

No. 93824-5
(Court of Appeals No. 74611-1-I)

**IN THE SUPREME COURT
OF THE STATE OF WASHINGTON**

FUTURESELECT PORTFOLIO MANAGEMENT, INC.,
FUTURESELECT PRIME ADVISOR II LLC, THE MERRIWELL
FUND, L.P., and TELESIS IIW, LLC

Plaintiffs/Petitioners,

v.

TREMONT GROUP HOLDINGS, INC., TREMONT PARTNERS, INC.,
OPPENHEIMER ACQUISITION CORPORATION,
MASSACHUSETTS MUTUAL LIFE INSURANCE CO., GOLDSTEIN
GOLUB KESSLER LLP, ERNST & YOUNG LLP and KPMG, LLP

Defendants/Respondents.

**SUPPLEMENTAL BRIEF OF PETITIONERS FUTURESELECT
PORTFOLIO MANAGEMENT, INC., FUTURESELECT PRIME
ADVISOR II LLC, THE MERRIWELL FUND, L.P., and
TELESIS IIW, LLC**

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I. INTRODUCTION

FutureSelect invested hundreds of millions of dollars on behalf of Washington investors, including Washington retirees' retirement funds. FutureSelect based its investment decisions on statements made by KPMG, one of the largest accounting firms in the world. KPMG's statements were false—KPMG signed its name to billions in fake assets—and FutureSelect's investments were worthless.

FutureSelect and its devastated investors are now being asked to pay millions to litigate their claims twice—first in a forced arbitration FutureSelect did not agree to, and then again in a Constitutionally-required jury trial. If it is a war of attrition, KPMG and its \$30 billion in world-wide revenues will win. FutureSelect asks that the outcome be about the correct law and facts.

This Court has the power to get the law right—parties should have the right to appeal orders to compel arbitration just like orders denying arbitration. Orders to compel arbitration breach a fundamental, Constitutional right—the right to a jury trial—and require parties to actually spend additional money and time just for the opportunity to have its Constitutional right enforced. Denying appeal until after the money is spent and the time is lost should *not* be the law in Washington. The Supreme Court respectfully should reverse the courts below.

II. ISSUE PRESENTED

The issue before this Court is whether orders compelling arbitration are immediately appealable.

III. FACTS RELEVANT TO THIS APPEAL

FutureSelect lost nearly \$200 million in its investments in the Rye Funds.¹ The Rye Funds had been audited by two auditors—KPMG from 2004-2007 and by Ernst & Young LLP (“EY”) from 2000-2003—pursuant to engagement letters to which FutureSelect was not a party and did not sign. Each year, KPMG and EY negligently stated that the Rye Funds’ financial statements contained no material misstatement. In fact, the financial statements contained nearly no real assets and were wrong by over a billion dollars.

In 2011, on defendants’ motions, the King County Superior Court dismissed FutureSelect’s claims against EY and four other defendants² and granted KPMG’s motion to compel FutureSelect to arbitrate. KPMG had submitted to the Superior Court a form order with two blank “check boxes”—one for arbitration and one to dismiss—and the trial court checked “arbitration.” CP 400-01.

¹ The “Rye Funds” include Rye Select Broad Market Fund, L.P., Rye Select Broad Market Prime Fund, L.P., and Rye Select Broad Market XL Fund, L.P. The Rye Funds invested almost exclusively with Bernard Madoff and his companies.

² The other defendants were Tremont Group Holdings, Inc., Tremont Partners, Inc., Oppenheimer Acquisition Corporation and Massachusetts Mutual Life Insurance Co.

Although every *other* order entered that day by the Superior Court was reversed, *see FutureSelect Portfolio Mgmt., Inc. v. Tremont Grp. Holdings, Inc.*, 175 Wn. App. 840, 894-95, 309 P.3d 555 (2013) (“*FutureSelect P*”) and *FutureSelect Portfolio Mgmt., Inc. v. Tremont Grp. Holdings, Inc.*, 180 Wn.2d 954, 972-74, 331 P.3d 29 (2014) (“*FutureSelect IP*”), the Court of Appeals did not even consider the merits of FutureSelect’s appeal of the check box order compelling arbitration, instead ruling that FutureSelect could not appeal until final judgment had been entered. Greer Decl. in Support of KPMG’s Answer to Motion to Modify, Ex. D (Order Denying Discretionary Review and Granting Motion to Dismiss Review, Nov. 21, 2011).

On September 12, 2013, deciding a different case, this Court held that the Courts of Appeals *must* consider the validity of an arbitration clause as to the parties involved before compelling arbitration. *Hill v. Garda CL Northwest, Inc.*, 179 Wn.2d 47, 55, 308 P.3d 635 (2013) (“We find no support in the rules of procedure or case law for the Court of Appeals’ decision to compel arbitration without considering whether the arbitration clause is even valid.”).

On September 3, 2014, EY moved to compel arbitration on substantially the same grounds as KPMG. CP 402. On December 3, 2014, the Superior Court denied the Motion in a written opinion. CP 678.

In explaining its denial of EY's motion, the Superior Court held that Plaintiffs are *not* bound by the arbitration clause in EY's audit engagement agreements because Plaintiffs did not sign EY's agreements and their claims are direct claims against EY, not derivative claims. CP 692.

On December 17, 2015, a final judgment was entered against EY after a jury verdict in Plaintiffs' favor. CP 716. All claims against all defendants were resolved, except for the claims against KPMG.

After reaching resolution of its claims against all other defendants, FutureSelect filed an appeal on January 15, 2016, requesting review of the June 3, 2011 order of the Superior Court granting KPMG's motion to compel arbitration. CP 712. KPMG moved to dismiss this appeal. On May 19, 2016, the Commissioner of the Court of Appeals, Division I (hereafter, the "Commissioner"), granted KPMG's motion to dismiss. The Commissioner did not consider the issue of enforceability of the arbitration provision in the audit engagement letter, and merely dismissed the appeal as untimely.

On October 5, 2016, the Court of Appeals, Division I denied Plaintiffs' motion to modify the May 19, 2016, ruling by Commissioner granting KPMG's Motion to Dismiss FutureSelect's appeal of the Superior Court's order compelling arbitration. *FutureSelect Portfolio*

Mgmt. v. KPMG LLP, Notation Ruling, No. 74611-1-I (Wn. App. Div. 1 May 19, 2016). This Court ultimately granted review.

IV. ARGUMENT

A. **The Superior Court’s Order Compelling Arbitration Was Clearly Wrong**

FutureSelect’s claims against KPMG are not subject to arbitration because FutureSelect has never agreed to arbitrate any claim with KPMG.

The trial court literally checked a box on a proposed order submitted by KPMG with no explanation for the decision.

It is undisputed that FutureSelect was not a party to the contracts containing the arbitration clauses at issue here. FutureSelect cannot be bound to somebody else’s agreement to arbitrate. *Townsend v. Quadrant Corp.*, 173 Wn.2d 451, 460, (2012) (“[N]onsignatories are not bound by arbitration clauses.”); *Satomi Owners Ass’n v. Satomi, LLC*, 167 Wn.2d 781, 810, 225 P.3d 213 (2009) (“[A]rbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.”) (internal quotation marks omitted); *Woodall v. Avalon Care Center-Federal Way, LLC*, 155 Wn. App. 919, 935, 231 P.3d 1252 (2010) (“The strong policy favoring arbitration does not overcome the policy that one who is not a party to an agreement to arbitrate cannot generally be required to arbitrate.”).

In fact, in *this case*, under substantially identical circumstances and involving a substantially identical contract, the subsequent Superior Court found that FutureSelect was **not** subject to an arbitration agreement to which it never agreed. In the intervening litigation against EY, whose engagement agreement contained an arbitration clause materially identical to the clause contained in KPMG's audit engagement agreements, the Court determined that the arbitration provision was not enforceable against FutureSelect. CP 692.

The underlying order of the Superior Court compelling arbitration, which KPMG has fought tooth and nail to protect, is obviously wrong.

B. Forbidding Appeal of an Order Compelling Arbitration Harms Citizens of Washington

Requiring victims who have lost millions of dollars and their retirement savings to pay for the privilege of having their Constitutionally guaranteed day in Court is wrong. As this Court has stated: "If a court compels arbitration without deciding the validity of the arbitration clause, a party may be forced to proceed through a potentially costly arbitration before having the opportunity to appeal." *Hill*, 179 Wn.2d at 54. Arbitration is expensive. "This is particularly a concern where an arbitration clause imposes all or some of the costs of arbitration on the disfavored party." *Id.* Here, FutureSelect is the disfavored party.

FutureSelect has unsuccessfully resisted an arbitration to which it never agreed, and faces the crippling prospect of engaging in potentially expensive and certainly pointless arbitration.

C. Washington Law Permits—and Should Permit—an Immediate Appeal of an Order Compelling Arbitration

Whether an arbitration clause is valid and enforceable is a “gateway” issue that a court must determine **before** compelling a party to arbitrate. *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 83-84, 123 S. Ct. 588 (2002) (“[R]eference of the gateway dispute to the court avoids the risk of forcing parties to arbitrate a matter that they may well not have agreed to arbitrate.”). *See also Saleemi v. Doctor’s Assocs., Inc.*, 176 Wn.2d 368, 376, 292 P.3d 108 (2013). Indeed, “[i]t is the court’s duty to determine whether the parties have agreed to arbitrate a particular dispute.” *Yakima Cty. Law Enforcement Officers Guild v. Yakima Cty.*, 133 Wn. App. 281, 285, 135 P.3d 558 (2006) (citation and internal quotation marks omitted).

If a party opposing a motion to compel arbitration raises a defense that there is no agreement to arbitrate, “the court shall proceed summarily to decide the issue.” RCW 7.04A.070(2). The reasoning behind this rule is simple: “If a court compels arbitration without deciding the validity of the arbitration clause, a party may be forced to proceed through a

potentially costly arbitration before having the opportunity to appeal.”

Hill, 179 Wn.2d at 54.

In *Hill*, this Court addressed a materially identical issue to that presented here and determined that the lower courts erred in failing to review the enforceability of the arbitration agreement prior to compelling arbitration. *Id.* at 54-55. This Court stressed that the interests of justice and economy are best served when the court examines the enforceability of an arbitration agreement *before* compelling the parties go to the tremendous expense and effort of actually arbitrating. *Id.* at 54. “When the trial court declines to compel arbitration, that decision is immediately appealable **While we have never addressed whether the opposite is always true**, similar considerations are at play We find no support in the rules of procedure or case law for the Court of Appeals’ decision to compel arbitration without considering whether the arbitration clause is even valid.” *Id.* at 54-55 (emphasis added).

The Court of Appeals in *Hill* had addressed the order compelling arbitration as a matter of discretionary review under RAP 2.3(b)(4). This Court did not. Instead, this Court rejected the application of RAP 2.3(b)(4), holding that arbitrability is a “‘gateway dispute’ that *the courts must resolve* because a party cannot be required to fulfill a bargain that should be voided.” *Hill*, 179 Wn.2d at 53-54. This Court recognized that

it *and* the Court of Appeals were obligated to decide the issue of arbitrability *before* forcing an unwilling party into arbitration. *Id.* at 54-55.

Washington's RUAA does *not* prohibit appeals from orders compelling arbitration. The RUAA is silent on the subject of claims compelling arbitration for good reason: An order compelling arbitration of claims which are the proper subject of arbitration (arbitrable claims) is a correct order; an order compelling arbitration of claims which are not arbitrable are not covered by the RUAA, because the RUAA only applies to arbitrable claims. RCW 7.04A.030 (“[T]his chapter governs agreements to arbitrate . . .”).

Moreover, because FutureSelect never agreed to arbitrate its claims, it is not subject to the RUAA. KPMG's reliance on the principle *expressio unius est exclusio alterius*, is misplaced. KPMG persists in interpreting RCW 7.04A.280(1)(a)-(f) as an all-inclusive list of the only appealable orders, however such an interpretation would prohibit appeal of the order to arbitrate even *after* arbitration was complete, which is a *right*.

Here, in ordering FutureSelect to arbitrate its claims with KPMG, the Superior Court failed to examine the threshold matter of whether there was an enforceable agreement to arbitrate between the parties. *See* CP 400-01. The Superior Court issued no written opinion and provided no

analysis of the existence of a valid and enforceable agreement to arbitrate between the parties. *Id.* The Superior Court did nothing more than check the first box on a form drafted by KPMG. *Id.* The Superior Court had a duty to make an initial determination that an agreement to arbitrate existed between the parties.

When it *did* consider the enforceability of an agreement to arbitrate by an auditor against FutureSelect—in the intervening litigation against EY, the engagement agreement contained a clause almost identical in form and substance to the clause contained in KPMG’s audit engagement agreements—the Court determined that the arbitration provision was not enforceable against FutureSelect. CP 678-94. The EY trial court’s written opinion explains that FutureSelect was not bound by the arbitration clause in its audit engagement agreements because Plaintiffs did not sign the agreements and their claims are direct claims against EY, not derivative claims. *Id.*

No court in the KPMG litigation has undertaken any enforceability analysis of the nearly identical clause in KPMG’s audit engagement agreements. It would be a miscarriage of justice to deny FutureSelect review of this “gateway” issue before the parties are both forced to expend considerable time and resources in an arbitration involving tens of millions of dollars in damages, only then to be able to address the issue of

enforceability currently before this Court. FutureSelect filed its claim against KPMG over six years ago—delaying its right to a jury trial by ordering a useless, lengthy, and expensive arbitration is antithetical to the pursuit of justice.

D. FutureSelect Timely Appealed—Twice

The Court of Appeals improperly dismissed FutureSelect’s appeal as untimely.

When FutureSelect was originally compelled to arbitrate in 2011, it immediately and timely appealed the order. That appeal was denied. Subsequently, and following the *Hill* decision, the denial of a similar motion to compel by EY, *the imposition of a stay pending the outcome of the EY trial*, and the conclusion of that EY trial—and upon entry of final judgment—FutureSelect timely filed the present appeal proceedings.

The Superior Court’s original order compelling arbitration should have been reviewed under both RAP 2.5(c)(2) and RAP 2.2(d).

Under RAP 2.5(c)(2), the Court of Appeals should have accepted FutureSelect’s January 15, 2016 appeal of the trial court’s order compelling arbitration because there had been an intervening change in the law that created a right of appeal from decisions compelling arbitration. *State v. Schwab*, 163 Wn.2d 664, 672-73, 185 P.3d 1151 (2008) (RAP 2.5(c)(2) “allows a prior appellate holding in the same case to be

reconsidered where there has been an intervening change in the law.”); *Roberson v. Perez*, 156 Wn.2d 33, 43, 123 P.3d 844 (2005) (“An appellate court’s discretion to disregard the law of the case doctrine is at its apex when there has been a subsequent change in controlling precedent on appeal.”)

The Court of Appeals declined to review its previous decisions based upon timeliness. The time limit imposed by the Court of Appeals expired before the intervening decision of this Court. No such time limit exists. *See In re Greening*, 141 Wn.2d 687, 697, 9 P.3d 206 (2000) (Litigants “should not be faulted for having omitted arguments that were essentially *unavailable* at the time.”) (emphasis in original). “[W]here an intervening opinion has effectively overturned a prior appellate decision that was originally determinative of a material issue, the intervening opinion constitutes a ‘significant change in the law’ for purposes of exemption from procedural bars.” *Id.* The failure of the lower court to even *consider* arbitrability is straightforward error. *Hill*, 179 Wn.2d at 54-55. Had it considered the issue, in light of *Hill*, it would have to acknowledge the right to appeal.

Furthermore, RAP 2.2(d) expressly allows that an appeal may be taken from decisions entered that do not dispose of all the claims or counts as to all the parties. An order with regard to one of multiple defendants is

a “part of the decision” ultimately rendered in the case. *See Fox v. Sunmaster Prods., Inc.*, 115 Wn.2d 498, 505, 798 P.2d 808 (1990) (“It therefore makes no sense to mandate an immediate appeal from a partial final judgment” because “[s]uch a requirement would simply encourage multiple and perhaps unnecessary appeals in multi-party and multi-claim cases.”). FutureSelect initiated appellate proceedings upon the issuance of the initial order compelling arbitration *and* upon issuance of a final judgment against EY. In either case, the appellate right has been preserved.

Even if the *Hill* opinion had not created a right to appeal an order compelling arbitration, the Commissioner should have granted FutureSelect discretionary review to promote justice and judicial economy. *See Huntley v. Frito-Lay, Inc.*, 96 Wn. App. 398, 400, 979 P.2d 488 (1999) (recognizing that even if an appeal is procedurally improper when compelled to arbitrate, the issue of enforceability of an arbitration agreement still merits discretionary review because “it would be a useless act to engage in an arbitration of state-law claims if they are not subject to arbitration”). *See also*, RAP 1.2(a) (appellate rules “will be liberally interpreted to promote justice and facilitate the decision of cases on the merits.”); *State v. Hathaway*, 161 Wn. App. 634, 651-52, 251 P.3d 253 (2011) (where a “challenge is not properly before [the Appellate Court] as

a matter of right . . . RAP 1.2(c) permits us to waive or alter the rules of appellate procedure ‘in order to serve the ends of justice.’”).

Forcing FutureSelect and KPMG to arbitrate the claims before FutureSelect has even the opportunity to have the arbitration clause applicability reviewed—particularly in light of the subsequent full opinion of the Superior Court holding that FutureSelect was *not* bound by a nearly identical arbitration clause between the Rye Funds and KPMG’s co-defendant, EY—would be costly, inefficient, and would only serve to delay the inevitable jury trial to which FutureSelect is entitled.

E. This Court Has the Power to Correct the Mistakes of the Court of Appeals

This Court has the power to overturn the Court of Appeals’ improper decisions declining review of the Superior Court’s order compelling arbitration under RAP 13.4 and RAP 13.5.

RAP 13.4 governs the “review of decisions terminating review.” RAP 12.3 defines a “decision terminating review” as “an opinion, order, or judgment of the appellate court or a ruling of a commissioner or clerk of an appellate court if it:

- (1) Is filed after review is accepted by the appellate court filing the decision; and
- (2) Terminates review unconditionally; and
- (3) Is . . . (iv) an order refusing to modify a ruling by the commissioner or clerk dismissing review.”

These requirements were met—the Court of Appeals’ October 5, 2016 Order (the “Order”) is a decision terminating review.

First, the Order was filed after review was accepted by the appellate court filing the decision. RAP 6.1 states that “[t]he appellate court ‘accepts review’ of a trial court decision upon the timely filing in the trial court of a notice of appeal from a decision which is reviewable as a matter of right.” Here, notice of appeal was timely filed and the appeal was taken from a decision that was reviewable as a matter of right. The Court of Appeals accepted review when FutureSelect filed its appeal and the Order was filed after review was accepted by that court.

Second, the Order terminated review unconditionally. The Order stated, “ORDERED, that the motion to modify is denied.” The Order created no conditions upon dismissal of the appeal.

Finally, the Order specifically states it was “an order refusing to modify a ruling by the commissioner or clerk dismissing review.”

Because the Order was filed after review was accepted, it terminated review unconditionally, and was an order refusing to modify a ruling by the commissioner or clerk dismissing review, it was an order terminating review, and review of the Order by this Court is appropriate under RAP 13.4.

This Court may also overrule the Court of Appeals' decisions under RAP 13.5 because (1) there is obvious error rendering further proceedings useless, and (2) there is probable error and FutureSelect's freedom to act is severely limited by the error.³ See RAP 13.5(b)(1) and (2).

Errors are multiple and obvious. As discussed *supra*, the Court of Appeals' timeliness basis for declining review was plain error, because no such time limit exists, and the failure to even consider arbitrability is straightforward error. *Hill*, 179 Wn.2d at 54-55.

Moreover, the lower court's errors do not merely "render future proceedings useless." Instead, they *create* a requirement that the parties engage in future proceedings that will be useless. The error requires the parties to participate in lengthy and expensive arbitration before having the opportunity to have the arbitrability of the matter decided. That arbitration is guaranteed to be useless if FutureSelect cannot be compelled to arbitrate.⁴

³ KPMG argues that FutureSelect had no right to appeal and that the Court of Appeals could not have "divined" a request for discretionary review. KPMG Answer in Opposition to Motion to Modify at 14, n. 17. However, under RAP 5.1(c), "[a] notice of appeal of a decision which is not appealable will be given the same effect as a notice for discretionary review."

⁴ See, e.g., *Askenazy v. KPMG LLP*, 83 Mass. App. Ct. 649, 659, 988 N.E.2d 463 (2013) (Where plaintiffs "neither were party, nor expressly assented, to the engagement letters . . . plaintiffs [were] neither implicitly nor equitably bound to arbitrate because their claims are extracontractual, neither contract-based nor dependent upon third-party beneficiary status."); *KPMG LLP v. Cocchi*, 88 So.3d 327, 330 (Fla. Dist. Ct. App. 2012)

Finally, and to the extent the lower court's error was "probable" instead of "obvious,"⁵ FutureSelect's freedom to act is clearly limited by that probable error. Requiring years of arbitration and millions of dollars spent as a prerequisite to FutureSelect's right to a jury trial is debilitating, and fatally so. Unlike KPMG, FutureSelect does not have the capacity to be exposed financially to multiple litigations of the same claims. The reason FutureSelect is forced to litigate in the first place is that it constructively lost all of its assets. Requiring it to litigate twice is tantamount to the forcible waiver of the constitutional right of access to the courts.

V. CONCLUSION

For the foregoing reasons, FutureSelect respectfully requests that this Court overturn the Court of Appeals' refusal to modify the ruling of the Commissioner dismissing FutureSelect's appeal of the decision of the Superior Court, and instruct that orders compelling arbitration are

(holding under Delaware law, claims asserted by investors in limited partnerships that lost millions of dollars in Ponzi scheme against the auditor of the partnerships' financial statements were direct, not derivative claims, and thus arbitration provision in contract between auditor and the manager of the partnerships did not apply).

⁵ KPMG's reference to other courts having found that arbitration agreements enforceable against Rye Fund investors like FutureSelect neglects to mention the critical distinction: in those cases, the courts found the claims to be derivative, **unlike here**. See KPMG Answer in Opposition to Motion to Modify at 4 n.3.

immediately appealable or simply remand this case to the Superior Court
for trial.

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DECLARATION OF SERVICE

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