

No. 44235-3II
(Thurston County No. 04-2-02427-4)

COURT OF APPEALS OF THE STATE OF WASHINGTON,
DIVISION II

JAMES S. FELTMAN, Chapter 11 Trustee
for the Estate of Certified HR Services Company,

Appellant,

v.

MIKE KREIDLER, Insurance Commissioner; and CASCADE
NATIONAL INSURANCE COMPANY,

Respondents.

APPELLANT'S OPENING BRIEF

Christopher M. Alston, WSBA No. 18823
Jason R. Donovan, WSBA No. 40994
Attorneys for Appellant

FOSTER PEPPER PLLC
1111 Third Avenue, Suite 3400
Seattle, WA 98101-3299
Telephone: (206) 447-4400
Telefax: (206) 447-9700
E-mail: alstc@foster.com
 donoj@foster.com

TABLE OF CONTENTS

	<i>Page</i>
I. INTRODUCTION	1
II. ASSIGNMENTS OF ERROR	2
A. Assignments of Error	2
B. Issues Pertaining to Assignments of Error.....	5
III. STATEMENT OF THE CASE.....	7
A. Cascade’s History of Financial Difficulties Lead To the Appointment of a Receiver and Liquidation.....	7
B. The Trustee is Appointed for the Bankruptcy Estate of Certified HR Services Company to Pursue Assets for Creditors.....	7
C. The Receiver Initially Denies the Trustee’s Proof of Claim and Makes the Unsupported Assertion That Midwest Received Ownership Interest In Cascade	9
D. The Trustee Timely Objects to the Receiver’s Initial Determination After the Receiver Refused To Produce All Documents Supporting the Assertions In the Initial Determination.....	10
E. Unable to Support Allegations in the Initial Denial of the Claim, the Receiver Raises New Arguments to Deny the Claim	12
F. The Receiver’s New Bases For Denying the Claim Force the Trustee to File Second Motion Seeking Discovery and for Continuance of Hearing	16
G. The Receiver Admits Facts Fatal To His Final Determination	18
H. Despite the Receiver’s Fatal Admissions, the Trial Court Abused Its Discretion By Confirming the Final Determination and Denying the Trustee’s Second Motion For Discovery.....	18
IV. ARGUMENT.....	20
A. Using the Receiver’s Own Documents, the Trustee Presented Undisputed Evidence Supporting the	

	Assigned Fraudulent Transfer Claim and Satisfying His Burden	20
B.	Receiver Failed To Present Any Evidence – Much Less “Substantial” Or “Clearly Sufficient” Evidence – Supporting His Final Determination.....	22
C.	Midwest Did Not Receive Reasonably Equivalent Value From Cascade.....	25
D.	Receiver Untimely Contradictory Arguments Demonstrate the Receiver’s Interest in Winning At All Costs	28
E.	The Trial Court Abused Its Discretion By Failing To Conduct An <i>In-Camera</i> Inspection and By Denying the Trustee’s Second Motion For Discovery	29
V.	CONCLUSION.....	31

TABLE OF AUTHORITIES

	Page(s)
CASES	
<i>Blue Cross & Blue Shield of Mass., Inc. v. Commissioner of Ins.</i> , 420 Mass. 707, 652 N.E.2d 135 (Mass. 1995).....	19
<i>Butler v. Insurance Commissioner of the State of Delaware</i> , 686 A.2d 1017 (Del. 1997)	19
<i>In re Bernard L. Madoff Investment Securities, LLC</i> , 458 B.R. 87 (S.D.N.Y. 2011).....	29
<i>In re Carrozella & Richardson</i> , 286 B.R. 480 (D.Conn. 2002).....	29
<i>Kueckelhan v. Federal Old Line Insurance Company</i> , 74 Wn.2d 304, 444 P.2d 667 (1968).....	18
<i>Ludington Services Corp. v. Acting Commissioner of Insurance</i> , 444 Mich. 481, 511 N.W.2d 661 (Mich. 1994)	19
<i>Pasternak v. Bourtis</i> , 99 Cal.App.4 th 907, 121 Cal.Rptr.2d 493 (Cal. Ct. App. 2002)	19
<i>Premera v. Kreidler</i> , 133 Wn.App. 23, 131 P.3d 930 (2006).....	19
<i>Sedwick v. Gwinn</i> , 73 Wn.App. 879, 873 P.2d 528 (1994).....	21

STATUTES

RCW 19.40.041	21
RCW 19.40.051	21
RCW 48.31.145	4
RCW 48.31.280(7).....	8
RCW 48.99.017	16

RCW 48.99.017(3).....30

I. INTRODUCTION

This appeal concerns the Cascade National Insurance Company (“Cascade”) receivership and the Receiver’s denial of a Proof of Claim submitted by James S. Feltman, who is serving as the trustee for the bankruptcy estate of Certified HR Services Company (the “Trustee”).¹

The Trustee is a court-appointed fiduciary for the creditors of that bankruptcy estate, and is pursuing the collection of assets all over the country. One of the assets is a cause of action against Cascade based on the fraudulent transfer of millions of dollars from Midwest Merger Management (“Midwest”) to Cascade shortly before this receivership action. Midwest assigned that cause of action to the bankruptcy estate as part of a settlement agreement in February 2006. The Trustee, consistent with his fiduciary duty, filed a Proof of Claim in Cascade’s receivership based on that cause of action.

The undisputed evidence supporting the Trustee’s Proof of Claim conclusively proved its validity. The Receiver’s own documents showed Midwest paid millions of dollars and received nothing in return from Cascade. As a consequence, the payments received by Cascade from the

¹ *On January 16, 2008, pursuant to a plan of liquidation, the Trustee became the Liquidating Trustee for the Certified HR Services Liquidating Trust, successor-in-interest to the debtors and trustee for the bankruptcy estate of Certified HR Services Company.*

insolvent Midwest constitute fraudulent transfers giving rise to a claim for repayment.

Instead of acknowledging the validity of the Trustee's Proof of Claim, the Receiver denied it and wasted significant receivership assets attempting to justify his denial with misrepresentations and untimely, contradictory arguments. Throughout these proceedings, he constantly changed his basis for denying the Trustee's claim and even relied on evidence that he later admitted does not exist.

The Receiver's handling of the Trustee's claim was capricious, untenable and an abuse of discretion. Similarly, the trial court's failure to properly supervise and review the Receiver's claims handling was an abuse of discretion as well.

II. ASSIGNMENTS OF ERROR

A. Assignments of Error

Trustee assigns error to the following rulings in the trial court's November 2, 2012 "Findings of Fact, Conclusions of Law, Order and Judgment (1) Confirming Receiver's Final Determination Denying Proof of Claim No. 4354 of James S. Feltman, Chapter 11 Trustee for the Estate of Certified HR Services Company, et al., and (2) Denying Trustee's Motion for Discovery and Continuance of Hearing":

1. “The Trustee has failed in his burden of proof that any transfer was fraudulent, and/or that there was no reasonably equivalent value given.”²

2. “The evidence identified by the Receiver in support of his Final Determination and his Petition for confirmation of the denial of the Trustee’s claim is clearly sufficient. There is no abuse of discretion by the Receiver in reaching his determination.”³

3. “The Receiver’s Final Determination is tied to the evidence presented, the jury’s verdict, and the appellate decision in the 9th Circuit upholding the May, 2010, district court judgment in *Mike Kreidler, Insurance Commissioner for the State of Washington and as Receiver for Cascade National Insurance Company, in Liquidation v. Danny Pixler, Anthony Huff, Sheri Huff, and Midwest Merger Management, LLC*, U.S.D.C., Western District of Washington, Case No. C06-697RSL. This is now a final judgment” (the “federal court litigation”).⁴

6. “The Trustee’s motion for discovery as to documentation and evidence relating to the Trustee’s Proof of Claim and the Receiver’s Final Determination on that claim is denied.”⁵

² CP 735:24-25.

³ CP 736:1-4.

⁴ CP 736:10-17.

⁵ CP 737:1-3.

7. “The Trustee’s motion for additional discovery which seeks broad discovery as to the Receiver’s actions in administration of the estate or as to the solvency of the estate is not permissible under the statutory proof of claim process, which is controlled by RCW 48.31.145. Even if such discovery request were properly before the Court, there is nothing in the record to support any such discovery. The Trustee’s motion for such discovery is denied.”⁶

9. “There is no evidence that the Receiver’s Determination constitutes an abuse of authority or discretion, or that the Receiver is engaging in a capricious, untenable or unlawful course, or that the Receiver’s Determination of claim review process is arbitrary, capricious, or based on an error of law. The Receiver’s Determination is further supported by substantial evidence.”⁷

10. “The Receiver’s Final Determination on the merits denying the Trustee’s Proof of Claim should be and is confirmed.”⁸

11. “The Trustee’s Motion For Discovery and Continuance of Hearing is denied.”⁹

12. “The Receiver’s Petition for Order Confirming Receiver’s Final Determination Denying the Proof of Claim of James S. Feltman,

⁶ CP 737:4-10.

⁷ CP 737:12-17.

⁸ CP 737:18-19.

Chapter 11 Trustee for the Estate of Certified HR Services Company, et al., is granted, confirmed and approved.”¹⁰

13. “Proof of Claim No. 4354 by the Trustee is denied in accordance with the Receiver’s Final Determination.”¹¹

B. Issues Pertaining to Assignments of Error

In reviewing the trial court’s rulings, the following issues must be addressed and resolved:

1. Did the trial court abuse its discretion in finding that the Trustee failed to satisfy his burden of proof of showing that Midwest did not receive reasonably equivalent value for the \$4.3 million Midwest paid to Cascade when the Receiver’s own documents conclusively prove that Midwest never received reasonably equivalent value? (ANSWER: YES)

2. Did the trial court abuse its discretion in finding that the Receiver’s Final Determination was supported by “substantial” and “clearly sufficient” evidence even though the Receiver’s Final Determination lacked any factual basis? (ANSWER: YES)

3. Did the trial court abuse its discretion in finding that there was no evidence the Receiver abused his discretion or engaged in a

⁹ CP 738:5-6.

¹⁰ CP 738:8-11.

¹¹ CP 738:12-13.

capricious, untenable or unlawful course even though the Receiver's Final Determination lacked any factual basis? (ANSWER: YES)

4. Did the trial court abuse its discretion in finding that the Receiver's Final Determination was tied to the evidence presented, the jury's verdict and the appellate decision in the 9th Circuit in the Federal Court Litigation even though the Receiver's Final Determination lacked any evidentiary basis? (ANSWER: YES)

5. Did the trial court abuse its discretion in confirming the Receiver's Final Determination denying Trustee's Proof of Claim? (ANSWER: YES)

6. Did the trial court abuse its discretion in denying Trustee's motion for discovery relating to the Trustee's Proof Of Claim and the Receiver's Final Determination even though the Receiver's Final Determination lacked any factual basis? (ANSWER: YES)

7. Did the trial court abuse its discretion in denying Trustee's motion for discovery relating to the Receiver's administration of the estate based on the lack of facts supporting Receiver's Initial Determination, the lack of facts supporting Receiver's Final Determination, the constantly changing bases for denying Trustee's Proof of Claim, and the continued waste of receivership estate resources? (ANSWER: YES)

8. Did the trial court abuse its discretion by failing to conduct an *in-camera* review of the documents requested in Trustee's Motion For Discovery and Continuance of Hearing and by denying that motion? (ANSWER: YES)

III. STATEMENT OF THE CASE

A. Cascade's History of Financial Difficulties Lead To the Appointment of a Receiver and Liquidation

Cascade operated as a domestic insurer in Washington and entered into the workers' compensation market in early 2004.¹² Unfortunately, Cascade already had a history of financial difficulties that led to increased scrutiny by the Office of the Insurance Commissioner, who issued a notice to Cascade to cure a deficiency in its capital and surplus back in March 2003.¹³ The Insurance Commissioner eventually petitioned for and obtained an order appointing a receiver for the purpose of seizing Cascade on November 30, 2004, and the trial court entered an Order of Liquidation and Approval of Plan of Liquidation on November 4, 2005.¹⁴

B. The Trustee is Appointed for the Bankruptcy Estate of Certified HR Services Company to Pursue Assets for Creditors

The Trustee is the Chapter 11 Trustee for the Estate of Certified HR Services Company in a bankruptcy case pending in the United States

¹² CP 11:11-12 & 12:3.

¹³ CP 13:19-20.

¹⁴ CP 10-42.

Bankruptcy Court for the Southern District of Florida.¹⁵ As a court-appointed fiduciary for the creditors of that bankruptcy estate, the Trustee is pursuing assets all over the country. Exercising his fiduciary duties, he entered into a Settlement Agreement in 2006 with Midwest, who transferred and assigned to him all of its claims against Cascade.¹⁶ After investigating potential claims of Midwest, the Trustee determined that Midwest had transferred millions of dollars to Cascade just prior to the receivership action and appeared to have received nothing in return.¹⁷ For the benefit of the creditors and of the bankruptcy estate, the Trustee decided to pursue a claim in Cascade's receivership to recover these fraudulent transfers.

On December 4, 2007, the Trustee filed a Proof of Claim against Cascade based upon fraudulent transfers of approximately \$12,745,720 from Midwest to Cascade.¹⁸ The Trustee's Proof of Claim was filed late and accordingly assigned Class 7 priority per RCW 48.31.280(7).¹⁹

¹⁵ CP 605.

¹⁶ CP 605.

¹⁷ CP 605.

¹⁸ CP 605.

¹⁹ CP 493:4-6.

C. The Receiver Initially Denies the Trustee’s Proof of Claim and Makes the Unsupported Assertion That Midwest Received Ownership Interest In Cascade

More than four years after the Trustee filed the Proof of Claim, the Receiver finally issued Receiver’s Initial Determination Denying Proof of Claim No. 4354 of James S. Feltman, Chapter 11 Trustee For the Estate of Certified HR Services Company, et al., and Notice of Further Proceedings (“Initial Determination”).²⁰

In the Initial Determination, the Receiver asserted the payments Midwest made to Cascade were not fraudulently transferred because Midwest received “reasonable equivalent value” in exchange for those payments. The Receiver claimed the \$8 million Midwest paid to Cascade between January 8, 2004 and March 13, 2005 were partial payments for insurance coverage which Cascade provided to Midwest between February 13, 2004 and February 13, 2005.²¹ The Receiver also acknowledged that Midwest made payments to Cascade in the amount of approximately \$4.3 million for an ownership interest in Cascade.²² But the Receiver offered no evidence that showed Midwest actually received the stock in Cascade for which it paid. It is important to note the Initial Determination did not contain a single reference to an entity called

²⁰ See CP 364 – 404.

²¹ CP 377:1-2 & CP 374:17-18.

²² CP 378:4-8.

Gudeman & Weiss (“G&W”) or any purported relationship between G&W and Midwest. As explained below, G&W would figure predominantly in the Receiver’s later attempts to justify his denial of Trustee’s claim.

The Initial Determination also contained an allegation that the Trustee would never receive a distribution on his claim. According to the Receiver, the receivership estate lacks sufficient funds, or has insufficient funds, to pay the Trustee or anyone else holding a claim in Class 7.²³

D. The Trustee Timely Objects to the Receiver’s Initial Determination After the Receiver Refused To Produce All Documents Supporting the Assertions In the Initial Determination

On May 10, 2012, the Trustee filed a Motion for Discovery to gather evidence in order to respond to the allegations in the Initial Determination. In order to avoid a contested hearing, the Receiver agreed to produce some of the documents requested by the Trustee.²⁴ But the Receiver refused to produce any documents concerning the alleged insolvency of the receivership estate despite the allegations in the Initial Determination that the receivership estate lacked the funds to pay Trustee’s Proof of Claim.²⁵ Without waiving the right to later seek additional documents, the Trustee withdrew the motion and the Receiver

²³ CP 368:5-13.

²⁴ CP 555:7-8.

produced certain documents concerning payments Midwest made to Cascade.²⁶

The documents produced by the Receiver clearly evidence that Midwest actually paid approximately \$4.3 million for purchase of Cascade preferred stock as follows:²⁷

Date	Amount
12/15/2003	\$1,000,000.00
12/23/2003	\$1,000,000.00
01/08/2004	\$1,000,000.00
03/09/2004	\$120,000.00
03/31/2004	\$250,000.00
04/06/2004	\$100,000.00
04/13/2004	\$132,000.00
04/14/2004	\$132,000.00
04/15/2004	\$132,000.00
04/16/2004	\$132,000.00
04/23/2004	\$2,000.00

Importantly, however, Midwest never received any of the Cascade stock.²⁸ Instead, the Cascade preferred stock was actually issued to the aforementioned G&W.²⁹

Directly contrary to the Receiver's findings in the Initial Determination, Midwest did not receive "reasonably equivalent value" for the \$4.3 million Midwest paid to Cascade. In fact, the Receiver's own

²⁵ CP 555:8-9.

²⁶ CP 555:9-15.

²⁷ See CP 625 – 650 (documents produced by Receiver).

²⁸ CP 592:3-13 & 625-51.

²⁹ CP 592:3-13 & 625-51.

documents conclusively prove that Midwest received zero in return for the \$4.3 million paid to Cascade.³⁰

The Trustee timely filed an objection raising these facts on May 29, 2012.³¹ Given the clear import of the documents produced by the Receiver in respect of these transfers, the Trustee fully expected the Receiver to abide by the documents in his possession and at least allow the Trustee a late filed, junior priority claim for the \$4.3 million paid to Cascade.³² Moreover, if the Receiver were correct that the estate lacked assets to pay Class 7 claims, then there would be literally no harm to the receivership estate to allow the Trustee's claim in the amount of \$4.3 million.³³ And given this purported insolvency, it made no sense for the Receiver to expend any legal fees to object to the Trustee's claim, as such expenses serve only to dilute the assets of the receivership estate that may be available to pay higher priority claims and generate no value to the receivership estate.³⁴

E. Unable to Support Allegations in the Initial Denial of the Claim, the Receiver Raises New Arguments to Deny the Claim

Notwithstanding the above, the Receiver issued the Receiver's Final Determination denying Trustee's claim in entirety on August 2,

³⁰ CP 592:14-17 & 625-51.

³¹ See CP 485 – 489.

³² CP 592:18-21.

³³ CP 592:21 – 593:1.

2012, and sought to have the Final Determination confirmed on August 6, 2012.³⁵ Incredibly and notably, the Receiver's bases for denying Trustee's claim in his Final Determination differed materially from those advanced in the Initial Determination.

1. The Receiver Now Denies the Trustee's Claim on the Theory That G&W Was a "Front" For Midwest

As described above, the Receiver initially asserted that Midwest paid Cascade approximately \$4.3 million in exchange for stock in Cascade.³⁶ After the Trustee pointed out how the Receiver's own documents conclusively prove that the Cascade stock for which Midwest paid millions actually went to G&W, the Receiver changed his basis for denying that part of the Trustee's claim. Conceding that the documents do not support his Initial Determination, the Receiver theorized in the Receiver's Final Determination that G&W was merely a "front" for Midwest. The Receiver represented that evidence in the federal court litigation the Receiver pursued against Midwest, G&W and others established this fact.³⁷ The Receiver asserted that G&W and Midwest were essentially alter egos, so when G&W received the stock, Midwest

³⁴ CP 593:1-5.

³⁵ See CP 461 – 550.

³⁶ CP 378:4-8.

³⁷ CP 500.

also received the stock and therefore received reasonably equivalent value for the amounts paid to Cascade.³⁸

But the Receiver's Final Determination failed to set forth any evidence (much less "substantial" or "clearly sufficient" evidence) supporting the Receiver's newly-asserted theory that G&W was a "front" for Midwest. The Receiver failed to identify any specific evidence in the federal court litigation upon which the Receiver purportedly relied to substantiate that newly-asserted theory. The Trustee was not a party to the federal court litigation, and it is important to note, as explained further below, the Receiver later admitted the federal court litigation did not even involve whether G&W was a "front" for Midwest.³⁹ Thus, the Receiver continued to miss the mark with his attack on the claim of the Trustee for the \$4.3 million paid to Cascade.

2. The Receiver Now Clearly Bases His Denial on the Alleged Lack of Funds to Pay Trustee's Claim

The Final Determination also declared again that there are insufficient funds to pay the Trustee's claim.⁴⁰ While the same allegation appeared in the Initial Determination, it did not appear to serve as a basis

³⁸ CP 499:16 – 500:4.

³⁹ Verbatim Report of Proceedings ("VRP") at 37.

⁴⁰ See also CP 493:7-13 and CP 494:1-3 ("In addition, for claims which are late-filed and therefore classified in Class 7 under the statute, such as here, and given the lack of assets to cover Class 7 claims, it is unnecessary to expedite review and decision by the Receiver.").

for denying the Trustee's claim. But in the Final Determination, the Receiver did deny the Trustee's claim on grounds that the receivership estate is insolvent and that no distributions will therefore be made on the Trustee's Class 7 claim.⁴¹

Again, the Trustee is at a loss as to why the Receiver, in the face of conclusive documentary evidence about the transfers, insisted on pursuing litigation with the Trustee in light of the Receiver's position that no distributions will be made on account of the Trustee's Class 7 claim. Such a position is simply not a valid objection to the merits of the claim. If the Receiver is correct about insolvency, then there is no harm to the receivership estate to allow the Trustee's late-filed claim. Even if the Receiver is not correct and the estate turns out to be solvent, then there is still no harm to allow the Trustee's claim, as any excess from the estate will be paid to the Trustee with respect to that claim after all senior claims are paid in full, and not to the equity owners of Cascade. Based on the above, there is simply no rational explanation for the Receiver's position. It was, in fact, a continued waste of the resources of this receivership estate without any justification.

⁴¹ CP 495:17-19.

F. The Receiver’s New Bases For Denying the Claim Force the Trustee to File Second Motion Seeking Discovery and for Continuance of Hearing

Considering the lack of facts supporting the Initial Determination, the lack of facts supporting the Final Determination, the constantly changing bases for denying the Trustee’s claim, and the continued waste of receivership estate resources, the Trustee filed a second Motion for Discovery Related to Receiver’s Final Determination and Continuance of Hearing pursuant to RCW 48.99.017 (“Second Discovery Motion”).⁴² In that motion, the Trustee satisfied his burden of showing a reasonable suspicion of negligence or malfeasance related to the administration of the receivership estate based, in part, on the following:

- The Receiver failed to issue the Receiver’s Initial Determination denying Trustee’s claim within four years.⁴³
- The Receiver spent over \$2.5 million in receivership estate assets on professional services prosecuting federal court litigation against several judgment-proof defendants to judgment and through appeal, even though the Receiver acknowledges there is “no reasonable expectation” of recovery.⁴⁴
- The Receiver expended receivership estate assets denying claims that, according to the Receiver, have no possibility of being paid even were they valid and approved.⁴⁵

⁴² CP 551-79.

⁴³ CP 466-89.

⁴⁴ CP 533-36 & 323-24.

⁴⁵ CP 495:17-19.

- The Receiver refused to provide information substantiating the bases for the Receiver's denial of claims.

The Court should be alarmed by the expenditure of over \$2.5 million in professional fees in the federal court litigation to pursue an admittedly uncollectible judgment. These fees come right from the pockets of creditors, and if the estate is indeed insolvent, it may be due to the Receiver's mismanagement of estate assets. Furthermore, the failure to timely process claims, the waste of receivership estate assets, and the refusal to provide information substantiating the Receiver's denial of claims, all call the Receiver's administration of the receivership estate into question.

The Receiver compounds these issues by an apparent desire to continue to litigate with the Trustee over the allowance of a claim that the Receiver contends will not receive a dividend in the receivership estate. There is simply no benefit to the receivership estate to litigate these issues with the Trustee. The Trustee accordingly believes that an examination of the documents, materials and other records concerning the Receiver's administration of the receivership estate is warranted.

In addition, the Trustee further requested additional time to adequately prepare and file an opposition to Receiver's Confirmation

Petition and Receiver's Final Determination based on the documents, materials and other records requested.⁴⁶

G. The Receiver Admits Facts Fatal To His Final Determination

On August 24, 2012, the trial court heard oral argument on Receiver's Petition To Confirm Final Determination and the Second Discovery Motion.⁴⁷ During oral argument, the Receiver conceded facts which confirm that the Receiver's Final Determination lacks a valid basis.

First, the Receiver conceded that Cascade's alleged insolvency did not serve as a legitimate basis to deny Trustee's claim.⁴⁸ The Receiver also conceded that the federal court litigation never established that G&W was an alter ego or a "front" for Midwest, as that issue was not even tried in the litigation.⁴⁹ That latter admission is fatal because the Receiver based his Final Determination on the allegation that G&W was a "front" for Midwest as purportedly established in that federal court litigation.

H. Despite the Receiver's Fatal Admissions, the Trial Court Abused Its Discretion By Confirming the Final Determination and Denying the Trustee's Second Motion For Discovery

While the Receiver's role involves a degree of discretion, the Receiver's authority is subject to the supervisory and reviewing role of the courts. *See Kueckelhan v. Federal Old Line Insurance Company*, 74

⁴⁶ CP 552:24 – 553:10.

⁴⁷ VRP.

⁴⁸ VRP at 7-9.

Wn.2d 304, 316, 444 P.2d 667 (1968) (“the trial court in its supervisory and reviewing role may not substitute its judgment for that of the Commissioner, but may and should only intervene or restrain when it is made to appear that the Commissioner is manifestly abusing the authority and discretion vested in his and/or is embarking upon a capricious, untenable or unlawful course.”). In that regard, trial courts apply a “substantial evidence” standard in reviewing decisions of the Receiver. *See, e.g., Premera v. Kreidler*, 133 Wn.App. 23, 31-32, 131 P.3d 930 (2006) (applying the substantial evidence standard and stating that “the evidence must be of a sufficient quantum to persuade a fair-minded person of the truth of the declared premise.”); *see also Pasternak v. Bourtis*, 99 Cal.App.4th 907, 121 Cal.Rptr.2d 493 (Cal. Ct. App. 2002) (applied the substantial evidence standard to reverse insurance commissioner’s denial of claim); *Blue Cross & Blue Shield of Mass., Inc. v. Commissioner of Insurance*, 420 Mass. 707, 652 N.E.2d 135 (Mass. 1995) (applied the substantial evidence standard to reverse insurance commissioner’s decision to prohibit insurer from increasing rates); *Butler v. Insurance Commissioner of the State of Delaware*, 686 A.2d 1017 (Del. 1997) (applied the substantial evidence standard to reverse insurance commissioner’s decision to revoke insurance agent’s license); *Ludington*

⁴⁹ *VRP at 36-37.*

Services Corp. v. Acting Commissioner of Insurance, 444 Mich. 481, 511 N.W.2d 661 (Mich. 1994) (applied the substantial evidence standard to reverse insurance commissioner’s decision to prohibit acquisition of an insurance agency).

Despite the Receiver’s fatal admissions at oral argument, the lack of any evidence supporting the Receiver’s Final Determination (much less “substantial” or “clearly sufficient” evidence), and the significant waste of receivership assets, the trial court nevertheless granted Receiver’s Petition Confirming Final Determination and denied Trustee’s Second Motion For Discovery.⁵⁰ That order is subject of this appeal.

IV. ARGUMENT

A. Using the Receiver’s Own Documents, the Trustee Presented Undisputed Evidence Supporting the Assigned Fraudulent Transfer Claim and Satisfying His Burden

The trial court ruled “[t]he Trustee has failed in his burden of proof that any transfer was fraudulent, and/or that there was no reasonably equivalent value given.”⁵¹ Yet the undisputed evidence conclusively proves that Midwest never received reasonably equivalent value for the \$4.3 million Midwest paid to Cascade. It was therefore an abuse of discretion for the Receiver to find – and for the trial court to confirm – that the Trustee failed to satisfy his burden of showing that Midwest never

⁵⁰ *VRP; CP 733-41*.

received reasonably equivalent value for the \$4.3 million Midwest paid to Cascade.

1. Burden of Proof For Fraudulent Transfer Claims

A fraudulent transfer claim under RCW 19.40.041 must be shown by “clear and satisfactory proof.”⁵² A fraudulent transfer claim under RCW 19.40.051 must be shown by “substantial evidence.”⁵³ The Trustee satisfied that showing by presenting the Receiver’s own undisputed evidence of fraudulent transfers.

2. Trustee Presented Undisputed Evidence Showing Fraudulent Transfers

As set forth above, the Trustee’s fraudulent transfer claim is based on Midwest’s payment of approximately \$4.3 million for Cascade stock that Midwest never received, as conclusively proven by the Receiver’s own documents. Importantly, that evidence remains undisputed and the Receiver even admits that the stock was never issued to Midwest.⁵⁴

Using the Receiver’s own documents, the Trustee demonstrated that Midwest paid approximately \$4.3 million to Cascade and received nothing in return. It was therefore an abuse of discretion for the Receiver to assert – and for the trial court to confirm – that the Trustee failed to

⁵¹ CP 735:24-25.

⁵² *Sedwick v. Gwinn*, 73 Wn.App. 879, 885-88, 873 P.2d 528 (1994).

⁵³ *Sedwick v. Gwinn*, 73 Wn.App. 879, 885-88, 873 P.2d 528 (1994).

⁵⁴ CP 499:16 – 500:4.

show there was no reasonably equivalent value given for those payments to Cascade.⁵⁵

B. Receiver Failed To Present Any Evidence – Much Less “Substantial” Or “Clearly Sufficient” Evidence – Supporting His Final Determination

The trial court ruled that “[t]he evidence identified by the Receiver in support of his Final Determination and Petition for confirmation of the denial of the Trustee’s claim is clearly sufficient. There is no abuse of discretion by the Receiver in reaching his determination.”⁵⁶ The trial court also ruled that the Receiver’s Final Determination “is further supported by substantial evidence.”⁵⁷ To the contrary, however, the Receiver failed to identify any evidence supporting his Final Determination with respect to the Trustee’s claim for the \$4.3 million, much less “substantial” or “clearly sufficient” evidence. Thus, it was an abuse of discretion for the Receiver to find – and for the trial court to confirm – that the Receiver’s Final Determination was supported by “substantial” or “clearly sufficient” evidence.

⁵⁵ CP 735:24-25 (“The Trustee has failed in his burden of proof that any transfer was fraudulent, and/or that there was no reasonably equivalent value given.”).

⁵⁶ CP 736:1-4.

⁵⁷ CP 737:16-17.

1. Insolvency Is Not A Legitimate Basis To Deny Trustee's Claim

The Receiver first asserted that Cascade's alleged insolvency precluded payment of Trustee's claim.⁵⁸ But as the trial court properly recognized and the Receiver admitted during oral argument, Cascade's alleged insolvency is not a legitimate basis to deny Trustee's Proof of Claim.⁵⁹

2. Receiver Admitted There Is No Evidence Supporting Receiver's Theory That G&W Was A "Front" For Midwest

After the Trustee pointed out the flaw in the Receiver's Initial Determination by showing how the Receiver's own documents proved that Midwest received nothing for the \$4.3 million paid to Cascade, the Receiver changed his basis for denying the Trustee's claim. Apparently conceding that the documents do not support his Initial Determination, the Receiver claimed that G&W was merely a "front" for Midwest and that Midwest accordingly received "reasonably equivalent value" for the \$4.3 million paid to Cascade. In fact, the Receiver went so far to assert and represent that the federal court litigation "established that even though the stock was not issued to Midwest, Gudeman & Weiss LLC was merely a

⁵⁸ See, e.g., CP 493:7-14 ("In light of the amount of expenses, claims, claims development, and all costs and obligations to date and anticipated of the receivership estate of Cascade, there will not be adequate funds or assets to pay all priority claims in

‘front’ for the purchase/ownership of the stock interest and future option in Cascade.” [emphasis added]⁶⁰

But the Receiver’s newly-asserted theory that the federal court litigation “established” G&W was a “front” for Midwest was actually false, and the Receiver knew the allegation was not true. Neither the jury verdict nor the Ninth Circuit decision found that G&W was a “front” for Midwest.⁶¹ Similarly, neither the Receiver nor the trial court ever identified any evidence presented in the federal court litigation establishing that G&W was a “front” for Midwest. To the contrary, the Receiver actually admitted during oral argument that the federal court litigation never established that G&W was a “front” for Midwest because “[t]hat wasn’t even an issue” in the federal court litigation.⁶²

In sum, the Receiver relied exclusively on the evidence presented in the federal court litigation to support the Receiver’s newly-asserted theory that G&W was merely a “front” for Midwest and that Midwest accordingly received “reasonably equivalent value” for the \$4.3 million Midwest paid to Cascade. But because the federal court litigation never established that G&W was merely a “front” for Midwest, the Receiver has

classes (1) through (6) with interest. Therefore, even if POC 4354 was accepted and approved, there will be no funds remaining to pay the Class 7 claims.”).

⁵⁹ VRP at 7:16 – 9:8.

⁶⁰ CP 499-500.

⁶¹ CP331-36; see also CP 540-48.

failed to present any evidence supporting the Receiver's newly-asserted theory to deny Trustee's Proof of Claim – a theory the Receiver advanced to rebut the undisputed evidence presented by the Trustee which conclusively proved that Midwest paid approximately \$4.3 million and received nothing in return. The Receiver's allegation in the Final Determination was patently false, and it was an abuse of discretion for the Receiver to find – and for the trial court to confirm – that the Receiver's Final Determination was supported by “substantial” or “clearly sufficient” evidence.

C. **Midwest Did Not Receive Reasonably Equivalent Value From Cascade**

As a default argument, the Receiver also argued that Midwest received reasonably equivalent value for the \$4.3 million Midwest paid to Cascade because those payments purportedly kept Cascade solvent and operational.⁶³ But that argument lacks merit as well.

First, the monies paid by Midwest did not keep Cascade solvent and operational. As the Receiver acknowledged, Cascade “had a history of financial difficulties requiring increased scrutiny of the company by the

⁶² *VRP at 37.*

⁶³ *CP 509:15 – 510:4; see also CP 711:11-17 (“all monies paid to or for Cascade’s benefit that were for capital and surplus in order to keep Cascade in business as a viable, solvent company were for the benefit of Midwest (and its affiliates, its owners, the Huffs and Pixler), because Midwest needed Cascade to be able to write and issue the workers’ compensation coverage that was desperately needed for the 15,000 workers in California.”).*

Office of the Insurance Commissioner” even before March 2003.⁶⁴ The Receiver’s documents reflect that Midwest paid \$4.3 million to Cascade between December 2003 and April 2004. A mere six months later, the state of Washington appointed a receiver to seize Cascade.⁶⁵ Twelve months after that, the state of Washington put Cascade into receivership, at which time Cascade had a deficiency of assets over liabilities exceeding \$17.5 million.⁶⁶ These facts defy the Receiver’s assertion that the \$4.3 million paid by Midwest somehow kept Cascade solvent and operational.

Furthermore, as the Receiver acknowledged, the term “value” for purposes of a fraudulent transfer claim means “property, or satisfaction or securing of a present or antecedent debt of the debtor or to a relative of the debtor.”⁶⁷ Notably, Midwest did not receive any “property” for the \$4.3 million Midwest paid to Cascade; nor did Midwest receive any “satisfaction or securing of a present or antecedent debt” for the payments Midwest made to Cascade, since Midwest owed nothing to Cascade at the time of transfers. Thus, Midwest received no reasonable equivalent “value” for the \$4.3 million paid to Cascade.

⁶⁴ CP 13:19-23 (*Receiver’s Verified Petition For Appointment Of Receiver For The Purpose Of Seizing A Domestic Insurer*).

⁶⁵ CP 31-36.

⁶⁶ CP 44:22-25.

⁶⁷ CP 504:18 – 505:1.

Similarly without merit is the Receiver's implied contention that Midwest received reasonably equivalent value because Midwest owed Cascade \$19 million in principal for workers' compensation coverage Cascade provided. But the \$19 million allegedly owing in additional premium was incurred between November 2005 and March 2011, which was *after* the commencement of this receivership, and the approval of the Receiver's liquidation plan in November 2005.⁶⁸ Midwest's payments for Cascade stock, on the other hand, were made between December 2003 and April 2004.⁶⁹ At the time those payments were made, there was no "present or antecedent debt" that Midwest owed to Cascade, so Midwest could not have received reasonably equivalent "value" for the \$4.3 million it paid to Cascade.

Moreover, it is important to acknowledge that the Trustee is the assignee of Midwest's claims against Cascade and *not* Midwest's successor-in-interest. That distinction is critical here because Midwest remains liable for Midwest's own liabilities, including the \$19 million allegedly owed for additional premiums that arose after the commencement of the receivership and years after the fraudulent transfers were made. To the extent the Receiver seeks to impose that liability upon Midwest, that burden properly rests with the Receiver and Midwest's

⁶⁸ *CP 510:13-24 & CP 550.*

independent liability has no bearing on the Receiver's claim. The Receiver never established a basis to collect anything from the Trustee, and therefore should not be allowed to deny allowance of the Trustee's claim based upon a debt owed by Midwest.

D. Receiver Untimely Contradictory Arguments Demonstrate the Receiver's Interest in Winning At All Costs

In the Receiver's Response to Trustee's Opposition to Receiver's Petition for Order Confirming Receiver's Final Determination Denying Proof of Claim, the Receiver also argued (for the first time on reply) that the Trustee failed to present any evidence concerning Midwest's insolvency during the period of time Midwest made payments to Cascade.⁷⁰ The Receiver's untimely argument did not serve as a basis for his Final Determination and the trial court did not rely on the Receiver's untimely argument as a basis to confirm the Receiver's Final Determination. Thus, the Receiver should be precluded from asserting that argument on appeal.

Furthermore, it is ironic that the Receiver asserted belatedly in his reply that Midwest was actually solvent when the Receiver spent millions of dollars in the federal court litigation attempting to show the exact

⁶⁹ CP 592:3-13.

⁷⁰ CP 714:18-21.

opposite: that Midwest was part of a Ponzi scheme.⁷¹ By definition, “an enterprise engaged in a Ponzi scheme is insolvent from inception and becomes increasingly insolvent as the scheme progresses.”⁷² And as the Trustee pointed out in oral argument, such last-minute, contradictory arguments merely demonstrate the Receiver’s interest in winning at all costs instead of doing what is right.⁷³

E. The Trial Court Abused Its Discretion By Failing To Conduct An In-Camera Inspection and By Denying the Trustee’s Second Motion For Discovery

The Washington Uniform Insurers Liquidation Act provides for the inspection of Cascade’s information or documents when a person demonstrates either an interest in Cascade’s receivership estate or reasonable suspicion of negligence or malfeasance by the Receiver.⁷⁴

The Trustee explained in his Second Motion For Discovery that he has an undisputed legal interest in Cascade’s receivership estate as a claimant.⁷⁵ Furthermore, the Trustee demonstrated “a reasonable suspicion of negligence or malfeasance” by the Receiver based on: (1) the lack of evidence supporting Initial Determination (e.g., evidence

⁷¹ VRP 13:1-8 (“And so in the final determination, the receiver presented and gave them more and more and more evidence showing this entire scheme, which the 9th circuit could, at oral argument, called a Ponzi scheme.”).

⁷² *In re Bernard L. Madoff Investment Securities, LLC* 458 B.R. 87, 110 (S.D.N.Y. 2011); quoting *In re Carozella & Richardson*, 286 B.R. 480, 483 (D.Conn. 2002).

⁷³ VRP 24:16-24.

⁷⁴ Upon showing, the statute clearly says the trial court shall conduct an in-camera review to determine if the information shall be provided to the requesting party.

supporting the Receiver's false assertion that Midwest actually received reasonably equivalent value for payments to Cascade); (2) the Receiver's false representations and allegations (e.g., the false assertion that the federal court litigation established G&W was merely a "front" for Midwest); (3) the repeated and material changes to the Receiver's bases for denying the Trustee's claim; (4) the Receiver's waste of estate resources attempting to justify the Receiver's denial of the Trustee's Proof of Claim at all costs; (5) raising illegitimate basis for denying the Trustee's claim (e.g., alleging Cascade estate was insolvent); and (6) the Receiver's waste of \$2.5 million in estate resources pursuing an uncollectible judgment in the federal court litigation.⁷⁶ This evidence alone shows the Receiver was more interested in fighting and winning than attempting to reach the right result and minimizing legal fees that are effectively paid by the creditors of the receivership estate.

Having demonstrated both a legal interest in the receivership estate and a reasonable suspicion of negligence or malfeasance by the Receiver, the trial court had a duty to conduct an *in-camera* review of the documents the Trustee requested. See RCW 48.99.017(3) ("The court shall conduct an *in-camera* review after notifying the commissioner and every party that produced the information."). But the trial court did not conduct an *in-*

⁷⁵ CP 551-79.

camera review and summarily denied the Trustee's Second Motion For Discovery without so much as requiring the Receiver to specifically identify what evidence presented in the federal court litigation actually supported the Receiver's Final Determination. The Receiver's blanket assertion that such evidence exists does not make it so, and it is patently unfair to deny the Trustee's claim for failure to satisfy his burden of proof (which, as explained above, the Trustee disputes) without affording access to information in the Receiver's own possession that further substantiates the Trustee's claim and/or rebuts the Receiver's purported defenses. Thus, the trial court abused its discretion by confirming the Receiver's Final Determination and denying the Trustee's Second Motion for Discovery.

V. CONCLUSION

The Trustee presented undisputed evidence showing that Midwest never received reasonably equivalent value for the \$4.3 million Midwest paid to Cascade. The Receiver, on the other hand, presented no evidence supporting his ever-changing bases for denying the Trustee's Proof of Claim. The lack of evidence supporting Receiver's Initial Determination, the lack of evidence supporting his Final Determination, his refusal to produce and/or specifically identify evidence that purportedly supports those determinations, and his continued waste of significant receivership

⁷⁶ CP 560-65.

estate assets, all confirm that the Receiver's handling of the Trustee's claim was capricious, untenable and an abuse of discretion.

The trial court had a duty to confirm that the Receiver's Final Determination was based on evidence that actually exists. Similarly, the trial court had a duty to confirm that the Receiver is properly administering the receivership estate. But the trial court failed to do so and abused its discretion by confirming the Receiver's Final Determination and denying Trustee's Second Discovery Motion.

Accordingly, the Trustee respectfully requests that the trial Court's November 2, 2012 Order be reversed with the following instructions:

1. That Receiver's Petition for Order Confirming Receiver's Final Determination Denying the Proof of Claim of James S. Feltman, Chapter 11 Trustee for the Estate of Certified HR Services Company, et al. be DENIED;

2. That Trustee's Second Discovery Motion be GRANTED;

and

3. That Trustee's Proof of Claim be ACCEPTED and APPROVED.

RESPECTFULLY SUBMITTED this 8th day of February, 2013.

FOSTER PEPPER PLLC

s/ Jason R. Donovan

Christopher M. Alston, WSBA No. 18823

Jason R. Donovan, WSBA No. 40994

Attorneys for Appellant

DECLARATION OF SERVICE

I, Jason R. Donovan, declare under penalty of perjury under the laws of the State of Washington that I am now and at all times mentioned herein, a resident of the State of Washington, over the age of eighteen years, not a party to or interested in the above-entitled action, and competent to be a witness herein.

On February 8, 2013, I caused to be served in the manner noted copies of the foregoing upon designated counsel:

Victoria L. Vreeland
Vreeland Law PLLC
500 108th Avenue NE, Suite 740
Bellevue, WA 98004
Phone: 425-623-1300
Email: vicky@vreeland-law.com

Attorneys for Respondent Cascade National Insurance Company

- Via U.S. Mail
- Via Facsimile
- Via Messenger
- Via Email
- Via ECF

Marta Uballe DeLeon
Office of the Attorney General
PO Box 40100
Olympia, WA 98504-0100
Phone: 360-664-9006
Email: martad@atg.wa.gov

Attorneys for Respondent Mike Kreidler, Insurance Commissioner

- Via U.S. Mail
- Via Facsimile
- Via Messenger
- Via Email
- Via ECF

DATED in Seattle, Washington on this 8th day of February, 2013.

s/Jason R. Donovan
Jason R. Donovan

FOSTER PEPPER LAW OFFICE

February 08, 2013 - 12:28 PM

Transmittal Letter

Document Uploaded: 442353-Appellant's Brief.pdf

Case Name: James S. Feltman, Chapter 11 Trustee for the Estate of Certified HR Services Company v. Mike Kreidler, Insurance Commissioner, and Cascade National Insurance Company

Court of Appeals Case Number: 44235-3

Is this a Personal Restraint Petition? Yes No

The document being Filed is:

- Designation of Clerk's Papers Supplemental Designation of Clerk's Papers
- Statement of Arrangements
- Motion: _____
- Answer/Reply to Motion: _____
- Brief: Appellant's
- Statement of Additional Authorities
- Cost Bill
- Objection to Cost Bill
- Affidavit
- Letter
- Copy of Verbatim Report of Proceedings - No. of Volumes: _____
Hearing Date(s): _____
- Personal Restraint Petition (PRP)
- Response to Personal Restraint Petition
- Reply to Response to Personal Restraint Petition
- Petition for Review (PRV)
- Other: _____

Comments:

No Comments were entered.

Sender Name: Jay Donovan - Email: donoj@foster.com

A copy of this document has been emailed to the following addresses:

donoj@foster.com
alstc@foster.com
vicky@vreeland-law.com
martad@atg.wa.gov
samud@foster.com