Pac Organic Fruit, LLC*, et al., Chelan County Superior Court Cause No. 07-2-00514-0, was commenced on May 23, 2007. CP 4-9. The Northwest Wholesale

Complaint named Pac-O, GHI, and Mr. and Mrs. Ostenson as defendants. CP 4-9. Northwest Wholesale, Inc. was a supplier of equipment to Pac-O that had previously obtained a judgment against Pac-O in the amount of $301,797.76 during a time when Mr. Holzman, through GHI, was managing Pac-O. CP 4-9. The Northwest Wholesale Complaint sought to hold GHI and the Ostensons liable for the judgment under theories of Fraudulent Conveyance and Constructive Fraudulent Transfer, alleging that the assets of Pac-O had been drained to avoid payment of creditors. CP 1-9.

On July 25, 2009, the Ostensons filed their Crossclaims and Third Party Complaint. CP 35-53. On September 28, 2009, the Ostensons filed their Amended Crossclaims and Third Party Complaint ("Complaint") CP 476-493.

The Complaint was filed pursuant to a Stipulation which was entered into by the Ostensons and Mr. Holzman, on behalf of himself as well as his entities GHI, Pac-O, Pacific Organic Produce, Inc. and Total Organic. The Stipulation arose in the context of the Ostensons' Chapter 11 bankruptcy, *In re Harold T. Ostenson and Shirley M. Ostenson,* No. 07-00058-FLK11 ("Ostenson Bankruptcy") which was initiated on

January 9, 2007. Defendants' Exhibit ("Ex D-") 5[2] (Voluntary Petition). The First Amended Plan of Reorganization, filed by the Ostensons on July 31, 2007, identified assets of the bankruptcy estate to include unliquidated claims against Holzman, and GHI. Ex D-5 (Amended Plan). The Stipulation was intended to resolve various claims of the parties against each other. Ex D-5 (Stipulation). The Stipulation was approved by the Bankruptcy Court on August 18, 2008 and was incorporated into the Ostensons' First Amended Plan of Reorganization on August 28, 2008. Ex D-5 (Order and Amendment). In pertinent part, paragraph 7 of the Stipulation **preserved** the following causes of action:

> a. Any purported claims of the Ostensons against Pac-O, including, but not limited to, claims for unpaid lease installments, wages, expense reimbursement, dividends, fruit proceeds, and/or failure to pay Keybank's line of credit, provided that the Ostensons shall not be entitled to assert those purported claims, whether derivatively or directly (including by way of a veil-piercing or similar theory) against Holzman, GHI or POP, such purported claims to be released; and
>
> b. Any purported claims of Pac-O (and Pac-O only) against Holzman, GHI, POP and/or Total Organic for their alleged failure to pay packing fees, expenses, and revenues earned solely by Pac-O or fruit proceeds or rent due Pac-O or for conversion of assets of Pac-O.

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[2] Ex D-5 consists of four separate documents which will be referred to as follows: (1) Order Approving Compromise Settlement and Shortening Time to Object ("Order"); (2) Amendment to Debtor's First Amended Plan of Reorganization ("Amendment"); (3) Chapter 11 Voluntary Petition ("Voluntary Petition"); and (4) First Amended Plan of Reorganization ("Amended Plan"). The Stipulation at issue is attached to items 1 and 2.

Ex D-5 (Stipulation).

With respect to these preserved claims, paragraph 7.c of the Stipulation specifically provided that such claims were to be asserted and pled in Chelan County Superior Court, *Northwest Wholesale, Inc. v. Pac Organic Fruit, LLC et al.*, No. 07-2-00514. Ex D-5 (Stipulation).

The Complaint filed by the Ostensons was structured so as to comply with the provisions of the Stipulation. The Complaint asserts eight causes of action. The first seven causes of action ("Counts I – VII") assert direct claims against Pac-O pursuant to paragraph 7.a of the Stipulation. Counts I – VII consist of four claims for breach of contract, as well as three claims for recovery of unpaid compensation, failure to make distributions and breach of fiduciary duties. CP 484-487.

Count VIII is a derivative claim brought by the Ostensons as minority members of Pac-O against third party defendants, Mr. Holzman, GHI and Total Organic pursuant to paragraph 7.b of the Stipulation. This cause of action seeks recovery by Pac-O of the assets seized from Pac-O by Mr. Holzman, GHI and Total Organic. CP 488-490.

In pertinent part, Count VIII alleged:

> 11.10 Greg Holzman, Inc. has refused to execute documents in order to continue Pac Organic Fruit, LLC's financing arrangements, causing the company to be at risk for foreclosure actions by its bank. Demands that Greg Holzman, Inc. execute

those documents have been to no avail, and attempting to persuade Greg Holzman, Inc. in his capacity as managing member of Pac Organic Fruit, LLC to sue himself for mismanagement would be futile.

11.11 Greg Holzman, Inc., as managing member of Pac Organic Fruit, LLC, has terminated and excluded Harold Ostenson, the general manager and Shirley Ostenson, the company's controller from the company's operations. In their stead, Greg Holzman, Inc. has engaged in management practices that have destroyed the capacity of Pac Organic Fruit, LLC to operate in a profitable manner, all to the damage to Pac Organic Fruit, LLC in an amount to be proven at the time of trial. Any attempts to have Greg Holzman, Inc., as managing member, sue itself for mismanagement would be futile.

11.12 Greg Holzman, Inc., as managing member of Pac Organic Fruit, LLC, has unlawfully transferred the assets of Pac Organic Fruit, LLC to various entities which are controlled by Greg Holzman, including, but not limited to, Greg Holzman, Inc. and Total Organic LLC, all to the damage to Pac Organic Fruit, LLC in an amount to be proven at the time of trial. Any attempts to have Greg Holzman, Inc., as managing member, sue itself for mismanagement would be futile.

11.13 Greg Holzman, individually, as the controlling shareholder of Greg Holzman, Inc., owed a fiduciary duty to Pac Organic Fruit, LLC to control the operations of his closely held corporation in a manner not to cause damage to Pac Organic Fruit, LLC and its members. Greg Holzman, individually, has breached his duty to Pac Organic Fruit, LLC and has caused the company to sustain damages in an amount to be proved at trial.

CP 489-490.

Trial commenced on July 11, 2011. Harold Ostenson and Paul M. Fruci, CPA were called as witnesses during the Ostensons' case in chief.

Mr. Ostenson first met Greg Holzman in 1997. RP 54:1-4. Mr.

Holzman was in the organic brokerage business (GHI) and wanted to expand his operations in Washington. RP 54:15-23. Initially, Mr. Holzman proposed a partnership where Mr. Ostenson would operate a business packing and storing organic fruit which Mr. Holzman would sell. RP 55:10-15. Over the next six months, Mr. Ostenson discussed this proposal with Mr. Holzman. RP 55:22-56:16. On May 29, 1998, the operating company, Pac-O was formed. RP 56:19-23, Plaintiffs' Exhibit ("Ex P-") 25. The Ostensons owned 49% of Pac-O while Holzman's company, GHI, owned 51%. Ex P-26. Because Mr. Holzman did not want to own property in the State of Washington, the Ostensons would own the packing house in Grant County which would be leased by Pac-O. RP 59:16-21; 60:7-9; 61:18-24. On December 28, 1999, Pac-O entered into a triple net Lease with the Ostensons. RP at 62:1-6; P-27. The term of the Lease was 20 years, with monthly payments beginning at $8,200. RP 62:17-24; P-27. Although the facility originally would operate as a three-month packing shed, the envisioned goal was to establish Pac-O as a year-round operation. RP 63:11-24. To accomplish this, a million dollar loan was obtained and improvements to the facility made from May to August of 1998, adding three packing lines, increasing the cold storage facilities fourfold and constructing four controlled atmosphere ("CA") rooms. RP 64:1-4; 66:14-6 7:10. The loan was personally guaranteed by

the Ostensons and Mr. Holzman. TR at 67:13-15.

Mr. Ostenson confirmed that the business operations of Pac-O were represented by Ex P-1, a flow chart introduced for demonstrative purposes at trial, which illustrated the following process: (1) Growers would deliver produce to Pac-O for packing and storage; (2) GHI would sell produce to distributors; (3) The distributor would pay GHI for the produce; (4) Pac-O would make delivery of the produce to the distributor;[3] (5) GHI would remit sales proceeds less the commission earned by GHI to Pac-O; and (6) Pac-O Fruit would pay the growers for their produce. RP 53:18-24; Ex P-1.

Under this business model, Pac-O operations began to grow. According to Mr. Ostenson, the Profit and Loss Statement for Pac-O from 1998 through 2004 showed that the business steadily grew in total income from $187,220.45 in 1998 to $3,244,523.50 in 2004. Mr. Ostenson further noted the number of bins packed similarly increased from 491 in 1998 to 24,539 in 2004 and the number of growers serviced rose from 3 in 1998 to over 30 in 2004. RP 73:22-73:1-16; P-28. Mr. Ostenson estimated that the net profit in 2005 would exceed $324,000. RP 78:3-5.

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[3] This fourth step recognizes a correction noted by counsel for GHI and Holzman. RP at 23:19-21.

In order to accommodate the increase in business, Pac-O entered into a Controlled Atmosphere Lease Agreement ("CA Lease") to lease CA rooms in a facility located in Valley Forge, Washington, effective May 1, 2000. The entire facility consisted of twelve CA rooms. Pursuant to the terms of the CA Lease, Pac-O would initially lease four CA rooms, increasing the number of CA rooms leased by two every two years thereafter. When all twelve rooms had been leased, Pac-O would have an option to purchase the entire facility. RP 140:3-142:2; P-29.

In 2004, GHI was beginning to experience cash flow problems. RP 88:11-20. As a result, in August of 2004, the business model was changed so that instead of GHI remitting sales proceeds to Pac-O and Pac-O paying the growers, GHI retained all sales proceeds and began paying growers directly. RP 89:17-91:4. The records of GHI confirmed monies owed by GHI to Pac-O steadily increased during 2004 from $310,560.63 in January to $717,816.88 in April to $833,272.73 in May. RP 93:15-95:15; Ex P-4.

Further, records of Pac-O showed that, as of April 19, 2005, GHI owed Pac-O $1,017,380.22 which was never paid. RP 96:20-98:25; 99:4-7; Ex. P-5. Records produced by GHI reflected the decreasing payments to Pac-O in 2004, from $502,411.90 in July to $72,494.82 in August to nothing in September. RP 105:19-106:22; Ex P-6.

By September of 2004, Pac-O was packing more than 24,000 bins but GHI was increasingly unable to sell the produce, so that inventory kept increasing, necessitating contacting other brokers to assist in sales. By November of 2004, given GHI's rate of sales, Mr. Ostenson estimated that 150,000 boxes of produce would remain unsold. RP 150:12-155:13.

On January 1, 2005, Pac-O defaulted on its operating line of credit because Holzman refused to sign the guarantee which the Ostensons had signed. RP 155:16-157:24. Additionally, because payments to Pac-O were being withheld by GHI, Pac-O, on January 5, 2005, defaulted on its lease payments, thereby causing the Ostensons to default on the mortgage. Key Bank subsequently began foreclosure proceedings on the packing shed and the Ostensons' orchard. RP 157:25-158:25; 162:4-24.

On March 8, 2005, Mr. Holzman fired the Ostensons from their positions with Pac-O. RP 159:7-25.

On July 27, 2005, unknown to the Ostensons, Mr. Holzman, as the managing member of Pac-O, executed a Demand Promissory Note ("Note") in favor of GHI in the amount of $1,023,009.38. The Note was also signed by Mr. Holzman on behalf of GHI as holder of the Note. Ex P-9. The amount of the Note was based in part on a series of itemized transactions totaling $978,009.38. Ex P-9 at G024858-G024859. Mr. Holzman subsequently executed three agreements which seized all assets

of Pac-O to ostensibly satisfy the Note. The agreements to accept collateral were dated September 2, 2005, January 7, 2006 and March 31, 2006. Each agreement was signed by Mr. Holzman on behalf of GHI and Pac-O. Ex P-9 at G024865-G024872. Mr. Ostenson was unaware of the conversion of assets until May 10, 2006. RP 116:6-9; 118:11-14. According to Mr. Ostenson, the transaction list supporting the Note was "not an honest document" and that "the assets were taken, not rightfully." RP 219:16-223:23.

In addition to converting the assets of Pac-O, on November 1, 2005, Mr. Holzman also engineered the transfer of the CA Lease from Pac-O to GHI and continued packing operations in a new limited liability company and never made any kind of accounting to Mr. Ostenson for the conversion. RP 142:3-18; P-29. Records of GHI reflect packing revenue beginning in 2005 which properly belonged to Pac-O. Ex P-2.

Mr. Ostenson testified that the value of the CA Lease with its option to purchase was $650,698.59. RP 146:9-13; P11. Mr. Ostenson further testified that given the growth of Pac-O, at the end of the term of the CA Lease, Pac-O would have been able to purchase the facility. RP 261:2-264:19.

Paul M. Fruci, CPA, a Certified Public Accountant since 1969, was qualified by the Court to testify as an expert in accounting matters. RP 358:24-359:4.

Mr. Fruci testified that based on his examination of GHI records, GHI was showing losses in 2004 and 2005 and packing revenue and expenses in 2005 and 2006. RP 369:12-371:7; Ex P-2. Mr. Fruci further testified that Pac-O records showed a growing balance owed to Pac-O by GHI. RP 382:7-383:8. Moreover, Mr. Fruci indicated that the GHI Balance Sheet for the period from December 31, 1999 to June 18, 2009 showed a significant jump in current liabilities from $1,328,204.56 as of December 31, 2004 to $2,815,219.14 as of December 31, 2005, which would be indicative of cash flow problems. RP 384:7-386:13; Ex P-7.

Given this background, Mr. Fruci testified as to his analysis of the Note which was used by Mr. Holzman to improperly convert the assets of Pac-O to GHI. Mr. Fruci's analysis was introduced as Ex. P-18. Mr. Fruci indicated that he began his analysis with the list of alleged debts used to support the Note. P-9 at G024858-G024859. These debts were recreated in a list and coded into ten groups identified alphabetically from A-J. Mr. Fruci then traced each debt into GHI's books to confirm whether it represented an obligation from Pac-O or something else. Mr. Fruci concluded that with respect to each group, the amounts claimed by GHI to

be owed by Pac-O were not supportable under generally accepted accounting standards and that the Note was based upon fabricated debts. RP 388:23-407:7; Ex P-18.

Mr. Fruci next testified as to his analysis regarding how the business operations of Pac-O should have been wound down, which was contained in a second report, introduced into evidence as Ex P-32. Mr. Fruci explained that two assets were improperly transferred from Pac-O as the result of the conversion of its assets by Mr. Holzman: (1) the business operations, and (2) the CA Lease. RP 414:18-416:2; 419:22-420:2.

In his testimony, Mr. Fruci explained how he valued the business operations of Pac-O. In Mr. Fruci's opinion, the value of the Pac-O business operations was $1,601,680.00, which he considered conservative. RP at 433:1-444:6; Ex P-32, at Exhibit "B".

Mr. Fruci next testified as to his valuation of the CA Lease. In Mr. Fruci's opinion, the CA Lease had a value of $208,007.48. RP 444:7-448:24; Ex P-32, at Exhibit "C".

Mr. Fruci then explained his analysis regarding the value of the Ostensons' 2004 crop proceeds. In Mr. Fruci's opinion, the value of the crops was $140,897.71. RP 448:25-449.25; Ex P-32, at Exhibit "D".

Mr. Fruci lastly testified as to the value of the packing and storage facility leased to Pac-O by the Ostensons which the Ostensons lost in

foreclosure due to the failure of Pac-O to make the lease payments. In Mr. Fruci's opinion, the value of the packing and storage facility was $386,067.99. RP 450:4-452:3; Ex P-32, at Exhibit "E".

In his testimony, Mr. Fruci made it clear that the amounts due to the Ostensons for their 2004 crop and the loss of the packing and storage facility were amounts owed by Pac-O and not Mr. Holzman or GHI. In this regard, the Ostensons were creditors of Pac-O. RP 420:5-421:5; 423:2-18.

Mr. Fruci's report summarized his analysis of damages based on the foregoing valuations in Exhibit "A" to his report, in which he concluded that Pac-O had a total value of $1,809,687.48. From that amount Pac-O directly owed the Ostensons a total of $526,357.70 for the 2004 crop sales and loss of the packing and storage shed. From the remaining equity of $1,283,329.78, the Ostensons would be owed $628,831.59 representing their 49% interest in Pac-O as well as an additional $51,303.75 in attorney fees awarded by the United States Bankruptcy Court.[4] Ex P-32, at Exhibit "A".

At the conclusion of the Ostensons' case, counsel for Respondents moved for dismissal pursuant to CR 41(b)(3). RP 580:22-593:1. In

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[4] On November 10, 2010, the Bankruptcy Court found that Mr. Holzman had acted in bad faith and awarded the Ostensons $51,303.75 in attorney fees. RP 420:19-421:11.

pertinent part, Respondents contended that the Ostensons, by filing for bankruptcy, became dissociated from, and were no longer members of Pac-O. Because of the dissociation, they lacked standing to bring Count VIII of the Complaint. RP 591:22-592:25. After hearing counsel's argument, the trial court suggested that the motion would better have been brought as a pretrial motion. RP 593:5-6. The Ostensons contended that under RCW 25.15.130, paragraph 7.b of the Stipulation constituted the consent of Mr. Holzman and GHI to allow the Ostensons to bring the derivative claim. In addition, the Ostensons argued that in light of the Stipulation, Mr. Holzman and GHI should be precluded from challenging the Ostensons' standing to bring Count VIII under doctrines of equitable and judicial estoppel. RP 593:4-597:9, 600:12-601:12. After hearing from counsels, the Court did not rule on the motion to dismiss. RP 602:19-603:4. Respondents thereafter proceeded to present their case, calling witnesses Charles Kay, Ed Suchow and Kathryn Dubsky. RP 604-829.

A rehearing on the motion to dismiss was held on September 7, 2012. RP 9/7/12, 2-65, CP 2043. At this hearing, the Ostensons contended that under RCW 25.15.130, paragraph 7.b of the Stipulation constituted the consent of GHI to allow the Ostensons, as members of Pac-O, to bring the derivative claim. The Ostensons briefed and argued the

issue that paragraph 7.b of the Stipulation, by reserving claims of Pac-O against Mr. Holzman, GHI and Total Organic LLC, constituted consent required under RCW 25.15.130(1)(d) for the Ostensons to continue as members of Pac-O and thereby assert the derivative claim set forth in Count VIII. RP 9/7/12 31:3-47:4; CP. The Ostensons also briefed the issue regarding application of doctrines of equitable and judicial estoppel as well as Respondents' waiver of their motion to dismiss by presenting evidence on their behalf. CP 1860-1890. At the conclusion of the hearing, the trial court granted the motion to dismiss Count VIII. RP 9/7/12 60:4-64:10. On October 3, 2012, the trial court entered its Findings of Fact, Conclusions of Law and Order Granting Motion to Dismiss Count VIII of Ostensons' Amended Crossclaims and Third Party Complaint ("Order of Dismissal"). CP 2043-2051.

On October 15, 2012, the Ostensons filed their Motion for Reconsideration. CP 2052-2055. The Motion for Reconsideration was heard on November 8, 2012. RP 11/8/12 2-61. In addition to the previously-cited issues, the Ostensons briefed and argued the issue that neither State law nor the Operating Agreement could divest them of their membership interest in Pac-O upon filing for bankruptcy under the Supremacy Clause of the United States Constitution and provisions of the Bankruptcy Code, 11 U.S.C. § 541, *et seq.* RP 11/8/12, 4:8-31:10, 47:7-

55:19; CP 2056-2069, 2222-2233, 2383-2390.

At the conclusion of the hearing, the trial court took the matter under advisement and on February 14, 2013, entered its Order Denying Ostensons' Motion for Reconsideration. RP 11/8/12 81:7-10; CP 2400-2404.

On March 12, 2013, the Ostensons filed their Notice of Appeal. CP 2405-2422.

V. ARGUMENT.

A. Respondents Waived Their Motion to Dismiss Pursuant to CR 41(b)(3) by Presenting Evidence on Their Behalf After the Appellants had Rested.

By electing to present their case, Holzman and GHI waived their CR 41(b)(3) motion to dismiss and the trial court erred in concluding to the contrary in its Conclusion of Law No. 1:

> 1. The Court concludes that it retains the discretion to consider the Motion and the CR 41(b)(3) Pleadings despite the fact that the Holzman Defendants began to put on evidence in support of their defense case after the Court took the Motion under advisement on July 13, 2011. *Hector v. Martin*, 51 Wash.2d 707, 321 P.2d 555 (Wash. 1958) is not to the contrary. *Hector*, which in any event does not purport to circumscribe a trial court's discretion on these matters, involved a challenge solely to the sufficiency of the plaintiff's evidence, while a motion under CR 41(b)(3) involves an analysis of both "the facts and the law." The Court retains the discretion to consider both the facts presented and applicable law for the purpose of addressing the matter before it, and it chooses to do so. While in certain respects the CR 41(b)(3) Pleadings are akin to a motion for summary judgment under CR

> 56, the Motion was filed under CR 41(b)(3) and the Court has considered and ruled upon this matter under CR 41(b)(3).

CP 2047-2048.

The case of Hector v. Martin, 51 Wn.2d 707, 321 P.3d 555 (1958) is controlling and hence, dispositive on this issue. In Hector, the plaintiffs filed a complaint seeking damages and injunctive relief based upon an alleged trespass by defendants. At the close of the plaintiffs' case in chief, defendants moved to dismiss all claims. While the claim for damages was dismissed, the court reserved ruling on the issue of injunctive relief. Defendants thereafter proceeded with their evidence. At the conclusion of the trial, the trial court denied defendants' renewed motion to dismiss and granted plaintiffs' claim for injunctive relief. On appeal, defendants claimed that the trial court erred in not dismissing plaintiffs' claim for injunctive relief at the close of the plaintiffs' case. Id., at 708-709. The Washington Supreme Court, in affirming the judgment of the trial court, stated:

> We have consistently adhered to the rule that a challenge to the sufficiency of the evidence at the close of the plaintiff's case is waived by a defendant who does not stand on his motion and proceeds to present evidence on his own behalf, after his motion to dismiss has been *denied,* ....
>
> The same rule should be applied where the court *fails to rule* or *reserves* its ruling and the defendant thereafter submits his evidence. Therefore, the failure of the trial court to rule on such

> motion before introduction of proof by a defendant, is tantamount to a denial of the motion.

Id., at 709-710 (citations omitted) (italics in original).

The waiver rule recognized by the Washington Supreme Court is applied in the context of motions to dismiss made during trial, either pursuant to CR 41(b)(3) (non-jury trials) or CR 50 (jury trials).

The trial court, in granting Respondent's motion to dismiss Count VIII pursuant to CR 41(b)(3) erred and should be reversed.

B. The Ostensons' Did Not Relinquish Membership in Pac Organic Fruit, LLC Upon Filing Bankruptcy and the Dissociation Provisions of Both RCW 25.15.130 and the Operating Agreement of Pac Organic Fruit, LLC Cannot be Enforced to Divest the Ostensons of Their Membership Interest.

1. The Dissociation Provisions Under Washington Law.

RCW 25.15.130 sets forth various "events of dissociation" which, upon occurrence, result in a member of a limited liability company ceasing to be a member. One such event of dissociation occurs when a member "files a voluntary petition in bankruptcy." RCW 25.15.130(1)(d)(ii). RCW 25.15.370 recognizes the right of a member to bring a derivative claim on behalf of a limited liability company. RCW 25.15.370. RCW 25.15.375 further provides that a plaintiff bringing a derivative claim on behalf of a limited liability company "must be a member at the time of

bringing the action and ... [a]t the time of the transaction of which the plaintiff complains." RCW 25.15.375(1).

Articles 8 and 9 of the Pac-O Limited Liability Company Agreement ("Pac-O Operating Agreement") adopt the events of dissociation set forth in RCW 25.15.130. Ex P-26, at 13.

2. The Trial Court's Conclusions of Law.

The Order dismissing Count VIII of the Complaint hinges upon two key Conclusions of Law made by the trial court. These Conclusions of Law, in turn, are based upon application of the statutory dissociation provisions. Specifically, in Conclusion of Law No. 5 and Conclusion of Law No. 6 the trial court stated:

> 5. The Court concludes that upon the filing of the bankruptcy, the Ostensons relinquished their membership in Pac O; that the Stipulation did not restore their membership in Pac O; and that there is nothing in the Stipulation which gives the Ostensons the legal right to pursue claims on behalf of Pac O.
>
> 6. In light of RCW § 25.15.130(1)(d)(ii), the Ostensons ceased being members of Pac O on January 9, 2007, when they commenced their voluntary bankruptcy proceeding. Accordingly, they were not members of Pac O when, on July 25, 2008, they filed the derivative claim set forth at Count VIII of their Crossclaims and Third Party Complaint. Under RCW § 25.15.370, however, a plaintiff may bring a derivative action on behalf of a limited liability company only if that person was both "a member at the time of bringing the action and . . . [a]t the time of the transaction of which the plaintiff complains." While it is arguable that the Ostensons were members of Pac O at the time of the transactions of which they complain (a matter the Court does not decide), they were not members of Pac O on July 25, 2008, when they brought

> the derivative claims at issue in this matter. Consequently, the Ostensons lacked, and continue to lack, authority to assert those derivative claims under Washington law.

CP 2049.

Both Conclusions of Law are incorrect under controlling provisions of the Bankruptcy Code (Title 11 U.S.C.).

3. The Ostensons' Bankruptcy Estate Under the Bankruptcy Code Included the Ostensons' Membership Interest in Pac-O.

While application of the Bankruptcy Code to the Ostensons' membership interest in Pac-O was not addressed in the hearings on July 13, 2011 or September 7, 2012, the controlling provisions of the Bankruptcy Code and applicable case law were briefed and argued by the Ostensons in their Motion for Reconsideration and the hearing held thereon on November 8, 2012. CP 2056-2069, 2222-2233, 2383-2390; RP 11/8/2012, 2-61.

The Supremacy Clause of the United States Constitution provides:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

U.S. CONST. art. VI, cl. 2.

The Bankruptcy Clause of the United States Constitution provides Congress with authority "[t]o establish ... uniform Laws on the subject of Bankruptcies throughout the United States." U.S. CONST. art. I, § 8, cl. 4. The Bankruptcy Code set forth in Title 11 of the United States Code is the embodiment of this Constitutional authority. "States may not ... interfere with or complement the Bankruptcy Act or ... provide additional or auxiliary regulations." International Shoe Co. v. Pinkus, 278 U.S. 261, 265, 49 S.Ct. 108, 73 L.Ed. 318 (1929). In the case of In re Pruitt, 410 B.R. 546 (Bankr. D. Conn. 2009), the Bankruptcy Court described the relationship between of State law to Title 11 as follows:

> Indeed, State Law plays important definitional and referential roles under Title 11. State Law's primary function under Title 11 is to define the *pre-existing, i.e.* pre-bankruptcy, rights of the parties to a bankruptcy case. This function is important, in that it establishes a baseline of rights and obligations that Congress can then modify, as necessary, so as to produce a set of *bankruptcy* rights and obligations for purposes of treatment and participation in the bankruptcy case itself. Prototypical of these principles is the relationship between bankruptcy law and State property law in the creation of a bankruptcy estate. **A debtor's estate pre-bankruptcy and post-bankruptcy are entirely different animals; the former being determined by State Law and the latter being the exclusive province of federal bankruptcy law. ... The base upon which that estate is constructed is *subsection 541(a)(1)* – 'all legal or equitable interests of the debtor in property as of the commencement of the [bankruptcy] case.'**

Id., at 553 (italics in original, emphasis added).

Under 11 U.S.C. § 541, the commencement of a bankruptcy case creates an estate comprised of "**all** legal or equitable interests of the debtor in property **as of the commencement of the case**." 11 U.S.C. § 541(a)(1) (emphasis added).

The reach of 11 U.S.C. § 541(a)(1) is broad; the extent of a debtor's estate under 11 U.S.C. 541 includes "[e]very conceivable interest of the debtor, future, nonpossessory, contingent, speculative, and derivative." In re Yonikus, 996 F.2d 866, 869 (7th Cir. 1993). Further, the debtor's estate is not limited to "economic" interests but also includes non-economic rights. Non-economic rights of members in a limited liability company include the right of "members [to] vote to fill a vacancy in the position of manager, remove a manager, to approve the sale a member's interest, to approve the substitution of a new member, and to continue the company if there is an event of dissolution." In re Warner, 480 B.R. 641, 653 (Bankr. N.D. W.Va. 2012). Such non-economic rights are clearly within the ambit of 11 U.S.C. § 541(a)(1) and as such, included in the debtor's estate. Id.

4. Unenforceability of Ipso Facto Bankruptcy Clauses.

The Bankruptcy Code disapproves of statutory and contractual provisions which are triggered by the commencement of a bankruptcy

case. Id. at 655. Forfeiture or termination of a debtor's interests is prohibited under 11 U.S.C. § 541(c), which provides, in pertinent part:

> [A]n interest of the debtor in property becomes property of the estate under subsection [11 U.S.C. §§] (a)(1), (a)(2), or (a)(5) of this section **notwithstanding** any provision in **an agreement**, transfer instrument, or **applicable nonbankruptcy law** . . . that restricts or conditions transfer of such interest by the debtor; or that is **conditioned** on the insolvency or financial condition of the debtor, **on the commencement of a case under this title**, or on the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

11 U.S.C. § 541(c)(1)(A)-(B) (emphasis added).

Similarly, 11 U.S.C. § 365(e)(1), provides:

> Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on [the insolvency of the debtor].

11 U.S.C. § 365(e)(1).

Both 11 U.S.C. § 541(c)(1) and 11 U.S.C. § 365(e)(1) invalidate or render unenforceable *ipso facto* bankruptcy clauses. Summit Inv. and Dev. Corp. v. Leroux, 69 F.3d 608, 611 (1st Cir. 1995).

RCW 25.15.130 is a nonbankruptcy law whose *ipso facto* dissociation provision is squarely within the scope of the 11 U.S.C. § 541(c) prohibition. It is unenforceable and cannot be used to divest the

Ostensons of their membership interests in Pac-O and their right to bring the derivative claim set forth in Count VIII of the Complaint.

A contract is executory if "the obligations of both parties are so unperformed that the failure of either party to complete performance would constitute a material breach and thus excuse the performance of the other." Griffel v. Murphy (In re Wegner), 839 F.2d 533, 536 (9th Cir. 1988); Unsecured Creditors' Comm. v. Southmark Corp. (In re Robert L. Helms Constr. & Dev. Co.), 139 F.3d 702, 705 (9th Cir. 1998); In re JZ L.L.C., 371 B.R. 412, 425 (BAP 9th Cir. 2007). In this regard, it does not matter whether the Pac-O Operating Agreement constitutes an executory contract or non-executory contract; Articles 8 and 9 constitute *ipso facto* provisions for dissociation of a member upon filing a voluntary petition for bankruptcy. Such provisions are unenforceable under 11 U.S.C. § 541(c)(1) and 11 U.S.C. § 365(e)(1).

The case of In re Daugherty Construction, Inc., 188 B.R. 607 (Bankr. D. Neb. 1995), appears to have been the first reported case to analyze the apparent conflict between the scope of a bankruptcy estate authorized under 11 U.S.C. § 541 and state law and agreements which divest the debtor's interests on commencement of a bankruptcy proceeding. In In re Daugherty Construction, Inc. the debtor was a member of a number of Nebraska limited liability companies. Id. at 609.

Under the Nebraska Limited Liability Companies Act, the filing of a bankruptcy case by a member dissolved a limited liability company unless remaining members voted to continue the business and the membership of the bankrupt member was terminated, the same as would occur upon the death or expulsion of a member. Upon commencing the bankruptcy, the remaining members voted to continue business and remove the President and sole shareholder of the debtor corporation as general manager of the limited liability companies pursuant to state law and the Operating Agreement. Id. at 609-610.

In rejecting the actions taken by the remaining members, the Bankruptcy Court held that the provisions of 11 U.S.C. § 541 and other pertinent provisions of the Bankruptcy Code trumped the provisions of the Nebraska Limited Liability Companies Act to the extent that they purported to terminate the debtor's membership interest, stating:

> In summary, notwithstanding provisions of the Nebraska Limited Liability Companies Act to the contrary, the membership of [debtor] in [the limited liability companies], did not terminate upon the commencement of this Chapter 11 bankruptcy case, the LLCs continued to exist and the LLC Articles and Agreements constitute an executory contract under section 365. Bankruptcy Code Sections 363(l), 365(e) and 541(c)(1) mandate this result and **state law to the contrary is unenforceable under the Supremacy Clause. U.S. CONST. art. VI, cl. 2.**

Id., at 614 (emphasis added).

Subsequent cases have followed the reasoning and conclusions of In re Daugherty Construction, Inc., in affirming the proposition that membership interests held by an individual in a limited liability company are not extinguished by state law or agreements upon commencement of a bankruptcy proceeding by that individual. In re Klingerman, 388 B.R. 677 (Bankr. E.D.N.C. 2008) (debtor's rights and interest in a limited liability company, economic and non-economic, became property of the estate upon the filing of his bankruptcy petition and he has standing to seek dissolution of the limited liability company); In re LaHood, 437 B.R. 330 (Bankr. C.D. Ill. 2010) (provisions of the Operating Agreement purporting to place limitations or restrictions on debtor's membership interest as a result of his bankruptcy filing are unenforceable); In re Warner, id. at 655 (debtor's economic and non-economic rights as member of limited liability company became part of debtor's estate upon filing for bankruptcy pursuant to 11 U.S.C. § 541).

Accordingly, under controlling Federal statutes and judicial precedent, at the time the Ostensons commenced their bankruptcy case, their 49% membership interest in Pac Organic Fruit, LLC and the Ostensons' rights under the Operating Agreements, were not relinquished but instead became property of the bankruptcy estate under 11 U.S.C. § 541(a)(1). Under 11 U.S.C. § 541(c), neither the dissociation provisions

of RCW 25.15.130 nor the dissociation provisions in the Operating Agreement can operate to divest the Ostensons of their membership interest in Pac Organic Fruit, LLC.

5. The Stipulation.

It was in this legal posture that the Ostensons, with their membership interest in Pac-O intact and part of their bankruptcy estate, entered into the Stipulation with Mr. Holzman, GHI, Total Organic and Pac-O. Under paragraph 7.b of the Stipulation, the Ostensons have the right, as members of Pac-O, to prosecute the following causes of action as derivative claims:

> Any purported claims of Pac-O (and Pac-O only) against Holzman, GHI, POP and/or Total Organic for their alleged failure to pay packing fees, expenses, and revenues earned solely by Pac-O or fruit proceeds or rent due Pac-O or for conversion of assets of Pac-O.

Ex D-5.

Because the Ostensons were not dissociated as members upon filing for bankruptcy, they continued as members of Pac-O. Under the terms of the Stipulation, approved by the Bankruptcy Court, the Ostensons were authorized, as members of Pac-O, to bring the derivative claims set forth in Count VIII of the Complaint. Ex D-5 (Order). As counsel for Mr. Holzman and GHI defendants has conceded, "the plaintiff in this suit is the bankruptcy estate of Harold and Shirley Ostenson." RP 30:12-15.

Under these circumstances, there is no question that the trial court erred in refusing to reconsider the dismissal of Count VIII. The dismissal should be reversed.

C. The Stipulation Constituted the Consent of All Members of Pac-O to Allow the Ostensons to Continue as Members.

As noted above, RCW 25.15.130 identifies events upon which a member will become dissociated from a limited liability company, which includes a member filing a voluntary petition for bankruptcy. RCW 25.15.130. However, dissociation does not occur if all individuals or entities, who were members at the time of the filing, consent. RCW 25.15.130(1)(d). This is what happened here.

The trial court erred in concluding that the Stipulation did not constitute the consent of all members of Pac-O allowing the Ostensons to retain their membership interests in Pac-O and thereby assert Count VIII. In Conclusion of Law No. 3 and Conclusion of Law No. 4 the trial court erroneously concluded that:

> 3. While the Court is of the view that the statute's [RCW 25.15.130(1)] inclusion in subparagraph (d) of the words "at the time" does not require that any "written consent" be contemporaneous with the occurrence of any particular event of dissociation (and rejects the Holzman Defendants' arguments to that effect), it also rejects the Ostensons' contention that the Stipulation itself constituted a "written consent" to the Ostensons' continuation as members of Pac O for purposes of subparagraph (d).

> 4. The Court concludes that the Stipulation simply does not address the question. Nothing about the terms of the Stipulation can be said to represent Greg Holzman, Inc.'s express or implied consent to the Ostensons' continuation as members of Pac O, or to the Ostensons' commencement of a derivative action. If anything, the language of the Stipulation suggests to the contrary when it emphasizes, at Paragraph 7.a, that the only claims excluded from the general release (as pertinent here) are "purported claims of Pac O (and Pac O only)." The Court concludes that the Stipulation does not constitute a "written consent" for purposes of RCW § 25.15.130(1)(d). The Ostensons did not argue that any other document in the record serves that purpose.

CP 2048.

The Stipulation is a blueprint for the orderly resolution of claims held, and not released by, the various parties. Ex P-5 (Stipulation). Paragraph 7.b of the Stipulation, which preserves the right of Pac-O to bring claims against Mr. Holzman, GHI and Total Organic, is a consent, signed by all other members of Pac-O (i.e., GHI), which allow the Ostensons to prosecute their derivative claim against Holzman and GHI.

In this regard, it is illustrative to consider the following exchange between Respondents' counsel and the trial court during opening statement:

> THE COURT: Under [paragraph] 7.b [of the Stipulation], ... that makes it look like claims could be asserted by Pac-O, against Mr. Holzman, POP, and Total Organic for certain things.
>
> MR. DUNCAN: Right.
>
> THE COURT: **Who would be bringing those claims, if not the Ostensons**?

> MR. DUNCAN: Well, the answer to that question is -- and I will tell you what the -- what the expectation was, when this document was entered into.
>
> First, you'll hear, from Mr. Holzman, that he agreed to this, as part of this resolution, in the bankruptcy court, **only because he didn't think there were any**. He wouldn't have done this.

RP 38:21-39:8 (emphasis added).

First, it is suggested that, the real answer to the court's query is "nobody" -- if the Stipulation is interpreted to exclude the Ostensons from Count VIII. Second, according to counsel, the only reason why Mr. Holzman signed the Stipulation was because he didn't think there were any derivative claims for the Ostensons to assert, a refrain which he reiterated during argument on the motion to dismiss, stating, "[w]hen this [Stipulation] was entered into, there was an expectation that we were never going to have to be here." RP 597:20-22. While Respondents' belief regarding existence of claims is irrelevant, it is significant in tending to confirm that they had, in fact, consented to the Ostensons' continued membership in Pac-O so as to pursue derivative claims they did not believe existed.

Furthermore, to preclude the Ostensons from prosecuting Count VIII would lead to an unreasonable result, where the claims reserved by Pac Organic Fruit, LLC are essentially unenforceable. This is not a

reasonable or just result. "When a [contractual] provision is subject to two possible constructions, one of which would make the contract unreasonable and imprudent and the other of which would make it reasonable and just, ... the latter interpretation [should be adopted]." Fisher Properties, Inc. v. Arden-Mayfair, Inc., 106 Wn.2d 826, 837, 726 P.2d 8 (1986) *citing* Dickson v. United States Fid. & Guar. Co., 77 Wn.2d 785, 790, 466 P.2d 515 (1970).

The trial court, in finding that the Stipulation did not constitute the consent of GHI allowing the Ostensons to continue as members of Pac-O, erred. The dismissal of Count VIII pursuant to CR 41(b)(3) should be reversed on this ground as well.

D. Respondents Should be Judicially Estopped from Challenging the Authority of the Ostensons to Assert Their Derivative Claim.

The doctrine of judicial estoppel should be applied to preclude the Mr. Holzman and GHI from denying the Ostensons' right to assert their derivative claim.

The equitable doctrine of judicial estoppel precludes a party from asserting one position in a court proceeding and later seeking an advantage by taking a clearly inconsistent position. Arkison v. Ethan Allen, Inc., 160 Wn.2d 535, 538, 160 P.3d 13 (2007). Three core factors guide a trial court's determination of whether to apply the doctrine: (1) whether a

party's later position is clearly inconsistent with its earlier position; (2) whether judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or the second court was misled; and (3) whether the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped. Id.

"Judicial estoppel precludes a party from gaining an advantage by taking a position inconsistent with a position the party previously took before a court [and]... is meant to prevent a party from gaining such an advantage or to maintain the integrity of judicial proceedings." DeVeny v. Hadaller, 139 Wn.App. 605, 161 P.3d 1059, 1066 (2007); Bartley-Williams v. Kendall, 134 Wn.App. 95, 98 138 P.3d 1103 (2006); In re JZ L.L.C., id. at 420 (judicial estoppel is a flexible equitable doctrine based on the estoppel of inconsistent positions in which a litigant who has obtained one advantage through the court by taking a particular position is not thereafter permitted to obtain a different and inconsistent advantage by taking a different position).

Without question, the doctrine of judicial estoppel is applicable to the facts and circumstances of this case. First, the Stipulation clearly permits the Ostensons to bring the claims they advanced in their Crossclaims and Third-Party Complaint in Chelan County Superior Court.

Ex D-5 (Stipulation). Further, the Stipulation was approved by the Bankruptcy Court in the Ostenson Bankruptcy on August 18, 2008. Ex D-5 (Order). The position taken by Respondents in Chelan County Superior Court is diametrically opposed to their position before the United States Bankruptcy Court for the Eastern District of Washington. Second, if this new position (i.e., lack of standing) were to be accepted, it would create the perception that either the Bankruptcy Court or the Superior Court was misled. Third, if not estopped, acceptance of Respondents' inconsistent position would deprive the Ostensons of the benefit of preserving their claim in the Stipulation and providing an unfair advantage to Respondents.

All three core factors for application of judicial estoppel are met and accordingly, the trial court should have precluded Mr. Holzman and GHI from challenging the right of the Ostensons to assert Count VIII.

The failure of the trial court to apply the doctrine of judicial estoppel to preclude Respondents from relying on the alleged dissociation of the Ostensons as members of Pac-O after filing their voluntary petition for bankruptcy was error and the dismissal of Count VIII should be reversed.

E. Respondents are Barred from Challenging the Ostensons' Right to Bring their Derivative Claim Under the Doctrine of Collateral Estoppel.

Collateral estoppel "means simply that when an issue of ultimate fact has once been determined by a valid and final judgment, that issue cannot again be litigated between the same parties in any future lawsuit." State v. Williams, 132 Wn.2d 248, 253-254, 937 P.2d 1052 (1997).

Collateral estoppel has four requirements: (1) the issue decided in the prior adjudication must be identical with the one presented in the second; (2) the prior adjudication must have ended in a final judgment on the merits; (3) the party against whom the plea of collateral estoppel is asserted must have been a party or in privity with a party to the prior litigation; and (4) application of the doctrine must not work an injustice. Id. at 254. The party asserting collateral estoppel bears the burden of proving all four requirements. Id. Additionally, "the issue to be precluded must have been actually litigated and necessarily determined in the prior action." Shoemaker v. City of Bremerton, 109 Wn.2d 504, 508, 745 P.2d 858 (1987) (emphasis added); Seattle-First Nat. Bank v. Kawachi, 91 Wn.2d 223, 228, 588 P.2d 725 (1978). "The question is always whether the party to be estopped had a full and fair opportunity to litigate the issue." State Farm Mut. Auto. Ins. Co. v. Avery, 114 Wash.App.299, 304, 57 P.3d 300 (2002).

All four requirements for application of collateral estoppel have been met in this case. First, by approving the Stipulation between the parties, the Bankruptcy Court necessarily decided the issue of the Ostensons' right to pursue their derivative claim, which was the exact issue being presented to the trial court. Ex D-5 (Order). Second, by the Bankruptcy Court's approval of the Stipulation and incorporation into the Ostensons' Amended Plan of Reorganization, a final decision on the merits thereof was obtained. Ex D-5 (Amendment). Third, Mr. Holzman and GHI were parties involved in the Ostenson Bankruptcy and are the parties involved in Count VIII of the Complaint. Ex D-5 (Amended Plan). Fourth, under these circumstances, application of the doctrine of collateral estoppel will preserve the rights of all parties under the Stipulation, furthering the interests of justice.

The failure of the trial court to apply the doctrine of collateral estoppel to preclude Respondents from relying on the alleged dissociation of the Ostensons as members of Pac-O after filing their voluntary petition for bankruptcy was error and the dismissal of Count VIII should be reversed.

F. Respondents are Barred from Challenging the Ostensons' Right to Bring their Derivative Claim Under the Doctrine of Res Judicata.

The doctrine of res judicata is similar to collateral estoppel, applying to claims instead of issues. The party asserting res judicata "bears the burden of proving, by competent evidence consistent with the record in the former cause, that such issue was involved and actually determined ...." Bradley v. State, 73 Wn.2d 914, 917, 442 P.2d 1009 (1968). To prove res judicata, the proponent must show "a concurrence of identity between two actions in four respects: (1) subject matter; (2) cause of action; (3) persons and parties; and (4) the quality of the persons for or against whom the claim is made." US Bank v. Hursey, 116 Wn.2d 522, 529, 806 P.2d 245 (1991); Seattle-First Nat. Bank, 91 Wn.2d 225. Res judicata should not be applied when it would work an injustice. Henderson v. Berdahl Int'l Corp., 72 Wn.2d 109, 119, 431 P.2d 961 (1967).

The doctrine of res judicata applies not only to points upon which the court was actually required by the parties to form an opinion and pronounce a judgment, but to every point which properly belonged to the subject of litigation, and which the parties, exercising reasonable diligence, might have brought forward at the time. Sayward v. Thayer, 9 Wash. 22, 24, 36 P. 966 (1894).

All four elements necessary to establish res judicata exist in this matter. First, the subject matter of the Stipulation specifically, the Ostensons right to bring their derivative claim against Holzman and GHI is identical to the challenge asserted in the instant matter. Ex D-5 (Order). Second, the cause of action is identical where the Bankruptcy Court approved the Ostensons' right to assert their derivative claim against Holzman and GHI and that approval is now being challenged by Holzman and GHI. Ex D-5 (Amendment). Third, the parties are the same, involving the Ostensons, Holzman and GHI. Ex D-5 (Amended Plan). Fourth, there is no doubt that the quality of the parties in the instant case, i.e., the Ostensons, Holzman and GHI are the same as the parties in the Ostenson Bankruptcy.

The failure of the trial court to apply the doctrine of judicial estoppel to preclude Respondents from relying on the alleged dissociation of the Ostensons as members of Pac-O after filing their voluntary petition for bankruptcy was error and the dismissal of Count VIII should be reversed.

G. Motion for Award of Attorney Fees and Costs.

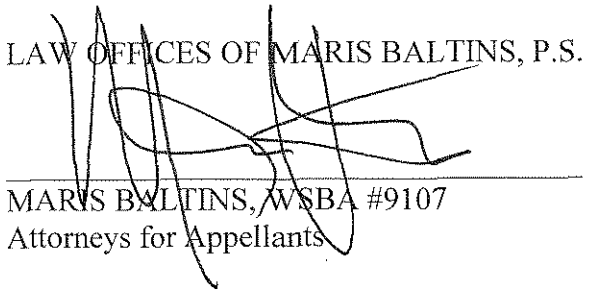
Pursuant to RAP 18.1, the Ostensons request an award to recover its attorney fees and expenses incurred in this appeal as allowed by law.

VI. CONCLUSION.

Wherefore, based upon the foregoing points and authorities, the Ostensons respectfully request that the Court of Appeals reverse the trial court's dismissal of Count VIII of the Complaint and allow the Ostensons to proceed with prosecution of their derivative claim on behalf of Pac-O.

DATED this 5th day of August, 2013.

LAW OFFICES OF MARIS BALTINS, P.S.



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Attorneys for Appellants

CERTIFICATE OF SERVICE

Seth Thompson hereby declares under penalties of perjury of the laws of the State of Washington that:

1. I am and at all times hereinafter mentioned was a citizen of the United States and a resident of the State of Washington, over the age of 18 years and not a party to this action.

2. On the 5th day of August, 2013, I caused to be served a true and correct copy of the foregoing document, by the method indicated below, upon the following party:

Bradley R. Duncan	[x] First Class Mail, Postage Prepaid
Davis Wright Tremaine LLP	[ ] Federal Express
1201 3rd Ave Ste 2200	[ ] Hand Delivery
Seattle, WA 98101-3045	[ ] Facsimile Transmission:
	[x] E-mail: bradleyduncan@dwt.com

DATED this 5th day of August, 2013.

Seth Thompson