

No. 74805-0-I  
COURT OF APPEALS, DIVISION I  
OF THE STATE OF WASHINGTON

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GLOBAL CHEMICAL SOLUTIONS, LLC,

Respondents,

v.

CENTECH LLC, JOHN GRAFF, and TERESA GRAFF,

Appellants.

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**BRIEF OF APPELLANTS**

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## I. INTRODUCTION

Appellant Centech, LLC bought the assets of Respondent Global Chemical Solutions, LLC (“GCS”) and took on its President, Robert Black as a full partner and co-manager. GCS had failed to disclose, however, that Black had been sabotaging GCS’s business and falsifying its records. After the deal failed, the parties each claimed breach of contract.

Shortly before trial, GCS settled its \$386,000 claim against defendant-guarantor Black for a security interest in real property, a contingent Confession of Judgement for \$386,000, and a \$225,000 note representing a discount from the judgment amount if paid in accordance with the note’s terms.

At trial, GCS’s manager admitted that GCS had miscalculated the balance due when it made demand on Centech and Black. Despite this, the trial court denied Centech’s motion under CR 50 to dismiss GCS’s claim for pre-judgment interest. The trial court also refused to instruct the jury, as requested by Centech, on the unambiguous meaning of key terms of the parties’ densely written contract. The jury, thus inadequately instructed, found for GCS, and the trial court entered judgment against Centech including pre-judgment interest. The trial court, while acknowledging that set-off was a matter for the court, failed to make any

ruling regarding any setoff for the undisputed pre-trial settlement payment by Black.

## II. ASSIGNMENTS OF ERROR

Appellants assign the following errors:

1. The trial court erred by failing to set off against the judgment, the amount recovered by the Plaintiff-Respondent from a settling co-defendant and co-guarantor.

Issue: Must the value received by a plaintiff from a 50-percent guarantor be credited against the principal obligor's obligation?

2. The trial court erred in failing to instruct the jury, as requested by Appellants, on the meaning of the parties' contract, leaving the legal interpretation of the contract to the jury.

Issue: Is it the Court's duty to interpret the contract as a matter of law and instruct the jury thereon?

3. The trial court erred by denying Appellants' motion for judgment as a matter of law dismissing claim for pre-trial interest (Dkt. No. 153) and therefore in entering judgment without making the requested adjustment.

Issue: Where there was a genuine dispute over the unliquidated amount due under a contract, as conceded by Respondent's

manager's testimony at trial, should pre-judgment interest be awarded?

### III. STATEMENT OF THE CASE

#### *A. GCS Passed Off Its Failing Assets and Its Dishonest CEO on Centech.*

Centech, LLC is a small business in Eastern Washington that deals in glycerin byproducts. RP 1019. Its CEO and indirect owner was John Graff. RP 1066-67. In 2011, a glycerin refinery company managed by Graff did some business with GCS, an industrial chemicals distributor, whose CEO was then a Mr. Robert Black. RP 1019, 1449.

GCS was owned by three partners: Black, Treasurer Greg Porter, and President John Hennessey. RP 326-27. GCS had been created to use Hennessey's good credit and Porter's accounting expertise to take advantage of a supposed business opportunity offered to them by Black—falsely represented by Black to be an exclusive distribution agreement with an up-and-coming Korean chemicals dealer, Nae Woi Korea, Ltd. RP 325-32.

But by late 2012, Black had completely failed to perform as represented, and Hennessey became fed up with Black's inability to make a profit or meet sales targets. RP 342-43, RP 583. The company's debt, which Hennessey and Porter had personally guaranteed, was

increasing. RP 332-34, 342-43. Black was out of control, refusing to obey the Board; in particular, Black flatly refused to obey the Board's orders to stop borrowing large sums to buy more unmarketable products from Nae Woi Korea. RP 579-80. Black's partners were also concerned that he may have been committing crimes in the company's name. RP 553-54, 557, 570.

Hennessey and Porter demanded that Black find a new investor to buy them out. RP 342. Black turned to Graff. RP 352-53. Black negotiated a deal with Centech, for Centech to procure financing secured by GCS's assets, buy out all of GCS's assets, and, vitally, to take on Black as a full partner. RP 438, RP 365, RP 356-57. The transaction was an exit for Porter and Hennessey, a way for them to get their money back and transfer the known bad assets and management to Centech, LLC. RP 557.

***B. GCS Failed to Make Full Disclosures***

GCS and Centech entered an Asset Purchase Agreement ("APA") in December 2012. RP 387; CP 7. Among the significant provisions of the APA was paragraph 4.15, which was part of the Seller's (GCS's) warranties and representations:

Neither this agreement nor any of the Schedules or Exhibits annexed hereto contains any untrue statement of any material fact or omits to state any material fact required to

be stated to make the statements contained herein or therein not misleading. To the best knowledge of Seller, there is no fact which has not been disclosed in writing to Buyer prior to the date hereof that materially adversely affects the prospects or the financial or other condition of the Business or the Assets.

CP 15.

GCS was selling its inventory and accounts receivable, and also its goodwill, its customer and supplier relationships, which is to say, Robert Black's. *See* Asset Purchase Agreement, CP 7-57; RP 418-21, RP 506. Black's character and ability were thus vital to the deal. It was undisputed at trial that GCS had passed resolutions identifying the severe defects of Black's management and his overt breaches of fiduciary duties toward GCS and his partners Hennessey and Porter. RP 541, 570-71. Black openly flouted the resolutions. For example, he diverted company funds to pay his own attorney to advise him of how to fight the Board, in direct violation of a resolution. RP 570:17-23. Even more egregiously, he ignored a resolution to control his overspending of the company's money on deals that benefited only his supplier: "Any expenditure in excess of \$5,000 must be approved by the board via e-mail." RP 573:14-16.

It was also undisputed at trial that these materially detrimental elements of Black's dishonesty in managing GCS's business were not disclosed to Graff or Centech before closing. RP 537-38, 1475:23-1476:4.

Nor was it disclosed that Black had not even reached 50 percent of his sales projections. RP 602:24-603:7, 1537:18-21. Instead, Centech was told that by Black that Porter and Hennessey had dealt dishonestly with him, and told by Porter that Black was a good salesman who would be a good partner and a good addition to Centech's team. RP 353-54, 1047,1455-56. It was further undisputed that Black repeated at Centech, as soon as he arrived after closing, the same destructive behavior that had characterized his partnership and management at GCS. RP 1460-75. Notably, Black surreptitiously placed a large order with Nae Woi Korea shortly before closing, after GCS's books had been disclosed, without funds to cover the order, leaving Centech with an immediate crisis with its supplier; Black then diverted the business to a company he solely owned. CP 1460-72.

Even apart from that last-minute discrepancy, there were significant defects in GCS's records known to GCS, which were not disclosed to Centech or Graff before closing. Centech was informed that there were some unpaid, possibly disputed receivables, and the parties agreed for Centech to pay GCS in installments, and to use a formula to reduce the purchase price based on inability to sell inventory or collect on those aged receivables. CP 9-12. But as it turned out, there was also a significant unrecorded account payable of \$124,900. RP 1621:14-16.

One receivable for \$72,670.87, it turned out, was not merely disputed, it was simply mis-booked, it had never been sold or delivered at all. 1519:19-1520:6; CP 32. The result of these and other mis-recorded transactions was that although GCS figured its annual margin at approximately 12.5 percent, the correct figure was closer to 5.5 percent, which was not a large enough margin, in 2013, for Centech to be able to pay off the rest of the purchase price to GCS. RP 1538-42.

At the close of trial, Centech proposed jury instructions explaining the meaning and impact of certain APA provisions, including paragraph 4.15, quoted *supra*. CP 318-21; CP 237-42.<sup>1</sup> Specifically, they sought instructions explaining that a warranty is an enforceable term of a contract, which may be breached without negligence or intent (unlike a mere representation) breach of which is always material, along with a ‘plain English’ explanation of what that paragraph means. *Id.* The Court rejected these proposed instructions, over Centech’s objections. RP 1646-51; CP 322-53. The Court also rejected Centech’s proposed pattern instruction on frustration of purpose as a defense to a breach of contract claim, holding that although hiring Mr. Black was one of Centech’s

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<sup>1</sup> The numbering of these proposed instructions changed from draft to draft exchanged between the parties and with the Court, so that the filed set of proposed instructions lists as Nos. 5-8, the same proposed instructions referred to in the pocket brief as Nos. 25-28.

contractual obligations, his failure to perform in the role for which he was hired could not support such a defense as a matter of law. RP 1651-53; CP 52.

### *C. The True-Up Dispute*

One of the factors for the ‘true-up’ adjustment to the purchase price under the APA, was whether Centech could collect all of GCS’s aging accounts receivable. CP 10; RP 416-17. These receivables were listed on an attachment to the APA. CP 32. By far the largest receivable, more than 15 percent of the whole purchase price, was from a company named Lusid Technologies, which GCS listed as \$142,787.53 owing to GCS. CP 32. When the parties, as agreed, came to calculate the true-up to the purchase price, GCS demanded full payment on account of that asset, and Centech disagreed. RP 479-81, 502. Centech would not pay the amount demanded by GCS, and GCS declared a default, and asked the Court to award default interest starting at the true-up date. RP 521-22. When the dispute came to trial, however, Mr. Porter admitted that there had been an accounting error whereby GCS had booked the Lusid Technologies sale as an account receivable rather than as a post-closing sale, meaning that under the APA’s formula, a third of the amount, or \$47,595.84, should have been deducted from the final purchase price. RP 636-40. Nevertheless, the jury inexplicably awarded the amount

originally claimed by GSC, including the \$47,595.84 conceded at trial, and the trial court, without explanation, awarded pre-trial default interest from the true-up date. CP 835.

***D. Black Settled A 50-Percent Guaranty Claim.***

As part of the exit by Porter and Hennessey, they required both Graff and Black to each sign personal guarantees for fifty percent of Centech's liability to GCS under the APA. CP 52-57. Graff's guaranty was induced by the same misrepresentations and non-disclosures as the APA. RP 1559:1-14. Of course, Black had no defenses to the Guarantees, because he was fully knowledgeable concerning his shortcomings and breaches of duties toward GCS. Given his clear liability to GCS, in contrast to that of Graff or Centech, shortly before trial, Black settled with GCS on its claim against him as guarantor. CP 390-91. GCS calculated (incorrectly) the amount owed by Centech as trial approached at \$386,000, including interest. CP 431. In exchange for a release of that claim, Black agreed to give GCS a judgment in the amount of \$386,000, and a secondary agreement that if he paid \$225,000 under a 36-month note, secured by his real property, strictly in accordance with the terms of the note, that he would get a credit for the amount due in excess of the amount paid under the \$225,000 note. CP 390-91. GCS thus accepted the note and judgment as payment in full of the stipulated liability of \$386,000.

During trial, the Court ruled that although the jury could be informed that there had been a settlement, as it could go to witness credibility, the amount of the settlement would not be disclosed to the jury, because any set-off or credit to Mr. Graff or Centech for the settlement would be determined by the Court if there was a verdict in favor of GCS, and would not be included on the special verdict form or jury instructions. RP 1441-43. Although Centech and Graff requested a setoff in the judgment, the judgment did not reflect any such setoff, nor did the trial court enter any findings or conclusions explaining why it denied the request. CP 384-85, CP 835-38.

#### IV. ARGUMENT

##### *A. Standard of Review.*

The Court reviews the trial court's decision as to whether to grant an offset for abuse of discretion. *Eagle Point Condo. Owners Ass'n v. Coy*, 102 Wn. App. 697, 701, 9 P.3d 898, 902 (2000).

The meaning of a contract, and thus the correctness, adequacy or completeness of jury instructions given as to the meaning of a contract are reviewed *de novo* by an appellate court. *Tapper v. State Empl. Sec. Dep't*, 122 Wn. 2d 397, 403, 858 P.2d 494, 498 (1993).

##### *B. The Trial Court Erred by Failing to Set Off Against the Judgment, the Amount Recovered by the Plaintiff-Respondent from Black*

During trial, the court made it clear that the matters of the Black guaranty and his settlement with GCS, and set-off or credit therefore to Centech, would not go to the jury, and would be handled by the court, and after the jury returned its verdict, Centech accordingly requested such a setoff or credit from the trial court. RP 1441-43; CP 384-85. However, the trial court made no findings of fact or conclusions of law on those issues, as required by CR 52, ruling *sub-silentio* that no set-off would be allowed. Because no findings of fact or conclusions of law were made on those issues, neither Centech nor this Court can know the thought process or reasoning of the trial court on those issues. However, the findings and conclusions proposed by Appellants are supported by authorities, should have been entered.

First, a basic principle imbedded in the law of Washington, in both tort and contract, is that there shall not be a double recovery. *Eagle Point Condo. Owners Ass'n v. Coy*, 102 Wn. App. 697, 702, 9 P.3d 898, 902 (2000). As in that case, a court must prevent a double recovery. Unlike that case, there is no basis for the liability of Black to be other than coincident with liability of Centech; a guaranty by definition covers coincident liability. Therefore, the full consideration given to Black by GCS must be set-off against the claims of GSC against Centech. *Id.*

The principle applies fully even if a settlement is other than a payment already made. In *Coulter v. Asten Group, Inc.*, 155 Wn. App. 1, 10-11, 230 P.3d 169 (2010), the full amount of settlements were set-off against the concurrent liability of the other liable parties, despite the fact that the full amounts of the settlements were not yet paid. That opinion also exemplifies the need for findings of fact and conclusions of law regarding set-offs for settlements, holding that, in the absence of evidence regarding the collectability of a settlement amount offered by the releasing party, the full amounts of the settlements were properly set-off against the liability of the other parties. *Id.* at 12. Although *Coulter* was a tort case, the rule against double recovery should not be any different in the context of contract.

The liability of Black was agreed between GCS and Black to be \$386,000, and a judgment for that amount was given by Black and received by GCS. The evidence is unequivocal and undisputed on that point. GCS may collect that amount. As important, there is no evidence in the record that GCS will not collect that amount, and there are no findings of fact by the court to give any guidance on the issue here on appeal. On the reasoning of *Coulter*, it is respectfully submitted that a set-off of \$386,000 should be granted, in that there was no presentation of evidence to the contrary. Looked at from another perspective, if GCS

collects on the full judgment amount, it will get an impermissible double recovery, contrary to basic principles. *Eagle Point Condo. Owners Ass'n v. Coy*, 102 Wn. App. 697, 702, 9 P.3d 898, 902 (2000). The only proper procedural alternative to a credit of \$386,000, is a remand for further proceedings and the entry of appropriate, necessary findings by the trial court.

***C. The Jury Instructions Were Not Adequate to Inform the Jury Regarding the Meaning of the Contract at Issue.***

In Washington, the respective roles of the jury and the court are immutably defined. “Judges shall not charge juries with respect to matters of fact, nor comment thereon, but shall declare the law.” Wash. Const. Art. IV, § 16. Once the facts of a case have been established, determining the meaning of a contract is a responsibility for the judge, applying settled rules of construction. *Washington State Major League Baseball Stadium Pub.Facilities Dist. v. Huber, Hunt & Nichols-Kiewit Const. Co.*, 176 Wn. 2d 502, 517, 296 P.3d 821,829 (2013). The legal effect of a contract is a matter of law that is reviewed de novo by the appellate court . *Tapper v. State Empl. Sec. Dep't*, 122 Wn. 2d 397, 403, 858 P.2d 494, 498 (1993).

In this case, the Appellants jury instructions nos. 25-28 provided the correct legal construction of the contract and necessary definitions under the applicable law (as cited in the proposed instructions for the trial

court's reference), so that the jury could apply the contract to the facts. By not giving these instructions, or any instructions on the meaning of the contract, the trial court left the jury to reach its own determination of the law, a determination outside its province. Construction of a contract raises a question of law while interpretation of the language involves a potential factual inquiry to determine the meaning of the language. Here the jury was left to determine both. It is fundamental that where a contract is unambiguous (which is itself a legal issue for the trial court to determine), interpretation is reduced to a question of law. *The Language Connection, LLC v. Empl. Sec'y. Dep't of Wash.*, 149 Wn. App. 575, 585, 205 P.3d 924, 929 (2009), *as modified* (July 21, 2009). In this case, there was no ambiguity as to certain provisions in the contract, and the jury should have been so advised, especially where the facts showing prior material breach of contract were so similar to the facts showing fraud or negligent misrepresentation, but the elements and standards of proof were so different. The jury needed clear instructions on what a warranty is, that scienter is not needed, that materiality is presumed, and what this particular warranty clause entailed.

Although the jury was instructed on contract interpretation, that is a question of law for the court's decision. Thus, the trial court incorrectly assigned to the jury 'the additional duty of resolving

the questions of law inherent in the factual situation.’

*Mega v. Whitworth*, 138 Wn. App. 661, 672, 158 P.3d 1211, 1216 (2007), (citing *Berg v. Hudesman*, 115 Wn. 2d 657, 668, 801 P.2d 222 (1990), and quoting *State v. Chambers*, 814 Wn.2d 929, 932, 506 P.2d 311 (1973)). Here, the jury wasn’t even instructed on contract construction or interpretation, but was just left on its own to guess about the law applicable to the language of a complex APA.

The jury should also have been instructed on the defense of frustration of purpose, where one of its obligations under contract, hiring Mr. Black as head of sales, made it impossible to even begin to perform the other obligations.

***D. The Trial Court should not have Awarded Pre-Judgment Interest.***

Pre-judgment interest on a contract may be awarded only “where the amount sued for may be arrived at by a process of measurement or computation from the data given by the proof, without any reliance upon opinion or discretion after the concrete facts have been determined, the amount is liquidated and will bear interest.” *Prier v. Refrigeration Eng'g Co.*, 74 Wn.2d 25, 33-34, 442 P.2d 621, 626 (1968) (quoting C. McCormick, *Damages* (Hornbook Series) s 54 (1935)). It is unfair to charge a defendant interest for not paying an uncertain amount. *Id.*

When the amount of damages cannot be mechanically measured, but depends on whether parts of the claimed sum were arrived at reasonably, “reliance upon opinion and discretion is necessary,” the damages are unliquidated, and prejudgment interest is not available. *Hansen v. Rothaus*, 107 Wn.2d 468, 477, 730 P.2d 662, 667 (1986).

Here, the APA § 2.2(b) provides for certain adjustments to the Purchase Price depending on whether Centech could or could not collect certain items using “Best Collection Efforts,” defined as “acting in good faith and using best efforts to collect...provided that Buyer shall not be required to make any effort that in its reasonable, good faith belief, does not constitute good business practice or that may injure its image or relationship with customers or its reputation in the industry.” CP 10-12 (APA at 4 ¶¶ 2.2(b)(1)-(4)). At the true-up date, July 31, 2013, when GCS claims Centech went into default by failing to make monthly payments of a percentage of the adjusted Purchase Price, GCS was challenging whether Centech had made “Best Collection Efforts” with respect to the Questionable Assets. RP 432-33. Thus, until trial, the Purchase Price was unliquidated—it could not be determined without relying upon opinion and discretion, whether Centech had acted in good faith, used best efforts, and been reasonable.

Furthermore, the APA plainly requires GCS to adjust the purchase price down proportionately to the difference between the actual sales made by Centech and the Earn-Out Target. CP 13 (§ 2.2(b)(5)). GCS finally conceded at trial, after refusing to acknowledge it for more than a year, that it miscalculated the total sales, increasing the putative Purchase Price by over \$47,000. Where GCS failed to perform and demanded too much under the contract, Centech should not have to pay a default interest rate for having refused to obey GCS's wrongful demand.

## V. CONCLUSION

For the reasons set forth above, the judgment should be vacated and the case remanded for further proceedings.

DATED this 31st day of October, 2016.

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**PROOF OF SERVICE**

The undersigned declares under penalty of perjury that the following facts are true and correct:

I am a citizen of the United States, over the age of 18 years, and not a party to or interested in the above-entitled action.

On October 31, 2016, I served or caused to be served a copy of the foregoing document upon counsel for Respondents by hand and email at

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SIGNED this 31st day of October, 2016,

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