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,

Petitioner,

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.

PETITION FOR REVIEW

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I. IDENTITY OF PETITIONER.

Harold Ostenson and Shirley Ostenson petition this Court for review of the Court of Appeals' decision terminating review designated in Section II below.

II. COURT OF APPEALS DECISION.

Mr. and Mrs. Ostenson seek review of the Decision filed by Division III of the Court of Appeals on September 4, 2014, sustaining the trial court's dismissal of Count VIII of their Amended Crossclaims and Third Party Complaint. The Decision is attached. Appendix 1-13.

III. ISSUES PRESENTED FOR REVIEW.

The Ostensons request review of the following issues:

1. Whether Appellants became dissociated as members from Pac Organic Fruit, LLC ("Pac-O") as a result of their bankruptcy filing.

2. Whether the dissociation provisions under RCW 25.15.130 or the Pac-O Limited Liability Agreement are unenforceable under the Supremacy Clause of the United States Constitution and provisions of the Bankruptcy Code, 11 U.S.C. § 541, *et seq.*

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

IV. STATEMENT OF THE CASE.

This matter involves claims brought by Mr. and Mrs. Ostenson against Greg Holzman and his company, Greg Holzman, Inc. ("GHI") stemming from the financial destruction of Pac-O in which both the Ostensons and GHI were members. CP 476-493.

The Ostensons' Crossclaims and Third Party Complaint was filed on July 25, 2009 in *Northwest Wholesale, Inc. v. Pac Organic Fruit, LLC*, et al., Chelan County Superior Court No. 07-2-00514-0. CP 4-9; 35-53.[1] The Complaint was filed pursuant to a Stipulation entered into between 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 Ostensons' Amended Plan identified unliquidated claims against Mr.

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[1] On September 28, 2009, the Ostensons filed an Amended Crossclaims and Third Party Complaint ("Complaint") CP 476-493.

[2] Ex D-5 consists of four separate documents: (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 is attached to items 1 and 2.

Holzman and GHI as assets of the bankruptcy estate. Ex D-5 (Amended Plan). The Stipulation was approved by the Bankruptcy Court on August 18, 2008. Ex D-5 (Order and Amendment). Paragraph 7.a of the Stipulation preserved claims the Ostensons might have against Pac-O. Paragraph 7.b of the Stipulation preserved claims of Pac-O against Mr. Holzman, GHI and/or Total Organic LLC. Ex D-5 (Stipulation).

The Complaint was structured to comply with the provisions of the Stipulation. Counts I – VII asserted direct claims against Pac-O pursuant to paragraph 7.a of the Stipulation. CP 484-487. Count VIII is a derivative claim brought by the Ostensons as minority members of Pac-O against Mr. Holzman, GHI and Total Organic pursuant to paragraph 7.b of the Stipulation. The derivative claim seeks recovery of assets seized from Pac-O by Mr. Holzman, GHI and Total Organic. CP 488-490.

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

Harold Ostenson and Shirley Ostenson have been fruit growers and packers in Wenatchee since 1976. RP 46:13-48:7. Mr. Ostenson first met Mr. Holzman in 1997. RP 54:1-4. Mr. Holzman was in the organic fruit brokerage business. RP 54:15-23. Mr. Holzman proposed a partnership wherein Mr. Ostenson would operate a company packing and storing organic fruit which would be sold by Mr. Holzman's company. RP 55:10-

15. 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 GHI owned 51% and was the manager. Ex P-26.

Pursuant to the Pac-O Limited Liability Operating Agreement (Pac-O Operating Agreement"), the Ostensons leased their packing house to Pac-O for a 20 year term, with monthly payments beginning at $8,200. RP 59:16-21; 60:7-9; 61:18-62:6; 62:17-24; P-26; P-27. In order to continue operations year-round, a million dollar loan was obtained in 1998 to finance improvements to the facility, including construction of four controlled atmosphere ("CA") rooms. RP 63:11-64:1-4; 66:14-67:10. The loan was personally guaranteed by the Ostensons and Mr. Holzman. TR at 67:13-15.

Under the Pac-O business model: (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 deliver the produce to the distributor; (5) GHI would remit sales proceeds less its commission to Pac-O; and (6) Pac-O would pay the growers for their produce. RP 23:19-21; 53:18-24; Ex P-1.

From 1998 to 2004, Pac-O's total income grew from $187,220.45 to $3,244,523.50. During this period the number of bins packed by Pac-O similarly increased from 491 to 24,539 and the number of growers

serviced rose from 3 to over 30. RP 73:22-73:1-16; P-28.

To accommodate this increase, in 2000 Pac-O entered into a Controlled Atmosphere Lease Agreement ("CA Lease") to lease CA rooms in a facility located in Valley Forge, Washington. Pac-O initially leased four of twelve available CA rooms. The number of CA rooms leased would increase by two every two years thereafter. When all twelve CA rooms were leased, Pac-O would have an option to purchase the facility. RP 140:3-142:2; P-29.

In 2004, GHI began experiencing cash flow problems. RP 88:11-20. 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. In August of 2004, GHI began retaining all sales proceeds and paid growers directly. RP 89:17-91:4. GHI payments to Pac-O dried up 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 became increasingly unable to sell the produce packed by Pac-O. Inventory kept increasing. By November of 2004, it was estimated that, given GHI's rate of sales, 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 when Mr. Holzman refused to sign the guarantee which the Ostensons had

signed. RP 155:16-157:24. The financial stranglehold exerted by GHI on Pac-O had a domino-like effect. 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, which in turn led to the Ostenson Bankruptcy in 2007. 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. 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.

On July 27, 2005, unbeknownst 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 satisfy the Note. These agreements to accept collateral, dated September 2, 2005, January 7, 2006 and March 31, 2006, were signed by Mr. Holzman on behalf of GHI and Pac-O. Ex P-9 at G024865-G024872.

On November 1, 2005, Mr. Holzman engineered the transfer of the

CA Lease from Pac-O to GHI, continued packing operations in a new limited liability company and never made any kind of accounting to Mr. Ostenson for packing revenue which properly belonged to Pac-O. RP 142:3-18; P-2; P-29.

Paul M. Fruci, CPA, testified as an expert in accounting matters. RP 358:24-359:4. Mr. Fruci testified that GHI records 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 was indicative of cash flow problems. RP 384:7-386:13; Ex P-7. Mr. Fruci analyzed the Note used by Mr. Holzman to seize the assets of Pac-O to GHI. Mr. Fruci's analysis found that the amounts claimed by GHI were not supportable under generally accepted accounting standards and that the Note was based upon fabricated debts. RP 388:23-407:7; Ex P-9 at G024858-G024859; Ex P-18.

The damage analysis offered by Mr. Fruci was premised upon an orderly winding down of the business operations of Pac-O. Ex P-32. In his report, Mr. Fruci 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 were 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.[3] 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 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. 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 proceeded to present their case, calling witnesses Charles Kay, Ed Suchow and Kathryn Dubsky. RP 604-829.

A rehearing was held on September 7, 2012. RP 9/7/12, 2-65, CP 2043. At the conclusion of the hearing, the trial court granted the motion

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[3] 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.

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. In its Order of Dismissal, the trial court ruled that: (1) as a result of their bankruptcy, the Ostensons were dissociated as members of Pac-O and therefore had no standing to bring the derivative action set forth in Count VIII; and (2) the defendants had not waived their motion to dismiss by presenting evidence on their behalf after the Ostensons had rested their case. CP 2043-2051; Appendix 14-22.

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. At this time, 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.

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; Appendix 23-27.

On March 12, 2013, the Ostensons filed their Notice of Appeal. CP 2405-2422. Oral arguments were held on March 18, 2014. On September 4, 2014, the Court of Appeals issued its Decision affirming the trial court's Order of Dismissal.

V. ARGUMENT IN SUPPORT OF REVIEW.

The evidence in this case demonstrates that the revenue stream of PAC-O was drained by Mr. Holzman for his own financial benefit which resulted in the Ostenson Bankruptcy. Simply stated, Mr. Holzman defrauded Mr. and Mrs. Ostenson. This is not a case of mismanagement or "a primer on how not to conduct business" as the Court of Appeals believes. Appendix 1. It was, in fact, a case of outright fraud.

The Court of Appeals' decision should be reviewed for three reasons. First, a significant question of law under the Constitution of the State of Washington or of the United States is involved. RAP 13.4(b)(2). Second, the decision of the Court of Appeals is in conflict with a decision of the Supreme Court. RAP 13.4(b)(1). Third, the petition involves an issue of substantial public interest that should be determined by the Supreme Court. RAP 13.4(b)(4).

A. Whether the Ostensons were Divested of Their Membership Interest in Pac Organic Fruit, LLC as a Result of Their Bankruptcy Involves a Significant Question of Law Under the Constitution of the State of Washington or of the United States.

Whether the provisions of RCW 25.15.130, which dissociate a member upon filing for bankruptcy, are rendered unenforceable by applicable provisions of the Bankruptcy Code as enacted pursuant to the Supremacy Clause and Bankruptcy Clause of the United States Constitution, presents a question of first impression in this State.

The Supremacy Clause provides:

> This Constitution, and the Laws of the United States ... shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby ....

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

The Bankruptcy Clause 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).

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, including "[e]very conceivable interest of the debtor, future, nonpossessory, contingent, speculative, and derivative." In re Yonikus, 996 F.2d 866, 869 (7th Cir. 1993). 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 of 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). The Bankruptcy Code disapproves of statutory and contractual provisions which are triggered by the commencement of a bankruptcy case. Id. at 655. 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).

Under 11 U.S.C. § 541(c):

> [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**, ... 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).

While RCW 25.15.370 recognizes the right of a member to bring a derivative claim on behalf of a limited liability company, the plaintiff "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 25.15.370; RCW 25.15.375(1). However, under RCW 25.15.130, a member of a limited liability company who "files a voluntary petition in bankruptcy" is dissociated and ceases to be a member. RCW 25.15.130(1)(d)(ii). RCW 25.15.130 is a nonbankruptcy law whose *ipso facto* dissociation provision is squarely within the prohibitory ambit of 11 U.S.C. § 541(c).

The case of In re Daugherty Construction, Inc., 188 B.R. 607 (Bankr. D. Neb. 1995), analyzed 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 Bankruptcy Court held that the provisions of 11 U.S.C. § 541 and other pertinent provisions of the Bankruptcy Code trumped 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).

However, the Court of Appeals rejected the reasoning of In re Daugherty Construction, Inc., and instead relied on the case of In re Garrison-Ashburn, L.C., 253 B.R. 700 (Bankr. E.D. Va. 2000) in which the Bankruptcy Court held that the bankruptcy estate only retained the rights of an assignee upon filing for bankruptcy. Id. at 708. It is submitted this conclusion does not make sense where the Bankruptcy

Court expressly acknowledged that "Section 541(a) clearly encompasses all of [the debtor's] ... interest in [the limited liability company] ..., whatever that interest may be, whether economic or non-economic.... [The debtor's] interest in [the limited liability company] ..., **both his membership interest and his non-economic rights and privileges as a member, became property of the bankruptcy estate.** Id., at 708 (emphasis added).

The conclusion in In re Garrison-Ashburn was expressly rejected in the case of In re Klingerman, 388 B.R. 677 (Bankr. E.D.N.C. 2008), noting that converting of the membership interest to that of an assignee would be a modification or termination of the interest that is rendered ineffective by § 541(c). Id. at 679; In re LaHood, 437 B.R. 330 (Bankr. C.D. Ill. 2010) (operating agreement purporting to place limitations or restrictions on debtor's membership interest as a result of bankruptcy filing is unenforceable); In re Warner, 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 under 11 U.S.C. § 541); In re First Protection, Inc., 440 B.R. 821 (BAP 9th Cir. 2010) (all of debtors' contractual rights and interest became property of the estate under 11 U.S.C. § 541(a)(1), including right to control management).

The ultimate holding of In re Garrison-Ashburn, L.C. was predicated on the finding that the operating agreement was not an executory contract and hence, the provisions of 11 U.S.C. § 365 (c) and (e) were not applicable to prevent dissociation. Id. at 709. This is not the case here.

Articles 8 and 9 of the Pac-O Operation Agreement adopt the events of dissociation set forth in RCW 25.15.130. Ex P-26, at 13. However, as discussed below, it is an executory contract and its *ipso facto* dissociation provisions cannot be enforced against the Ostensons.

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); In re JZ L.L.C., 371 B.R. 412, 425 (BAP 9th Cir. 2007).

Not only does the Pac-O Operating Agreement contain a provision regarding the obligation of the Ostensons to provide additional capital, Article 3, paragraph 3.4(b) specifically obligates Mr. Ostenson to lease the business premises to Pac-O and obtain and pay a loan against the premises for improvements which Mr. Holzman would guarantee. *See* Ex P-26, at 3-4. These obligations are definite, continuing and sufficient to satisfy the definition of an executory contract under 11 U.S.C. § 365(e). *See* In re

Allentown Ambassadors, Inc., 361 B.R. 422, 443-444 (Bankr. E.D. Pa. 2007) (operating agreement which imposed management obligations and provide additional capital if necessary was an executory contract).

The Court of Appeals, while acknowledging that these obligations could suffice to create an executory contract, completely by-passed the issue and instead, relying on the case of Finkelstein v. Securities Properties, Inc., 76 Wn.App. 733, 888 P.2d 161 (1995), applied state partnership law to the Pac-O Operating Agreement to arrive at the wrong conclusion. According to the Court of Appeals, because "partnerships are voluntary associations, and partners are not obligated to accept a substitution for their choice of partner," 11 U.S.C. § 365(e) is inapplicable to prohibit the dissociation. Appendix at 11-12. This was error. Finkelstein involved the effect of a partner's Chapter 7 bankruptcy and its effect on the standing of the bankrupt partner to bring a derivative action on behalf of limited partners. Finkelstein was based upon RCW 25.04.310(5) (since repealed), which provided that a partnership would be dissolved upon a partner's bankruptcy filing. Id. at 738. Since the partnership dissolved, 11 U.S.C. § 365 was not applicable to obligate assumption of the partnership agreement. Id. at 737-738.

A limited liability company is not a partnership. Application of Finkelstein to the instant case is error. Under Washington law, a

member's bankruptcy filing does not dissolve the limited liability company; it continues until dissolution. *Compare* RCW 25.15.130 *with* RCW 25.04.310.

The holding of the Court of Appeals, if adopted, would mean that 11 U.S.C. § 365 would **never** be applicable to the terms of a limited liability company operating agreement. This result is illogical; it is based upon non-existent law, flies in the face of precedent including In re Daugherty Construction, Inc. and In re Garrison-Ashburn, L.C. and contravenes the United States Constitution.

The Court of Appeals erred in determining this issue.

B. The Decision of the Court of Appeals is in Conflict with a Decision of the Supreme Court.

After making their motion to dismiss at the close of the Ostensons' case in chief, the trial court did not rule and Mr. Holzman and GHI elected to present their case. Under established case law, Mr. Holzman and GHI waived their motion to dismiss. In Hector v. Martin, 51 Wn.2d 707, 321 P.3d 555 (1958), the controlling case on this issue, the Washington Supreme 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 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).

To this bright-line rule, the Court of Appeals has carved out an exception, to-wit: there is no waiver where the court fails to rule or reserves its ruling and the defendant thereafter submits his evidence and the motion is subsequently granted. Appendix, at 6.

This modification draws an unwarranted dichotomy based upon the outcome of a motion to dismiss. There is no authority in existing case law to support such a modification and it is, in fact, directly contrary to the rule enunciated in Hector.

C. The Petition Involves Issues of Substantial Public Interest that Should be Determined by the Supreme Court.

It is submitted that both issues involve substantial public interest and should be reviewed by the Supreme Court pursuant to RAP 13.4(b)(4).

The issue as to whether the bankruptcy dissociation provisions of RCW 25.15.130 are preempted by 11 U.S.C. § 541 and 11 U.S.C. § 365 affects every member of a limited liability company who declares bankruptcy and thereafter seeks to file a derivative action on behalf of the limited liability company.

Similarly, the Court of Appeals' modification of the waiver rule enunciated in Hector disrupts well-settled precedent and applies to all litigants in the courts of this State.

These issues are likely reoccur, and a determination on the merits would provide guidance to lower courts. *See* State v. Blilie, 132 Wn.2d 484, 488 n.1, 939 P.2d 691 (1997); Grays Harbor Paper Co. v. Grays Harbor County, 74 Wn.2d 70, 73, 442 P.2d 967 (1968).

VI. CONCLUSION.

Wherefore, it is respectfully requested that, based upon the foregoing arguments, the Supreme Court grant the Ostensons' Petition for Review.

DATED this 6th day of October, 2014.

LAW OFFICES OF MARIS BALTINS, P.S.

MARIS BALTINS, WSBA #9107
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 6th day of October, 2014, I delivered a true and correct copy of the foregoing document and attached appendix to A2Z Legal Support Services who will make personal service upon the following party:

Daniel J. Appel
Law Offices of Dale M. Foreman, P.S.
124 N. Wenatchee Avenue, Ste. A
Wenatchee, WA 98801

3. On the 6th say of October, 2014 also served a copy of the foregoing document and attached appendix on said party by electronic mail, addressed to: daniel@daleforeman.com.

DATED this 6th day of October, 2014.

Seth Thompson

APPENDIX

NORTHWEST WHOLESALE, INC., *Plaintiff*, v. PAC ORGANIC FRUIT, LLC, *Defendant.*
HAROLD OSTENSON ET AL., *Appellants*, v. GREG HOLZMAN, INC., ET AL., *Respondents.*

No. 31491-0-III

COURT OF APPEALS OF WASHINGTON, DIVISION THREE

2014 Wash. App. LEXIS 2197

September 4, 2014, Filed

PRIOR HISTORY: [*1] Appeal from Chelan Superior Court. Docket No: 07-2-00514-0. Judge signing: Honorable Lesley a Allan. Judgment or order under review. Date filed: 02/14/2013.

COUNSEL: For Appellant(s): Maris Baltins, Law Offices of Maris Baltins, P.S., Spokane, WA.

For Respondent(s): Daniel J Appel, Attorney at Law, Wenatchee, WA.

JUDGES: Authored by George B. Fearing. Concurring: Stephen M. Brown, Laurel H. Siddoway.

OPINION BY: George B. Fearing

OPINION

¶1 FEARING, J. --

INTRODUCTION AND RULING

¶2 This case revolves around business disputes, between local orchardists Harold and Shirley Ostenson, husband and wife, and San Francisco businessman Greg Holzman, concerning the operation of a Grant County orchard packing facility. Although the Ostensons and Holzman were ostensibly partners, the parties jointly established a limited liability company, Pac Organic Fruit, LLC, (Pac Organic), through which they conducted business with one another. Greg Holzman formed additional companies to shield himself from individual liability and inserted those companies into his business relationships with the Ostensons. Greg Holzman, Inc., (GHI) was the company that became a member of Pac Organic. Both Greg Holzman and the Ostensons blame the other for the deterioration [*2] of the packing business. The Ostensons eventually filed a Chapter 11 bankruptcy petition that complicates and controls the outcome of this case. The Ostensons' story presents a primer on how not to conduct business.

¶3 Harold and Shirley Ostenson sued Pac Organic, claiming the limited liability company breached a lease for a fruit packing facility, failed to pay for orchard crops, owes them unpaid wages, undercompensated them, owes reimbursement for expenses incurred on behalf of the company, failed to distribute profits, and breached fiduciary duties. Shirley and Harold Ostenson also bring a derivative action, on behalf of Pac Organic against Greg Holzman and his companies, GHI, and Total Organic Fruit, LLC (Total Organic). The derivative action alleges Holzman and his companies mismanaged Pac Organic. This appeal concerns only the derivative action.

¶4 The trial court granted Greg Holzman's, GHI's, and Total Organic's (collectively the Holzman defendants) *CR 41(b)(3)* motion to dismiss, ruling that the Ostensons' bankruptcy dissociated them as members from Pac Organic. According to the trial court, because they were dissociated, *RCW 25.15.370* precludes the Ostensons from bringing a derivative action. The Ostensons' [*3] nonderivative claims against Pac Organic survive the trial court's ruling, but presumably are worthless because of the financial condition of Pac Organic. The trial court directed a final judgment be entered, under *CR 54(b)*, in favor of the Holzman defendants, because there was no just reason to delay entry of final judgment.

¶5 The Ostensons appeal the ruling dismissing the Holzman defendants. They argue their bankruptcy filing

did not remove them from membership in Pac Organic and does not disqualify them from asserting a derivative action on behalf of the limited liability company. They also argue that, in the bankruptcy proceeding, the Holzman defendants consented to their membership in Pac Organic and this derivative action. Finally, the Ostensons argue that the Holzman defendants are judicially and collaterally estopped and res judicata bars them from denying the Ostensons' standing to bring the derivative action. We address all of these arguments and more. We affirm the trial court's grant of the Holzman defendants' motion to dismiss, because the Ostensons' bankruptcy filing rendered them ineligible to maintain a derivative action.

FACTS

¶6 Harold Ostenson and Greg Holzman met in 1997. Holzman [*4] owned Greg Holzman, Inc., an organic brokerage business, and desired to expand into Washington State. To this end, the Ostensons and GHI formed, in June 1998, Pac Organic Fruit, LLC, a Washington limited liability company. The Ostensons owned 49 percent of Pac Organic. GHI owned the remaining 51 percent, allowing Greg Holzman, through his corporation, to control business decisions.

¶7 The Ostensons' and Holman's operating agreement for Pac Organic designated GHI as the manager of the limited liability company. The manager could be removed by a vote of all members, but remember that GHI was a member. Under the agreement, a member became dissociated upon the occurrence of any event considered a dissociation under the Washington Limited Liability Company Act. The agreement required both the Ostensons and GHI to contribute additional capital at GHI's discretion. Finally the limited liability company agreement obligated Harold Ostenson to lease a packing facility to Pac Organic, obtain a loan towards improving that facility, and pay that loan.

¶8 Shirley and Harold Ostenson were more than Pac Organic's minority owners. Harold Ostenson oversaw Pac Organic's operations. Shirley Ostenson served as [*5] Pac Organic's accountant. The Ostensons owned the packing facility in Grant County, which they leased to Pac Organic for 20 years with monthly payments beginning at $8,200.

¶9 Under Pac Organic's business model, growers delivered fruit to Pac Organic for packing and storage, and Pac Organic paid the growers for their fruit. GHI sold the fruit to distributors, and the distributors paid GHI for the produce. GHI remitted sales proceeds, less its commission, to Pac Organic, rendering Pac Organic financially vulnerable to business practices of GHI. Pac Organic conveyed the fruit to the distributor.

¶10 Pac Organic first operated only three months a year. With the goal of operating year-round, Pac Organic added packing lines and constructed four controlled atmosphere rooms. Pac Organic financed this expansion by borrowing almost one million dollars. The Ostensons and Holzman personally guaranteed the loan.

¶11 According to the Ostensons, Pac Organic steadily grew from 1998 to 2004. Growers delivering fruit to Pac Organic increased from 3 to over 30. The number of bins packed increased from 491 to 24,539. To accommodate the growth, Pac Organic leased controlled atmosphere rooms from another facility, effective [*6] May 1, 2000. Under the terms of the lease, Pac Organic initially leased 4 rooms. Pac Organic promised to increase the number of rooms leased by 2 biannually, such that Pac Organic would eventually lease all 12 of the facility's rooms. At that point, the lease provided Pac Organic the option of purchasing the facility. Total income increased from $187,220 to $3,244,523. Harold Ostenson expected Pac Organic's net profit for 2005 to exceed $324,000.

¶12 According to Harold Ostenson, GHI stopped remitting sales proceeds to Pac Organic in 2004, and instead paid growers directly. GHI's records show it owed Pac Organic more and more as 2004 progressed: $310,560 in January, $717,816 in April, and $833,272 in May. Similarly, Pac Organic's records show that GHI remitted less and less: $502,411 in July, $72,494 in August, and nothing in September. The Ostensons accuse GHI of meeting its cash flow needs at the expense of Pac Organic, by paying orchardists directly.

¶13 Greg Holzman's version of Pac Organic's decline differs from the Ostensons' testimony. According to Holzman, Pac Organic lost money every year from 1998 to 2003. Holzman maintains that he tried to work with the Ostensons to turn Pac Organic [*7] around, but Harold Ostenson was uncooperative. Harold Ostenson, according to Holzman, refused sales of stored fruit because he and buyers disagreed on pricing, which caused fruit to sit past its prime and Pac Organic to lose revenue.

¶14 Regardless of who, if anyone, was to blame, Pac Organic financially collapsed. In early January 2005, Pac Organic defaulted on its operating line of credit. The company also defaulted on its lease payments to the Ostensons. On March 8, 2005, Holzman fired the Ostensons from employment with Pac Organic. Later that year, KeyBank foreclosed on the Pac Organic packing facility and the Ostensons' orchard.

¶15 On July 27, 2005, Greg Holzman executed, as agent of Pac Organic, a demand promissory note in favor of GHI in the amount of $1,023,009.38. The Ostensons claim that the note is, at worst, fraudulent, and, at best, constituted mismanagement by Greg Holzman and GHI

of Pac Organic's affairs. Holzman maintains the promissory note Pac Organic executed in favor of GHI was legitimate and, if anything, understated the amount Pac Organic owed to GHI. As agent for Pac Organic, Holzman transferred the limited liability company's assets to GHI to satisfy the note. Holzman [*8] assigned Pac Organic's lease with the cold storage facility to GHI. The Ostensons claim Holzman, through GHI, wrongfully gutted Pac Organic of any value.

¶16 On January 9, 2007, Harold and Shirley Ostenson filed for bankruptcy protection under Chapter 11. On August 18, 2008, the bankruptcy court approved a "stipulation," which attempted to resolve claims of the Ostensons, Holzman, and affiliated entities against one another. Clerk's Papers (CP) at 2046; Ex. D-5. Under the stipulation, the Ostensons agreed to arbitrate some claims and litigate others. In relevant portion, that stipulation reads:

> 5. *Mutual Releases.* The parties shall incorporate into the Ostenson's [sic] plan of reorganization a general and mutual release of all claims not expressly addressed or treated herein.
>
> ... .
>
> 7. This Stipulation does not affect nor release the following claims:
>
> a. Any purported claims of the Ostensons against Pac Organic, including, but not limited to, claims for unpaid lease installments, wages, expense reimbursement, dividends, fruit proceeds, and/or failure to pay Keybank's [sic] line of credit, provided that the Ostensons shall not be entitled to assert those purported claims, whether derivatively or directly (including by [*9] 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 Organic] (and [Pac Organic] only) against Holzman, GHI, POP and/or Total Organic for their alleged failure to pay packing fees, expenses, and revenues earned solely by Pac Organic or fruit proceeds or rent due [Pac Organic] or for conversion of assets of [Pac Organic].
>
> c. To avoid multiple suits, any claims described in "b" above shall be asserted and pled in that litigation presently pending in the Superior Court of the State of Washington, Chelan County, case number 07-2-00514-0, captioned Northwest Wholesale, Inc., a Washington corporation, Plaintiff v. Pac Organic 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 provided the Superior Court allows the same.

CP at 2045-46.

¶17 On October 5, 2010, Greg Holzman filed, in the bankruptcy proceeding, a "Motion of Creditors Greg Holzman and Purity Organic Holdings, Inc., to Confirm Extent of Estate Property." CP at 1933. In this motion, Holzman argued for the first time that [*10] the Ostensons were no longer members of Pac Organic because *RCW 25.15.130* dissociated them from the limited liability company when they filed for bankruptcy. In opposition, the Ostensons wrote:

> Holzman and the Holzman entities, in signing the Stipulation, agreed that these claims, including the stance which Holzman and the Holzman entities now appear to be advancing, to-wit, that the Ostensons have no right to bring their derivative claims, is a matter which the parties agreed would be determined by the Chelan County Superior Court as directed by paragraph 7(c) of the Stipulation[.]

CP at 2320-21. The bankruptcy court did not rule on Greg Holzman's motion.

¶18 In October 2009, on the eve of one trial in this pending state case, Pac Organic Fruit, LLC, also filed a Chapter 11 bankruptcy petition. The bankruptcy court dismissed Pac Organic's petition on the grounds it was filed in bad faith. The bankruptcy judge ordered Pac Organic to pay reasonable attorney fees and costs of two of its creditors, Northwest Wholesale, Inc., and the Ostensons, for time spent in responding to the bankruptcy filing. GHI, on behalf of Pac Organic, appealed the award of attorney fees to the federal district court judge, who affirmed the [*11] award but remanded the award for further review of the amount. In his written ruling, the district court judge commented that the Ostensons' "cross-claims against GHI and a derivative claim on behalf of Pac Organic against GHI, Mr. Holzman, and Total Organics LLC" were "[c]onsistent with the stipulation." CP at 1926.

PROCEEDINGS

¶19 Meanwhile, back in Chelan County, Northwest Wholesale, Inc., a creditor of Pac Organic, filed this suit, in May 2007, against Pac Organic, GHI, and the Ostensons, claiming fraudulent conveyances and constructive fraudulent transfers of Pac Organic's assets to GHI. In July 2008, the Ostensons filed cross claims against Pac Organic and GHI, and a third-party complaint against Greg Holzman and Total Organic, Inc. The cross claims against Holzman, GHI, and Total Organic, are in the nature of a derivative action on behalf of Pac Organic.

¶20 On January 24, 2011, the trial court dismissed all of Northwest Wholesale's claims against GHI and Pac Organic with prejudice after those parties settled outside of court. The Ostensons' seven claims against Pac Organic and derivative claims against Holzman, GHI, and Total Organic remained.

¶21 Trial commenced in Chelan County Superior Court on July 11, 2011. [*12] After the Ostensons rested their case on July 13, Greg Holzman, GHI, and Total Organic, moved to dismiss count VIII, the derivative action claim, under *CR 41(b)(3)*. The Holzman defendants argued that the Ostensons were no longer members of Pac Organic and, thus, lacked authority to bring their derivative claim. In response, the Ostensons argued that the Holzman defendants consented, in the bankruptcy stipulation, to the Ostensons' continued membership. The trial court took the motion under advisement, because it needed time to study it. The trial court directed the Holzman defendants to proceed with their evidence in the meantime. For the rest of July 13, 2011 and July 14, these defendants called witnesses, but did not finish their testimony.

¶22 The court continued the remainder of trial to February 21, 2012, and then to May 24, 2012. At the Ostensons' request, the court again continued the remainder of trial to November 8, 2012.

¶23 In May and June 2012, the Holzman defendants filed a supplemental memoranda in support of their motion to dismiss. On July 13, the Ostensons responded with their own memorandum and a declaration from their attorney, Maris Baltins. Baltins declared Daniel O'Rourke and he represented [*13] the Ostensons through bankruptcy. Regarding the bankruptcy stipulation, Maris Baltins declared:

> 6. In addressing the outstanding disputes between the Ostensons and Holzman and his business entities, on or about April 28, 2008, the parties entered into a Stipulation under which the parties agreed, in pertinent part, as follows:
>
> ... .
>
> d. The Ostensons would be permitted to assert claims against [Pac Organic], including, but not limited to, claims for unpaid lease installments, wages, expense reimbursement, dividends, fruit proceeds and/or failure to pay a Key Bank line or credit.
>
> e. [Pac Organic] would be permitted to bring claims against Holzman, individually, GHI and/or Total Organic LLC for their alleged failure to pay packing fees, expenses and revenue earned solely by [Pac Organic] or fruit proceeds or rent due.
>
> f. [Pac Organic] would be permitted to bring claims against Holzman, individually, GHI and/or Total Organic LLC for conversion of the assets of [Pac Organic] Fruit, LLC. *See* Aff. O'Rourke, at ¶ 11.
>
> 7. With respect to the claims described in paragraphs d, e and f, the parties specifically stipulated that such actions were to be asserted and pled in Chelan County Superior Court, [*14] *Northwest Wholesale, Inc. v. Pac Organic Fruit, LLC et al.*, No. 07-2-00514, the instant matter.

CP at 1894-95.

¶24 Daniel P. O'Rourke similarly declared:

> 11. Under the terms of the Stipulation, I believe the parties agree, in pertinent part, as follows:
>
> ... .
>
> d. The Ostensons would be permitted to assert claims against [Pac Organic], including, but not limited to, claims for unpaid lease installments, wages, expense reimbursement, dividends, fruit proceeds and/or failure to pay a Keybank [sic] line of credit.
>
> e. The Ostensons would be permitted to bring derivative claims by [Pac Organic] against Greg Holzman, individually, [GHI] and/or Total Organic LLC for the alleged failure to pay packing fees, expenses and revenue earned solely by [Pac Organic] or fruit proceeds or rent due.

> f. The Ostensons would be permitted to bring derivative claims by [Pac Organic] against Greg Holzman, individually, [GHI] and/or Total Organic LLC for conversion of the assets of [Pac Organic].

CP at 1907.

¶25 In response to the Holzman defendants' renewal of the motion to dismiss, the Ostensons argued that the defendants waived their *CR 41* motion by putting on evidence, in their defense, at trial. In turn, the defendants moved to strike Maris Baltins' [*15] declaration.

¶26 The trial court heard argument on the Holzman defendants' *CR 41* motion on September 7, 2012, and granted the motion. On October 3, the court entered written findings of fact and conclusions of law, upon which we cannot improve. In its ruling, the trial court rejected the Ostensons' argument that the defendants waived their right to assert the motion to dismiss by presenting evidence at trial. The court also rejected the Ostensons' contention that the bankruptcy stipulation constituted a consent, under state law, by the Holzman defendants to the Ostensons' continuation as members of Pac Organic. The trial court concluded that, upon filing bankruptcy, the Ostensons relinquished their membership in Pac Organic and thus could not sustain a derivative action on the company's behalf.

¶27 The trial court also granted the Holzman defendants' motion to strike attorney Baltins' declaration. The Ostensons do not challenge this ruling on appeal.

¶28 On October 15, 2012, the Ostensons moved for reconsideration. For the first time, the Ostensons argued that federal bankruptcy law preempted Washington's statute on the dissociation of LLC members upon filing bankruptcy, and to the same extent preempted [*16] Pac Organic's operating agreement. In support of their motion for reconsideration, the Ostensons submitted a declaration from their bankruptcy counsel, Daniel O'Rourke: O'Rourke stated:

> 3. I have received and read a copy of the Opposition to Motion for Reconsideration ("Opposition") filed by Greg Holzman and Greg Holzman, Inc.
>
> 4. The Opposition contains the statement that the Ostensons "had emphasized to the Bankruptcy Court that all issues pertaining to dissociation were to be litigated by this Court." *See* Opposition, at 6:4-6.
>
> 5. This statement is untrue. The issue of dissociation was never presented to the Bankruptcy Court by this office.
>
> 6. The Opposition contains the further statement that "the Ostensons expressly rejected characterization of the Pac O limited liability agreement as an executory contract under Section 365 ... ." *See* Opposition, at 9:1-3.
>
> 7. This statement is untrue. The Ostensons in fact never accepted or rejected the Limited Liability Agreement of Pac Organic Fruit, LLC as an executory contract because they were not required to do so by the express terms of the plan.

CP at 2265.

¶29 On January 23, 2013, the court denied the Ostensons' motion for reconsideration.

LAW AND ANALYSIS

Waiver of Motion to Dismiss

¶30 The Ostensons first [*17] contend that the Holzman defendants waived their motion to dismiss, by presenting evidence at trial. They rely principally upon our Supreme Court's holding in *Hector v. Martin, 51 Wn.2d 707, 321 P.2d 555 (1958)*. Presumably the Ostensons seek a remand of the case for a further trial for the Holzman defendants to complete their evidence and for the Ostensons to present rebuttal evidence.

¶31 *CR 41(b)(3)*, upon which the Holzman defendants based their motion to dismiss, reads, in relevant part:

> (3) *Defendant's Motion After Plaintiff Rests.* After the plaintiff, in an action tried by the court without a jury, has completed the presentation of his evidence, the defendant, without waiving his right to offer evidence in the event the motion is not granted, may move for a dismissal on the ground that upon the facts and the law the plaintiff has shown no right to relief. ...

¶32 Washington courts 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. *Hume v. Am. Dispos-*

al Co., 124 Wn.2d 656, 666, 880 P.2d 988 (1994); *Goodman v. Bethel Sch. Dist., No. 403, 84 Wn.2d 120, 123, 524 P.2d 918 (1974)*; *Heinz v. Blagen Timber Co., 71 Wn.2d 728, 730, 431 P.2d 173 (1967)*; *Guyton v. Temple Motors, Inc., 58 Wn.2d 828, 365 P.2d 14 (1961)*; *Hector, 51 Wn.2d at 709*; *LeMaine v. Seals, 47 Wn.2d 259, 287 P.2d 305 (1955)*; *System Tank Lines, Inc. v. Dixon, 47 Wn.2d 147, 286 P.2d 704 (1955)*; *James v. Ellis, 44 Wn.2d 599, 269 P.2d 573 (1954)*; *McDonald v. Wockner, 44 Wn.2d 261, 267 P.2d 97 (1954)*; *McCormick v. Gilbertson, 41 Wn.2d 495, 250 P.2d 546 (1952)*; *Reninger v. Dep't of Corr., 79 Wn. App. 623, 640, 901 P.2d 325 (1995)*. This rule even applies to criminal cases. *State v. Thomas, 52 Wn.2d 255, 256, 324 P.2d 821 (1958)*; *State v. Eide, 2 Wn. App. 789, 790, 470 P.2d 220 (1970)*.

¶33 Our trial court did not [*18] deny the Holzman defendants' motion to dismiss at the close of plaintiffs' case, but instead reserved ruling for a later time. *Hector, 51 Wn.2d at 707*, addresses this situation. There, the court reasoned the same rule should apply when the court *fails to rule* or *reserves* its ruling and the defendant thereafter submits his evidence. *Hector, 51 Wn.2d at 709*. Therefore, the failure of the trial court to rule on a motion to dismiss before introduction of proof by a defendant, is tantamount to a denial of the motion. *Hector, 51 Wn.2d at 709-10*.

¶34 All of the Washington reported cases came before the appellate courts in the context of the defendant having lost the motion to dismiss. The question before the reviewing courts was whether the appellate court may entertain evidence presented after the plaintiff rested when determining the merits of the appeal. Such is not the context in which the Ostensons' appeal arrives before us. The Holzman defendants' motion to dismiss was granted. The Ostensons do not contend that further evidence would have changed the trial court's mind. The trial court's ruling, and our ruling as issued later, is based upon undisputed facts concerning the Ostensons' filing of bankruptcy. Waiver should not apply when the trial court reserves [*19] a motion to dismiss forwarded at the close of plaintiffs' case, but then grants the motion while defendant is presenting its case.

¶35 The principal reason behind the waiver rule is to allow both parties, on appeal, the benefit of all evidence in the case, including evidence presented by the defense, when determining if the plaintiff's evidence was sufficient to sustain a claim. *Hector, 51 Wn.2d at 710*; *Petersen v. Dep't of Labor & Indus., 40 Wn.2d 635, 641, 245 P.2d 1161 (1952)*. By putting in a defense, the defendant risks supplying any existing deficiency of evidence in plaintiff's case. *Petersen, 40 Wn.2d at 641*; *Olympia Brewing Co. v. Dep't of Labor & Indus., 34 Wn.2d 498, 208 P.2d 1181 (1949), overruled on other grounds by Windust v. Dep't of Labor & Indus., 52 Wn.2d 33, 40, 323 P.2d 241 (1958)*. When the appellate court decides whether sufficient evidence sustained plaintiffs' claims, the reviewing court may include evidence presented by the defendant, not just evidence presented by the plaintiff before denial of a motion to dismiss. *Reserve Life Ins. Co. v. W. T. Gay, 101 Ga. App. 96, 112 S.E.2d 786, 788-89 (1960)*; *Abramson v. W. T. Grant, 170 A. 815, 12 N.J. Misc. 192 (1934)*. Here we allow plaintiffs Ostensons the use of any evidence presented by the defense after the trial court reserved her ruling on the motion to dismiss. The motion to dismiss was not as much based upon the insufficiency of the evidence, but based upon a legal point that the Ostensons' bankruptcy filing terminated the Ostensons' standing to maintain a derivative action.

¶36 In short, we reject the Ostensons' contention that the [*20] trial court could not grant the Holzman defendants' motion to dismiss after defendants began presenting their evidence. Under *CR 54(b)*, any decision of the trial court that did not adjudicate all claims in the suit is subject to revision. Under this rule, the trial court would hold authority to revise and grant a motion to dismiss earlier denied. Therefore, the trial court should retain authority, during the presentation of defendants' case, to grant a pending motion to dismiss.

Derivative Action Standing

¶37 We now address the merits of the motion to dismiss. At issue is whether Harold and Shirley Ostenson have standing to assert a derivative action on behalf of the limited liability company, Pac Organic, against GHI, Greg Holzman, and Total Organic.

¶38 To bring a derivative claim on behalf of a limited liability company, the plaintiff must be a member at the time of bringing the action. *RCW 25.15.370* reads:

> A member may bring an action in the superior courts in the right of a limited liability company to recover a judgment in its favor if managers or members with authority to do so have refused to bring the action or if an effort to cause those managers or members to bring the action is not likely to succeed.

As [*21] the controlling member of Pac Organic, GHI would have authority to determine if a suit should be brought against Greg Holzman, Total Organic, and itself for mismanagement of the limited liability company. We assume that GHI would not approve a suit against itself, its owner, and related company.

¶39 *RCW 25.15.375* controls our decision and reads:

> In a derivative action, the plaintiff must be a member at the time of bringing the action and:
>
> (1) At the time of the transaction of which the plaintiff complains; or
>
> (2) The plaintiff's status as a member had devolved upon him or her by operation of law or pursuant to the terms of a limited liability company agreement from a person who was a member at the time of the transaction.

¶40 Under *RCW 25.15.130(1)(d)(ii)*, a member of a limited liability company loses his or her membership upon the filing of bankruptcy. The statute provides:

> (1) A person ceases to be a member of a limited liability company, and the person or its successor in interest attains the status of an assignee as set forth in *RCW 25.15.250(2)*, upon the occurrence of one or more of the following events:
>
> ... .
>
> (d) Unless otherwise provided in the limited liability company agreement, or with the written consent of all other members at the time, [*22] the member ... (ii) files a voluntary petition in bankruptcy ... .

¶41 Under Washington law, the Ostensons thus forfeited a right to bring a derivative action on behalf of Pac Organic when they petitioned for bankruptcy. The limited liability company agreement did not allow continued membership, but conversely ended the bankrupt petitioning as a member in the limited liability company. As an assignee, the dissociated member retains rights to share in profits, but loses any management rights. *RCW 25.15.250(2)*. We now review whether GHI consented in writing to continued membership of the Ostensons in Pac Organic.

Consent to Continued Membership

¶42 The Ostensons argue that Holzman, as GHI's owner, consented, in the bankruptcy stipulation, to their continued membership in Pac Organic. The Ostensons thus assign error to the trial court's conclusion that the stipulation does not constitute a written consent for purposes of *RCW 25.15.130(1)(d)*. To resolve the issue, we must interpret that stipulation.

¶43 Normal contract principles apply to the interpretation of stipulations. *In re Marriage of Pascale, 173 Wn. App. 836, 841, 295 P.3d 805 (2013)* (interpreting a *CR 2A* agreement). The stipulation at issue here served as a "general and mutual release of all claims not expressly addressed or treated herein." CP at 2045. [*23] But, as quoted above, paragraph 7 of the stipulation excluded from that release:

> a. Any purported claims of the Ostensons against [Pac Organic], including, but not limited to, claims for unpaid lease installments, wages, expense reimbursement, dividends, fruit proceeds, and/or failure to pay Keybank's [sic] 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 Organic] (and [Pac Organic] only) against Holzman, GHI, POP and/or Total Organic for their alleged failure to pay packing fees, expenses, and revenues earned solely by [Pac Organic] or fruit proceeds or rent due [Pac Organic] or for conversion of assets of [Pac Organic].

CP at 2046.

¶44 Paragraph 7(b) reserves claims of Pac Organic against the Holzman defendants. But the paragraph does not address whether the Ostensons can assert those claims. Although unlikely, Pac Organic itself could assert the claims.

¶45 We agree with the trial court that the bankruptcy stipulation does not address the Ostensons' continuation [*24] as members of Pac Organic. Long before the stipulation, the Ostensons' membership had been ended, because their rights ended with the bankruptcy filing, not the stipulation. The Ostensons' resurrection of membership in the limited liability company and the Ostensons' ability to file a derivative action on behalf of Pac Organic is contrary to the tenor of the stipulation and the law. If the Ostensons intended to reserve such rights, such language should have been expressly inserted in the stipulation.

¶46 The Ostensons' bankruptcy attorney, by affidavit, testified he "believe[d]" that the parties agreed in the bankruptcy stipulation that the Ostensons may bring derivative claims on behalf of Pac Organic against Greg Holzman, GHI, and Total Organic for debts owed and conversion of assets. CP at 1907. This testimony is worthless since testimony based upon "belief" is inadmissible. *Am. Linen Supply Co. v. Nursing Home Bldg. Corp., 15 Wn. App. 757, 765, 551 P.2d 1038 (1976).* The attorney provides no testimony concerning negotiations leading to the stipulation nor concerning any discussions with the Holzman defendants to the effect that the Ostensons reserved the right to bring derivative actions or that they sought continued membership in the limited liability company.

¶47 The Ostensons emphasize that the [*25] bankruptcy court judge, in a bankruptcy petition filed by Pac Organic, indicated that the Ostensons cross claims against GHI and a derivative claim on behalf of [Pac Organic] against GHI, Mr. Holzman, and Total Organics LLC were "[c]onsistent with the stipulation." CP at 1926. Nevertheless, the bankruptcy judge, when rendering the comments, addressed whether attorneys' fees should be granted parties for a bad faith filing of bankruptcy. The court did not directly address whether the Ostensons had standing to bring a derivative action or if the Holzman defendants consented to the Ostensons continued membership in the limited liability company, Pac Organic.

¶48 Since the Holzman defendants did not consent in writing to the Ostensons' continued membership in Pac Organic through the stipulation or otherwise, the Ostensons lack statutory authority and standing, under Washington law, to bring their derivative claim.

Motion for Reconsideration

¶49 Shirley and Harold Ostenson argued for the first time, in a motion for reconsideration, that federal bankruptcy law preempts Washington's dissociation statutes for LLCs and the bankruptcy law requires that they remain members with management rights in Pac Organic. The Ostensons [*26] forward this argument again on appeal. Before addressing the merits of the argument, we must decide whether the Ostensons could raise the contention for the first time on a motion for reconsideration.

¶50 "By bringing a motion for reconsideration under *CR 59*, a party may preserve an issue for appeal that is closely related to a position previously asserted and does not depend upon new facts." *River House Dev. Inc. v. Integrus Architecture, P.S., 167 Wn. App. 221, 231, 272 P.3d 289 (2012).* The law provides no guidelines for determining whether a new position is "closely related" to a previous position. We give the Ostensons the benefit of the doubt, for several reasons. Their bankruptcy law argument reasserts the underlying argument that they remained members of the limited liability company. We find no prejudice to the Holzman defendants by the late assertion of the new contention. The argument does not rely on any new facts. The trial court was free to review the bankruptcy law argument and we will review the argument on appeal.

Bankruptcy Law

¶51 This court reviews a trial court's denial of a motion for reconsideration for abuse of discretion, that is, discretion manifestly unreasonable, or exercised on untenable grounds, or for untenable reasons. *River House, 167 Wn. App. at 231.* Deferring to the trial court's discretion [*27] here, however, benefits the Holzman defendants none since the bankruptcy law argument raises a pure question of law, with no weighing of facts. A ruling based on an erroneous legal interpretation is necessarily an abuse of discretion. *Wash. State Physicians Ins. Exch. & Ass'n v. Fisons Corp., 122 Wn.2d 299, 339, 858 P.2d 1054(1993).*

¶52 Harold and Shirley Ostenson argue that either *11 U.S.C. § 541(c)(1)* or *11 U.S.C. § 365* preempts *RCW 25.15.130* from dissociating them as members of the limited liability company, Pac Organic. In resolving this question we stumble into an esoteric discussion of partnership law, limited liability company law, the nature of dissociation of a member or partner, economic and noneconomic interests in partnerships and LLCs, and executory contracts. We bounce to and from federal and state law. A key to answering the issue is distinguishing between economic and noneconomic interests in shares of a limited liability company. An economic interest is limited to sharing in any profits of the company. A noneconomic interest is voting on and managing company affairs.

¶53 Washington limited liability company statutes address the implication of a company member's filing of bankruptcy. *RCW 25.15.130(d)* declares that the member is dissociated from the company. The statute reads, in relevant part:

> (1) A person ceases to be a member of a limited [*28] liability company, and the person or its successor in interest attains the status of an assignee as set forth in *RCW 25.15.250(2)*, upon the occurrence of one or more of the following events:
>
> ... .
>
> (d) Unless otherwise provided in the limited liability company agreement, or with the written consent of all other

> members at the time, the member ... (ii) files a voluntary petition in bankruptcy; (iii) becomes the subject of an order for relief in bankruptcy proceedings.

The dissociation of one member, however, does not terminate the limited liability company. *RCW 25.15.270* lists the events that spawn a dissolution and all members must be dissociated before a dissolution. The dissociated member, having assumed the shoes of an assignee of an ownership interest, has no rights of management in the company. *RCW 25.15.250* declares:

> (1) A limited liability company interest is assignable in whole or in part except as provided in a limited liability company agreement. The assignee of a member's limited liability company interest shall have no right to participate in the management of the business and affairs of a limited liability company except:
>
> (a) Upon the approval of all of the members of the limited liability company other than the [*29] member assigning his or her limited liability company interest; or
>
> (b) As provided in a limited liability company agreement.

¶54 We now turn to federal bankruptcy law. *Section 541(c)(1)* provides:

> Except as provided in *paragraph (2)* of this subsection, an interest of the debtor in property becomes property of the estate under *subsection (a)(1)*, *(a)(2)*, or *(a)(5)* of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law--(A) that restricts or conditions transfer of such interest by the debtor; or (B) 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.

¶55 The Ostensons maintain that their interest in Pac Organic became part of their bankruptcy estate. This contention is correct, but does not end our inquiry. This appeal does not ask us to address whether the Ostensons retained some ownership interest in the assets of Pac Organic. We are asked to determine if the Ostensons retained [*30] management rights and the right to file a derivative action.

¶56 Under *11 U.S.C. § 541*, the commencement of a bankruptcy case creates an estate comprising all legal or equitable interests of the debtor in property, including any interest in a limited liability company. *In re Daugherty Constr., Inc., 188 B.R. 607, 611 (Bankr. D. Neb. 1995)*. Modifying this rule, however, is the rule that, while *§ 541(a)* provides whether an interest of the debtor is property of the estate, a debtor's property rights are defined at state law. *Butner v. United States, 440 U.S. 48, 55, 99 S. Ct. 914, 59 L. Ed. 2d 136 (1979)*; *In re Pettit, 217 F.3d 1072, 1078 (9th Cir. 2000)*. Therefore, Washington law still defines what property rights the Ostensons held upon filing bankruptcy.

¶57 The Ostensons rely on *In re Daugherty Constr., Inc., 188 B.R. 607 (Bankr. D. Neb. 1995)*, to support their contention that they retained membership and management rights in Pac Organic. There the Chapter 11 debtor, Daugherty Construction, Inc., was a member of a number of Nebraska limited liability companies formed to develop apartment complexes in Lincoln. The *Daugherty* court found that, under the Nebraska Limited Liability Companies Act, bankruptcy of a member in an LLC causes the membership to terminate, and that, if the remaining members vote to continue the business of the LLC, the bankruptcy debtor is not a member of the LLC. Such termination, under state law, included Daugherty's *noneconomic and economic interests* [*31] in the LLCs. The *Daugherty* court concluded that federal law trumped the state law, such that the debtor's management rights were not terminated. The court ruled: "the debtor's interest in the LLCs constitutes property of the bankruptcy estate and state law purporting to terminate that interest is unenforceable under *section 541(c)*." *188 B.R. at 611*.

¶58 *Daugherty* is persuasive authority whose reasoning does not apply to Washington law. Unlike the Nebraska limited liability company law at issue in *Daugherty*, Washington law does not operate to deny the debtor's bankruptcy estate both the debtor's economic and noneconomic interests in LLCs. Instead, *RCW 25.15.130* dissociates a member. If, as is the case here, result in a dissolution. *RCW 25.15.270*. The dissociated member retains his or her economic rights. *RCW 25.15.250*.

¶59 *Chapter 25.15 RCW* is similar to the Virginia limited liability company statutes at issue in *In re Garrison-Ashburn, L.C., 253 B.R. 700 (Bankr. E.D. Va. 2000)*. In *Garrison-Ashburn*, the court addressed a similar issue: whether the dissociation of a member upon filing a petition in bankruptcy is effective in light of *Sections 365(c), 365(e)* and *541(c) of the Bankruptcy Code*? Like Washington, Virginia law dissociated a member of a limited liability company upon their becoming a debtor in bankruptcy. *Va. Code § 13.1-1040.1(6)(a)*. Since a dissociated [*32] member is no longer a member of the company, he does not have any management rights under *§ 13.1-1022* and may not bind the company under *§ 13.1-1021.1*. While he retains his membership interest, he stands in the same relationship to the company as an assignee of his membership interest. The *Garrison-Ashburn* court reasoned that all the rights and privileges the debtor possessed prior to filing, including his economic and noneconomic interest in an LLC, became property of the bankruptcy estate. But, unless otherwise provided in the Bankruptcy Code, the rights and benefits were burdened with all of the duties and obligations that came with them. Thus, instead of dissociating the debtor, Virginia law operated to dissociate the bankruptcy estate itself. The court concluded, "Consequently, unless precluded by *§ 365(c)* or *(e)*, his bankruptcy estate has only the rights of an assignee." *Garrison-Ashburn, 253 B.R. at 708*.

¶60 Given the similarities between Virginia's and Washington's treatment of LLC members who file for bankruptcy, we adopt the reasoning of *Garrison-Ashburn*. By applying Washington law, we conclude that *RCW 25.15.130* dissociates a bankruptcy estate such that it retained the rights of an assignee under *RCW 25.15.250(2)*, but not membership or management rights, despite the provisions [*33] of *11 U.S.C. § 541(c)(1)*.

¶61 We now address whether another section of the bankruptcy code, *11 U.S.C. § 365* operates to the favor of the Ostensons. Under *§ 365(a)*, "the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor." *Section 365(c)* provides:

> The trustee may not assume or assign any executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--
>
> (1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and
>
> (B) such party does not consent to such assumption or assignment.

In turn, *Section 365(e)* reads:

> (1) 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 [*34] a provision in such contract or lease that is conditioned on--
>
> (A) the insolvency or financial condition of the debtor at any time before the closing of the case;
>
> (B) the commencement of a case under this title; or
>
> (C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.
>
> (2) *Paragraph (1)* of this subsection does not apply to an executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--
>
> (A)(i) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or to an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and
>
> (ii) such party does not consent to such assumption or assignment.

Section 365(c)(1) and *(e)(2)(A)* were designed to protect nondebtor third parties whose rights may be prejudiced by having a contract performed by an entity other than the one with which they originally contracted. *In re First Protection, Inc., 440 B.R. 821, 832 (B.A.P. 9th Cir. 2010)*; *C.O.P Coal Dev. Co. v. C.W. Mining Co., 422 B.R. 746, 761 (B.A.P. 10th Cir. 2010)*.

¶62 We must decide whether the Pac Organic limited liability company agreement is an executory [*35] contract, and, if so, whether applicable law excuses GHI, the other signatory to the operating agreement, from continuing to accept performance of the Ostensons under the agreement. Although the Bankruptcy Code does not define "executory contract," courts define such a contract as one on which performance is due to some extent on both sides. *In re Wegner, 839 F.2d 533, 536 (9th Cir. 1988)*. The Ninth Circuit has adopted the "Countryman Test," under which a contract is executory if the obligations of both parties are so far unperformed that the failure of either party to complete performance would constitute a material breach and thus excuse the performance of the other. *Unsecured Creditors' Comm. v. Southmark Corp., 139 F.3d 702, 705 (9th Cir. 1998)*; *Griffel v. Murphy, 839 F.2d 533, 536 (9th Cir. 1988)*; Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 MINN. L. REV. 439, 460 (1973). Factors relevant in evaluating whether a limited liability company operating agreement remains executory include whether the agreement imposes remote or hypothetical duties, requires ongoing capital contributions, and the level of managerial responsibility imposed on the debtor. *In Re Warner, 480 B.R. 641, 651 (Bankr. N.D.W. Va. 2012)*. If there are no material obligations that must be performed by the members of a limited liability company or the limited partners in a limited partnership, then the contract is not executory and is not governed by Code [*36] *§ 365. In Re Ehmann, 319 B.R. 200, 205 (Bkrtcy. D. Ariz. 2005)*.

¶63 The Ostensons again rely on *Daugherty*, which observed that under the debtor's limited liability company agreements, all members maintained a continuing obligation to participate in the management of the LLCs and to contribute capital in the event of a fiscal net loss. On these facts, the court held that the limited liability company operating agreements were executory in nature.

¶64 The Ostensons characterize the Pac Organic LLC operating agreement as an executory contract because of several provisions. The agreement requires both the Ostensons and Holzman to contribute additional capital at GHI's discretion. Harold Ostenson is obligated to lease a packing facility to Pac Organic, obtain a loan towards improving that facility, and pay that loan. GHI is to manage Pac Organic. These provisions may suffice to create an executory contract. *See, e.g., In re Allentown Ambassadors, Inc., 361 B.R. 422, 444 (Bankr. E.D. Pa. 2007)*. In the end, however, we need not decide if the operating agreement is an executory contract, because we otherwise hold that *§ 365(e)* of the bankruptcy code excuses further performance under the agreement.

¶65 If the Pac Organic LLC agreement is an executory contract for purposes of *§ 365*, the "final step in the analysis" is to evaluate the applicability [*37] of *§ 365(e)(2)*, which exempts certain executory contracts from continued performance. *In Re Tsiaoushis, 383 B.R. 616, 620 (Bankr. E.D. Va. 2007)*. Limited liability companies are relatively new statutory creations and little law addresses the question of whether a limited liability company's operating agreement is an executory contract to be further performed upon a member's filing of bankruptcy. *Tsiaoushis, 383 B.R. at 618*. "Because of the similarities between LLCs and partnerships in this area of inquiry, the cases involving partnerships also provide guidance regarding the appropriate consequences of the bankruptcy of a member or member-manager of a LLC." Sally S. Neely, *Partnerships and Partners and Limited Liability Companies and Members in Bankruptcy: Proposals for Reform, 71 AM. BANKR. L.J. 271, 317 (1997)*. Thus, we turn to a Washington decision concerning partnerships, *Finkelstein v. Sec. Properties, Inc., 76 Wn. App. 733, 888 P.2d 161 (1995)*, to decide the applicability of *§ 356(e)(2)*.

¶66 In *Finkelstein v. Security Properties, Inc.*, this court affirmed a trial court order dismissing most of Stephen Finkelstein's claims against Security Properties. The court held that, under state partnership law, which is not superseded by federal bankruptcy law, a limited partnership dissolves upon the Chapter 7 bankruptcy filing of one of the partners. Finkelstein therefore lacked standing to bring a [*38] derivative action on behalf of the limited partners. Finkelstein became a minority partner in two general partnerships. The partnerships each served as general partner for several limited partnerships. Each general partnership agreement provided that the partnership would not dissolve or terminate upon the death, incapacity, or bankruptcy of any partner. Finkelstein filed bankruptcy. Each general partnership then amended its partnership agreement to exclude Finkelstein as a partner. Finkelstein continued to receive correspondence and tax forms from Security Properties which referred to him as a partner in the two general partnerships. Finkelstein filed suit against Security Properties and the general partnerships for an accounting, breach of fiduciary duties, and a derivative action on behalf of several limited partnerships.

¶67 On appeal, the *Finkelstein* court addressed whether U.S.C. *§ 365* saved Finkelstein's membership in the partnerships. The court observed that partnership agreements are, at least in part, executory contracts, for purposes of the Bankruptcy Code. Nevertheless, under *§ 365*, the other partners are not obligated to accept an assumption of the partnership agreement. Partnerships [*39] are voluntary associations, and partners are not obligated to accept a substitution for their choice of partner. The restraint on assumability also makes the deemed rejection provision of *§ 365* inapplicable to the

partnership agreement. Therefore, *§ 365(e)*'s invalidation of ipso facto provisions does not apply, and state partnership law is not superseded. The debtor-partner's economic interest is protected by other sections of the bankruptcy code, but he no longer is entitled to membership.

¶68 Stephen Finkelstein's Chapter 11 bankruptcy petition was later converted to a Chapter 7. During bankruptcy protection, Shirley and Harold Ostenson remained under a Chapter 11 plan. We conclude, however, that the same reasoning applies to a Chapter 11 filing. The provisions of *§ 365* are applied to both Chapter 7 and Chapter 11 filings.

¶69 We conclude that *11 U.S.C. § 541* and *§ 365* did not preempt Washington law that removed the Ostensons as members in the limited liability company, Pac Organic, upon their filing bankruptcy. The trial correctly denied the Ostensons' motion for reconsideration.

Judicial Estoppel

¶70 The Ostensons contend that the trial court erred by not estopping the Holzman defendants from denying the Ostensons' authority to bring [*40] their derivative action. The Ostensons raise the related, but distinct, doctrines of judicial estoppel, collateral estoppel, and res judicata. We will address those doctrines in such order.

¶71 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. *Arkison v. Ethan Allen, Inc., 160 Wn.2d 535, 538, 160 P.3d 13 (2007)*; *Bartley-Williams v. Kendall, 134 Wn. App. 95, 98, 138 P.3d 1103 (2006)*. The doctrine seeks to preserve respect for judicial proceedings and to avoid inconsistency, duplicity, and waste of time. *Cunningham v. Reliable Concrete Pumping, Inc., 126 Wn App. 222, 225, 108 P.3d 147 (2005)*; *Johnson v. Si-Cor, Inc., 107 Wn. App. 902, 906, 28 P.3d 832 (2001)*. We review a trial court's decision to apply the equitable doctrine of judicial estoppel for abuse of discretion. *Arkison, 160 Wn.2d at 538*.

¶72 Three core factors guide a trial court's determination of whether to apply the judicial estoppel 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. *N.H. v. Me., 532 U.S. 742, 750-51, 121 S. Ct. 1808, 149 L. Ed. 2d 968 (2001)*; *Arkison, 160 Wn.2d at 538-39*. These factors are not an exhaustive formula [*41] and additional considerations may guide a court's decision. *Arkison, 160 Wn.2d at 539*.

¶73 The Ostensons claim that the Holzman defendants consented, in the bankruptcy stipulation, to the Ostensons bringing their derivative claim in Chelan County Superior Court and they now, inconsistently, claim the Ostensons lack authority to bring those claims. But, as discussed above, the Holzman defendants reserved the right of Pac Organic bringing claims, not the Ostensons filing a derivative action. Also, the Holzman defendants, in paragraph 7 of the stipulation, consented to a particular forum for resolving the Pac Organic claims, not any particular outcome. The Holzman defendants' position in this suit is not "clearly inconsistent" with the bankruptcy stipulation. The trial court did not abuse its discretion in refusing to apply the doctrine of judicial estoppel.

Collateral Estoppel

¶74 Collateral estoppel means 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, 253-54, 937 P.2d 1052 (1997)*; *Ashe v. Swenson, 397 U.S. 436, 443, 90 S. Ct. 1189, 1195, 25 L. Ed. 2d 469 (1970)*. Collateral estoppel has four requirements: (1) the issue decided in the prior adjudication must be identical with the one presented in the [*42] 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. *Williams, 132 Wn.2d at 254*. The party asserting collateral estoppel bears the burden of proving all four requirements. *Williams, 132 Wn.2d at 254*. 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)*; *Seattle-First Nat'l 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 Wn. App. 299, 304, 57 P.3d 300 (2002)*.

¶75 The Ostensons argue the bankruptcy court ruled that they had the right to pursue their derivative claim. But the bankruptcy stipulation approved a particular forum for Pac Organic to pursue claims. The bankruptcy court never adjudicated whether the Ostensons had standing to pursue a derivative action.

Res Judicata

¶76 "Res judicata, or claim preclusion, prohibits the relitigation of claims and issues that were litigated, or could have been litigated, in a prior action." *Pederson v. Potter, 103 Wn. App. 62, 67, 11 P.3d 833 (2000)*; *Lover-*

idge v. Fred Meyer, Inc., 125 Wn.2d 759, 763, 887 P.2d 898 (1995). The doctrine is designed to prevent relitigation of already determined causes and curtail multiplicity [*43] of actions and harassment in the courts. *Bordeaux v. Ingersoll Rand Co., 71 Wn.2d 392, 395, 429 P.2d 207 (1967)*. For the doctrine to apply, a prior judgment must have a concurrence of identity with a subsequent action in (1) subject matter, (2) cause of action, *and* (3) persons and parties, and (4) the quality of the persons for or against whom the claim is made. *See Rains v. State, 100 Wn.2d 660, 663, 674 P.2d 165 (1983)*.

¶77 The Ostensons and Holzman did not litigate the issue of whether *RCW 25.15.130* dissociated the Ostensons from Pac Organic in bankruptcy court. The subject matter and causes of action in the bankruptcy court were not the same.

Attorney Fees

¶78 The Ostensons requests attorney fees and costs pursuant to *RAP 18.1*. "The court rule requires more than a bald request for attorney expenses on appeal. The party seeking costs and attorney fees must provide argument and citation to authority to establish that such expenses are warranted." *Henne v. City of Yakima, 177 Wn. App. 583, 590, 313 P.3d 1188 (2013)* (citations omitted). The Ostensons ask for fees "allowed by law," but cite no authority. We deny the Ostensons an award of fees on appeal, particularly since they are the losing party on appeal.

CONCLUSION

¶79 We affirm the trial court's dismissal of Harold and Shirley Ostenson's derivative action brought on behalf of Pac Organic Fruit, LLC, against Greg Holzman, Greg Holzman, Inc., and Total Organic. [*44]

SIDDOWAY, C.J., and BROWN, J., concur.

FILED

OCT 03 2012

KIM MORRISON
CHELAN COUNTY CLERK

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON
IN AND FOR THE COUNTY OF CHELAN

NORTHWEST WHOLESALE, INC., a Washington corporation, Plaintiff, v. PAC ORGANIC 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.	No. 07-2-00514-0 FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER GRANTING MOTION TO DISMISS COUNT VIII OF OSTENSONS' AMENDED CROSSCLAIMS AND THIRD PARTY COMPLAINT

On September 7, 2012, the Court heard additional argument on the motion to dismiss submitted by the defendants Greg Holzman, Greg Holzman, Inc. (now known as Purity Organic Holdings, Inc.) and Total Organic, LLC (collectively, the "Holzman Defendants") under CR 41(b)(3) (the "Motion").

By way of background, the Holzman Defendants initially made the Motion orally on July 13, 2011, at the conclusion of the evidence submitted by the plaintiffs, Harold and Shirley Ostenson (the "Ostensons"), at trial (see Trial Transcript ("Tr. __") at pp. 580-83). After hearing argument from counsel, the Court took the matter under advisement that day (Tr. at 602-03). On July 13 and 14, the Holzman Defendants put on certain testimony in their defense case, after which the Court continued the remainder of trial to February 21, 2012. The Court

later continued trial to May 24, 2012, and thereafter, at the Ostensons' request, to November 8, 2012. On May 16, 2012, the Holzman Defendants filed a Supplemental Memorandum in Support of Motion to Dismiss Claims under CR 41(b)(3).

On May 30, 2012, following a telephonic scheduling conference with the Court, the parties filed a Notice of Hearing and Agreed Briefing Schedule, pursuant to which they thereafter submitted the following: (i) a pleading entitled Supplemental Authority in Support of Motion to Dismiss Claims under CR 41(b)(3) (by the Holzman Defendants, on June 15, 2012); (ii) a Response to Defendants' Motion to Dismiss Claims Under CR 41(b)(3) (by the Ostensons, on July 13, 2012); and (iii) a Reply in Support of Motion to Dismiss Claims under CR 41(b)(3) (by the Holzman Defendants, on August 3, 2012). On August 28, 2012, the Holzman Defendants also filed a motion to strike a declaration submitted by the Ostensons' trial counsel in support of their Response (ii above), which the Ostensons opposed by pleading filed on September 5, 2012, and as to which the Holzman Defendants filed a Reply on September 6, 2012. The foregoing shall be referred to collectively as the "CR 41(b)(3) Pleadings."

The Court heard argument from counsel on the Motion and the CR 41(b)(3) pleadings on September 7, 2012. At the conclusion of the hearing, the Court made oral findings of fact and delivered oral conclusions of law. Based upon these oral findings and conclusions, the Court granted the Holzman Defendants' Motion and dismissed Count VIII of the Ostensons' Amended Crossclaims and Third Party Complaint, which purported to assert derivative claims against the Holzman Defendants by Pac Organic Fruit, LLC ("Pac O"). As contemplated by CR 41(b)(3) and CR 52(a), the following constitute the Court's written findings of fact and conclusions of law with respect to that ruling.

Findings of Fact

1. Effective as of June 1, 1998, Harold Ostenson, Shirley Ostenson and Greg Holzman, Inc. entered into a Limited Liability Company Agreement of Pac Organic Fruit, LLC (the "LLC Agreement"). Under the LLC Agreement, the Greg Holzman, Inc. held 51% of the equity interest in Pac O and functioned as Manager, while the Ostensons together held 49% of the equity interest in Pac O. The LLC Agreement was entered into evidence at trial as the Ostensons' Exhibit No. 26 (Tr. p. 61).

2. Pac O functioned as a packing facility for organic fruit from approximately 1998 through 2005.

3. On January 9, 2007, the Ostensons commenced a bankruptcy proceeding by filing a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code in the United States District Court for the Eastern District of Washington. That proceeding was styled *In re Harold T. Ostenson and Shirley M. Ostenson*, Case No. 07-00058-FLK11 (Bankr. E.D. Wa.). Materials reflecting this filing, including the voluntary petition for relief, were admitted into evidence at trial as the Holzman Defendants' Exhibit No. 5 (Tr. p. 188).

4. On or about April 5, 2008, the Ostensons, the Holzman Defendants and Pac O entered into a document entitled "Stipulation." The Stipulation was included among the materials introduced into evidence at trial as the Holzman Defendants' Exhibit No. 5. In the Stipulation, the parties agreed to resolve their various claims against each other as set forth in the Stipulation. The Stipulation provided:

> 5. Mutual Releases. The parties shall incorporate into the Ostenson's plan of reorganization a general and mutual release of all claims not expressly addressed or treated herein.

* * * *

7. This Stipulation does not affect nor release the following claims:

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.

c. To avoid multiple suits, any claims described in "b" above shall be asserted and pled in that litigation presently pending in the Superior Court of the State of Washington, Chelan County, case number 07-2-00514-0, captioned Northwest Wholesale, Inc., a Washington corporation, Plaintiff v. Pac Organic 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 provided the Superior Court allows the same.

5. There is no language in the Stipulation which preserves the Ostensons' status as members of Pac O. The Stipulation contains no language whereby Pac O or the Holzman Defendants, as signatories to that document, consented to relieve the Ostensons from the effects of the dissociation from Pac O which resulted under RCW § 25.15.130(1)(d) when they filed for bankruptcy, or which authorized the Ostensons derivatively to assert any claims against the Holzman Defendants on Pac O's behalf.

6. The United States Bankruptcy Court for the Eastern District of Washington entered an order granting the Ostensons' motion for approval of the Stipulation on August 18, 2008. This order is included among the materials admitted into evidence at trial as Holzman Defendants' Exhibit No. 5. The terms of the Stipulation thereafter were incorporated into an

amended plan of reorganization confirmed in the Ostensons' bankruptcy case (see Tr. p. 187; Defense Exhibit No. 5).

7. On July 25, 2008, the Ostensons filed their Crossclaims and Third Party Complaint against Pac O and the Holzman Defendants in this Court. This pleading (which later was amended to incorporate certain additional allegations and a verification) includes eight causes of action. The first seven causes of action involve the Ostensons' assertion of personal claims against Pac O. The eighth and final cause of action is designated "Derivative Action – Minority Members on behalf of Pac Organic Fruit, LLC against Greg Holzman, Total Organic LLC and Greg Holzman, Inc." In this last cause of action, the Ostensons purport to assert derivatively against the Holzman Defendants claims they contend Pac O possesses against the Holzman Defendants.

Conclusions of Law

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).

2. Under RCW §25.15.130(1), "[a] person ceases to be a member of a limited liability company, and the person or its successor in interest attains the status of an assignee . . . upon the occurrence of" any of the events described in that paragraph. Under subparagraph (d), a person is dissociated if, "[u]nless otherwise provided in the limited liability company agreement, or with the written consent of all other members at the time, the member . . . (ii) files a voluntary petition in bankruptcy. . . ."

3. While the Court is of the view that the statute's 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.

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.

ORDER

After considering the Motion, the CR 41(b)(3) Pleadings, the evidence adduced at trial and the arguments of counsel, and based upon the foregoing findings of fact and conclusions of law, it is, by the Court,

ORDERED, that the Motion is granted, and Count VIII of the Ostensons' Amended Crossclaims and Third Party Claims, which purports to assert derivative claims on behalf of Pac O against Greg Holzman, Greg Holzman, Inc. and Total Organic, LLC, is hereby dismissed with prejudice as an adjudication on the merits; and it is further

ORDERED, that, because the only claims remaining in this proceeding are those asserted by the Ostensons against Pac O, and no claims remain to be asserted either against or by any of Greg Holzman, Greg Holzman, Inc. or Total Organic, LLC, there is no just reason to delay entry of final judgment as to the foregoing, and the Court, acting pursuant to CR 54(b), hereby expressly directs the entry of final judgment in favor of Greg Holzman, Greg Holzman, Inc. and Total Organic, LLC, consistent with this Order; and it is further

ORDERED, that, for the reasons articulated from the bench on September 7, 2012, the Holzman Defendants' motion to strike the Declaration of Maris Baltins is granted, and the Declaration of Maris Baltins shall be stricken to the extent it incorporates materials and testimony not previously admitted into evidence at trial.

Dated October 3, 2012

Judge Lesley A. Allan
Superior Court of Chelan County

PRESENTED BY:

Davis Wright Tremaine LLP

By /s/ Bradley R. Duncan
Bradley R. Duncan, WSBA #36436
Counsel for Defendants Greg Holzman, Greg Holzman, Inc. (now known a Purity Organic Holdings, Inc.) and Total Organic, LLC

SEEN AND ALL OBJECTIONS RESERVED;
APPROVED AS TO FORM ONLY:

Law Offices of Maris Baltins, P.S.

By: /s/ Maris Baltins
Maris Baltins, WSBA # 9107
Counsel for Harold Ostenson and Shirley Ostenson

Appendix 22

FILED

FEB 14 2013

Kim Morrison
Chelan County Clerk

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON
IN AND FOR THE COUNTY OF CHELAN

NORTHWEST WHOLESALE, INC., a Washington corporation,

Plaintiff,

v.

PAC ORGANIC 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.

No. 07-2-00514-0

ORDER DENYING OSTENSONS' MOTION FOR RECONSIDERATION

On October 15, 2012, the plaintiffs, Harold and Shirley Ostenson (the "Ostensons"), filed a Motion for Reconsideration of the relief set forth in the Findings of Fact, Conclusions of Law, and Order Granting Motion to Dismiss Count VIII of Ostensons' Amended Crossclaims and Third Party Complaint which this Court entered on October 3, 2012 (the "Dismissal Order"). After consideration of the briefing, argument of counsel and certain other materials relating to the Motion for Reconsideration, it is, for the reasons set forth in the Court's letter to counsel, dated January 23, 2012, a copy of which is attached hereto as Exhibit A,

ORDERED, that the Ostensons' Motion for Reconsideration shall be, and hereby is, DENIED, and the final judgment entered on October 3, 2012, in favor of Greg Holzman, Greg Holzman, Inc. and Total Organic on all claims against them in this proceeding shall not be modified or altered.

Dated February 14, 2013

Judge Lesley A. Allan
Superior Court of Chelan County

PRESENTED BY:

Davis Wright Tremaine LLP

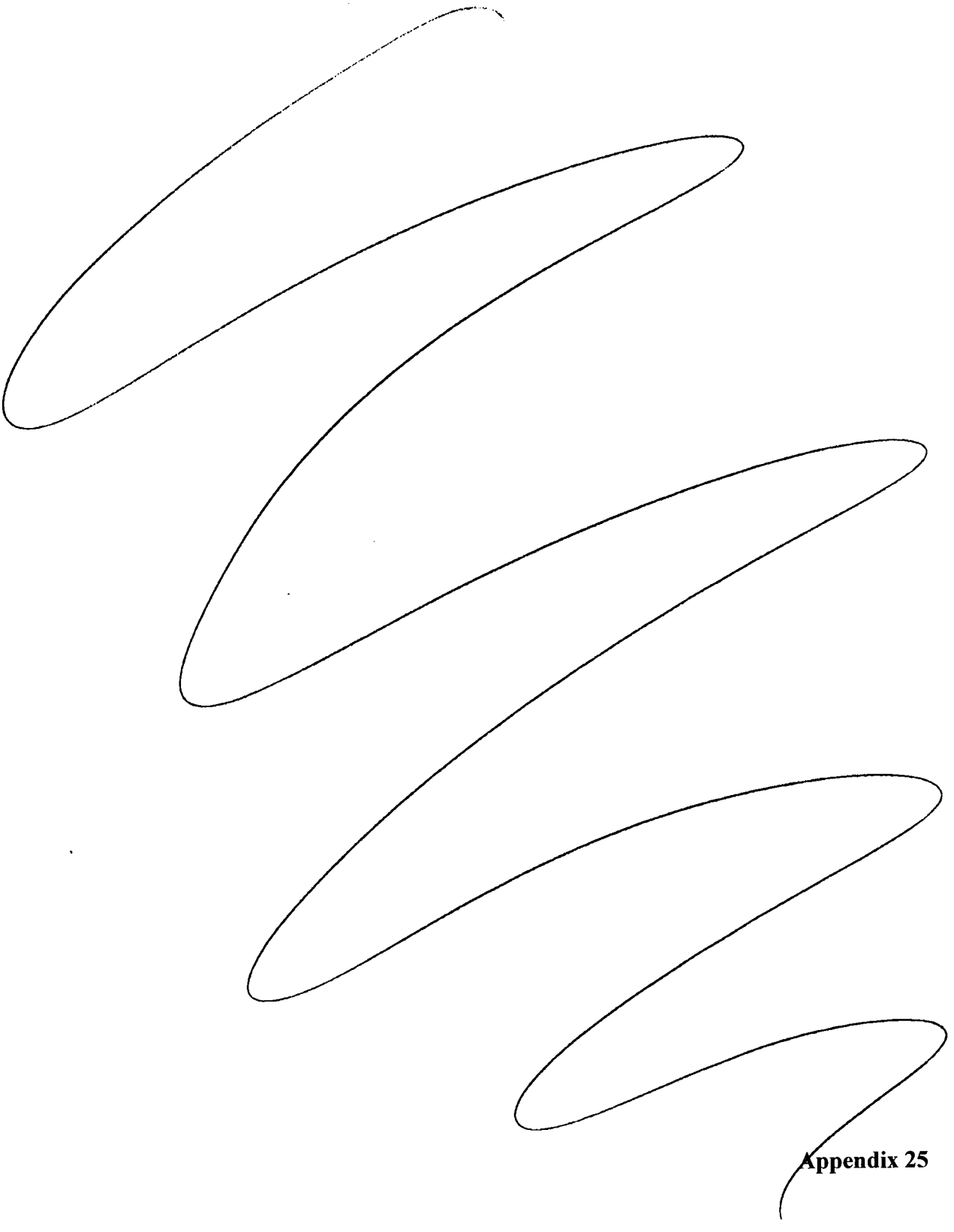
By /s/ Bradley R. Duncan
Bradley R. Duncan, WSBA #36436
Counsel for Defendants Greg Holzman, Greg Holzman, Inc. (now known a Purity Organic Holdings, Inc.) and Total Organic, LLC

SEEN AND ALL OBJECTIONS RESERVED;
APPROVED AS TO FORM ONLY:

Law Offices of Maris Baltins, P.S.

By: /s/ Maris Baltins
Maris Baltins, WSBA # 9107
Counsel for Harold Ostenson and Shirley Ostenson

Exhibit A



Superior Court of the State of Washington
For Chelan County

Lesley A. Allan, Judge
Department 1
T.W. Small, Judge
Department 2

Alicia H. Nakata, Judge
Department 3
Bart Vandegrift
Court Commissioner

401 Washington Street
P.O. Box 880
Wenatchee, Washington 98807-0880
Phone: (509) 667-6210 Fax (509) 667-6588

January 23, 2013

Ms. Maris Baltins
Baltins & Murock, PS
7 South Howard, Suite 220
Spokane, WA 99201

Mr. Bradley Duncan
Davis Wright Tremaine, LLP
2600 Century Square
1501 Fourth Avenue
Seattle, WA 98101-1688

In Re: Northwest Wholesale v. Pac Organic
Chelan County Cause No.: 07-2-00514-0

Dear Counsel:

This matter came before the court on November 8, 2012 on a motion for reconsideration filed by Harold and Shirley Ostenson. Specifically, the Ostensons ask the court to reconsider its order of October 3, 2012 dismissing count VIII of the Ostensons' cross-claim. Attorney Maris Baltins appeared for the Ostensons; attorney Bradley Duncan appeared for defendants Greg Holzman, Greg Holzman, Inc., and Total Organic, LLC.

The court has reviewed all materials submitted in connection with the motion for reconsideration, including supplemental briefing submitted in the week following argument. The court has also considered selected portions of the materials submitted for the original motion to dismiss and arguments of counsel.

Based on all information before the court, the motion for reconsideration is denied. As set forth in its written order, the court is persuaded that Washington law controls the ability of Ostensons to assert a derivative claim on behalf of Pac Organic

against defendants Holzman, *et.al.* As the court previously concluded, Ostensons became dissociated as members of Pac Organic when they filed their bankruptcy action. The Stipulation upon which Ostensons rely in an effort to resuscitate their standing to file a claim on behalf of Pac Organic does not contain the requisite written agreement to override the plain language of RCW 25.15.130 and 370. There is nothing in the motion for reconsideration which causes the court to reconsider this decision.

Mr. Duncan shall prepare and present an appropriate order. Thank you.

Sincerely,

Lesley A. Allan
Superior Court Judge

cc: Superior Court File

*** Current through PL 113-165, approved 9/19/14 ***

CONSTITUTION OF THE UNITED STATES OF AMERICA
ARTICLE VI. MISCELLANEOUS PROVISIONS

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USCS Const. Art. VI, Cl 2

Cl 2. Supreme law.

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.

NOTES:

Research Guide:

Federal Procedure:

10 Moore's Federal Practice (Matthew Bender 3d ed.), ch 54, Judgments; Costs § 54.171.

15 Moore's Federal Practice (Matthew Bender 3d ed.), ch 100, The Structure of the Federal Judicial System §§ 100.20, 100.21, 100.25.

15 Moore's Federal Practice (Matthew Bender 3d ed.), ch 101, Issues of Justiciability § 101.40.

15 Moore's Federal Practice (Matthew Bender 3d ed.), ch 103, Federal Question Jurisdiction §§ 103.20, 103.40, 103.44.

16 Moore's Federal Practice (Matthew Bender 3d ed.), ch 107, Removal § 107.14.

17A Moore's Federal Practice (Matthew Bender 3d ed.), ch 120, Dual State and Federal Judicial Structure §§ 120.10-120.12, 120.23, 120.30.

17A Moore's Federal Practice (Matthew Bender 3d ed.), ch 123, Access to Courts: Eleventh Amendment and State Sovereign Immunity §§ 123.03, 123.21, 123.40.

17A Moore's Federal Practice (Matthew Bender 3d ed.), ch 124, The Erie Doctrine and Applicable Law §§ 124.02, 124.08, 124.09, 124.40, 124.46, 124.60.

18 Moore's Federal Practice (Matthew Bender 3d ed.), ch 133, Intersystem Preclusion §§ 133.02, 133.12, 133.14.

30 Moore's Federal Practice (Matthew Bender 3d ed.), ch 810, Lawyer Communication with Person Represented by Another Lawyer § 810.03.

2 Federal Habeas Corpus Practice and Procedure (Matthew Bender), ch 32, The Determination Whether to Grant Relief: Section 2254(d) §§ 32.3, 32.5.

1 Civil Rights Actions (Matthew Bender), ch 1, Overview PP 1.12, 1.21.

1 Civil Rights Actions (Matthew Bender), ch 2, Institutional and Individual Immunity PP 2.01, 2.06, 2.12.

2 Civil Rights Actions (Matthew Bender), ch 3, The Relationship Between State and Federal Courts PP 3.06, 3.21.

*** Current through PL 113-165, approved 9/19/14 ***

CONSTITUTION OF THE UNITED STATES OF AMERICA
ARTICLE I. LEGISLATIVE DEPARTMENT

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USCS Const. Art. I, § 8, Cl 4

Sec. 8, Cl 4. Naturalization--Bankruptcy.

To establish an uniform Rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States;

HISTORY; ANCILLARY LAWS AND DIRECTIVES

Explanatory notes:
Parts of this clause are popularly known as the "Naturalization Clause" and the "Bankruptcy Clause".

NOTES:

Related Statutes & Rules:
Persons born or naturalized in United States as citizens, generally, *USCS Constitution, Amendment 14, § 1.*
Immigration and nationality, generally, *8 USCS §§ 1101* et seq.
Bankruptcy Act, *11 USCS §§ 101* et seq.

Research Guide:

Am Jur:
3A Am Jur 2d, Aliens and Citizens § 3.
3B Am Jur 2d, Aliens and Citizens § 1940.
3C Am Jur 2d, Aliens and Citizens § 2270.
9 Am Jur 2d, Bankruptcy §§ 8-11, 795, 829.
9A Am Jur 2d, Bankruptcy §§ 1401-1403, 1522.
9D Am Jur 2d, Bankruptcy § 3582.
42 Am Jur 2d, Insolvency § 7.
65 Am Jur 2d, Receivers § 95.

*** Current through PL 113-165, approved 9/19/14 ***

TITLE 11. BANKRUPTCY
CHAPTER 5. CREDITORS, THE DEBTOR, AND THE ESTATE
SUBCHAPTER III. THE ESTATE

Go to the United States Code Service Archive Directory

11 USCS § 541

THE CASE NOTES SEGMENT OF THIS DOCUMENT HAS BEEN SPLIT INTO 2 DOCUMENTS.
THIS IS PART 1.
USE THE BROWSE FEATURE TO REVIEW THE OTHER PART(S).

§ 541. Property of the estate

(a) The commencement of a case under section 301, 302, or 303 of this *title [11 USCS § 301, 302,* or *303*] creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is--

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this *title [11 USCS § 329(b), 363(n), 543, 550, 553,* or *723*].

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this *title [11 USCS § 510(c)* or *551*].

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date--

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include--

(1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;

(2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;

(3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (*20 U.S.C. 1001* et seq.; *42 U.S.C. 2751* et seq.), or any accreditation status or State licensure of the debtor as an educational institution;

(4) any interest of the debtor in liquid or gaseous hydrocarbons to the extent that--

(A) (i) the debtor has transferred or has agreed to transfer such interest pursuant to a farmout agreement or any written agreement directly related to a farmout agreement; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 544(a)(3) of this *title [11 USCS § 365* or *544(a)(3)*]; or

(B) (i) the debtor has transferred such interest pursuant to a written conveyance of a production payment to an entity that does not participate in the operation of the property from which such production payment is transferred; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 542 of this *title [11 USCS § 365* or *542*];

(5) funds placed in an education individual retirement account (as defined in *section 530(b)(1) of the Internal Revenue Code of 1986* [*26 USCS § 530(b)(1)*]) not later than 365 days before the date of the filing of the petition in a case under this title, but--

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds--

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in *section 4973(e) of the Internal Revenue Code of 1986* [*26 USCS § 4973(e)*]); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $ 6,225;

(6) funds used to purchase a tuition credit or certificate or contributed to an account in accordance with *section 529(b)(1)(A) of the Internal Revenue Code of 1986* [*26 USCS § 529(b)(1)(A)*] under a qualified State tuition program (as defined in section 529(b)(1) of such Code [*26 USCS § 529(b)(1)*]) not later than 365 days before the date of the filing of the petition in a case under this title, but--

(A) only if the designated beneficiary of the amounts paid or contributed to such tuition program was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were paid or contributed;

(B) with respect to the aggregate amount paid or contributed to such program having the same designated beneficiary, only so much of such amount as does not exceed the total contributions permitted under section 529(b)(6) of such Code [*26 USCS § 529(b)(6)*] with respect to such beneficiary, as adjusted beginning on the date of the filing of the petition in a case under this title by the annual increase or decrease (rounded to the nearest tenth of 1 percent) in the education expenditure category of the Consumer Price Index prepared by the Department of Labor; and

(C) in the case of funds paid or contributed to such program having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $ 6,225;

(7) any amount--

(A) withheld by an employer from the wages of employees for payment as contributions--

(i) to--

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 [*29 USCS §§ 1001* et seq.] or under an employee benefit plan which is a governmental plan under *section 414(d) of the Internal Revenue Code of 1986* [*26 USCS § 414(d)*];

(II) a deferred compensation plan under *section 457 of the Internal Revenue Code of 1986* [*26 USCS § 457*]; or

(III) a tax-deferred annuity under *section 403(b) of the Internal Revenue Code of 1986* [*26 USCS § 403(b)*]; except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2) [*11 USCS § 1325(b)(2)*]; or

(ii) to a health insurance plan regulated by State law whether or not subject to such title; or

(B) received by an employer from employees for payment as contributions--

(i) to--

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 [*29 USCS §§ 1001* et seq.] or under an employee benefit plan which is a governmental plan under *section 414(d) of the Internal Revenue Code of 1986* [*26 USCS § 414(d)*];

(II) a deferred compensation plan under *section 457 of the Internal Revenue Code of 1986* [*26 USCS § 457*]; or

(III) a tax-deferred annuity under *section 403(b) of the Internal Revenue Code of 1986* [*26 USCS § 403(b)*];

except that such amount under this subparagraph shall not constitute disposable income, as defined in section 1325(b)(2) [*11 USCS § 1325(b)(2)*]; or

(ii) to a health insurance plan regulated by State law whether or not subject to such title;

(8) subject to subchapter III of chapter 5 [*11 USCS §§ 541* et seq.], any interest of the debtor in property where the debtor pledged or sold tangible personal property (other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where--

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b) [*11 USCS § 108(b)*]; or

(9) any interest in cash or cash equivalents that constitute proceeds of a sale by the debtor of a money order that is made--

(A) on or after the date that is 14 days prior to the date on which the petition is filed; and

(B) under an agreement with a money order issuer that prohibits the commingling of such proceeds with property of the debtor (notwithstanding that, contrary to the agreement, the proceeds may have been commingled with property of the debtor),

unless the money order issuer had not taken action, prior to the filing of the petition, to require compliance with the prohibition.

Paragraph (4) shall not be construed to exclude from the estate any consideration the debtor retains, receives, or is entitled to receive for transferring an interest in liquid or gaseous hydrocarbons pursuant to a farmout agreement.

(c)

(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law--

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) 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.

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

(e) In determining whether any of the relationships specified in paragraph (5)(A) or (6)(A) of subsection (b) exists, a legally adopted child of an individual (and a child who is a member of an individual's household, if placed with such individual by an authorized placement agency for legal adoption by such individual), or a foster child of an individual (if such child has as the child's principal place of abode the home of the debtor and is a member of the debtor's household) shall be treated as a child of such individual by blood.

(f) Notwithstanding any other provision of this title, property that is held by a debtor that is a corporation described in *section 501(c)(3) of the Internal Revenue Code of 1986* [*26 USCS § 501(c)(3)*] and exempt from tax under section 501(a) of such Code [*26 USCS § 501(a)*] may be transferred to an entity that is not such a corporation, but only under the same conditions as would apply if the debtor had not filed a case under this title.

HISTORY:

(Nov. 6, 1978, P.L. 95-598, Title I, § 101, 92 Stat. 2594; July 10, 1984, P.L. 98-353, Title III, Subtitle C, § 363(a), Subtitle H, § 456, 98 Stat. 363, 376; Nov. 5, 1990, P.L. 101-508, Title III, Subtitle A, § 3007(a)(2), 104 Stat. 1388-28; Oct. 24, 1992, P.L. 102-486, Title XXX, Subtitle B, § 3017(b), 106 Stat. 3130; Oct. 22, 1994, P.L. 103-394, Title II, §§ 208(b), 223, 108 Stat. 4124, 4129; April 20, 2005, P.L. 109-8, Title II, Subtitle C, § 225(a), Title III, § 323, Title XII, §§ 1212, 1221(c), 1230, 119 Stat. 65, 97, 194, 196, 201; Feb. 14, 2007, *72 Fed. Reg. 7082.)*

(As amended Feb. 25, 2010, *75 Fed. Reg. 8747;* Dec. 22, 2010, P.L. 111-327, § 2(a)(22), 124 Stat. 3560; Feb. 21, 2013, *78 Fed. Reg. 12089.)*

HISTORY; ANCILLARY LAWS AND DIRECTIVES

Prior law and revision:

Legislative Statements

Section 541(a)(7) is new. The provision clarifies that any interest in property that the estate acquires after the commencement of the case is property of the estate; for example, if the estate enters into a contract, after the commencement of the case, such a contract would be property of the estate. The addition of this provision by the House amendment merely clarifies that section 541(a) is an all-embracing definition which includes charges on property, such as liens held by the debtor on property of a third party, or beneficial rights and interests that the debtor may have in property of another. However, only the debtor's interest in such property becomes property of the estate. If the debtor holds bare legal title or holds property in trust for another, only those rights which the debtor would have otherwise had emanating from such interest pass to the estate under section 541. Neither this section nor section 545 will affect various statutory provisions that give a creditor a lien that is valid both inside and outside bankruptcy against a bona fide purchaser of property from the debtor, or that creates a trust fund for the benefit of creditors meeting similar criteria. See Packers and Stockyards Act § 206, *7 U.S.C. 196* (1976).

Section 541(c)(2) follows the position taken in the House bill and rejects the position taken in the Senate amendment with respect to income limitations on a spend-thrift trust.

Section 541(d) of the House amendment is derived from section 541(e) of the Senate amendment and reiterates the general principle that where the debtor holds bare legal title without any equitable interest, that the estate acquires bare legal title without any equitable interest in the property. The purpose of section 541(d) as applied to the secondary mortgage market is identical to the purpose of section 541(e) of the Senate amendment and section 541(d) will accomplish the same result as would have been accomplished by section 541(e). Even if a mortgage seller retains for purposes of servicing legal title to mortgages or interests in mortgages sold in the secondary mortgage market, the trustee would be required by section 541(d) to turn over the mortgages or interests in mortgages to the purchaser of those mortgages.

The seller of mortgages in the secondary mortgage market will often retain the original mortgage notes and related documents and the seller will not endorse the notes to reflect the sale to the purchaser. Similarly, the purchaser will often not record the purchaser's ownership of the mortgages or interests in mortgages under State recording statutes. These facts are irrelevant and the seller's retention of the mortgage documents and the purchaser's decision not to record do not change the trustee's obligation to turn the mortgages or interests in mortgages over to the purchaser. The application of section 541(d) to secondary mortgage market transactions will not be affected by the terms of the servicing agreement between the mortgage servicer and the purchaser of the mortgages. Under section 541(d), the trustee is required to recognize the purchaser's title to the mortgages or interests in mortgages and to turn this property over to the purchaser. It makes no difference whether the servicer and the purchaser characterize their relationship as one of trust, agency, or independent contractor.

The purpose of section 541(d) as applied to the secondary mortgage market is therefore to make certain that secondary mortgage market sales as they are currently structured are not subject to challenge by bankruptcy trustees and that purchasers of mortgages will be able to obtain the mortgages or interests in mortgages which they have purchased from trustees without the trustees asserting that a sale of mortgages is a loan from the purchaser to the seller.

*** Current through PL 113-165, approved 9/19/14 ***

TITLE 11. BANKRUPTCY
CHAPTER 3. CASE ADMINISTRATION
SUBCHAPTER IV. ADMINISTRATIVE POWERS

Go to the United States Code Service Archive Directory

11 USCS § 365

THE CASE NOTES SEGMENT OF THIS DOCUMENT HAS BEEN SPLIT INTO 2 DOCUMENTS.
THIS IS PART 1.
USE THE BROWSE FEATURE TO REVIEW THE OTHER PART(S).

§ 365. Executory contracts and unexpired leases

(a) Except as provided in sections 765 and 766 of this *title [11 USCS §§ 765* and *766]* and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.

(b) (1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

(A) cures, or provides adequate assurance that the trustee will promptly cure, such default other than a default that is a breach of a provision relating to the satisfaction of any provision (other than a penalty rate or penalty provision) relating to a default arising from any failure to perform nonmonetary obligations under an unexpired lease of real property, if it is impossible for the trustee to cure such default by performing nonmonetary acts at and after the time of assumption, except that if such default arises from a failure to operate in accordance with a nonresidential real property lease, then such default shall be cured by performance at and after the time of assumption in accordance with such lease, and pecuniary losses resulting from such default shall be compensated in accordance with the provisions of this paragraph;

(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

(C) provides adequate assurance of future performance under such contract or lease.

(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to--

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title;

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement; or

(D) the satisfaction of any penalty rate or penalty provision relating to a default arising from any failure by the debtor to perform nonmonetary obligations under the executory contract or unexpired lease.

(3) For the purposes of paragraph (1) of this subsection and paragraph (2)(B) of subsection (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance--

(A) of the source of rent and other consideration due under such lease, and in the case of an assignment, that the financial condition and operating performance of the proposed assignee and its guarantors, if any, shall be similar to the financial condition and operating performance of the debtor and its guarantors, if any, as of the time the debtor became the lessee under the lease;

(B) that any percentage rent due under such lease will not decline substantially;

(C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other lease, financing agreement, or master agreement relating to such shopping center; and

(D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center.

(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.

(c) The trustee may not assume or assign any executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--

(1) (A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

(B) such party does not consent to such assumption or assignment; or

(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor; or

(3) such lease is of nonresidential real property and has been terminated under applicable nonbankruptcy law prior to the order for relief.

(d) (1) In a case under chapter 7 of this *title [11 USCS §§ 701* et seq.], if the trustee does not assume or reject an executory contract or unexpired lease of residential real property or of personal property of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected.

(2) In a case under chapter 9, 11, 12, or 13 of this *title [11 USCS §§ 901* et seq., *1101* et seq., *1201* et seq., or *1301* et seq.], the trustee may assume or reject an executory contract or unexpired lease of residential real property or of personal property of the debtor at any time before the confirmation of a plan but the court, on the request of any party to such contract or lease, may order the trustee to determine within a specified period of time whether to assume or reject such contract or lease.

(3) The trustee shall timely perform all the obligations of the debtor, except those specified in section 365(b)(2) [*11 USCS § 365(b)(2)*] [subsec. (b)(2) of this section], arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this *title [11 USCS § 503(b)(1)*]. The court may extend, for cause, the time for performance of any such obligation that arises within 60 days after the date of the order for relief, but the time for performance shall not be extended beyond such 60-day period. This subsection shall not be deemed to affect the trustee's obligations under the provisions of subsection (b) or (f) of this section. Acceptance of any such performance does not constitute waiver or relinquishment of the lessor's rights under such lease or under this title.

(4) (A) Subject to subparagraph (B), an unexpired lease of nonresidential real property under which the debtor is the lessee shall be deemed rejected, and the trustee shall immediately surrender that nonresidential real property to the lessor, if the trustee does not assume or reject the unexpired lease by the earlier of--

(i) the date that is 120 days after the date of the order for relief; or

(ii) the date of the entry of an order confirming a plan.

(B) (i) The court may extend the period determined under subparagraph (A), prior to the expiration of the 120-day period, for 90 days on the motion of the trustee or lessor for cause.

(ii) If the court grants an extension under clause (i), the court may grant a subsequent extension only upon prior written consent of the lessor in each instance.

(5) The trustee shall timely perform all of the obligations of the debtor, except those specified in section 365(b)(2) [*11 USCS § 365(b)(2)*], first arising from or after 60 days after the order for relief in a case under chapter 11 of this *title [11 USCS §§ 1101* et seq.] under an unexpired lease of personal property (other than personal property leased to an in-

dividual primarily for personal, family, or household purposes), until such lease is assumed or rejected notwithstanding section 503(b)(1) of this *title [11 USCS § 503(b)(1)]*, unless the court, after notice and a hearing and based on the equities of the case, orders otherwise with respect to the obligations or timely performance thereof. This subsection shall not be deemed to affect the trustee's obligations under the provisions of subsection (b) or (f). Acceptance of any such performance does not constitute waiver or relinquishment of the lessor's rights under such lease or under this title.

(e) (1) 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--

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title; or

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

(2) Paragraph (1) of this subsection does not apply to an executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--

(A) (i) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or to an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

(ii) such party does not consent to such assumption or assignment; or

(B) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor.

(f) (1) Except as provided in subsections (b) and (c) of this section, notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law, that prohibits, restricts, or conditions the assignment of such contract or lease, the trustee may assign such contract or lease under paragraph (2) of this subsection.

(2) The trustee may assign an executory contract or unexpired lease of the debtor only if--

(A) the trustee assumes such contract or lease in accordance with the provisions of this section; and

(B) adequate assurance of future performance by the assignee of such contract or lease is provided, whether or not there has been a default in such contract or lease.

(3) Notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law that terminates or modifies, or permits a party other than the debtor to terminate or modify, such contract or lease or a right or obligation under such contract or lease on account of an assignment of such contract or lease, such contract, lease, right, or obligation may not be terminated or modified under such provision because of the assumption or assignment of such contract or lease by the trustee.

(g) Except as provided in subsections (h)(2) and (i)(2) of this section, the rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease--

(1) if such contract or lease has not been assumed under this section or under a plan confirmed under chapter 9, 11, 12, or 13 of this *title [11 USCS §§ 901* et seq., *1101* et seq., *1201* et seq., or *1301* et seq.], immediately before the date of the filing of the petition; or

(2) if such contract or lease has been assumed under this section or under a plan confirmed under chapter 9, 11, 12, or 13 of this *title [11 USCS §§ 901* et seq., *1101* et seq., *1201* et seq., or *1301* et seq.]--

(A) if before such rejection the case has not been converted under section 1112, 1208, or 1307 of this *title [11 USCS § 1112, 1208*, or *1307*], at the time of such rejection; or

(B) if before such rejection the case has been converted under section 1112, 1208, or 1307 of this *title [11 USCS § 1112, 1208*, or *1307*]--

(i) immediately before the date of such conversion, if such contract or lease was assumed before such conversion; or

(ii) at the time of such rejection, if such contract or lease was assumed after such conversion.

(h) (1) (A) If the trustee rejects an unexpired lease of real property under which the debtor is the lessor and--

(i) if the rejection by the trustee amounts to such a breach as would entitle the lessee to treat such lease as terminated by virtue of its terms, applicable nonbankruptcy law, or any agreement made by the lessee, then the lessee under such lease may treat such lease as terminated by the rejection; or

(ii) if the term of such lease has commenced, the lessee may retain its rights under such lease (including rights such as those relating to the amount and timing of payment of rent and other amounts payable by the lessee and any right of use, possession, quiet enjoyment, subletting, assignment, or hypothecation) that are in or appurtenant to the real property for the balance of the term of such lease and for any renewal or extension of such rights to the extent that such rights are enforceable under applicable nonbankruptcy law.

(B) If the lessee retains its rights under subparagraph (A)(ii), the lessee may offset against the rent reserved under such lease for the balance of the term after the date of the rejection of such lease and for the term of any renewal or extension of such lease, the value of any damage caused by the nonperformance after the date of such rejection, of any obligation of the debtor under such lease, but the lessee shall not have any other right against the estate or the debtor on account of any damage occurring after such date caused by such nonperformance.

(C) The rejection of a lease of real property in a shopping center with respect to which the lessee elects to retain its rights under subparagraph (A)(ii) does not affect the enforceability under applicable nonbankruptcy law of any provision in the lease pertaining to radius, location, use, exclusivity, or tenant mix or balance.

(D) In this paragraph, "lessee" includes any successor, assign, or mortgagee permitted under the terms of such lease.

(2) (A) If the trustee rejects a timeshare interest under a timeshare plan under which the debtor is the timeshare interest seller and--

(i) if the rejection amounts to such a breach as would entitle the timeshare interest purchaser to treat the timeshare plan as terminated under its terms, applicable nonbankruptcy law, or any agreement made by timeshare interest purchaser, the timeshare interest purchaser under the timeshare plan may treat the timeshare plan as terminated by such rejection; or

(ii) if the term of such timeshare interest has commenced, then the timeshare interest purchaser may retain its rights in such timeshare interest for the balance of such term and for any term of renewal or extension of such timeshare interest to the extent that such rights are enforceable under applicable nonbankruptcy law.

(B) If the timeshare interest purchaser retains its rights under subparagraph (A), such timeshare interest purchaser may offset against the moneys due for such timeshare interest for the balance of the term after the date of the rejection of such timeshare interest, and the term of any renewal or extension of such timeshare interest, the value of any damage caused by the nonperformance after the date of such rejection, of any obligation of the debtor under such timeshare plan, but the timeshare interest purchaser shall not have any right against the estate or the debtor on account of any damage occurring after such date caused by such nonperformance.

(i) (1) If the trustee rejects an executory contract of the debtor for the sale of real property or for the sale of a timeshare interest under a timeshare plan, under which the purchaser is in possession, such purchaser may treat such contract as terminated, or, in the alternative, may remain in possession of such real property or timeshare interest.

(2) If such purchaser remains in possession--

(A) such purchaser shall continue to make all payments due under such contract, but may, offset against such payments any damages occurring after the date of the rejection of such contract caused by the nonperformance of any obligation of the debtor after such date, but such purchaser does not have any rights against the estate on account of any damages arising after such date from such rejection, other than such offset; and

(B) the trustee shall deliver title to such purchaser in accordance with the provisions of such contract, but is relieved of all other obligations to perform under such contract.

(j) A purchaser that treats an executory contract as terminated under subsection (i) of this section, or a party whose executory contract to purchase real property from the debtor is rejected and under which such party is not in possession, has a lien on the interest of the debtor in such property for the recovery of any portion of the purchase price that such purchaser or party has paid.

(k) Assignment by the trustee to an entity of a contract or lease assumed under this section relieves the trustee and the estate from any liability for any breach of such contract or lease occurring after such assignment.

(l) If an unexpired lease under which the debtor is the lessee is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the debtor's obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.

(m) For purposes of this section 365 [*11 USCS § 365*] and *sections 541(b)(2)* and *362(b)(10)* [*11 USCS §§ 541(b)(2)* and *362(b)(10)*], leases of real property shall include any rental agreement to use real property.

(n) (1) If the trustee rejects an executory contract under which the debtor is a licensor of a right to intellectual property, the licensee under such contract may elect--

(A) to treat such contract as terminated by such rejection if such rejection by the trustee amounts to such a breach as would entitle the licensee to treat such contract as terminated by virtue of its own terms, applicable nonbankruptcy law, or an agreement made by the licensee with another entity; or

(B) to retain its rights (including a right to [to] enforce any exclusivity provision of such contract, but excluding any other right under applicable nonbankruptcy law to specific performance of such contract) under such contract and under any agreement supplementary to such contract, to such intellectual property (including any embodiment of such intellectual property to the extent protected by applicable nonbankruptcy law), as such rights existed immediately before the case commenced, for--

(i) the duration of such contract; and

(ii) any period for which such contract may be extended by the licensee as of right under applicable nonbankruptcy law.

(2) If the licensee elects to retain its rights, as described in paragraph (1)(B) of this subsection, under such contract--

(A) the trustee shall allow the licensee to exercise such rights;

(B) the licensee shall make all royalty payments due under such contract for the duration of such contract and for any period described in paragraph (1)(B) of this subsection for which the licensee extends such contract; and

(C) the licensee shall be deemed to waive--

(i) any right of setoff it may have with respect to such contract under this title or applicable nonbankruptcy law; and

(ii) any claim allowable under section 503(b) of this *title [11 USCS § 503(b)]* arising from the performance of such contract.

(3) If the licensee elects to retain its rights, as described in paragraph (1)(B) of this subsection, then on the written request of the licensee the trustee shall--

(A) to the extent provided in such contract, or any agreement supplementary to such contract, provide to the licensee any intellectual property (including such embodiment) held by the trustee; and

(B) not interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such embodiment) including any right to obtain such intellectual property (or such embodiment) from another entity.

(4) Unless and until the trustee rejects such contract, on the written request of the licensee the trustee shall--

(A) to the extent provided in such contract or any agreement supplementary to such contract--

(i) perform such contract; or

(ii) provide to the licensee such intellectual property (including any embodiment of such intellectual property to the extent protected by applicable nonbankruptcy law) held by the trustee; and

(B) not interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such embodiment), including any right to obtain such intellectual property (or such embodiment) from another entity.

(o) In a case under chapter 11 of this *title [11 USCS §§ 1101* et seq.], the trustee shall be deemed to have assumed (consistent with the debtor's other obligations under section 507 [*11 USCS § 507*]), and shall immediately cure any deficit under, any commitment by the debtor to a Federal depository institutions regulatory agency (or predecessor to such agency) to maintain the capital of an insured depository institution, and any claim for a subsequent breach of the obligations thereunder shall be entitled to priority under section 507 [*11 USCS § 507*]. This subsection shall not extend any commitment that would otherwise be terminated by any act of such an agency.

(p) (1) If a lease of personal property is rejected or not timely assumed by the trustee under subsection (d), the leased property is no longer property of the estate and the stay under section 362(a) [*11 USCS § 362(a)*] is automatically terminated.

(2) (A) If the debtor in a case under chapter 7 [*11 USCS §§ 701* et seq.] is an individual, the debtor may notify the creditor in writing that the debtor desires to assume the lease. Upon being so notified, the creditor may, at its option, notify the debtor that it is willing to have the lease assumed by the debtor and may condition such assumption on cure of any outstanding default on terms set by the contract.

(B) If, not later than 30 days after notice is provided under subparagraph (A), the debtor notifies the lessor in writing that the lease is assumed, the liability under the lease will be assumed by the debtor and not by the estate.

(C) The stay under section 362 [*11 USCS § 362*] and the injunction under section 524(a)(2) [*11 USCS § 524(a)(2)*] shall not be violated by notification of the debtor and negotiation of cure under this subsection.

(3) In a case under chapter 11 [*11 USCS §§ 1101* et seq.] in which the debtor is an individual and in a case under chapter 13 [*11 USCS §§ 1301* et seq.], if the debtor is the lessee with respect to personal property and the lease is not assumed in the plan confirmed by the court, the lease is deemed rejected as of the conclusion of the hearing on confirmation. If the lease is rejected, the stay under section 362 [*11 USCS § 362*] and any stay under section 1301 [*11 USCS § 1301*] is automatically terminated with respect to the property subject to the lease.

HISTORY:

(Nov. 6, 1978, P.L. 95-598, Title I, § 101, 92 Stat. 2574; July 10, 1984, P.L. 98-353, Title III, Subtitle C, § 362, Subtitle G, §§ 402-404, 98 Stat. 361, 367; Oct. 27, 1986, P.L. 99-554, Title II, Subtitle B, §§ 257(j), (m), 283(e), 100 Stat. 3115, 3117; Oct. 18, 1988, P.L. 100-506, § 1(b), 102 Stat. 2538; Nov. 29, 1990, P.L. 101-647, Title XXV, Subtitle B, § 2522(c), 104 Stat. 4866; Sept. 3, 1992, P.L. 102-365, § 19(b)-(e), 106 Stat. 983; Oct. 22, 1994, P.L. 103-394, Title II, §§ 205(a), 219(a), (b), Title V, § 501(d)(10), 108 Stat. 4122, 4128, 4145; Oct. 31, 1994, P.L. 103-429, § 1, 108 Stat. 4377; April 20, 2005, P.L. 109-8, Title III, §§ 309(b), 328(a), Title IV, Subtitle A, § 404, 119 Stat. 82, 100, 104.)

HISTORY; ANCILLARY LAWS AND DIRECTIVES

Prior law and revision:

Legislative Statements

Section 365(b)(3) represents a compromise between H.R. 8200 as passed by the House and the Senate amendment. The provision adopts standards contained in section 365(b)(5) of the Senate amendment to define adequate assurance of future performance of a lease of real property in a shopping center.

Section 365(b)(4) of the House amendment indicates that after default the trustee may not require a lessor to supply services or materials without assumption unless the lessor is compensated as provided in the lease.

Section 365(c)(2) and (3) likewise represent a compromise between H.R. 8200 as passed by the House and the Senate amendment. Section 365(c)(2) is derived from section 365(b)(4) of the Senate amendment but does not apply to a contract to deliver equipment as provided in the Senate amendment. As contained in the House amendment, the provision prohibits a trustee or debtor in possession from assuming or assigning an executory contract of the debtor to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or the issuance of a security of the debtor.

Section 365(e) is a refinement of comparable provisions contained in the House bill and Senate amendment. Sections 365(e)(1) and (2)(A) restate section 365(e) of H.R. 8200 as passed by the House. Sections 365(e)(2)(B) expands the section to permit termination of an executory contract or unexpired lease of the debtor if such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or for the issuance of a security of the debtor. Characterization of contracts to make a loan, or extend other debt financing or financial accommodations, is limited to the extension of cash or a line of credit and is not intended to embrace ordinary leases or contracts to provide goods or services with payments to be made over time.

Section 365(f) is derived from H.R. 8200 as passed by the House. Deletion of language in section 365(f)(3) of the Senate amendment is done as a matter of style. Restrictions with respect to assignment of an executory contract or unexpired lease are superfluous since the debtor may assign an executory contract or unexpired lease of the debtor only if such contract is first assumed under section 364(f)(2)(A) of the House amendment.

Section 363(h) of the House amendment represents a modification of section 365(h) of the Senate amendment. The House amendment makes clear that in the case of a bankrupt lessor, a lessee may remain in possession for the balance of the term of a lease and any renewal or extension of the term only to the extent that such renewal or extension may be obtained by the lessee without the permission of the landlord or some third party under applicable non-bankruptcy law.

Senate Report No. 95-989

Subsection (a) of this section authorizes the trustee, subject to the court's approval, to assume or reject an executory contract or unexpired lease. Though there is no precise definition of what contracts are executory, it generally includes contracts on which performance remains due to some extent on both sides. A note is not usually an executory contract if

*** Statutes current through 2013 3rd special session ***

TITLE 25. PARTNERSHIPS
CHAPTER 25.15. LIMITED LIABILITY COMPANIES
ARTICLE 3. MEMBERS

GO TO REVISED CODE OF WASHINGTON ARCHIVE DIRECTORY

Rev. Code Wash. (ARCW) § 25.15.130 (2013)

§ 25.15.130. Events of dissociation

(1) A person ceases to be a member of a limited liability company, and the person or its successor in interest attains the status of an assignee as set forth in *RCW 25.15.250(2)*, upon the occurrence of one or more of the following events:

(a) The member dies or withdraws by voluntary act from the limited liability company as provided in subsection (3) of this section;

(b) The member ceases to be a member as provided in *RCW 25.15.250(2)(b)* following an assignment of all the member's limited liability company interest;

(c) The member is removed as a member in accordance with the limited liability company agreement;

(d) Unless otherwise provided in the limited liability company agreement, or with the written consent of all other members at the time, the member (i) makes a general assignment for the benefit of creditors; (ii) files a voluntary petition in bankruptcy; (iii) becomes the subject of an order for relief in bankruptcy proceedings; (iv) files a petition or answer seeking for himself or herself any reorganization, arrangement, composition, readjustment, liquidation, dissolution, or similar relief under any statute, law, or regulation; (v) files an answer or other pleading admitting or failing to contest the material allegations of a petition filed against him or her in any proceeding of the nature described in (d) (i) through (iv) of this subsection; or (vi) seeks, consents to, or acquiesces in the appointment of a trustee, receiver, or liquidator of the member or of all or any substantial part of the member's properties;

(e) Unless otherwise provided in the limited liability company agreement, or with the consent of all other members at the time, one hundred twenty days after the commencement of any proceeding against the member seeking reorganization, arrangement, composition, readjustment, liquidation, dissolution, or similar relief under any statute, law, or regulation, the proceeding has not been dismissed, or if within ninety days after the appointment without his or her consent or acquiescence of a trustee, receiver, or liquidator of the member or of all or any substantial part of the member's properties, the appointment is not vacated or stayed, or within ninety days after the expiration of any stay, the appointment is not vacated;

(f) Unless otherwise provided in the limited liability company agreement, or with written consent of all other members at the time, in the case of a member who is an individual, the entry of an order by a court of competent jurisdiction adjudicating the member incapacitated, as used and defined under chapter 11.88 RCW, as to his or her estate;

(g) Unless otherwise provided in the limited liability company agreement, or with written consent of all other members at the time, in the case of a member that is another limited liability company, the dissolution and commencement of winding up of such limited liability company;

(h) Unless otherwise provided in the limited liability company agreement, or with written consent of all other members at the time, in the case of a member that is a corporation, the filing of articles of dissolution or the equivalent for the corporation or the administrative dissolution of the corporation and the lapse of any period authorized for application for reinstatement; or

(i) Unless otherwise provided in the limited liability company agreement, or with written consent of all other members at the time, in the case of a member that is a limited partnership, the dissolution and commencement of winding up of such limited partnership.

(2) The limited liability company agreement may provide for other events the occurrence of which result in a person ceasing to be a member of the limited liability company.

(3) A member may withdraw from a limited liability company at the time or upon the happening of events specified in and in accordance with the limited liability company agreement. If the limited liability company agreement does not specify the time or the events upon the happening of which a member may withdraw, a member may not withdraw prior to the time for the dissolution and commencement of winding up of the limited liability company, without the written consent of all other members at the time.

HISTORY: 2000 c 169 § 2; 1995 c 337 § 17; 1994 c 211 § 304.

NOTES: EFFECTIVE DATE -- 1995 C 337: See note following *RCW 25.15.005*.

LexisNexis 50 State Surveys, Legislation & Regulations

Limited Liability Companies

USER NOTE: For more generally applicable notes, see notes under the first section of this heading, part, article, chapter or title.

TITLE 25. PARTNERSHIPS
CHAPTER 25.15. LIMITED LIABILITY COMPANIES
ARTICLE 10. DERIVATIVE ACTIONS

GO TO REVISED CODE OF WASHINGTON ARCHIVE DIRECTORY

Rev. Code Wash. (ARCW) § 25.15.370 (2013)

§ 25.15.370. Right to bring action

A member may bring an action in the superior courts in the right of a limited liability company to recover a judgment in its favor if managers or members with authority to do so have refused to bring the action or if an effort to cause those managers or members to bring the action is not likely to succeed.

HISTORY: 1994 c 211 § 1001.

NOTES:

LexisNexis 50 State Surveys, Legislation & Regulations

Limited Liability Companies

NOTES APPLICABLE TO ENTIRE TITLE

CROSS REFERENCES.

Powers of appointment: Chapter 11.95 RCW.

Probate provisions relating to partnership property: Chapter 11.64 RCW.

TEXTBOOKS AND TREATISES.

Washington Corporate Forms; Donald D. Hoff, Morris G. Kremen, Craighton E. Goeppele (Michie).

NOTES APPLICABLE TO ENTIRE CHAPTER

CROSS REFERENCES.

Limited liability partnerships: Chapter 25.04 RCW.

GONZAGA LAW REVIEW.

Operational overview of the Washington limited liability company act. *30 Gonz. L. Rev. 183.*

SEATTLE UNIV. LAW REVIEW.

A step in the right direction: Washington passes the Limited Liability Company Act. *18 Seattle U. L. Rev. 197.*

TEXTBOOKS AND TREATISES.

Washington Corporate Law: Corporations and LLCs; Stewart M. Landefeld, Barry M. Kaplan, Steven R. Yentzer (Michie).

*** Statutes current through 2013 3rd special session ***

TITLE 25. PARTNERSHIPS
CHAPTER 25.15. LIMITED LIABILITY COMPANIES
ARTICLE 10. DERIVATIVE ACTIONS

GO TO REVISED CODE OF WASHINGTON ARCHIVE DIRECTORY

Rev. Code Wash. (ARCW) § 25.15.375 (2013)

§ 25.15.375. Proper plaintiff

In a derivative action, the plaintiff must be a member at the time of bringing the action and:

(1) At the time of the transaction of which the plaintiff complains; or

(2) The plaintiff's status as a member had devolved upon him or her by operation of law or pursuant to the terms of a limited liability company agreement from a person who was a member at the time of the transaction.

HISTORY: 1994 c 211 § 1002.

NOTES:

LexisNexis 50 State Surveys, Legislation & Regulations

Limited Liability Companies

USER NOTE: For more generally applicable notes, see notes under the first section of this heading, part, article, chapter or title.