

FILED

SEP 16 2016

COURT OF APPEALS
DIVISION III
STATE OF WASHINGTON
BY _____

**COURT OF APPEALS, STATE OF WASHINGTON
DIVISION III**

CASE NO. 286827

JACK KRYSTAL,

Appellant,

vs.

**THOMAS R. DAVIS and
STAT NETWORK SOLUTIONS, LLC,**

Respondents,

and

LANCE B. HAYNIE,

Defendant.

BRIEF OF APPELLANT

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STATUTES

RCW 7.24.01021

RCW 7.24.02021

RCW 25.15.24523

1. Introduction.

This case involves Appellant Jack Krystal's interest in STAT Network Solutions LLC ("STAT"). Mr. Krystal sued Mr. Davis and STAT under a variety of theories but the parties agreed to try the issue of Mr. Krystal's ownership of STAT first. That trial was to the court, held October 12 through 15, 2009. At the end of that trial the Trial Court entered *Findings of Fact, Conclusions of Law and Judgment* (CP 423-429) which found for STAT and Mr. Davis. Mr. Krystal appeals.

The issue in this case is not purely legal. That is, while Mr. Krystal is the first to admit that his ownership interest in STAT was never proved by a specific written and signed document – the legal analysis – Mr. Krystal provided the Trial Court with abundant evidence of his recognition as an owner of that company by others, including Mr. Davis, demonstrating that during the critical times all parties and STAT itself recognized Mr. Krystal's ownership interest. It was only after Mr. Davis recognized that Mr. Krystal could not produce the necessary specific document that Mr. Krystal's ownership was discarded. The equities in the case require the Court to right that wrong.

2. Assignments of Error.

1. The Trial Court erred when it completely ignored substantial evidence proving Appellant Jack Krystal's equitable claim of ownership of a 30% interest in STAT Network Solutions, LLC.

Issue Pertaining: When a case is presented to the court under both legal and equitable claims, may a court dispense with the entire case by merely ruling on one claim over the other?

Issue Pertaining: Are the formal members of a limited liability company estopped from denying the membership of a person not formally admitted to the company after the company itself has represented to others, including a governmental creditor, that the person claiming membership does in fact have an ownership interest?

2. Conclusion of Law Nos. 4 and 7 are not supported by substantial evidence, in light of the testimony of witnesses and documents produced at trial, which demonstrate that Jack Krystal was a recognized as a 30% owner of STAT Network Solutions LLC, from its inception.

Issue Pertaining: When a case is presented to the court under both legal and equitable claims, may a court dispense with the entire case by merely recognizing the facts that disprove the legal claim but not the equitable claim?

3. Conclusions of Law Nos. 4 and 7 are inconsistent with the substantial evidence produced at trial, showing significant equitable bases for the Court to rule that Jack Krystal was a 30% owner of STAT Network Solutions LLC, from its inception.

Issue Pertaining: When a case is presented to the court under both legal and equitable claims, may a court simply rule that because the legal claim has been denied, the equitable claim must follow?

3. Statement of the Case.

Plaintiff Jack Krystal is a California businessman with diverse business interests. RP 183. Mr. Krystal met Defendant Lance Haynie in 1998 or 1999 while Mr. Krystal was in Spokane on business. RP 187, 189. At the time, Mr. Haynie worked for Skyway Partners, a cable television design, installation and programming company which was owned by a friend of Mr. Krystal's. RP 187-188.

In the spring of 2003 Messrs. Krystal and Haynie began planning to start a limited liability company together. RP 190-191. They tentatively called the company "Boomerang" (EX. 1) but later decided on the name "STAT Network Solutions." RP 100-101, 228-229, 276-277. The plan was to purchase Sanswire from Tsunami and its owners Mike Funk and Cory Colvin (RP 232-236) who did business with Davis Communications, Inc., owned by Mr. Davis, and Eastern Washington University. RP 239-240.

The intent was to incorporate the Sanswire business into STAT, including the Davis Communications and Eastern Washington University business. RP 241.

On May 23, 2003, Messrs. Haynie and Krystal drafted "Deal Points" concerning the new business. EX 1. An entity known as "LBH Communications" was to manage the company with 70% ownership, 40% of which was to be sold to investors. *Id.* It was agreed that Mr. Krystal would act as Chief Executive Officer (CEO) but that he would be an equal partner with Mr. Haynie, each holding a 30% stake in the company, reserving 40% to raise additional funds from investors. RP 230. Mr. Krystal held final decision-making authority. EX. 1; RP 231. The Deal Points also included a recitation "reach agreement with Tsunami [Sanswire] to take over EWU/Cheney/Medical Lake" (EX. 1, p. 2), how investors would be added to the company, and the like.

Mr. Krystal had agreed to front money for the venture in the form of loans (EX. 111, 112, 113), beginning in June 2003. EX. 111. During that time Mr. Haynie and Mr. Krystal were discussing the terms of the notes and also the ownership agreement. EX. 4; RP 287. Mr. Krystal was in Northern California. RP 288. Mr. Haynie worked with Spokane attorney Cynthia Schwartz to prepare an LLC agreement for STAT. RP 195, 262; EX. 2. Mr. Krystal kept tabs on that project as well as in

lending money to the venture for start-up, pursuant to the Deal Points memo. EX. 4. However, Ms. Schwartz could not recall any conversations with Mr. Krystal regarding the formation of STAT. RP 195-196. By the time of the first loan, June 15, 2003, Mr. Haynie had already signed the LLC Agreement for STAT. EX. 2. Mr. Krystal's name was not included in the LLC Agreement. RP 263. Also, Mr. Haynie was named as manager whereas LBH Communications was the intended manager. RP 240-241. While he did not find out about those issues until perhaps a month later (RP 235), Mr. Krystal addressed that concern and others to Mr. Haynie and was assured that the document would be corrected. RP 236-237.

After the LLC was formed by Mr. Haynie, Messrs. Krystal and Haynie continued negotiations with Mr. Funk and Mr. Colvin regarding the purchase of Sanswire. RP 238-239. At that time Sheila Selder, the Sanswire bookkeeper, understood Mr. Krystal to own a portion of STAT. RP 136-137. Funk and Colvin issued a memorandum of terms for an "Asset Purchase Agreement" to Mr. Krystal and Mr. Haynie dated June 11, 2003, regarding the sale of Sanswire to Krystal and Haynie. EX. 3; RP 238. Mr. Funk understood "Boomerang" to be STAT. RP 101. Mr. Funk also testified that the deal would not have been considered if Mr. Krystal was not involved. RP 102. That deal included continuing "agreements with EWU and Davis Communications." EX. 3, p. 1.

On August 19, 2003, the Asset Purchase Agreement between STA and Sanswire was executed. EX. 6. As part of the deal, Messrs. Funk and Colvin each acquired a 5% stake in STAT. *Id.* The Agreement transferred all of Sanswire's interest in contracts with EWU and Davis Communications. EX. 6, p. 6. Knowing Boomerang to be STAT, Mr. Funk also believed that Mr. Krystal owned a percentage of STAT. RP 101. Mr. Krystal conducted a majority of the negotiation with Mr. Funk. RP 107-108. Ms. Schwartz also provided legal services regarding the asset purchase from Funk and Colvin (EX. 6) and worked directly with Mr. Krystal on that project. RP 196-197. Mr. Colvin and Mr. Funk were formally admitted as members of STAT on August 19, 2003. EX. 7.

After Messrs. Funk and Colvin purchased their respective 5% interests in STAT, at Mr. Haynie's instruction attorney Schwartz prepared meeting minutes for execution in August 2003 admitting Mr. Krystal as a member of STAT. EX. 5; RP 199. Mr. Krystal continued to press Mr. Haynie for his formal admission to the company, either by amendment of the LLC Agreement or by some other formal document. EX 11; RP 299. Yet Mr. Krystal was not concerned, given his experience with business deals for over 40 years. RP 329-330.

Ms. Schwartz continued to work with both Mr. Haynie and Mr. Krystal on other matters, into the fall of 2003. EX. 8. Mr. Haynie inquired

about documents formally admitting Mr. Krystal in October 2003. EX. 9. In November 2003 Ms. Schwartz prepared a document entitled "Minutes of the Meeting of Members" of STAT wherein Mr. Krystal was added as a member of STAT holding a 30% interest. EX. 10; RP 200. Email traffic demonstrates that Mr. Krystal was directly involved in that project. EX. 11. Ms. Schwartz emailed Mr. Haynie regarding Mr. Krystal's membership and what was necessary to complete that formality. EX. 11. Ms. Schwartz testified that she was also familiar with the email exchanges between Mr. Haynie and Mr. Krystal. RP 203, 208, 210. Thereafter Ms. Schwartz found it impossible to get Mr. Haynie to act on those documents, to secure signatures. RP 201. Her written plea to Mr. Haynie in January 2004 was unanswered (EX 108); the "Minutes" document was never signed by the admitting members. While Mr. Haynie apparently did not pursue signature on either of the LLC documents that Ms. Schwartz had prepared at his direction, on December 16, 2003, he did sign both the handwritten Deal Points of May 2003, as well as a typed copy of the Deal Points which provided for Mr. Krystal's interest. EX. 1, 12; RP 101. Mr. Funk testified that the typed and signed "Deal Points" memo of December 16, 2003, supported the STAT purchase of Sanswire. *Id.* That is, he understood Jack Krystal to own 30% of STAT.

In the spring of 2004 Mr. Davis inquired about buying into STAT. RP 8. Mr. Haynie advised Mr. Krystal of the potential transaction and Mr. Krystal replied that STAT was not for sale. EX.13. Mr. Krystal discussed the matter with Mr. Davis at that time. RP 306-308. He testified that he had several meetings with Mr. Davis on the subject of ownership and percentage. RP 309; EX. 16. Even though Mr. Davis was interested in buying 49% of the company, no more than 30% of the company was for sale. *Id.*

Mr. Krystal also called Ms. Selder to direct that tax returns were required for STAT for the years 2003 and 2004. RP 137-138. Ms. Selder was responsible for preparing the Form K-1 documents, representing ownership of the company. RP 138. She worked with CPA Ralph Coston. *Id.* Mr. Krystal and Mr. Haynie were adamant that the returns be completed. RP 138-139. Therefore, a meeting was held which included Messrs. Davis, Krystal, Haynie, Funk and Colvin, along with Ms. Selder. RP 139. The meeting was held at Mr. Davis's office (RP 139) and Mr. Krystal attended by telephone. RP 140, 317.

During that meeting the ownership of STAT was discussed. Mr. Funk testified that the owners were agreed to be Funk and Colvin at 5% each, Krystal owned 30% and Haynie owned 60%. RP 111-112, 317. According to Mr. Funk, Mr. Davis knew of Mr. Krystal's ownership in

STAT because of that meeting. RP 126. In fact, Mr. Krystal participated in ownership meetings on a regular basis. RP 113. Ms. Selder testified that Mr. Coston required proof of the ownership interest of each member. RP 140. Mr. Krystal directed her to get the information from Mr. Haynie. RP 318. Ms. Selder asked Mr. Haynie to provide that information, and Mr. Haynie provided a copy of the unsigned Meeting Minutes from August 2003. RP 141, 148-149; EX. 5. Ms. Selder presented that copy to Mr. Davis, who authorized its use as proof of ownership. RP 141. Ms. Selder testified that Mr. Davis instructed her in the preparation of the 2003 and 2004 tax returns – "how he wanted them done." RP 153.

Two tax returns were necessary for 2004 because there had been a change in ownership – Mr. Davis had purchased a portion of the company. RP 142. Ms. Selder explained at trial that the first half 2004 return required Mr. Haynie's signature. RP 142. That return also contained a Form K-1 representing Mr. Krystal to be a 30% owner of STAT. RP 143. The second half 2004 return also showed Mr. Krystal to be a 30% owner but Mr. Haynie's interest had dropped to 10%. RP 143. However, that second half 2004 return was never filed, at the instruction of Mr. Davis and STAT counsel. RP 143-144.

While records are incomplete, it is undisputed that Mr. Krystal was issued a 2003 Schedule K-1 (Form 1065) by STAT Network Solutions

LLC on November 3, 2004, memorializing Mr. Krystal's 30% ownership interest in STAT for the 2003 Federal tax return. EX. 17 pp. 18-21. Likewise, the 2004 Federal tax return for STAT for the period January 1 through July 31, 2004, contained a Schedule K-1 for Mr. Krystal indicating Mr. Krystal's 30% ownership interest in STAT. EX. 17, pp. 16-17. Please note that the end-date of that first half 2004 return coincides with Mr. Davis' purported purchase of 50% of STAT. And, Mr. Davis testified that he could not deny the accuracy of the representations of Mr. Krystal's ownership in those returns. RP 37.

Mr. Davis was fully aware that Mr. Krystal was directly involved in the determination of what might be sold to Mr. Davis. RP 17; EX. 16 p. 2. On July 11, 2004, Mr. Haynie wrote to Mr. Davis to explain discrepancies between what he wanted to sell to Mr. Davis. EX.16. Obviously Mr. Krystal had told Mr. Davis something that Mr. Davis found unacceptable and Mr. Davis had turned to Mr. Haynie to straighten that out. *Id.* Mr. Haynie represented to Mr. Davis that he could purchase up to 35% of STAT. *Id.* Mr. Haynie also made it very clear that he was in a great hurry to make the sale to Mr. Davis. *Id.*, p. 2. Mr. Krystal was not made aware of those communications until the following February. *Id.*, p. 1. By then it was too late for Mr. Krystal to do anything to prevent what ultimately led to this lawsuit.

Unknown to Mr. Krystal, on July 29, 2004, Mr. Haynie attempted to sell of 50% of STAT to Mr. Davis. RP 9-11; EX. 14. Pursuant to that "Deal Points" memorandum, signed by both Haynie and Davis, each would own 50% of STAT. Neither Mr. Funk's nor Mr. Colvin's 5% interest were mentioned. In fact, Mr. Funk testified that he had no idea that transaction was taking place, at that time. RP 126. Mr. Krystal did not find out about that "deal" until February 2005. RP 310-311; EX. 16.

Sheila Selder, who had been employed by Sanswire, knew Mr. Krystal as an owner of STAT. RP 136-137, 138. At the time Mr. Davis proposed buying a part-ownership in STAT – spring 2004 – Ms. Selder specifically told both Mr. Haynie and Mr. Davis that Mr. Haynie could sell only 50% of what he owned in STAT and not 50% of the company since Mr. Krystal owned 30% of STAT. RP 144-146. Mr. Davis admitted at trial that he understood Mr. Krystal to be an owner at that time, July 11, 2004. RP 17-18. Mr. Davis also admitted talking with Mr. Krystal about purchasing a portion of STAT. RP 25.

Regardless, Mr. Davis and Mr. Haynie had consulted Spokane attorney Mike Perrizo to prepare the documentation necessary for the sale of an interest in STAT to Mr. Davis. RP 22. By letter dated August 4, 2004, Mr. Perrizo advised Mr. Davis and Mr. Haynie of several issues attendant to that transaction, including:

Regarding Jack Krystal, I was not provided with any agreement showing whether he made a capital contribution in the LLC, or a loan. I would suggest that it would be prudent to obtain a statement from Mr. Krystal prior to completing this transaction, indicating the balance necessary for a pay off and an acknowledgement that he holds no equity in the LLC.

EX. 15, p. 2. Mr. Davis testified that he understood Mr. Perrizo's advice but that he personally did not follow up on it, to secure some sort of relinquishment of ownership from Mr. Krystal. RP 28-29. He relied on Mr. Haynie to take care of the issue. *Id.* Mr. Davis has never seen a document whereby Mr. Krystal's interest in STAT was extinguished. RP 20, 30.

Mr. Davis then turned his attention to pushing Messrs. Colvin and Funk out of STAT. RP 146-147. According to Ms. Selder, there was tension between Mr. Davis, Funk and Colvin, and "one of them was going to push them out by force." RP 147. Mr. Davis also initiated litigation against Mr. Haynie regarding ownership. RP 155, 49. Mr. Davis testified that he directed that lawsuit. RP 49. Therefore at trial Mr. Davis was questioned regarding numerous representations made in briefs from that case, verifying Mr. Krystal's ownership of STAT.

Mr. Davis was asked about representations made by STAT forensic accountant Dan Harper (RP 53) but acknowledged that Ms. Selder worked with Mr. Harper "95% of the time." RP 57. Mr. Harper

represented that Mr. Krystal owned 30% of STAT in that lawsuit, and yet Mr. Davis could not agree with that during the trial herein. RP 57-58. When asked about Ms. Selder's January 2006 Declaration from that lawsuit, representing that Mr. Krystal was in fact an owner of STAT, again in this suit Mr. Davis denied that fact. RP 60-61, 62. He also disputed the accuracy of a statement in a motion *in limine* that represented STAT ownership as including Davis, Colvin, Funk and Krystal (RP 62-63) stating "I wouldn't necessarily include Mr. Krystal in that." RP 63. Likewise, Mr. Davis testified that a previous argument in STAT and Davis v. Haynie – that "Lance Haynie is accountable for his actions to Michael Funk, Cory Colvin, Jack Krystal and Thomas Davis, all of whom claim rights as members of STAT Network Solutions at various points in time" – was incorrect (RP 64-65) but only with regard to the inclusion of Jack Krystal as a member. RP 65. Yet Mr. Davis cannot testify as to when Mr. Krystal ceased to be a member of STAT. RP 65.

Ms. Selder was also questioned about representations made in that litigation and specifically about the same Declaration that Mr. Davis had rejected, which she submitted on behalf of STAT and Mr. Davis at the direction of counsel for STAT, and she agreed that the testimony in that Declaration was accurate; that Mr. Krystal was in fact an owner of STAT during the time period in 2004. RP 156-157, 159-160. Ms. Selder had

nothing to gain from her testimony at trial and everything to lose since she was still employed by Mr. Davis and STAT at that time. RP 133.¹

Mr. Davis entered into an agreement with Messrs. Colvin and Funk the first week of December 2004, which ratified Mr. Haynie's 50% transfer of membership in STAT to Davis. EX. 114. Also in 2004 Mr. Davis sued Mr. Haynie, which resulted in Mr. Davis becoming the majority stockholder of STAT. RP 39. Mr. Davis testified that he then voted himself in as the managing member of STAT in January 2005 and seized control of the company. RP 4-5. Mr. Haynie did not agree to that. RP 5. That left Mr. Colvin and Mr. Funk as 5% owners, and while Mr. Davis was then successful in buying Mr. Colvin's interest (RP 67), he did not secure Mr. Funk's 5%. RP 96. By the end of the process Mr. Davis purported to own 95% of STAT. RP 94-95.

Even with all of that Mr. Krystal was not merely standing by. In April 2005 Mr. Krystal served as a mediator between Mr. Davis and Mr. Haynie. RP 43-45. Even at that time Mr. Davis knew Mr. Krystal had an ownership interest in STAT. RP 45. Yet he had to make sure that Mr. Krystal was out of the way.

As the *coup d'grace*, Mr. Davis and his counsel instructed Ms. Selder and the company's accountant, Ralph Coston, to *amend* the 2003 and 2004 Federal tax returns for STAT to include different K-1 forms. RP

90-91, 161-164. Mr. Krystal was not consulted regarding those amendments. RP 319. When that was accomplished in November 2006, Lance Haynie was represented to own 90% of STAT in 2003 and the first half of 2004 (with Colvin and Funk each owning 5%). EX. 117 and 118. Haynie had nothing to do with the amended tax returns, even though he was required to sign the 2003 return. RP 175-176. According to Mr. Davis, the amended tax returns for 2003 and 2004 are the only documents that "prove" that Mr. Krystal's 20% interest was extinguished. RP 67, 70. Mr. Krystal's 30% interest, previously reported to the IRS in the original 2003 and 2004 returns, simply vanished.

On April 20, 2007, Mr. Krystal filed an Amended Complaint against STAT Network Solutions, LLC, Mr. Davis and Mr. Haynie under a number of theories (CP 1-11), including a declaration that Mr. Krystal was in fact a 30% owner of STAT. CP 1-11. On May 12, 2008, the parties stipulated that the claims for accounting would be tried separately from Mr. Krystal's claim of ownership. CP 114-115. A bench trial was held between October 12 and 15, 2009, after which Judge Paul Bastine ruled in favor of Mr. Davis and STAT on that issue. Over Mr. Krystal's Objections (CP 419-422), Judge Bastine entered *Findings of Fact, Conclusions of Law and Entry of Judgment In Favor Of Defendants Davis*

And STAT Network Solutions, LLC, on November 18, 2009, which included the following legal conclusion:

Plaintiff Jack Krystal has failed to meet his burden of proving that he has any legal *or equitable right* to be declared the owner of any Membership Interest in Stat Network Solutions, LLC.

Conclusion of Law No. 7, CP 428 (emphasis added).

Mr. Krystal has never been able to produce a single STAT corporate document – executed – which confirms his status as a member of STAT. While Mr. Haynie testified that he had seen such a document at some point (RP 265, 273), he also testified that Mr. Davis had taken control of all company documents during the litigation with Mr. Haynie. RP 265-266. At trial Mr. Krystal asked the Court to recognize the totality of the circumstances, the testimony of witnesses and the many documents that were admitted – signed and unsigned – to rule that Mr. Krystal was in fact a 30% owner of STAT. The Trial Court disagreed by completely dismissing Mr. Krystal's claim in equity for the reformation of the STAT records, to reflect his ownership interest in that company from the start.

Mr. Krystal is now frozen out of his rightful ownership interest in STAT Network Solutions, LLC, and seeks the appropriate relief from this Court. Based upon the exhibits and testimony admitted at trial, it is equitable to order that the STAT Network Solutions books be amended to

recognize Mr. Krystal as a 30% owner of that company from the date of its formation, June 4, 2005.

4. Argument and Authorities

A. The Standard of Review.

In reviewing the outcome of a bench trial the appellate court will consider all of the evidence presented to the trial court. Generally, the appellate court will review a trial court's decision following a bench trial to determine whether substantial evidence supports the trial court's findings of fact and whether those findings support the trial court's conclusions of law. *Hegwine v. Longview Fibre Co. Inc.*, 132 Wn.App. 546, 555, 132 P.3d 789 (2006), *aff'd*, 162 Wn.2d 340, 172 P.3d 688 (2007). Substantial evidence exists when there is a sufficient quantity of evidence to persuade a fair-minded, rational person that a finding is true. *In re Estate of Jones*, 152 Wn.2d 1, 8, 93 P.3d 147 (2004). Unchallenged findings of fact are verities on appeal. *Davis v. Dep't of Labor & Indus.*, 94 Wn.2d 119, 123, 615 P.2d 1279 (1980). The appellate court will view the evidence in the light most favorable to the prevailing party and defer to the trial court on issues regarding witness credibility and conflicting testimony. *Weyerhaeuser v. Tacoma-Pierce County Health Dep't*, 123 Wn.App. 59, 65, 96 P.3d 460 (2004). However, the appellate court will

review the trial court's conclusions of law *de novo*. *Sunnyside Valley Irrigation Dist. v. Dickie*, 149 Wn.2d 873, 880, 73 P.3d 369 (2003).

In this case several of the *Findings and Conclusions* were challenged by Mr. Krystal. CP 419-422. The Court entered *Findings of Fact* which found that documents admitting Mr. Krystal were never signed (FF 17) and that Mr. Krystal had never spoken with the attorney tasked by Mr. Haynie with preparing those documents. FF 18. CP 426. Mr. Krystal objected to both. CP 420. That merely set up the remainder of the Court's decision.

Mr. Krystal offered proposed Findings of Fact which memorialized the facts that (1) Mr. Davis understood that Mr. Krystal had an ownership interest in STAT in July 2004, when Mr. Davis purportedly purchased 50% of the company; (2) that Ms. Selder had warned Mr. Davis that Jack Krystal was an owner and that Mr. Haynie could only sell 50% of what Mr. Haynie owned, not the entire company; (3) that Mr. Colvin was never sure whether Mr. Krystal was an owner; (4) that Mr. Funk knew that Mr. Krystal was an owner even before Funk bought 5% in August 2003; (5) that attorney Perrizo had warned Mr. Davis and Mr. Haynie that there was uncertainty in Mr. Krystal's involvement, owner or lender; and (6) that neither Haynie nor Davis took any steps recommended by attorney Perrizo. CP 421. The Trial Court ignored those proposed Findings.

Furthermore, Mr. Krystal proposed additional Findings that were absolutely critical to the equity argument made by Mr. Krystal, being the preparation of federal tax returns for 2003 and 2004 that included Form K-1's specifically representing to the government that Mr. Krystal was a 30% owner, until November 2006, when those returns were amended and Mr. Krystal's ownership was erased. CP 421. The Trial Court ignored those proposed Findings as well. Therefore, the Court's basis for its Conclusions was entirely the fact that Mr. Krystal could not produce a signed document admitting him as a member of STAT. To that end Mr. Krystal proposed a Finding which memorialized Mr. Haynie's testimony that he had seen such a document but that Mr. Davis had taken control of all of the records (CP 421; RP 265-266) but the Trial Court rejected it, too.

Mr. Krystal submitted a Conclusion of Law which stated that "the only Members of STAT Network Solutions that had been recognized in formal written form were Lance Haynie, Corey Colvin and Michael Funk." CP 421. That was likewise rejected. Given the facts of Mr. Haynie's sale of an interest in STAT to Mr. Davis, Mr. Krystal proposed a Conclusion which recognized Mr. Haynie's ability to convey 50% of the company to Mr. Davis on July 14, 2004. CP 422. That was rejected and yet that was another critical aspect of the case supporting the Trial Court's decision. Mr. Krystal proposed a Conclusion that recognized the Court's

Findings regarding the lack of a signed document and the result that such a legal result excluded the equity case. CP 422. The Court rejected that too.

But even in light of all of that, it is *Conclusion of Law Nos. 4 and 7* (CP 428) that is simply unsupportable. Those *Conclusions* state:

4. As of July 29, 2004, when Lance Haynie and Tom Davis executed their "Deal Points" agreement whereby Davis purchased a 50% Membership Interest in Stat Network from Haynie in consideration for payment of \$650,000.00, the only Members of Stat Network Solutions, LLC were Lance Haynie, Cory Colvin and Michael Funk.

...

7. Plaintiff Jack Krystal failed to meet his burden of proving that he has any legal or equitable right to be declared the owner of any Membership Interest in Stat Network Solutions, LLC.

CP 428. Mr. Krystal took exception to those *Conclusions* (CP 422) since they completely ignored his equity case.

From the evidence produced at trial, including witness testimony acknowledging that Mr. Krystal had an ownership interest, the failed attempt at completing the STAT books to so reflect (EX. 5 and 10), Ms. Schwartz's testimony that those documents were produced at Mr. Haynie's direction (RP 199), Mr. Perrizo's warning to Mr. Davis (EX. 15), Mr. Davis's own admissions that he knew Mr. Krystal had an ownership interest in STAT (RP 16, 17, 18, 37, 45), and beyond that, the 2003 and 2004 federal Form K-1 documents specifically listing Mr. Krystal as a 30% owner of STAT (EX. 17), it is impossible to imagine a better case for

equitable reformation under *de novo* review of *Conclusion No. 7*. If anything, the evidence showed that in the end – November 2006 – Mr. Davis took full advantage of a technical omission from the STAT books and extinguished Mr. Krystal's ownership of STAT, once and for all. The inference from the timing of that event is striking: that Mr. Davis kept Mr. Krystal around until Davis could claim all but Mr. Funk's 5% interest. Once that had occurred, he instructed Ms. Selder to amend the returns. RP 162-163. Evidence of Mr. Krystal's ownership simply vanished. That inequitable conduct can only be remedied by reversing the Trial Court and remanding for the entry of an Order which requires the amendment of the STAT company books to reflect Mr. Krystal's ownership of that company, from June 4, 2003. The evidenced supports such a result.

B. Declaratory Judgment Authority.

Courts have the statutory authority to declare rights, status and other legal relations between parties to a civil action. RCW 7.24.010. Such declaratory judgments have the "force and effect of a final judgment or decree." *Id.* The Court's power to issue declaratory judgments includes the rights, status or legal relations of persons under a "deed, will, written contract or other writings constituting a contract..." RCW 7.24.020. Courts likewise have the power to determine questions of fact when such determinations are necessary or incidental to the declaration of legal

relations. *Trinity Universal Ins. Co. v. Willrich*, 13 Wn.2d 263, 124 P.2d 950 (1942). Mr. Krystal sought a declaratory judgment confirming that he owns a 30% ownership interest in STAT LLC, based primarily on equitable principals. The Trial Court simply ignored that evidence.

C. It Is Irrefutable That Mr. Krystal Was A Member of STAT LLC.

"The obligation to do justice rests upon all persons," including this Court. *Bill v. Gattavara*, 34 Wn.2d 645, 648, 209 P.2d 457 (1949). This obligation can be achieved through equity because "[t]he goal of equity is to do substantial justice to the contracting parties." *Mendez v. Palm Harbor Homes, Inc.*, 111 Wn.App. 446, 460, 45 P.3d 594 (2002). "Equity requires that to be done which ought to have been done." *Paullus v. J.B. Fowler*, 59 Wn.2d 204, 214, 367 P.2d 130 (1961). "Equity does not permit a wrong without a remedy" therefore "[a] court in equity has broad discretion to fashion a remedy to do substantial justice and end litigation." *Cogdell v. 1999 O'Ravez Family, LLC*, 153 Wn.App. 384, 390, 220 P.3d 1259 (2009). Mr. Krystal submitted a case in equity, which was rejected on legal grounds after a bench trial. CP 423-429. In the end the entire case depended on the fact that Mr. Krystal could not provide an executed document admitting his ownership in STAT. CP 427-428, *Conclusions 2, 3,6 and 7.*

There is no requirement either by statute or as a term of the LLC Agreement that as a condition precedent to membership a member's name must be listed in the LLC Agreement. *See*, RCW 25.15.245. It does not matter whether Mr. Krystal was listed in the LLC Agreement: the fact of the matter is that he formed the company with co-owner Lance Haynie, which provided him a 30% interest in STAT LLC, then "Boomerang." Both Mr. Krystal and Mr. Haynie testified to that fact. RP 228-229, 276-277.

Reformation is an equitable remedy designed to bring into writing that which is materially at variance with the parties' agreement in order to conform that agreement to reflect the intent of the parties. *Denaxas v. Sandstone Court of Bellevue*, 148 Wn.2d 654, 669, 63 P.3d 125 (2003). The purpose of reformation is to adequately express the agreement the parties made. *Childes v. Alexander*, 18 Wn.App. 706, 710, 571 P.2d 591 (1977). The principals stated in these cases apply directly to this case. Mr. Krystal seeks formal acknowledgement of his membership in STAT after all had agreed, either by writings or by conduct, that he was in fact a 30% owner of that limited liability company.

In Washington, the intent of the parties to a particular agreement may be discovered not only from the actual language of the agreement, but also from "viewing the contract as a whole, the subject matter and objective of the contract, all circumstances surrounding the making of the contract, and subsequent acts and

conduct of the parties to the contract, and the reasonableness of the interpretations advocated by the parties."

Bort v. Parker, 110 Wn.App. 561, 573, 43 P.3d 980 (2002), citing *Scott Galvanizing, Inc. v. N.W. EnviroServices, Inc.*, 120 Wn.2d 573, 579-580, 844 P.2d 428 (1993).

Of course this is not a contract formation case. The point is that Washington law makes it clear that matters outside the four corners of a document – such as the LLC Agreement (EX. 2) – are relevant and indeed important to the analysis of the parties' intent. In this case all manner of documents and testimony demonstrate that all parties concerned, and most notably Mr. Davis, understood Mr. Krystal to be a 30% owner of STAT. In fact, they all agreed that to be the case when reporting to the IRS. EX. 17, pp. 8, 16-17, 18-20. It would be incredibly unfair to now allow Mr. Davis and STAT to ignore those previous representations by self-serving convenience. Reformation is appropriate in order to protect the intent of the parties, even when one is not named in a critical document. See *Metropolitan Mortgage and Securities Company v. Reliable Insurance Company*, 62 Wn.2d 98, 390 P.2d 694 (1964), reforming a fire insurance policy to name the proper party in interest even though the policy contained a restriction on assignment.

If equitable claims are presented, "the focus remains on the equities involved between the parties" and those claims "are not dependent on the legality of the relationship between the parties. . ." *Vasquez v. Hawthorne*, 145 Wn.2d 103, 107, 33 P.3d 735 (2001). Equitable claims have no hard and fast rules, rather "must be analyzed under the specific facts presented in each case." *Id.* Equity and its subsequent doctrines "are generally designed to relieve certain parties under special circumstances from the harshness of strict legal rules." *Hyatt v. Dept. of Labor and Indus.*, 132 Wn.App. 387, 398, 132 P.3d 148 (2006).

Further, a trial court has equitable power to reform an instrument if there is clear, cogent and convincing evidence of a mutual mistake or a unilateral mistake coupled with inequitable conduct. *Wilhelm v. Beyersdorf*, 100 Wn.App. 836, 843, 999 P.2d 54 (2000). "Mutual mistake occurs if the intention of the parties is identical at the time of the transaction and the writing executed by them does not express that intention." *Id.*; *Snyder v. Peterson*, 62 Wn.App. 522, 527, 814 P.2d 1204 (1991). "The party seeking reformation only has to show that the parties agreed to accomplish a certain objective and that the instrument is insufficient to execute their intention." *Wilhelm*, at 845. Relief is not granted for the purpose of relieving against a hard or oppressive bargain or to give either party a better one, but simply to enforce the agreement as it

was made and to prevent an injustice which would result if this were not done. 45 Am.Jur. 584, § 3; *Meyer v. Young*, 23 Wn.2d 109, 115, 159 P.2d 908 (1945).

In this case at the very least a unilateral mistake by Mr. Krystal – the absence of a formal admitting document – coupled with Mr. Davis's inequitable conduct, requires the reformation of the STAT LLC Agreement. At most the evidence is clear that both Mr. Krystal and Mr. Davis were mistaken since Mr. Krystal thought his interest was certain and Mr. Davis knew that Mr. Krystal had such an interest, used it to his advantage when the opportunity presented itself and then in the end arranged to have it extinguished. In either case, the equities require the reformation of the STAT Network Solutions, LLC Agreement.

(1) Equity Will Prevent Mr. Davis And STAT From Asserting Mr. Krystal Lacks Ownership Interest in STAT LLC And Must Reverse Mr. Davis's Unconscionable Enrichment Scheme.

"There is no question but that equity has a right to step in and prevent the enforcement of a legal right whenever such an enforcement would be inequitable." *Arnold v. Melani*, 75 Wn.2d 143, 152, 449 P.2d 800 (1968) (citing *Thisius v. Sealand*, 26 Wn.2d 810, 818, 175 P.2d 619 (1946)). Prior cases have engaged in measuring equities between the parties and refused to enforce a legal right. *E.g. Malo v. Anderson*, 62

Wn.2d 813, 816, 384 P.2d 867 (1963) (stating "[t]he manner in which she [obtained her divorced husband's realty] . . . merits no stamp of judicial approval").

In prior cases the relief . . . afforded has been somewhat incorrectly referred to as a "balancing of equities." This doctrine is rather the judicial recognition of a circumstance in which one party uses a legal right to gain purchase of an equitable club to be used as a weapon of oppression rather than in defense of a right. It is a contradiction of terms to adhere to a rule which requires a court of equity to act oppressively or inequitable and by rote rather than through reason.

Arnold, at 153.

This case is no different than prior cases refusing to enforce a legal right. Here, there is no single document, signed by the members of STAT LLC, which admits Mr. Krystal into membership. Although the current members of STAT LLC have the *legal* right to deny Mr. Krystal as a member, the equities of the action merit no such stamp of judicial approval. The *Findings of Fact and Conclusions of Law* in this case simply disregard the equitable claim made by Mr. Krystal, other than to merely state that the claim failed. CP 428, *Conclusion* No. 7.

The record cited in Section 3. of this *Brief* amply demonstrates that from the outset of the formation of STAT, Mr. Krystal was recognized as a member and was actively involved in STAT business. Mr. Krystal was the prime negotiator in matters involving Mr. Funk and Mr. Colvin. RP

102, 106, 108. Attorney Schwartz, hired by Mr. Haynie, testified that the formal documents admitting Mr. Krystal were prepared and forwarded to Mr. Haynie, who merely never got around to signing them. RP 201. She also dealt directly with Mr. Krystal. RP 196-197; EX. 8, 9, 11. In the meantime Mr. Krystal was represented as a 30% member to the IRS. EX. 17. It was only after Mr. Davis assumed control, litigated Mr. Haynie's interest into oblivion and purportedly bought out all but 5% of the company that Mr. Davis decided to leave no loose ends: he and counsel then instructed Ms. Selder to see to the preparation of amended tax returns (RP 162-163; EX. 117, 118) which erased even the memory of Jack Krystal from STAT. The unfairness is obvious and yet the Trial Court seemingly ignored all of that evidence because there was no single sheet of paper that admitted Mr. Krystal as a member of STAT. CP 427-428, *Conclusions* 2, 3, 6 and 7. A court should not, in good conscience, allow a party to avoid its responsibilities on a mere technicality. *Metropolitan Mortgage and Securities Company v. Reliable Insurance Company*, 62 Wn.2d 98, 102, 390 P.2d 694 (1964). That is exactly the result of the bench trial in this case.

(2) Equity Must Recognize The Actions Of The Parties As Acknowledgement Of Mr. Krystal's Ownership Interest In STAT.

During the trial counsel for Mr. Krystal inquired of Mr. Davis and Ms. Selder regarding previous litigation between Messrs. Davis and Haynie. Questions were presented exploring the fact that in an attempt to demonstrate the gravity of the situation involving STAT, Mr. Davis and STAT counsel directed STAT bookkeeper Sheila Selder to sign a declaration in which she swore that Mr. Krystal was an "owner" of STAT. RP 157-160, 176. Even though Mr. Davis denied the accuracy of identical representations made in other pleadings in that previous litigation (RP 53, 57-58, 60-61, 62-63, 64-65), it was clear from Ms. Selder's testimony that when it suited Mr. Davis, Mr. Krystal was trotted out before the Court as an owner of STAT. This state recognizes the concept of judicial estoppel. See Deveny v. Hadaller, 139 Wn.App. 605, 161 P.2d 1059 (2007). Those representations, along with the affirmative representation of Mr. Krystal's ownership to the IRS (EX. 17), should be deemed conclusive evidence that Mr. Krystal was in fact a member of STAT from its inception. Stated another way, if there is no document which formally admitted Mr. Krystal, all of the evidence shows that he was recognized as an owner from the outset of the company in 2003.

Mr. Krystal and Mr. Haynie formed a contract on May 23, 2003 when they arrived upon the "Deal Points." EX. 1, 12. The fact that Mr. Haynie did not sign the document until later that year is of no legal consequence, as he had expressed his unequivocal acceptance of the points. The Deal Points concluded that Mr. Krystal was to hold a 30% stake in STAT LLC. *Id.* Mr. Funk recognized that fact at that time. RP 101. Whatever name the company subsequently took, the fact of the matter remained: Jack Krystal was entitled to 30% of STAT. Mr. Davis presented nothing to rebut that testimony.

Instead of honoring Mr. Krystal's ownership interest, Mr. Haynie sold Mr. Krystal's interest to Tom Davis. EX. 14. Mr. Davis was by no means an innocent purchaser. Instead, testimony and documentary evidence demonstrated without question that he knew or should have known of Mr. Krystal's interest in the company at the time he purchased his shares from Mr. Haynie.

Even before he was a member of STAT himself Mr. Davis had been a part of the team that prepared the 2003 and 2004 federal income tax returns which both represented, to the Internal Revenue Service, that Mr. Krystal was a 30% owner of STAT. EX. 17; RP 32-36, 111-112, 139, 317. Mr. Davis had been warned by Ms. Selder that Mr. Haynie could only sell half of what Mr. Haynie owned (RP 144-146) and Mr. Davis stated "I

have heard it stated, but I did not accept it." RP 20. Attorney Michael Perrizo warned Mr. Davis that the issue of Mr. Krystal's ownership was very real. EX. 15. Mr. Davis failed to rebut any of that evidence, he merely denied it.

Mr. Davis blames Mr. Haynie for his own failure to perform due diligence, to ensure that Mr. Krystal did not in fact have an ownership or that his ownership had been extinguished by the repayment of the promissory notes. RP 16, 18,19, 20, 24, 28, 29, 30. It is striking that even after consulting attorney Perrizo, Mr. Haynie and Mr. Davis could not decide how much of the company was really for sale. EX. 13, 14, 16. Mr. Davis later tried to clean that up by Agreement with Messrs. Colvin and Funk (EX. 114) and then he attacked Haynie with litigation, using Mr. Krystal's ownership as a weapon. The inference is blaring: Mr. Davis *knew* that Mr. Krystal was an owner and held on to that fact so long as it was useful to him.

In the end, in 2006 Mr. Davis commanded the amendment of the tax returns (RP 68-69, 162-163; EX. 117, 118) and then denied any ownership to Mr. Krystal. By doing that Mr. Davis acknowledged that Jack Krystal did in fact have an ownership interest in STAT, just not formally on the books of the company. A common law conversion occurs where the defendant willfully interferes with, or deprives an owner of his

property without justification. *Richards v. Seattle Metropolitan Credit Union*, 117 Wn.App. 30, 36, 68 P.3d 1109 (2003), *rev. denied* 150 Wn.2d 1035 (2004):

An innocent third party purchaser from a willful trespasser/converter may be held liable for conversion because knowledge that the goods are converted is not essential to establish culpability...Such a good faith purchaser may be held liable if plaintiff demonstrates intent to exercise control over plaintiff's property inconsistent with plaintiff's rights...proof of identification of the converted property in the hands of a third party purchaser must be reasonably certain.

Id. Using the law of conversion by analogy, Mr. Davis merely extinguished the evidence of Mr. Krystal's ownership by amending the tax returns in 2006. He was the managing partner, having forced his way into that seat in January 2005. RP 4-5. Mr. Davis merely kept Jack Krystal involved until he was finished with Mr. Haynie (RP 161), and then he directed the amendment of the tax returns. Why would Mr. Davis do that if there was not concern over Mr. Krystal's lack of ownership in STAT?

The inequity of allowing Mr. Davis to lay claim Mr. Krystal's 30% ownership in STAT as his own is stunning. It was only after the 2006 amendment of the first half 2004 federal tax returns (EX. 117, 118) was completed that Mr. Davis had completed his paper trail, starting with his "deal points" of July 29, 2004. EX. 14. Since that document purported to sell 50% of STAT to Mr. Davis when 50% was not available, Mr. Davis

sought ratification from Messrs. Funk and Colvin in December 2004. EX. 114. He then sued Lance Haynie into the ground. "As of January 7th [2005], the court said that I had the majority stockholder (*sic*)." RP 39. That was a federal lawsuit in which Mr. Krystal was not a party. RP 92-93. When that was completed, he directed a new Form K-1 for Mr. Haynie for 2003 and 2004 (EX. 117, 118) which magically stated a 90% STAT ownership in Mr. Haynie which retroactively supported the "deal points" of July 2004, selling 50% of the company to Mr. Davis. EX. 14. The circuit was closed and Mr. Krystal was out.

5. Conclusion.

The entire defense of the case was based upon the fact that Mr. Krystal could not produce a copy of a signed document admitting him to membership in STAT. By the same token there is no corporate document that extinguishes Mr. Krystal's 30% ownership, much the same as there is no corporate document that reduced Mr. Haynie's membership in STAT from 50% to 40% (RP 87-89) or that transferred Mr. Haynie's membership interest to Mr. Davis. It just happened. There was a representation to the IRS that Mr. Haynie owned 60% of STAT (EX. 17, p. 5, 14) for the first half of 2004, later amended to 90% for that period. EX. 118 p. 5. None of those variations are reconciled in any LLC books. With all of these percentages floating around in the case Mr. Davis now claims to own 95%

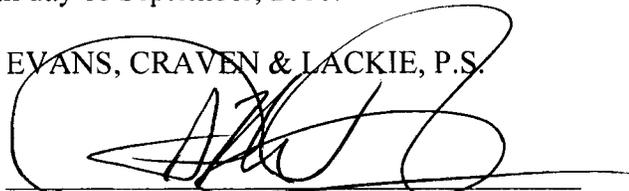
of STAT and relies on purely legal argument in the defense that Mr. Krystal has failed to prove ownership by documentation. The Trial Court apparently agreed, dismissing the equity claim without any specific Findings of Fact or in any specific Conclusion of Law.

Mr. Krystal respectfully submits that he presented layer after layer of evidence supporting his request for reformation of the STAT corporate books, to formally document his 30% ownership interest. Equity goes beyond the legal requirements for contract or company formation and looks at the conduct of the parties themselves. In this case Mr. Davis clearly saw a fantastic opportunity in STAT and there is no crime in that. What is unconscionable is a result which allowed Mr. Davis to systematically eliminate all but one member, through purchase or litigation and finally, in one stroke, through the amendment of tax returns. Everyone involved in this matter knew Mr. Krystal was an owner of STAT, from the outset.

With all respect due to the Trial Court, Mr. Krystal submits that the Findings of Fact and Conclusions of Law rejecting his case on purely legal grounds are erroneous. The case was tried as an equity case and that claim received merely a one word reference in the decision. It is within this Court's discretion to order the reformation of the STAT corporate records to reflect Mr. Krystal's 30% ownership of that limited liability company.

SUBMITTED this 16th day of September, 2010.

EVANS, CRAVEN & LACKIE, P.S.

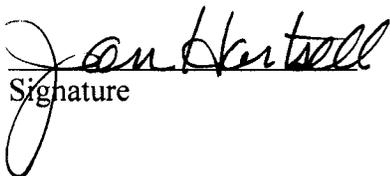


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CERTIFICATE OF SERVICE

Pursuant to RAP 18.5, the undersigned hereby certifies under penalty of perjury under the laws of the state of Washington, that on the 16 day of Sept., 2010, the foregoing was delivered to the following persons in manner indicated:

Robert Hailey Randall & Danskin, P.S. 1500 Bank of America Bldg. 601 W. Riverside Avenue Spokane, WA 99201-0653	Via Regular Mail <input type="checkbox"/> Via Certified Mail <input type="checkbox"/> Via Facsimile <input type="checkbox"/> Hand Delivered <input checked="" type="checkbox"/>
Lance Haynie 2170 Bellerive Lane Coeur d'Alene, ID 83814	Via Regular Mail <input checked="" type="checkbox"/> Via Certified Mail <input type="checkbox"/> Via Facsimile <input type="checkbox"/> Hand Delivered <input type="checkbox"/>


Signature

9/16/10
Date

Spokane
Place