UNITED STATES BANKRUPTCY COURT

DISTRICT OF ARIZONA

In Re ARIZONA APPLE ORCHARDS INC., Debtor.	Chapter 11 Case No. 03-14269-GBN
ARIZONA APPLE ORCHARDS INC., Plaintiff, v. VALLEY FARMS, LTD., an Illinois corporation, Defendant.	Adv. No. 03-01048
VALLEY FARMS, LTD., an Illinois corporation, Counterclaimant, v. ARIZONA APPLE ORCHARDS INC., Counterdefendant.	
VALLEY FARMS, LTD., an Illinois corporation, Third Party Plaintiff, v. JACQUELINE CHAWAFATY and JOHN DOE CHAWAFATY, CHARLES CHAWAFATY and JANE DOE CHAWAFATY, and ALAN RICHARDSON and JANE DOE RICHARDSON,	FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER

Third Party Defendants.)
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A portion of the adversary complaint of Chapter 11 debtor in possession Arizona Apple Orchards, Inc., regarding the scope of the bankruptcy claim of Valley Farms, Ltd. was tried to this court as a bench trial on November 14-17 and December 2, 2005. Post trial briefing was completed on January 3, 2006. An interim order was entered on February 7 of 2006, announcing the court's decision.

The court has considered sworn witness testimony, admitted exhibits, adversary pleadings and the facts and circumstances of this case. The following findings and conclusions are now entered:

FINDINGS OF FACT

1. Arizona Apple Orchards, Inc. is an Arizona corporation, qualified to do business in Arizona. Valley Farms, Ltd. is a Watseka, Illinois corporation, also qualified to do business in Arizona. Arizona Apple or its predecessor in 1993 acquired organic and conventional fruit groves and in 1994 or thereafter located a juice processing plant near Wilcox, Arizona. Arizona Apple filed a voluntary Chapter 11 bankruptcy petition in this judicial district on August 13, 2003. Debtor Arizona Apple filed a complaint in this adversary proceeding against Valley Farms on December 4, 2003. The complaint sought a determination that Valley's claimed lien should be set aside and that any unsecured bankruptcy claims it held be determined and liquidated. A counterclaim and third party complaint were subsequently filed.

Grading of apples is pursuant to U.S. Department of Agriculture regulations. Fresh pack is considered the most expensive way to produce product: apples are left in their natural state after machine sorting. Peeler grade apples are often of lesser quality or appearance and are processed by slicing or juicing. Charles Chawafaty, represented his sister, a principal in Arizona Apple, in dealings with Valley Farms. He testified debtor did not utilize fresh pack, but only processed apples, using culls, which are rejects from the fresh pack grading process. While Arizona Apple had juiced peeler apples since 1996, it lacked peeling or slicing capacity and had to rely on contractors. In 1998, debtor embarked on a new process by acquiring the ability to automatically peel, core and slice product through investment in equipment, including a late 1998 to early January of 1999 installation of a color sorting machine. Trial testimony ("test") of Charles Chawafaty, stipulated joint pretrial statement filed September 6, 2005 at III (a), (b), dockets for 03-14269-GBN and adversary 03-01048.

2. Debtor lost its entire 1998 apple crop due to frost and codling moth damage. Arizona Apple received an April 23, 1999 abatement order restricting movement of apples from the Arizona Agriculture Department because of codling moth infestation. In November of 1998, Mr. Chawafaty started discussions with Anthony J. Imburgia, president of Valley Farms, for the purchase of harvested and stored apples from Valley Farms' Wilcox, Arizona organic orchards. Discussions continued telephonically and through faxed documents. When a written

Valley Farms proposal was rejected, Mr. Chawafaty would draw a line through it and fax it back. He also submitted his own written proposals to Valley Farm, in writings signed by debtor's vice president Mary Hoffman or by himself.

In late November of 1998, before written correspondence started,[1] Mr. Chawafaty traveled from debtor's Phoenix offices to Valley Farms' Arizona cold storage facility to determine if Valley had sufficient inventory for debtor's purposes. He and debtor's president, Allen Richardson, were granted full access to the facility and chose 10-12 apples at random from different bins. Although Mr. Chawafaty could not reach the very top bins, he did not request assistance in selecting from those bins. The fruit appeared good. Mr. Imburgia had represented the product was free of codling moth damage, which was prevalent in the area. Later, after inspecting and slicing open the selected fruit, Mr. Chawafaty instituted purchase negotiations. Although he could have conducted further inspections of Valley's stored apples, he chose not to do so. Admitted exhibits ("ex.") 76-79, 90, Chawafaty *id.*, test. of Luis Nava.

3. Mr. Imburgia credibly testified that on December 14, 1998 he reached a final agreement with Mr. Chawafaty for debtor's purchase of all of Valley Farm's remaining bins of cold

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1Mr. Imburgia's recollection is that Mr. Chawafaty, whom he had known since 1996, appeared at the cold storage facility and conducted an apple inspection before negotiations had even started. Test. of Anthony J. Imburgia.

stored apples, rental of 6-7,000 empty apple bins (to be returned steam cleaned) and for storage of the subsequently processed apples on terms. Imburgia provided the terms to corporate secretary Lori Hasselbring to prepare a document and transmit it to Arizona Apple. She did so by faxed letter of December 14 addressed to debtor's vice president Mary Hoffman, known by Valley Farms to have contracting authority. The letter specifically referenced: "PER ANTHONY IMBURGIA AND CHARLES CHAWAFATY TELEPHONE AGREEMENT TODAY." The apple purchase was identified as: "...ALL OF VALLEY FARMS PEELER FRUIT. PEELER FRUIT BEING 2 1/4 INCH SIZE WITH UP TO 10% ALLOWABLE SMALLER FRUIT." The purchased crop included some of the more valuable fresh pack apples. Mr. Imburgia credibly testified he agreed to include the higher grade apples, as Mr. Chawafata requested them and the bulk sale eliminated Valley Farm's labor costs of having to load the move valuable fruit into trays, box the trays and weigh them for sale as fresh pack. He estimates four to five per cent of the purchase was fresh pack. The confirmation letter concluded: "MARY-IF I LEFT ANYTHING OUT, PLEASE CONTACT ME IMMEDIATELY OR VALLEY FARMS LTD WILL CONSIDER THIS A BINDING AGREEMENT." No one contacted Valley Farms to indicate the writing was not the agreement reached. There are no documents that reflect this was not the parties' agreement.[2] Unlike previous Valley proposals

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2Mr. Chawafaty's testimony was that exhibit 86 represented his written rejection of the December 14 letter. This December 21, 1998 cover sheet memo from Ms. Hoffman does no such thing. Ex. 86, Chawafaty *id.*

that were rejected, Mr. Chawafaty did not draw a line through the December 14 document and return it to Mr. Imburgia.

Valley Farms' Wilcox General Manager Luis Nava credibly testified that he believed, from statements and conduct of debtor's plant supervisor Mike Kerr, as well as from Mr. Richardson and Mr. Chawafaty, that Arizona Apple had purchased the entire remaining apple crop. He had accompanied Mr. Chawafaty and Mr. Richardson in their November 1998 inspections of Valley's cold stored apple stock. In December of 1998, he was instructed to stop boxing and shipping apples by Mr. Imburgia. He was further instructed to conduct a bin count of the remaining apples and fax it to Imburgia's Illinois headquarters. Debtor's own president, Alan Richardson, wrote to Mr. Chawafaty in an April 15, 1999 memo that: "Your agreement for AAO to purchase all of the apples in VFL storage puts us in an extremely onerous position." Imburgia *id.*, test. of Lori L. Hasselbring, Nava *id.*, ex. 76, 77, 85, 116.

4. Debtor's position that the contract was for Arizona Apple to purchase whatever amounts of apples it wished, in 100 or 50 bin lots at a time, is based on Mr. Chawafaty's testimony and his earlier written offer of December 10, 1998[3]. Under this theory, all the unprocessed apples setting in cold storage belonged to Valley Farms and could be sold to anyone else at any

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3Mr. Chawafaty's memo does support Mr. Imburgia's testimony that both peeler fruit and fresh pack were contemplated in the purchase. "...let us start with 100 bins from the peeler size and 100 bins of the packaging size..." Ex. 79.

time-leaving Arizona Apple with no dedicated source of supply for its ongoing juicing, peeling and slicing operations. It defies logic for the parties to have agreed on indefinite small lot purchases and for debtor, at the same time, to commit to rent thousands of apple bins. In fact, Mr. Chawafaty himself testified he rejected Mr. Imburgia's initial proposal to only sell debtor apples on an "if available" basis. Nothing in the parties' subsequent behavior supports debtor's view. This certainly includes Valley Farms' increasingly agitated demands for debtor to pay for the apples and move them out of cold storage, to allow maintenance on the cooling equipment and clear space for Valley's 1999 apple and cherry harvest. When debtor finally committed to remove the apples by a date certain, Mike Kerr's written authorization of July 1, 1999 identified them as debtor's apples. Mr. Chawafaty also testified that under his version of the agreement, there was no time limit on when his processed fruit had to be removed from cold storage, even though apples are a perishable commodity. The fact finder does not find this testimony credible. This is not a case of mutual mistake of essential contract terms. Debtor's theory of the contract is neither logical nor credible. The court finds the parties agreed to a purchase of the entire remaining Valley Farms apple crop. Chawafaty *id.*, Imburgia *id.*, Ex. 79, 88-89, 91, 98-100-102.

5. Arizona Apple seeks to offset the Valley Farms' claim by damages from codling moth infested or otherwise inferior apples, which compromised debtor's juicing, peeling or slicing

operations. Debtor supports this allegation by direct evidence, through the testimony of Mr. Chawafaty and by circumstantial evidence, through the testimony of two other witnesses and a document[4]. Clearly, codling moths were active in the area: debtor had lost its entire crop and was under an abatement order from the state agriculture department. Mr. Chawafaty's testimony is that he personally observed codling moth infested apples as early as February of 1999, during visits to debtor's processing operations. Mr. Chawafaty, who is a creditor or shareholder[5], rather than an officer or an employee of the debtor, was not constantly on the premises of debtor's rural operations. Company headquarters are in Phoenix.

Curiously although Valley Farms had allegedly supplied defective produce, Mr. Chawafaty nonetheless entered a stock purchase agreement with Mr. Imburgia in March of 1999, in connection with a buy out or merger of the two companies. This agreement was in effect through May of 1999, while Valley's alleged breaches continued. Mr. Chawafaty describes Valley's breaches as (1) undersized fruit that could not be machine processed, (2) Valley Farm's alleged practice of returning for processing fruit that had already been rejected and (3) Apple

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4Findings six and seven, *infra*.

5Mr. Chawafaty's status was apparently unclear to the U.S. Trustee at the first meeting of creditors. *See* minutes of October 21, 2003 in docket 03-14269-GBN.

quality[6]. When he observed browning of processed fruit in cold storage, he concluded the problem was caused either by Valley's inadequate cold storage or apple quality. Yet Mr. Richardson's memorandum of April 15, 1999 to Mr. Chawafaty identifies the ineffectiveness of the chemical process ("SNOW FRESH") used by debtor as implicated in the browning, without ascribing fault to Valley. *See* ex. 116.

Mr. Chawafaty also concluded Valley was returning rejected apples back to debtor. He reached this conclusion by inspecting Valley's bills of lading. He did not personally inspect returned fruit. He calculated a loss or rejection rate of 60%, based on comparison of input and output records. The witness believes that the processing output records also establish a moth infestation. On two of his plant visits, he personally witnessed undersized fruit at the slicing facility. He insists he orally advised Valley Farms of his complaints, although this did not include Mr. Nava, Valley's on site manager. There are no documents to support his assertions. Mike Kerr was the local Arizona Apple person authorized to select and remove apples from cold storage for slicing. (It would be his job to reject bad apples, according to Mr. Chawafaty). Mr. Kerr was not called as a witness. In fact, no Arizona Apple plant employees testified. Mr. Chawafaty did not personally reject any defective

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6He also complained in his November 16 direct testimony that the slicing plant machinery was damaged through improper adjustments by Valley employee "Veronica." He conceded on cross examination that she was debtor's employee.

apples. Alan Richardson's April memorandum, discussing "our dilemma," fails to mention that it was caused by infestation and small sizing of Valley apples–although Mr. Chawafaty testified he had advised Mr. Richardson of his complaints by this date. Mr. Imburgia, Mr. Nava and Ms. Hasselbring all credibly deny receiving such complaints. None of the extensive correspondence sent by Valley Farms acknowledges receipt of such complaints. Vice president Hoffman's letter of March 25, 1999 encloses payment of $8,000 ". . . on account for the fruit purchase . . ." without mentioning any infestation or quality complaints. She thanks Mr. Imburgia ". . . once more for everything." She signed the letter ". . . for Charles Chawafaty." Ex. 97. By this date Mr. Chawafaty believed the valley apples were bad. Nonetheless he authorized her to make this payment. Now he is requesting it be returned. Three partial payments were made, the first in the amount of $3,000 in 1998. The last payment of $20,000 was received on April 30, 1999. None of the Valley Farms bills of lading evidence fruit returned to cold storage from the processing plant due to rejection by Arizona Apple for moth infestation. Some bills of lading reflect fruit was returned to cold storage because the production line did not run. *See, e.g.* ex. 22. Others indicate fruit returned as culls from the machinery. Ex. 23. It is unclear whether debtor's machinery was rejecting fruit due to apple quality or because of an equipment malfunction. *See* finding eight *infra.* Bills of lading were also used to reflect the return of empty bins when fruit was successfully processed. *See* ex. 27-28. Valley's bills of lading

also track the return of empty bins when attempts to salvage debtor's apples ceased. *See* ex. 43-50, 52-53. Chawafaty *id.*, Imburgia *id.*, Nava *id.*, Hasselbring *id.*, ex. 1-75, 97, 116.

6. Dr. Gerry Bohmfolk is a consulting entomologist who has dealt with codling moth as a grower's consultant and expert witness since 1972. During the growing season of 1997 to 1998 he was retained by Valley Farms regarding its codling moth problem. He dealt often with Luis Nava and occasionally with Mr. Imburgia. He seldom has contact with Mr. Nava today and is no longer retained by Valley Farms. He considered Valley Farms' moth infestation sufficiently serious, that it could have restricted its harvest. He personally inspected Valley's fields and estimated a 50-80% infestation to Valley's crop. He was critical of Valley's compliance with regulators' directives regarding moth infestation and felt it was common for Valley not to timely comply with his recommendations. Dr. Bohmfolk has routinely destroyed his notes and memos regarding these events. He was the supplier of the chemical treatments used by Valley in fighting the infestation. Valley stopped purchasing his products. In 1998 he would also consult with debtor's president, Alan Richardson on a non-contractual basis. He was not asked by debtor's officers to accompany them to Valley's cold storage. When Dr. Bohmfolk visited debtor's slicing plant, no one asked him to inspect the apples there. He heard no complaints nor saw any problems regarding apples being rejected at the plant due to codling moth infestation. He did observe a few unsliced apples. It would be unusual for mature peeler fruit to be used for

slicing if it was as small as 2 1/4 inches in diameter. He believes cold storage facilities should be completely cleaned out at least once a year. Old harvested apples should not be stored with a new crop, in his opinion.

During this time Dr. Bohmfolk did not look or inspect the apples in storage. Normally his job is done by harvest time. He doesn't know if Valley had buyers for its apples or whether any Valley customer rejected apples due to moth damage. It might be possible to select out infected apples to keep stored apples unaffected. Frustrated with Valley, on March 29, 2001 he wrote a letter to the Arizona Department of Agriculture complaining of Valley's lack of compliance with codling moth control requirements. The letter was also signed by two other members of a committee that monitored compliance with control directives, including Jerry C. Cranford. Dr. Bohmfolk does not know what resulted from his letter.

Luis Nava does. Mr. Cranford provided Mr. Nava with a copy of the Bohmfolk letter. Surprised by the complaint, Nava took Cranford to the cold storage facility to verify that Valley did stock and use moth control products. Mr. Nava testified that in July of 2000 he started using abatement products from a Tucson dealer. Valley accordingly no longer purchased product, such as moth pheromones and poisonous fungi from Dr. Bohmfolk. He also responded with an April 3, 2001 memorandum to the Codling Moth Abatement Committee, outlining what Valley Farms had done and would continue to do to meet agriculture department directives.

Nothing more regarding Dr. Bohmfolk's complaint was heard by Valley.

Creditor's 1998 apple harvest was approximately 10,000 bins from five different varieties. Debtor had no crop. Valley had a "real heavy" moth incursion on its orchards' edges, which Mr. Nava principally blames on debtor's nearby infested fields. With Dr. Bohmfolk's help, Valley's three orchards were successfully treated with organic compounds. The consultant would never walk to the interior of Valley's orchards. At most he would walk in the first few exterior rows. Valley maintains spraying and treatment records, as required by law, including records from 1998. Valley has been an organic grower since 1992, as certified by two separate organizations. It has never lost its certification. Test. of Dr. Gerry Bohmfolk, ex. 93-94, Nava *id.*, Imburgia *id.*

7. Ms. Nancy Dudney testified that in 1998 to 1999 she was the fresh pack marketing manager for Valley Farms in Cochise County, Arizona. She left in October of 1999. She remembers rejections of Valley apples in 1998 because of codling moth damage. She first learned of the problem when a shipment to Banning, California was rejected. The problem was discussed with Mr. Imburgia and Mr. Nava, so they would be aware of it. She recalls a 1997 to 1998 moth infestation as well, but no fresh pack apples were rejected at that time. She denies suggestions on cross examination that she has her years confused or that she provided different information during a 1999 meeting with counsel, Mr. Imburgia and Mr. Nava. She recalls up to four truck

loads being rejected. Sometimes Valley would share a truck load with the produce of other growers. Most states where Valley ships product have more stringent fruit handling standards than does Arizona. The rejected apples would be returned to cold storage, placed in bins and sold to fruit processors.

Mr. Nava testified that in 1999 all infected apples on Valley's edges were plowed into the ground at Dr. Bohmfolk's instruction. Valley pickers are trained to look for codling moth damage. Moth damage more than a week old is easy to observe. The infected apple is thrown on the ground in front of a tractor and plow. Valley's five different apple varieties are picked at different times, based on field tests of maturity and sugar content per university extension training. Mr. Nava is in the orchards daily during harvest. It was Dr. Bohmfolk that alerted Mr. Nava to the infestation of debtor's fields.

Valley sorts its apples at the cold storage facility. A defective apple, damaged by discoloration, gouges, bruising or moth infection is discarded before entering cold storage. He has no recollection of a shipment of 1998 apples being returned for moth infestation. He recalls a shipment returned from the Banning, California inspection station for an unknown reason. The apples were unloaded and repacked. Mr. Nava saw nothing wrong with the fruit. No apples were removed or destroyed. The next day they were reshipped to the same customer and not returned. He recalls no other returns or rejections. He does concede that pickers or inspections could miss an infected fruit and some might end up in cold storage. The court finds Mr.

Nava's testimony to be credible on this issue. Debtor has not met its burden to establish a significant moth infestation of inventory purchased from Valley. Test. of Nancy Dudney, Nava *id.*

8. When debtor's employees would pick up a load of apples from storage, Valley personnel would load the fruit, create a bill of lading and require debtor's driver to sign it. Two copies were given to the driver. In early March of 1999 apples were taken for processing at debtor's slicing plant, located less than a mile away. Mr. Imburgia directed Nava to help with problems debtor was having at the plant. Since Valley was charging debtor for Mr. Nava's time, Mr. Imburgia required detailed notes to be kept concerning this work, for reimbursement by Arizona apple. The notes, drafted as memos to Mr. Imburgia and Ms. Hasselbring, were signed by Mr. Nava and included descriptions of the identities and work done by Valley employees at debtor's plant, including his own time. The witness identified Ex. 112 as including a copy of these memos. The notes would be faxed daily, or by the following day, to Valley's Illinois office.

In March, neither conveyor belts nor size chains had yet been installed at debtor's plant. The chains prevent undersized apples from loading into the slicer. Mr. Nava helped assemble and install the chain and belts, but did not obtain, purchase or adjust debtor's chain. He was directed by debtor not to touch the machinery without permission. Acceptable wedges of apples were observed being blown into the reject ("cull") bin. He notified Kerr and debtor employee Philip Ramirez. They

advised another of debtor's employees to adjust the scanner. The problem continued. Even following adjustment, apple wedges continued to be blown into the cull bin, instead of a bin of Snow Fresh preservation solution. Mr. Nava overheard Mr. Kerr request that Ms. Hoffman order more Snow Fresh, as debtor had run out of the product. In March, Mr. Nava also observed evidence of a party at the plant, including empty beer bottles. One bottle was in the Snow Fresh bin, which could be a source of contamination. In his opinion, none of debtor's personnel had been properly trained for the plant, which is why Arizona Apple had to engage Valley's employees for assistance. In his opinion, this inexperience created delay and the processed fruit ran out of shelf life.

In Mr. Nava's opinion, the plant never properly operated for a consistent time. Personnel from the Atlas Company were sent to adjust the equipment. This improved performance, but then the plant ran out of Snow Fresh. When slicing problems occurred, debtor would sometimes store unsliced apples outside the plant in bins. When apples were successfully sliced, the bins would be returned. Valley was required to steam clean the bins, to ensure they were clean, as well as insect and disease free. Not to steam clean returned bins would risk Valley's organic grower certification. Specifications for apple size of at least two 1/4 inch diameter were set into the size chain, ordered by Mike Kerr. Smaller fruit was supposed to be juiced, but debtor's separate juice plant, located 15 to 17 miles away, was not consistently running. Debtor's employees handled all

transportation of the fruit to its plants. Barrels of stored sliced apples started turning brown. Mr. Nava notified Mike Kerr. No one suggested this was caused by moth infestation. Debtor's juice plant became operational, but the juice lines leaked and were drained into the city sewer system. When the high sugar in the juice threatened to destroy the sewer system's bacteria, debtor was prohibited from operating the juice plant. Smaller apples were returned to cold storage without being juiced. These events occurred before July of 1999. The court finds this testimony to be credible. No witnesses from debtor's plants were called as witnesses. Nava *id.*, Ex. 1-75, 112.

9. May is the last date Valley has ever kept apples in cold storage. In May of 1999, Mr. Nava observed that debtor's apples had begun to decay, drip juice and lose their ability to be sliced. This was not caused by moth infestation. No one from Arizona Apple claimed the contrary. The last date the slicer operated was believed to be in March. He can recall no movement of apples by debtor from storage in May. In July of 1999, debtor's apples were still in storage, yet Valley needed space for the next harvest and to do maintenance on the cooling equipment. This was reported to Tony Imburgia. He made a formal written demand for debtor to remove its apples on June 29, 1999. Mr. Chawafaty was granted two time extensions. Mr. Imburgia refused a third requested extension on July 8, 1999. On July 9, 1999 debtor agreed in writing to begin removing fruit and requested Valley employees do the work. The signed writing recites: ". . . Arizona Apple . . . will start moving 30% of

their apples . . . " Mike Kerr brought a flat bed truck and all the fruit was eventually removed. Valley employees loaded debtor's flat bed. Bills of lading were again utilized to keep a record.

Bins holding the decayed fruit had to be steam cleaned. Ordinarily Valley won't charge a customer for steam cleaning bins. The December 14 contract required this cost, since the bins were to leave the premises, beyond Valley's control. Purchased fruit does not remain in cold storage in Valley's bins long term, but is usually promptly shipped to the customer. The parties did not anticipate that debtor's fruit would remain long in Valley's Wilcox facility. This event was caused by disruptions and failures at Arizona Apple's plants. Valley was not responsible for the disruptions and plant difficulties. Because debtor failed to timely remove its produce, Valley was unable to conduct routine maintenance on cooling equipment. It blames debtor for resulting breakdowns and has billed $16,921.74 for emergency repairs, although this charge was not included in the original contract. The cooling system requires both gas and electric service. Debtor was charged for both utilities, although the contract only requires payment for electricity. The court finds the charge for gas utilities is improper, as not within the December 14 written contract. It was Valley's responsibility to correctly specify contractually the utilities for which it sought reimbursement. Debtor was billed for cold storage for the period March 3 through July 31 of 1999. The contract identifies cold storage rent commencing ". . . UPON

THE 1ST RECEIPT OF PROCESSED PRODUCT INTO STORAGE . . . . Invoice 4706 identifies that initial delivery date as March 3, 1999. *See* ex. 109. Debtor is not liable for earlier storage expenses, including electricity, if any were billed.

Valley was required to steam clean the residue from debtor's decayed apples to retain its organic grower designation. Creditor charged its normal five dollars per bin steam cleaning cost for this work. Although invoices were mailed to Arizona Apple, it did not make billing objections. Nonetheless, Ms. Hasselbring would make adjustments or changes to billings when the need arose. She concedes that invoices 4610-11, 4614, 4652, and 4655-56 erroneously list net ten day terms rather than the net 60 day terms reflected in the contract. She made this error out of habit, as the company's usual terms are net ten days. Mr. Chawafaty had negotiated a special rate with Mr. Imburgia.

The December contract required full payment in sixty days. Debtor did not timely or fully pay. Valley accordingly began charging its customary two per cent per month finance charge effective March 31, 1999 in invoice 4733, listing a finance charge of $6,819.42. Debtor made a $20,000 payment the next month "on account" without objecting to the finance charge. The court finds that given debtor's failure to timely make full payment, imposition of Valley's customary finance charge is reasonable. Creditor however, must ensure that all finance charges are based on the contractual net 60 day terms, not its

customary net ten day terms. Nava *id.*, Ex. 85, 100-102, 106, 109-111, 119, Imburgia *id.*, Hasselbring *id.*

10. After the fruit was removed from cold storage in July, it was dumped or buried on debtor's land at debtor's expense. Mr. Chawafaty explains this circumstance by asserting Mr. Imburgia falsely told regulators the apples belonged to debtor and needed dumping. There are no documents or supporting evidence for this claim. It is not credible. It is undisputed debtor agreed in writing to pay Valley for using its employees to dump 3,200 to 3,400 bins of the fruit on debtor's land. It is undisputed that the dumping was preceded by a series of oral and written requests and a final demand that debtor's fruit be removed. Mr. Chawafaty previously requested, and received a number of extensions for removal[7]. His testimony, that he agreed to pay $6,000 to $10,000 for the removal of "Valley's" apples and permitted the dumping of thousands of bins of fruit on debtor's land, "to close the chapter" as a gesture to Mr. Imburgia is not credible. Chawafaty *id.*, Ex. 89, 91, 98-102, Nava *id.*

11. In summary, debtor's attempt to essentially present its case through the testimony of one witness, apparently neither an officer nor an employee of the debtor, who generated few contemporaneous documents, who was not constantly on the scene and apparently did not keep debtor's president and vice president informed of his oral agreements was not persuasive to

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7His testimony that his extension requests instead involved an alleged side agreement to juice "Valley's" apples is unsupported by other evidence and is not credible.

this fact finder. Valley created and maintained contemporaneous business records. Its witnesses presented more logical, reasonable testimony about disputed factual issues.

12. To the extent any of the following conclusions of law should be considered findings of fact, they are hereby incorporated by reference.

CONCLUSIONS OF LAW

1. To the extent any of the above findings of fact should be considered conclusions of law, they are hereby incorporated by reference.

2. Jurisdiction of debtor's Chapter 11 reorganization case is vested in the United States District Court for the District of Arizona. 28 U.S.C. §1334(a) (1994). That court has referred all cases under Title 11 of the United States Code and all adversary proceedings and contested matters arising under Title 11, or related to a bankruptcy case to the United States Bankruptcy Court for the District of Arizona. 28 U.S.C. §157(a), Amended District Court General Order 01-15. This adversary having been appropriately referred, this court has core bankruptcy jurisdiction to determine the scope of Valley's claim against the bankruptcy estate. 28 U.S.C. §157 (b) (2) (B). No party suggested to the contrary.

3. This court's conclusions of law are reviewed *de novo*. Its factual findings are reviewed for clear error. *Hanf v. Summers (In re Summers)*, 332 F. 3d 1240, 1242 (9th Cir. 2003). Findings of fact, whether based on oral or documentary evidence, will not be set aside unless clearly erroneous. Due regard is

given to the opportunity of the bankruptcy court to judge the credibility of witnesses. Rule 8013, *F.R.B.P.* The appellate court accepts the bankruptcy's court's findings, unless upon review, it is left with the definite, firm conviction that a mistake has been committed. *Ganis Credit Corp. v. Anderson (In re Jan Weilert RV, Inc.)*, 315 F. 3d 1192, 1196 (9th Cir.) *Amended by* 326 F. 3d 1028 (9th Cir. 2003).

4. A contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the contract's existence. A.R.S. 47-2204 A. The statute of frauds applies to a contract for the sale of goods of $500 or more. 47-2201 A. The requisite writing must be sufficient to indicate that a contract has been made and must be signed by the party sought to be charged. The writing is not insufficient because it omits or incorrectly states an agreed term. *Id.*

The December 14, 1998 written agreement was drawn by Valley to place in writing the parties' oral agreement regarding the sale of apples, rental of apple bins and cold storage space. The document is signed by Lori L. Hasselbring, Valley's corporate secretary. It is not signed by an authorized representative or agent of debtor. This fact is not conclusive as to the document's binding effect, due to the statutory exception for confirmatory memos between merchants. Both companies clearly qualify as merchants. *See* A.R.S. 47-2104 A. If within a reasonable time, a writing in confirmation of the contract and sufficient against the sender is received and the receiving party

has reason to know its contents, it satisfies the requirement for a writing, unless written notice of an objection to its contents is given within ten days. A.R.S. 47-2201 B. The court concludes the December agreement is binding against Arizona Apple as a confirmatory memo between merchants. Subsequent contracts were made for provision of labor by Valley to clear debtor's orchards of infected fruit, assist at debtor's slicing plant and dispose of debtor's ruined apples. To the extent the Arizona statute of frauds applies to these service contracts, the statue is met by the signed statements of March 12 and July 1 of 1999 and Valley's billings, to which debtor made no objection.

5. Acceptance of the goods sold pursuant to the contract occurs when the buyer, after a reasonable opportunity to inspect, signifies to the seller that the goods are conforming or that buyer will take or retain them in spite of their non-conformity or fails to make an effective rejection after a reasonable opportunity to inspect. A.R.S. 47-2606 A. Once goods are accepted, the buyer must pay their contract price, rejection is precluded and buyer must notify the seller within a reasonable time of any breach with respect to the accepted goods. The burden is on the buyer to establish any breach. A.R.S. 47-2607 A-D. The court concludes that under the facts of this case, debtor accepted the goods and failed to timely notify Valley of any breach. Further, debtor failed to meet its burden to establish a breach of the contract by Valley.

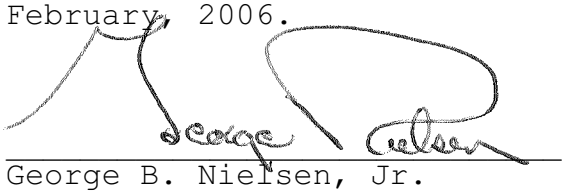
6. When the buyer fails to pay the price as it becomes due, the seller may recover the price of the accepted goods and

any incidental damages. A.R.S. 47-2709 A. Incidental damages to an aggrieved seller include any commercially reasonable charges, expenses or commissions in the transportation, care and custody of goods or otherwise resulting from the breach. A.R.S. 47-2710. The court concludes debtor has breached the contract by failing to pay the contract price as it became due. Valley's claim includes all unpaid charges reflected in the contract, the customary finance charge of two per cent monthly, accruing prepetition and all unpaid amounts from the additional contracts between the parties for provision of Valley employee services and labor to debtor. Incidental damages include emergency repair costs caused by debtor's failure to remove its produce from cold storage within a reasonable time, following repeated demands.

ORDER

Debtor's offsetting damage claim is dismissed. Creditor's claim against the estate will be sustained, with the proviso that cold storage costs and reimbursement for electric service will commence no earlier than March 3, 1999. The claim for reimbursement for gas utility service will be denied. Compounded finance charges of two per cent monthly, from March 31, 1999 until debtor's bankruptcy filing of August 13, 2003 on the unpaid claim balance will be sustained.

DATED this 22nd day of February, 2006.



George B. Nielsen, Jr.
United States Bankruptcy Judge

Copies e-mailed this 22nd day
of February, 2006, to:

John M. McKindles
MCKINDLES LAW FIRM, PLLC
1108 E. Greenway, Suite 1
Mesa, AZ 85203
Email: john.mckindles@azbar.org
Special Counsel for Arizona Apple
Orchards Inc.

Lawrence D. Hirsch
HIRSCH LAW OFFICE, P.C.
5020 E. Shea Blvd., #150
Scottsdale, AZ 85254
Email: Lawrence.Hirsch@azbar.org
Attorney for Plaintiff Arizona Apple
Orchards, Inc.

Steven M. Cox
WATERFALL ECONOMIDIS CALDWELL ET AL
Williams Center Eighth Floor
5210 E. Williams Cr
Tucson, AZ 85711
Email: smcox@wechv.com
Attorney for Valley Farms, Ltd.

By:/s/Rachael M. Stapleton
Judicial Assistant