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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA
FRESNO DIVISION

In re Coast Grain Company, Debtor.	Case No. 01-19647-B-11
Greg Braun, Plan Agent and Successor to Chapter 11 Trustee of Coast Grain Company, a California Corporation, Plaintiff, v. Dutch Star Dairy, a Partnership, Dykstra Family Dairy, a Partnership, Theodore J. Dykstra, Jeannette Dykstra, John Dykstra, Jr., Deborah D. Dykstra, David Dykstra and Kari Dykstra, Defendants.	Adversary Proc. No. 03-6038 DC No. HLB-1

MEMORANDUM DECISION REGARDING BIFURCATED SETTLEMENT ISSUES AND DEFENDANTS' MOTION FOR LEAVE TO AMEND RESPONSIVE PLEADING

Bradley A. Silva, Esq., of the Law Offices of Bradley A. Silva, appeared for plaintiff Greg Braun, plan agent and successor to chapter 11 trustee of Coast Grain Company, a California Corporation (the "Plaintiff").

Tres A. Porter, Esq., of Henry, Logoluso & Blum, appeared for defendants Dutch Star Dairy, a Partnership, Dykstra Family Dairy, a Partnership, Theodore J. Dykstra, Jeannette Dykstra, John Dykstra, Jr., Deborah D. Dykstra, David Dykstra and Kari Dykstra ("Defendants" or "Dykstra").

This Memorandum Decision is not approved for publication and may not be cited except when relevant under the doctrine of law of the case or the rules of res judicata and claim preclusion.

Introduction.

In this adversary proceeding, the court is asked to interpret the effect of a settlement agreement that was negotiated between the parties in a state court lawsuit almost five years ago. The Dykstras paid over one-quarter million dollars for what they believed was a complete and final settlement of their account with the Debtor. As it turns out, the Debtor had a different agenda, their attorneys actually negotiated a partial settlement, and the parties now find themselves in this court fighting over Dykstra's obligation to pay the remainder of the account.

This adversary proceeding was set for a five-day trial. Upon review of the pre-trial statements and the proposed trial exhibits, the court noted that Dykstra's exhibits included a Mutual Release and Compromise Agreement and a Request for Dismissal with prejudice, both relating to a prior action filed in Fresno County Superior Court, case number 01-CE-CG-03816 (Defendants' proposed trial exhibits "A" & "B": the "Settlement Documents"). The Settlement Documents indicate that the breach of contract claims and defenses have already been the subject of litigation between the same parties in the state court. Pursuant to the Settlement Documents, Dykstra paid all of Plaintiff's breach of contract claims against Dykstra, except the amount which Plaintiff now seeks to recover in this adversary proceeding based, *inter alia*, on essentially the same breach of contract claims.

Based thereon, the court set a further pre-trial conference for the purpose of discussing: (1) the effect of the Settlement Documents on the claims asserted in this adversary proceeding, and (2) alternatives, including bifurcation of claims and defenses, for an early resolution of any disputed issues regarding the Settlement Documents prior to a lengthy trial on the breach of contract claims. The court offered to hold a separate trial on the bifurcated issues. The parties agreed to bifurcate the "settlement" related issues, waive the right to an evidentiary hearing, and submit the bifurcated issues for trial through briefs, declarations, and other admissible evidence. On February 9, 2006, the court entered an order vacating the trial date, bifurcating the settlement issues, and setting

a briefing schedule.

Dykstra subsequently filed a motion for leave to amend its responsive pleading to include the "accord and satisfaction" affirmative defense based on the Settlement Documents and its payment of money to the Debtor. Plaintiff did not oppose that motion. After oral argument, the court resubmitted the bifurcated issues and took Dykstra's motion to amend under submission for ruling together. For the reasons set forth below, the court finds and concludes that the Settlement Documents do not preclude the Plaintiff from litigating the breach of contract claims in this adversary proceeding to collect the money that was expressly reserved for future litigation in the bankruptcy court. Dykstra's unopposed motion to amend its responsive pleading will be granted.

This Memorandum contains findings of fact and conclusions of law required by Federal Rule of Civil Procedure 52 (made applicable to this adversary proceeding by Federal Rule of Bankruptcy Procedure 7052). The bankruptcy court has jurisdiction over this matter pursuant to 28 U.S.C. § 1334 and 11 U.S.C. §§ 542, 549 & 553.[1] The parties have consented to this court's ability to hear and determine and enter appropriate orders and judgment on the non-core breach of contract claim. The remainder on the claims constitute a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(O).

Background.

The Dispute.

Prior to this bankruptcy, Coast Grain Company ("Coast Grain" or the "Debtor") was in the business of buying, processing, and selling grain and other livestock feed products. The individual defendants own and operate two dairy facilities in the San Joaquin Valley known as Dykstra Family Dairy, a partnership, and Dutch Star Dairy, a

[1]Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9036, as enacted and promulgated prior to October 17, 2005, the effective date of The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. 109-8, Apr. 20, 2005, 119 Stat. 23.

partnership. Dykstra had been a customer of the Debtor for several years and had annually purchased hundreds of thousands of dollars of dairy feed products on open account (the "Feed Account").

In 2000, Dykstra began to experience some performance, quality control, and billing problems with Coast Grain. Dykstra's managing partner, Theodore Dykstra, made numerous efforts to resolve the problems with Coast Grain's sales and management staff and was repeatedly assured that Coast Grain would "make things right." Dykstra made payments on its Feed Account. However, as Coast Grain continued to bill Dykstra for allegedly undelivered, over-priced and poor quality product, Dykstra began to withhold payment on its Feed Account waiting for Coast Grain to make the appropriate adjustments. The performance and billing problems continued into 2001 when Coast Grain also began billing a "fuel surcharge," which Dykstra had not agreed to pay.

In August 2001, Coast Grain was in serious financial difficulty. It gave notice to its customers, including Dykstra, that it was cancelling the remainder of all outstanding feed contracts. Thereafter, Coast Grain refused to honor the prices previously negotiated for feed shipments, or in some cases refused to deliver certain products altogether. This caused Dykstra to incur damages in its efforts to "cover" the cancelled contracts. Coast Grain never adjusted Dykstra's Feed Account as promised, but continued to add finance charges to the growing unpaid balance. When this bankruptcy case commenced, there was a balance on Dykstra's Feed Account in excess of $431,000.

In October 2001, an involuntary chapter 11 bankruptcy petition was filed against Coast Grain. An Order for Relief under chapter 11 was entered on November 28, 2001, and for a time, Coast Grain continued operating as a debtor-in-possession. On a motion of the unsecured creditors' committee, Greg Braun was appointed to act as the chapter 11 trustee in March 2002.

In November 2001, the Debtor filed a complaint in Fresno County Superior Court against Dykstra for, *inter alia*, breach of contract to recover the unpaid balance on the Feed Account (the "State Court Litigation"). The complaint in the State Court Litigation

alleged the following causes of action: (1) breach of contract; (2) goods sold and delivered; (3) account stated; and (4) enforcement of livestock feed liens. The State Court Litigation dealt solely with the collection of the Feed Account for goods purportedly sold and delivered to Dykstra prior to the bankruptcy. Dykstra asserted defenses based, *inter alia*, on failure to perform, overbilling, and breach of contract.

The State Court Settlement.

In February 2002, after negotiations between the attorneys, Coast Grain and Dykstra entered into a Mutual Release and Compromise Agreement to settle the State Court Litigation (the "Settlement" or the "Settlement Agreement"). The terms of Settlement Agreement contemplated that Dykstra would pay $255,082.51 in exchange for the release and discharge of "any and all claims . . . suspected or claimed, or which might have been alleged in the litigation . . . ." In addition, the Settlement Agreement provided, "Plaintiffs will file a dismissal, with prejudice, of the entire action against Defendants." In conjunction with the Settlement, Plaintiff also recorded two UCC-3 releases (one for each dairy) of its dairy cattle supply lien with the California Secretary of State.

The Settlement contemplated a "setoff" to Dykstra's Feed Account in the amount of $164,950 based on Dykstra's calculation of damages incurred as a result of alleged performance and overbilling problems in 2001. Dykstra agreed to forego its damages for problems that occurred prior to 2001, and paid the balance due on the Feed Account. Theodore Dykstra states in his declaration that he understood the Settlement would end all disputes between the parties. Dykstra did not file a proof of claim in the bankruptcy case for any damages which it did not recover through the "setoff" in the Settlement. Dykstra paid the agreed amount with check number 8846. That check bore the inscription "payment in Full on Account." Plaintiff accepted and deposited the check without protesting or deleting the notation. The dismissal with prejudice was executed and filed in the State Court Litigation (the "Dismissal With Prejudice").

The Settlement Agreement was not absolute. The parties acknowledged that the Debtor was in a chapter 11 bankruptcy proceeding and they agreed to reserve certain

disputed issues referred to as "setoff" issues for subsequent adjudication in the Debtor's bankruptcy case.[2] Specifically, paragraph 14 of the Settlement Agreement (the "Bankruptcy Litigation Clause") provided:

> INDEMNIFICATION; BANKRUPTCY PROCEEDINGS
>
> *Notwithstanding the foregoing*, Defendants acknowledge that Plaintiff is currently in an involuntary bankruptcy proceeding and that *any setoff achieved by this settlement is still subject to any action that the bankruptcy court may take regarding same*. (Emphasis added.)

The Settlement Negotiations.

The correspondence between Debtor's counsel, Bradley A. Silva, Esq., and Dykstra's counsel, Jerry Henry, Esq., is profoundly ambiguous with regard to what the attorneys actually agreed to settle. The evolution of the Settlement Agreement is critical to the court's interpretation of its meaning. The communications began after Dykstra was served with the summons and complaint in the State Court Litigation. Before the Defendants responded to the complaint, Mr. Dykstra instructed his counsel, Mr. Henry, to make an offer to pay the entire Feed Account less an "offset" for the alleged damages. On November 29, 2001, Mr. Henry sent a letter to Mr. Silva, to formally initiate the settlement discussion. The letter included extensive documentation to summarize and support Dykstra's damage claims and the "offset" calculation. It then concluded:

> [I]n order to effectuate a quick settlement as we discussed, [Mr. Dykstra] would be willing to write a check for the difference between your complaint amounts as stated, $420,032.51 and the offset of $164,950.00 or [$]255,082.51. Please let me know as early as possible if we may effectuate mutual releases and a dismissal of your complaint based on this settlement proposal.

It appears clear from the plain language of Mr. Henry's letter that Dykstra was offering to pay a large sum of money in exchange for a full and final settlement of its Feed Account. On December 14, 2001, Mr. Silva telefaxed a response to Mr. Henry which began:

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[2]Even though the State Court Litigation was commenced while the Debtor was in chapter 11, it did not plead any causes of action that arose under the Bankruptcy Code.

> I am responding to your letter of November 29, 2001. For purposes of these settlement discussions only, Coast Grain Company will acknowledge the Dykstra Family Dairy and Dutch Star Dairy *claim of offset* and will accept the sum of $255,082.51 *as payment in full on its account*. However, this sum must [be] received at my office or the Ontario office of Coast Grain Company by next week. (Emphasis added.)
>
> This sum is arrived at by applying the *full setoff* alleged by your clients against an account balance of $420,032.51, which does not take into account service charges for October and November. (Emphasis added.)

At this point, the correspondence becomes conflicting. After first stating that the Settlement would constitute "payment in full" on Dykstra's account, Mr. Silva then qualified the apparent scope of the Settlement to reserve the balance of the Feed Account, specifically the "setoff" or "offset" referred to previously, for litigation in the bankruptcy court. Mr. Silva also referred to Dykstra's settlement offer, for the first time, as the "undisputed sum" owed on the Feed Account. Mr. Silva's response concludes with the following:

> This offer is subject to any actions that may be taken in future U.S. Bankruptcy Court proceeding as *to the claim of setoff*. Coast Grain Company is currently a Debtor in Possession under Chapter 11 of the U.S. Bankruptcy Code. It is expected that *all setoff claims* will be handled in a like manner, but at this point that is an unknown. *This is a settlement of the undisputed sum owed Coast Grain Company*. (Emphasis added.)

In a reply letter of the same date, December 14, 2001, Mr. Henry acknowledged the limited scope of the Settlement, the "undisputed" characterization of Dykstra's payment, and the proposed reservation for future "bankruptcy" litigation:

> This will confirm our telephone conversation of the other day, in which we *discussed my client paying the undisputed amount*. You will issue a release, but it would be *contingent upon further proceedings by the bankruptcy court*. (Emphasis added.)

In support of Dykstra's defense in this adversary proceeding, Mr. Henry filed a declaration denying that he ever discussed any reservation to the proposed Settlement

with Mr. Silva.[3] However, Mr. Henry prepared the initial draft of the Settlement Agreement with the reservation term included. A few days after the telefaxed communications, on December 19, 2001, Mr. Henry sent to Mr. Silva an initial draft of the Settlement. It was a typical boiler-plate litigation settlement and release agreement. However, Mr. Henry's initial draft included a provision inserted at the end of last paragraph, the indemnity clause, which stated:

> However, Defendants acknowledge that Plaintiff is currently in an involuntary bankruptcy proceeding and that *any setoff achieved by this settlement is still subject to any action that the bankruptcy court may take regarding same*. (Emphasis added.)

Thereafter, the attorneys exchanged at least one more draft of the Settlement Agreement before circulating the final draft to their clients for signature. The final draft included the Bankruptcy Litigation Clause referenced above. The Settlement Agreement was signed by all of the Defendants and the money was paid within a few days.

Plaintiff contends that the Debtor never intended to release Dykstra from the unpaid balance of its Feed Account. Plaintiff argues, specifically with reference to the Bankruptcy Litigation Clause, that the Debtor was in bankruptcy, it "needed the cash," and only agreed to settle the "undisputed" amount due on the Feed Account, reserving all

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[3]Mr. Henry's reply letter of December 14, 2001, was attached as an exhibit to both Bradley Silva's and John Stellingwerf's declarations. Notably, it was omitted from the exhibits attached to Mr. Henry's declaration, as was any mention of its content or existence. The language in the Bankruptcy Litigation Clause, together with Mr. Henry's acknowledgment that the Settlement would be "contingent upon further proceedings by the bankruptcy court," both squarely contradict the statement in his declaration:

> In negotiating the settlement, it was never discussed between Mr. Silva and myself, and never contemplated by me or my clients that Coast Grain had any intent of "reserving" any claims to the amount setoff in the settlement. . . . Had I any reason to believe that Coast Grain or Mr. Silva intended to make any further claims regarding the alleged debt, I would not have advised my clients to settle the dispute and I certainly would not have instructed by clients to perform under the terms of the settlement agreement. (Henry Decl. ¶ 5.)

of the disputed, or "setoff" issues for subsequent adjudication in the bankruptcy court. Plaintiff's contention here appears to be consistent with the attorneys' correspondence. Indeed, Mr. Henry acknowledged in his reply letter of December 14, 2001, that the Settlement was "contingent" and that Dykstra's payment of more than one-quarter million dollars only represented the "undisputed amount" due.

Conversely, Theodore Dykstra's declaration suggests that Dykstra left many "disputed" issues on the table and paid substantially more than he believed was actually due, in the interest of reaching a complete and final compromise. Mr. Dykstra stated in his declaration: "It was my intent to completely resolve all claims between the dairies and Coast Grain by virtue of the settlement." Mr. Dykstra's statement here is consistent with the fact that Dykstra did not file a proof of claim in this bankruptcy for any remaining damages. Mr. Dykstra understood that "Coast Grain was involved in a bankruptcy and that Mr. Silva wanted that fact acknowledged in the agreement." Mr. Dykstra's declaration, and his professed understanding of the Settlement, suggests that Mr. Dykstra was either not informed, or did not understand the background or the meaning of the Bankruptcy Litigation Clause in the Settlement Agreement.[4]

Other portions of the Settlement Agreement relevant to this dispute, and which further illustrate the inherent ambiguity between the attorneys' correspondence and the actual Settlement Agreement, are set forth below:

RECITALS

1. On November 6, 2001, Coast Grain Company filed action No. 01 CE CG03816 in the Superior Court of California, County of Fresno, entitled COMPLAINT FOR DAMAGES AND ENFORCEMENT OF DAIRY CATTLE SUPPLY LIENS.

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[4]It is not clear whether Mr. Dykstra received any of the letters that were sent between the attorneys leading up to the Settlement. The letters from Mr. Henry do not bear the traditional "cc" inscription at the end showing that a "courtesy copy" was sent to Mr. Dykstra. Further, there is no evidence that Mr. Dykstra and his attorney met or conferred over the terms of the Settlement Agreement before it was circulated for signatures.

2. . . . All parties to the action now desire to compromise and terminate said litigation, and as more particularly provided herein, to reach a full and final settlement of all claims arising out of or in any way related to said complaint.

AGREEMENT

. . .

3. RELEASE. In consideration of the payment of the total sum of two hundred fifty-five thousand, eighty-two dollars and fifty-one cents ($255,082.51) paid to Coast Grain Company . . . each party hereby releases and forever discharges the other, its officers, employees, agents, accountants, attorneys and all other acting for, under or in concert, with such party, past or present, of and from any and all claims, demands, actions, causes of action, allegations, damages, liabilities, loss, cost or expenses, including attorney's fees of any kind or nature whatsoever, past or present, ascertained or unascertained, whether or not know, suspected or claimed, or which might have been alleged in the litigation referred to in the Recitals and any claim of any kind regarding the relationship which existed between the parties which gave rise to said litigation.

. . . The parties agree that in consideration of said payment as set forth above, Plaintiffs will file a dismissal, with prejudice, of the entire action against Defendants.

4. NO ADMISSION. This Mutual Release and Compromise Agreement is the compromise of disputed claims and fully and finally settles all claims between the parties to the described litigation, and is intended to buy peace and to prevent any further involvement in said disputes. . . .

5. FINAL SETTLEMENT. Each party understands and agrees that this Mutual Release and Compromise Agreement shall act as a full and final release of all claims, known or unknown, whether or not asserted, arising from the above-mentioned disputes. . . .

6. DISMISSAL OF ACTION. Provided Defendants comply with the settlement terms set forth above, Plaintiffs will dismiss with prejudice all causes of action, whether stated or not, arising out of or connected with the litigation described herein above, including the contest filed in Fresno County, Superior Court of California, Case No. 01 CE CG 03816 . . . .

. . .

The Adversary Proceeding.

On October 28, 2003, the Debtor confirmed its chapter 11 plan of reorganization. Plaintiff, Greg Braun, is the successor-in-interest to the Debtor as the "Plan Agent" through the chapter 11 plan. Notwithstanding the Settlement Agreement and Dismissal with Prejudice, the Plaintiff filed this adversary proceeding against Dykstra in November 2003 to recover the sum of $176,071.74, the unpaid balance of the Feed Account which

was "setoff" or "offset" from the total Feed Account pursuant to the Settlement Agreement ($164,950 plus finance charges) (the "Adversary Proceeding"). The claims for relief in this Adversary Proceeding are summarized as: (1) recovery of money owed for the "sale of goods" (the "First Claim for Relief"), (2) disallowance of a setoff under § 553(b) (the "Second Claim for Relief"), (3) recovery of post-petition transfers under § 549 (the "Third Claim for Relief"), and (4) disallowance of Dykstra's claim under § 502(d) (the "Fourth Claim for Relief"). All of the claims for relief seek to recover, on alternative theories, the same money, the "offset" that was deducted from the Feed Account in the prior Settlement negotiations. Notably, the Adversary Proceeding completely fails to mention the State Court Litigation or the fact that the money Dykstra did pay on its Feed Account, was paid pursuant to a Settlement Agreement. Plaintiff alleges simply that Dykstra paid $255,082.51 "on account."[5]

Oddly, Dykstra's responsive pleading also fails to mention the State Court Litigation and specifically the Settlement Documents. As noted above, it was this court that first raised the Settlement as a material issue just prior to trial. At the final pre-trial conference, the court inquired of Dykstra's counsel why the Settlement had not been pled as an affirmative defense and aggressively pursued by way of a dispositive motion. Dykstra's counsel replied that Dykstra did intend to raise the Settlement at sometime during the trial.

In paragraph 14 of its responsive pleading, Dykstra admits paying the amount prescribed in the Settlement Agreement and affirmatively alleges, without specifics, that it was paid "as full and final settlement." The court construes Dykstra's reference to a "full and final settlement" as sufficient to put the settlement issue before the court, even

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[5]Plaintiff's attorney in this adversary proceeding, Bradley A. Silva, Esq., is the same attorney that represented the Debtor in the State Court Litigation. Mr. Silva was fully aware of the Settlement, having negotiated the Settlement Agreement with Dykstra's counsel, having accepted Dykstra's check upon consummation of the Settlement, having signed and filed the dismissal documents in the State Court Litigation, and having signed and filed the two UCC-3 lien releases with the Secretary of State.

though it was not separately pled as an affirmative defense.[6] The court notes too that the Settlement Documents were produced with the exhibits to be introduced at trial. Plaintiff did not object to the Settlement Documents. There is no prejudice to Plaintiff since Plaintiff clearly knew about the State Court Litigation and the Settlement Documents before it filed this Adversary Proceeding. The parties had an opportunity to fully brief all bifurcated issues relating to the Settlement Documents after the final pre-trial conference. Accordingly, the court will allow and consider the Settlement Documents as a new affirmative defense and rule on the bifurcated "settlement" issue accordingly. Dykstra also asserts, *inter alia*, the affirmative defense of recoupment which the court will not address here because "recoupment" falls outside of the bifurcated "settlement" issue. Finally, by way of a proposed amendment, Dykstra seeks to add the affirmative defense of "accord and satisfaction" to the extent that it may be relevant to the court's evaluation of the Settlement Documents.[7]

Issue.

What effect does the Settlement Agreement in the State Court Litigation, and the Dismissal With Prejudice have on the claims for relief filed in this adversary proceeding?

Analysis and Conclusions of Law.

The bankruptcy court must look to state law to interpret the meaning of a contract. *Gerwer v. Salzman (In re Gerwer)*, 253 B.R. 66, 73 (9th Cir. BAP 2000) (citation omitted). "A settlement agreement is a contract, and the legal principles which apply to

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[6]In this court's Order Vacating Trial, Bifurcating Claims, and Setting Briefing Schedule for Trial of Bifurcated Claims, the court noted that the complaint and the answer both failed to reference the Settlement Documents. The court is now satisfied that the "settlement" issue was adequately, though inartfully pled.

[7]Plaintiff did not oppose Dykstra's motion to amend its responsive pleading, but he does object to the court's consideration of the "accord and satisfaction" defense on the grounds that it is outside of the bifurcated "settlement" issue. However, the issue is properly raised here because Dykstra contends that the Settlement Agreement itself, and the related payment of money constitutes an accord and satisfaction of the Feed Account.

contracts generally apply to settlement contracts." *Weddington Productions, Inc. v. Flick* 60 Cal.App.4th 793, 810 (1998) (citation omitted).

The goal of contract interpretation is to ascertain the parties' mutual intent at the time of contracting. *Founding Members of the Newport Beach Country Club v. Newport Beach Country Club, Inc.* 109 Cal.App.4th 944, 955 (2003). The mutual intent of the parties is determined by the words used in the agreement which are to be understood in their ordinary and popular sense. *Id. Cal. Civ. Code § 1644*.

Conversely, "[w]here a contract is so uncertain and indefinite that the intention of the parties in material particulars cannot be ascertained, the contract is void and unenforceable." *Cal. Lettuce Growers, Inc. v. Union Sugar Co.* 45 Cal.2d 474, 481 (1955).

One party's subjective understanding as to the meaning of a contract term cannot be credited when it is not a reasonable interpretation of the language of the agreement. *Blumenfeld v. R.H. Macy & Co., Inc.* 92 Cal.App.3d 38, 46 (1979).

The general principles of contract interpretation under California law were summarized in *Southern Pacific Transportation Co. v. Santa Fe Pacific Pipelines, Inc.* 74 Cal.App.4th 1232, 1240-41 (1979) as follows:

> The overriding goal of contract interpretation is to give effect to the mutual intention of the parties at the time of contracting, "so far as the same is ascertainable and lawful." (Cal.Civ.Code § 1636.) Faced with contract language that is reasonably susceptible to more than one meaning, certain general rules of contract interpretation come into play to aid the court in resolving the ambiguity. (See *id.* § 1637.) To begin with, the words of a contract are to be understood in their ordinary and popular sense unless the parties use them in a technical sense or "a special meaning is given to them by usage. . . ." (*Id.* § 1644.) Technical words generally are interpreted "as usually understood by persons in the profession or business to which they relate. . . ." (*Id.* § 1645.)
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> Further, we can explain a contract by reference to the circumstances under which it was made, as well as the matter to which it relates. (Cal.Civ.Code § 1647.) The circumstances under which a contract was made include "the situation of the subject of the instrument, and of the parties to it. . . ." (Cal.CodeCiv.Proc. § 1860.)
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> The terms of a writing can also "be explained or supplemented by course of dealing or usage of trade or by course of performance." (Cal.CodeCiv.Proc. § 1856, subd. (c).) . . . .
>
> Extrinsic evidence on all these circumstances and matters can be offered where it

is obvious that a contract term is ambiguous, but also to expose a latent ambiguity "The test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible." (*Pacific Gas & E. Co. v. G.W. Thomas Drayage etc. Co.* (1968) 69 Cal.2d 33, 37, 39 Cal.Rptr. 561, 442 P.2d 641 (Pacific Gas).)

The Settlement Agreement in this case is a complicated paradox. Throughout the document, the parties agreed to finally resolve, release and dismiss all claims between them, with prejudice. At the same time, they also agreed to carve out and reserve certain issues related to the negotiated "setoff" for subsequent litigation in the bankruptcy court. As a general rule, if the language of a settlement agreement is susceptible to only one meaning, then no amount of protestation could relieve the parties from its terms. See *Roden v. Bergen Brunswig Corp.* 107 Cal.App.4th 620, 629 (2003). However, the Settlement Agreement here is not clear and unambiguous and it is susceptible to more than one meaning.

Despite numerous references to "payment in full" and "release of claims," the Settlement Agreement is qualified by the Bankruptcy Litigation Clause which purports to reserve for future litigation any "setoff achieved by this Settlement." Without the Bankruptcy Litigation Clause, the Settlement Agreement would appear to be enforceable as a "full and final settlement" according to Mr. Dykstra's understanding at the time he paid the money. The Bankruptcy Litigation Clause plainly contradicts the remainder of the Settlement Agreement. Its reference to "any setoff achieved by this settlement" renders the Settlement Agreement sufficiently ambiguous that the court must resort to extrinsic evidence, in this case the attorneys' correspondence, to determine what the parties actually did and did not agree to settle. It is clear from the way the term "setoff" and "offset" are used interchangeably in the attorneys' correspondence, and the parties' declarations, that the terms were intended to refer to the "damage" calculation which Dykstra deducted from its Feed Account and did not pay with the Settlement; the $164,958 plus finance charges now at issue in this Adversary Proceeding. It is also clear

that the parties agreed to reserve those "setoff" issues for future litigation.

Accord and Satisfaction.

Dykstra argues, and Plaintiff disputes, that the money it paid pursuant to the Settlement Agreement constituted an "accord and satisfaction" of all claims between the parties. The court is not so persuaded. The concept of an "accord and satisfaction" is defined as:

> An agreement to substitute for an existing debt some alternative form of discharging that debt, coupled with the actual discharge of the debt by the substituted performance. The new agreement is called the *accord*, and the discharge is called the *satisfaction*.

Black's Law Dictionary 17 (8th ed. 2004). (Emphasis original.)

An "accord and satisfaction" requires some agreement between two parties, one of which owes some performance to the other. The agreement must be supported by consideration. However, the essence of the agreement is the substituted performance. *Id.*, citing 1 E.W. Chance, *Principles of Mercantile Law* 101 (P.W. French ed., 13th ed. 1950).

Under California law, a defendant asserting the defense of "accord and satisfaction" must establish three elements:

> (1) that there was a "bona fide dispute" between the parties, (2) that the debtor made it clear that acceptance of what he tendered was subject to the condition that it was to be in full satisfaction of the creditor's unliquidated claim, and (3) that the creditor clearly understood when accepting what was tendered that the debtor intended such remittance to constitute payment in full of the particular claim in issue.

BII Finance Company Ltd. v. U-States Forwarding Services Corp., 95 Cal.App.4th 111, 126 (2002) (citation omitted).

"The question of whether an agreement amounts to an accord and satisfaction is one of the intention of the parties and is therefore a question of fact." *Id.*, quoting *Conderback, Inc. v. Standard Oil Co. of California*, 239 Cal.App.2d 664, 680 (1966). Dykstra bears the burden of proof on this issue. *Id.*, quoting *Rabinowitz v., Kandel*, 1 Cal.App.3d 961, 965 (1969).

Applying these principles to the facts of this case, there is no dispute as to the first

element of Dykstra's new affirmative defense. The evidence establishes conclusively that there was a material dispute between the parties over Dykstra's total obligation on the Feed Account. Dykstra had been complaining to Coast Grain for about two years regarding performance and billing problems. Coast Grain had promised to make compensatory "adjustments" to the Feed Account. Shortly before the bankruptcy, Coast Grain unilaterally cancelled all of its contracts to deliver feed products for a negotiated price. Dykstra was withholding payment of hundreds of thousands of dollars which precipitated the State Court Litigation in the first place.

However, the Second and Third elements of the "accord and satisfaction" defense are more problematic for Dykstra. Theodore Dykstra clearly understood that the payment he made would fully discharge all of Dykstra's obligation under the disputed and unliquidated Feed Account. As Mr. Dykstra stated, "If I had any suspicion that the matter was not completely resolved, I never would have paid the $225,082.51." Unfortunately, Mr. Dykstra's understanding of the Settlement did not equate with Debtor's understanding and intent when it entered into the Settlement Agreement and accepted Dykstra's money. Neither is it consistent with the correspondence between the attorneys that culminated with the inclusion of the Bankruptcy Litigation Clause in the final draft of the Settlement Agreement.

Based on the declaration of John Stellingwerf, Coast Grain's credit manager, it appears that the Debtor was systematically suing its customers to collect its accounts receivable, and then quickly negotiating qualified "settlements" to collect as much cash as possible, fully intending to sue the same parties later in the bankruptcy court for the "setoffs," meaning the balance of the accounts. In the words of Mr. Stellingwerf:

> [I]n March 2002, GREG BRAUN was appointed as Chapter 11 Trustee. At Mr. Braun's request, I began to work for the Trustee in same capacity, that is as Credit Manager, collecting delinquent accounts receivable. In the course of performing those duties, I authorized Mr. Silva to file approximately 80 adversary proceedings to collect delinquent accounts receivable, including this action against DUTCH STAR DAIRY and DYKSTRA FAMILY DAIRY. We had collected all sums not in dispute; this action was an effort to collect the damages that had been subtracted or set off from the account balance in the settlement negotiation process, and remained unpaid.

Mr. Stellingwert's testimony, that the Debtor was trying to collect all accounts receivable "not in dispute," to "setoff" the disputed issues and reserve the "setoffs" for subsequent litigation in the bankruptcy court, appears to be consistent with the above-referenced correspondence between Mr. Silva and Mr. Henry. Mr. Henry clearly described Dykstra's payment as "the undisputed amount" and agreed that any "release" granted in favor of Dykstra would be "contingent upon further proceedings by the bankruptcy court."

Dykstra asks the court to find an "accord and satisfaction" based on the "payment in full on account" inscription on its check. Dykstra relies here on California Civil Code Section 1526 which states in pertinent part:

> (a) Where a claim is disputed or unliquidated and a check or draft is tendered by the debtor in settlement thereof in full discharge of the claim, and the words "payment in full" or other words of similar meaning are notated on the check or draft, the acceptance of the check or draft does not constitute an accord and satisfaction if the creditor protests against accepting the tender in full payment by striking out or otherwise deleting that notation . . . .
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> . . .
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> (c) Notwithstanding subdivision (a), the acceptance of a check or draft by a creditor constitutes an accord and satisfaction when the check or draft is issued pursuant to or in conjunction with a release of a claim.

The problem with this argument lies in the facts that (1) Mr. Silva and Mr. Henry both agreed in negotiations that Dykstra was only paying the "undisputed" portion of its Feed Account. The requisite "disputed claim" did not apply to the amount which Dykstra paid; and (2) the attorneys' correspondence, coupled with the Bankruptcy Litigation Clause of the Settlement Agreement, support the conclusion that there was no intention to release the Debtor's claim for the "disputed" money, the "setoff" amount that was deducted from the Feed Account.

Based on the foregoing, the court cannot find that the Settlement Agreement constitutes an "accord and satisfaction." Mr. Dykstra may have understood and believed in good faith that he was fully and finally paying all that was owed on the Feed Account, but that is not what the attorneys negotiated and documented in the Settlement Agreement

as evidenced by their correspondence and by inclusion of the Bankruptcy Litigation Clause. While Mr. Dykstra was trying to pay off his account, Coast Grain was playing a much different game. Dykstra's counsel apparently understood the Debtor's "game plan" to reserve further litigation in the bankruptcy court as evidenced by his reply letter of December 14, 2001. The court is persuaded that the meeting of the minds, the predicate "agreement" that could support the accord and satisfaction defense, does not exist here.

The Dismissal With Prejudice.

The court now turns to the Dismissal With Prejudice which concluded the State Court Litigation. The bankruptcy court looks to state law to determine the effect of the Dismissal with Prejudice. One California court wrestled with this issue in *Manning v. Wymer*, 273 Cal.App.2d. 519, 78 Cal.Rptr. 600 (Cal.Ct.Appt. 1969). In that case, each party had filed a personal injury lawsuit against the other, for damages arising out of an automobile accident. Wymer settled his dispute in exchange for a payment from Manning's insurance carrier and the parties agreed to dismiss the Wymer action with prejudice. As part of the Wymer settlement, however, the attorneys agreed that dismissal of Wymer's action would not prejudice Mannings' action, even though the reciprocal claims arose out of the same "transaction" for estoppel purposes. Looking first to the "dismissal with prejudice" in Wymer's action, the court stated the general rule that a dismissal with prejudice has the effect of a final judgment on the merits:

> We further recognize that when a dismissal with prejudice is executed and filed in return for a consideration moving from the defendant that such dismissal operates as a complete bar to any future action and has the same legal effect as a common law retraxit. It is the equivalent to a verdict and judgment on the merits and is deemed to bar another suit for the same cause between the same parties.

Id. at 604 (citations omitted).

The court went on to qualify its pronouncement regarding the Wymer dismissal in recognition of the attorneys' agreement to limit its affect:

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> It is clear that the parties here could agree that the dismissal of [the Wymer action] was not to act as a retraxit by Manning. (See *Rothtrock v. Ohio Farmers Ins. Co., 233 Cal.App.2d 616, 623, 43 Cal.Rptr. 716*.) It is also clear that the parties entered into such an agreement. Not only did each of the attorneys execute declarations to that effect, but also they evidenced their understanding by the execution of a stipulation which purported to nullify the dismissal with prejudice on the records and substituted in its place a dismissal without prejudice.
>
> . . .
>
> We believe that attorneys representing [litigants] in settling claims, after obtaining the consent of all parties and by their agreement, as here, may settle a pending suit and receive in exchange therefor a release and dismissal, even a dismissal with prejudice, *[a]nd limit by the terms of their agreement the legal effect of such dismissal to the party who executes it.*

Id. at 604-05. (Emphasis added.)

After reviewing all of the declarations, and the attached evidence which illustrates and explains the Settlement Agreement in this case, the court is persuaded that the Settlement Agreement was not intended to act as a retraxit of all claims arising from or relating to Dykstra's Feed Account. The evidence leads the court to two alternative and mutually exclusive conclusions, either of which fully supports the court's ultimate ruling on the bifurcated issues.

First, the court could find and conclude that the parties agreed in substance to bifurcate the Feed Account into two parts, the "undisputed" portion and the "setoff" portion. Dykstra paid the part which the attorneys agreed was "undisputed" soon after commencement of the State Court Litigation in exchange for an early termination of that proceeding. The remainder of the Feed Account, the part which represented Dykstra's damage claim, was "setoff" from the Feed Account and expressly reserved for litigation in the bankruptcy court. Although, the Settlement Documents purport on their face to provide for a dismissal with prejudice of all claims on the Feed Account, the Bankruptcy Litigation Clause in the Settlement Agreement effectively converts the Settlement to a dismissal without prejudice.

Alternatively, the court could find and conclude that the Settlement Agreement does not reflect the mutual intent of the parties. Dykstra thought he was buying finality - an end to all further litigation with the Debtor. In exchange, Dykstra paid over one-

quarter million dollars and waived any further claim for damages from the bankruptcy estate. The Debtor, in turn, thought that Dykstra was just agreeing to mitigate its damages and to defer the litigation of all disputed issues, which may not have ever been necessary depending upon the outcome of the bankruptcy case. If the Settlement Agreement is so conflicting that the intention of the parties cannot be ascertained, then the Settlement is void and unenforceable. *Cal. Lettuce Growers v. Union Sugar Co.* supra, 45 Cal. 2d at 481. If the court were to conclude that the Settlement is void and unenforceable, then the money Dykstra paid with the Settlement was indeed paid "on account" as alleged in the Plaintiff's first claim for relief. Either way, the Settlement Documents do not preclude the Plaintiff from moving forward with its litigation on all claims for relief.

Conclusion.

Based on the foregoing, the court finds and concludes that the disputed portion of Dykstra's Feed Account, the breach of contract claim in this Adversary Proceeding, was expressly reserved in the Settlement Agreement for future litigation in the bankruptcy court. The state court Settlement does not preclude Plaintiff from proceeding with any claims for relief alleged herein.

By separate order, Dykstra's unopposed motion to amend its responsive pleading will be granted. The court has fully considered and ruled on the new "accord and satisfaction" affirmative defense in this Memorandum.

The court will reset a further final pre-trial conference.

Dated: October 23, 2006

/s/ W. Richard Lee
W. Richard Lee
United States Bankruptcy Judge