68178-8

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No. 681788 -I

IN THE COURT OF APPEALS
STATE OF WASHINGTON
DIVISION ONE

WASHINGTON FEDERAL SAVINGS & LOAN ASSOCIATION,

Respondent/Plaintiff,

v.

MARK A. McNAUGHTON and MARNA L. McNAUGHTON, husband and wife, individually and the marital community comprised thereof,

Appellants/Defendants.

APPELLANTS' REPLY BRIEF

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I. INTRODUCTION

Two issues arise in this appeal. First, the trial court failed to apply the correct legal definition of "Fair Value" when granting Washington Federal ("WaFed") summary judgment. Without the correct legal definition, no standard exists against which to apply the facts.

Second, the trial court failed to recognize that genuine issues of material fact do exist. That is, the foreclosure sale of this property occurred in the midst of the worst economic downturn in generation. WaFed's appraiser neither adjusted his valuation for "normal" economic conditions nor did he include the value of the sewer lift station servicing the property (by his own admission). Both of these facts, and others discussed below, created material issues of fact that should have precluded summary judgment.

In defending the trial court's decision, WaFed mistakenly asserts that Appellants, the McNaughtons, must affirmatively prove their case on summary judgment. But the standard required by Civil Rule 56 requires that the defending party must show either (1) that the moving party has not met their burden of proof, or (2) that material issues of fact preclude summary judgment. Moreover, all evidence submitted must be construed in the light most favorable to the non-moving party. The trial court did

not properly apply this standard and, therefore, erred in granting summary judgment against the McNaughtons.

II. MEA CULPA AND STATEMENT OF ISSUES

WaFed is correct that Appellant's opening brief erroneously left out the Statement of Issues. For that the undersigned is deeply embarrassed and begs the Court's forgiveness.

The first two issues identified by WaFed are correctly stated; however, they should be reversed. The issue of whether the correct legal standard was applied (and it was not) should be decided before determining whether issues of material fact exist (and they do). Moreover, the third issue identified by WaFed, whether latecomer's fees were included in the appraiser's value of the properties is not a separate issue in and of itself. Moreover, it is not the receipt of latecomers' fees that is at issue, but rather the actual value of the sewer lift station that WaFed's appraiser failed to include in his appraisal.

III. THE TRIAL COURT APPLIED THE WRONG LEGAL STANDARD

"Fair value" and "market value" do not have the same legal definition. Like an upset price set in judicial foreclosures, "fair value"

adjusts for the duress under which the parties are acting; "market value" does not.

A. The Correct Legal Standard Must be Determined Before Applying the Facts to the Law

Attempting to determine whether issues of fact exist before establishing the correct legal standard puts the proverbial cart before the horse. For example, in Martin v. Abbot Lab., 102 Wn.2d 581, 689 P.2d 368 (1984), the Washington Supreme Court reversed summary judgment because of the application of the wrong legal standard to successor corporations for strict product liability: "Given the trial court's apparent application of an incorrect legal standard – one that does not take into account our adoption of the Ray v. Alada Corp., 19 Cal. 3d 22, 560 P.2d 3 (1977) criteria – and given the facts recited above which arguably support a finding of successor liability, we hold that the trial court erred in granting ... summary judgment." Id. at 616-17. The trial court remanded the case to the trial court for further proceedings.

And in Antonius v. King Cnty., 153 Wn.2d 256, 103 P.3d 729 (2004), the Washington Supreme Court reversed summary judgment on statute of limitations grounds for King County on a hostile work environment claim under the Washington Law Against Discrimination:

"[T]he trial court did not assess the County's motion for summary judgment under Morgan [536 U.S. 101, 122 S.Ct. 2061, 152 L.Ed.2d 106 (2002)]. In these circumstances, where the trial court applied the wrong legal standard to determine whether summary judgment was appropriate, the proper course is to remand this case to the trial court." Id. at 271.

The same analysis applies here. The McNaughtons challenge the legal definition WaFed uses to come to the conclusion that Horizon's (WaFed's predecessor-in-interest) credit bid at the trustee's sale in September 2009 represents "fair value" for the property. Before that analysis can happen; however, the definition of fair value must be established.

As WaFed concedes, the definition of market value does not mirror that of fair value as defined in the statute. Opp. p. 28 (This definition practically mirrors the definition of "fair value.") (emphasis added). The market value definition used by WaFed fails to include any requirement that the parties NOT be under duress – in stark contrast to how fair value is defined under RCW 61.24.005(6). ("...the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under duress") (emphasis added). Indeed, WaFed cites to no legal authority for the proposition that fair value is synonymous with market

value. Without adjusting for the duress under which the McNaughtons and WaFed found themselves – foreclosure of a property with preliminary plat approval in the worst economic downturn seen by the Puget Sound Area in over 80 years – a trier-of-fact cannot determine whether or not the price Horizon paid at the trustee's sale equals fair value.

B. Upset Price Definitions Apply to Fair Value

Further, and contrary to WaFed's arguments, the only practical difference between "fair value" in the Deeds of Trust Act and the "upset price" in the Foreclosure Act is timing. In a judicial foreclosure action, a borrower or guarantor has a statutory right to request that the court determine an upset price either before or after the foreclosure. Under the Deeds of Trust Act, only a guarantor has the statutory right to a fair value determination but only after the nonjudicial foreclosure. Compare RCW 61.12.060 with 61.24.100(5). That is, the fact that a fair value hearing is "in lieu of" a right to establish an upset price means only that fair value must be determined after – not before – a nonjudicial foreclosure. See RCW 61.24.100(5) ("This section is in lieu of any right any guarantor would otherwise have to establish an upset price … prior to a trustee's sale.") (emphasis added).

This limitation in the case of nonjudicial foreclosures makes sense as one of the purposes of the Deeds of Trust Act is to provide an expedited process by which lenders may foreclose. Cox v. Helenius, 103 Wn.2d 383, 387, 693 P.2d 683 (1985) ("[T]he nonjudicial foreclosure process should remain efficient and inexpensive."). Allowing a fair value determination before a nonjudicial foreclosure would run counter to such an expeditious purpose. Indeed, WaFed cites to no legal authority in arguing against such an interpretation.

Furthermore, the Foreclosure Act uses "upset price" and "fair value" interchangeably. See Nat'l Bank of Wash. v. Equity Inv., 81 Wn.2d 886, 926, 506 P.2d 20 (1973) ("We think that the statute means that the upset price should reflect 'the fair value of the property,' for the term 'fair value' appears twice and the term 'value' once in the statute.") RCW 61.12.060 provides that if an upset price has not been determined before the foreclosure sale, then "the fair value of the property be credited upon the foreclosure judgment." (Emphasis added). The use of "upset price" and "fair value" interchangeably by the Foreclosure Act, and the incorporation of "fair value" in the Deeds of Trust Act, demonstrates that the legislature knew what they were doing when they used the term "fair value" in the context of nonjudicial foreclosures. Accord Simpson Inv.

Co. v. State, Dep't of Revenue, 141 Wn.2d 139, 3 P.3d 741 (2000) ("It is well settled that when the same words are used in different parts of a statute ... the meaning is presumed to be the same throughout."); see also State v. McNeal, 156 Wn. App. 340, 352, 231 P.3d 1266 (2010) ("In discerning the plain meaning of a provision, [the court] consider[s] the entire statute in which the provision is found, as well as related statutes or other provisions in the same act that disclose legislative intent.") (emphasis added); Graffell v. Honeysuckle, 30 Wn.2d 390, 191 P.2d 858 (1948) ("In construing statutes which reenact, with certain changes, or repeal other statutes, or which contain revisions or codification of earlier laws, resort to repealed and superseded statutes may be had, and is of great importance, in ascertaining the intention of the legislature.")

C. Public Policy Considerations Support Using a Definition of Fair Value Consistent With That of an Upset Price

Under WaFed's interpretation of the law (in which "upset price" and "fair value" are substantively different), a guarantor's legal defenses are subject to the whims of the lender because the decision on how to foreclose is entirely up to the lender. That is, if market conditions were not "normal" at the time a lender wanted to foreclose (as was the case in 2009 when Horizon foreclosed), the lender would choose to foreclose

nonjudicially to prevent the guarantor from arguing that the deficiency under "normal market conditions" would have been lower with an upset price determination. Said another way, WaFed seeks the right to limit a guarantor's legal protections by avoiding a judicial foreclosure in which an "upset price" could be set that took into account "normal" economic conditions.

But public policy seeks only to make the lender whole, not to enable excess recovery. See, e.g., Crown Controls, Inc. v. Smiley, 110 Wn.2d 695, 703, 756 P.2d 717 (1988) (finding that imposition of joint and several liability would not result in a windfall to the creditor because "his aggregate recovery is limited by the amount of the judgment."); Epley v. Hunter, 154 Wash. 163, 281 P. 327 (1929) (reversing j.n.o.v. because sufficient evidence existed that creditor and sheriff took possession of property well in excess of amount to which creditor was entitled); see also Walter E. Heller Western, Inc. v. Bloxham, 221 Cal. Rptr. 425, 427-28 & 430 (1985) (discussing California's deficiency statute as "designed to prevent creditors from buying in at their own sales at deflated prices and realizing double recoveries by holding debtors for large deficiencies;" and also providing that "[t]he unmistakable policy of California is to prevent excess recoveries by secured creditors.") Even WaFed concedes that the

point of the Deed of Trust Act's fair value provision "is to protect against the possibility that the property was sold at an artificially low price by virtue of the context in which it was sold." Opp. at 26. Accordingly, it makes no sense that the legislature intended for a guarantor under a fair value determination following a nonjudicial foreclosure to be subject to the possibility of excess recovery by a lender where a guarantor seeking an upset price determination in a judicial foreclosure is not.

IV. DISPUTED MATERIAL FACTS ALSO PRECLUDED SUMMARY JUDGMENT

It is undisputed that the McNaughtons have the burden at trial of producing evidence that the fair value of the foreclosed property exceeded WaFed's (by Horizon) credit bid of $6 million. But the question on summary judgment is different than that at trial. At summary judgment the question is what evidence is necessary for the McNaughtons to demonstrate issues of fact precluding summary judgment. Without citation to any authority, WaFed incorrectly argues the only way the McNaughtons can survive summary judgment is to produce in response to its motion the evidence that they ultimately intended to rely on at trial – i.e. an appraisal. Such an interpretation places an unfair burden on the McNaughtons and does not correctly reflect Washington law.

WaFed makes a lot of noise about what McNaughtons did or did not do in responding to summary judgment (e.g. asserting they didn't produce their own statement of value or an appraisal of fair value), but the McNaughtons' burden was to produce evidence raising genuine issues of material fact, not to prove their case. The McNaughtons presented sufficient evidence showing that the credit bid price (and the appraisals relied on by WaFed) did not reflect "fair value" – an issue of fact. Thus, the credibility of the concluded value of the Sommerwood and King's Corner properties is an issue of fact that must be decided at trial. See, e.g., Morinaga v. Vue, 85 Wn. App. 822, 830, 935 P.2d 637 (1997) (finding that evidence at summary judgment showed both competency and incompetency of the plaintiff; thus, summary judgment was not proper). In other words, the McNaughtons did much more than just "speculate" or "make argumentative assertions that unresolved factual issues remain," as WaFed assets. See Opp. at 29. As discussed below, they presented concrete facts that refute WaFed's assertion that $6 million represents fair value.

A. The Appraiser Failed to Include an Important Comparable

The McNaughtons provided competent evidence that WaFed's appraiser failed to include the Bear Creek Highlands sale in September 2008 as a comparable sale. This sale garnered a much higher price per approved lot than WaFed's concluded value.

WaFed's argument (in a footnote) that this sale was not used because the property was bought by a school district is disingenuous. Property is appraised based on its "highest and best use" not the potential future use anticipated by the owner. In September 2008, the Bear Creek Highlands sold for $110,500 per lot in the "raw," just like Sommerwood. CP 40 (McNaughton Decl. ¶9). Had $110,500 per undeveloped lot been used to value Sommerwood, its value would be in excess of $10 million, and the McNaughtons' deficiency significantly reduced. Even if the Bear Creek Highlands sale were discounted by 35 percent to account for the fact it took place in 2008 rather than 2009, the value per lot would be still higher than WaFed's concluded value: approximately $72,000 per lot (substantially higher than the $40,000 per lot suggested by WaFed's appraiser). This per lot valuation is substantiated by Frontier appraisals

submitted by the McNaughtons (discussed infra) and is significantly higher than the credit bid price.

B. Appraisals of Property in the Immediate Vicinity Value the Properties Higher Than WaFed's Bid Price

The McNaughtons also submitted three appraisals prepared for Frontier Bank for other properties in the immediate vicinity of Sommerwood and Kings Corner that have concluded values much higher than WaFed's.[1] WaFed would make much of the fact that these appraisals are for concluded values of different dates than that of the trustee's sale: July 10, 2009, July 15, 2009, and August 7, 2009. See CP 46, 107, 158. But WaFed undercuts its own argument by relying on its own appraiser's opinion that market conditions remained the same in the time period in which these appraisals were done, which it must do because its own appraisals are dated April 24, 2009, and June 10, 2009. See CP 367-68 (Bryan Decl.); CP 1033, 1151. Moreover, the appraisals presented by the McNaughtons are closer in time to date of the foreclosure sale than appraisals on which WaFed relies.

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[1] WaFed tries to make much of the fact that the McNaughtons did not provide their own conclusion of value. While it is true that the McNaughtons did not produce their own conclusion as to the ultimate value of the properties, the fact remains that they did in fact present information regarding comparable properties, and the valuation of those properties, to demonstrate that Horizon's $6 million credit bid was low and does not represent fair value.

WaFed cannot have it both ways. It cannot rely on its own appraisals without recognizing the relevance of the McNaughton's appraisals of comparable properties – appraisals that demonstrate the existence of issues of fact.

These three appraisals have concluded values of $10,000-$20,000 per lot higher than WaFed's appraisals. CP 60, 119, 170; see generally CP 46-213. Using those values, the Sommerwood property would have been worth more than $7 million, not the $6 million as bid by Horizon Bank – a significant difference to the McNaughtons!

That these appraisals were for different properties is of no moment. Creekstone is located within three hundred yards of Sommerwood, and King's Corner 1 and 2 are located immediately west of and adjacent to Sommerwood. See CP 215. Because of their proximity and similarity to Sommerwood and King's Corner, these three properties are directly relevant to the validity and credibility of WaFed's valuation.

Whether these Frontier appraisals ultimately support the conclusion that the value of the Sommerwood property exceeded Horizon's $6 million credit bid will never be answered if the trial court's ruling stands. But the question is not whether those appraisals demonstrate THE fair value of the properties. Rather the question is

whether these appraisals of comparable properties raise genuine issues of material fact as to whether the fair value exceeds Horizon's $6 million credit bid. And they do.

C. Internal Horizon Documents Valued the Foreclosed Properties Higher Than WaFed's Bid Price

WaFed does not attempt to respond to the fact that Horizon's internal documents value the foreclosed properties at $7,985,000 – much higher than the credit bid at the trustee's sale. See CP 349-59. These documents also call into question the viability and credibility of WaFed's theory that Horizon's credit bid of $6 million represents fair value.

Contrast the concrete facts presented by the McNaughtons:

(1) The Bear Creek Highland's sale at a significantly higher price;

(2) Three appraisals of property adjacent to the property at issue also with significantly higher per lot values;

(3) Horizon's own internal documents valuing the property at more than $6 million; and

(4) As discussed infra, the absence of any valuation of the sewer lift station;

with the absolute lack of any evidence presented in opposition to summary judgment by the non-moving party in Young v. Key Pharmaceuticals, 112 Wn.2d 216, 770 P.2d 182 (1989). There, the non-moving party failed to present any evidence whatsoever that the doctors she sued committed malpractice. Id. at 226-27.

Likewise, in Seven Gables Corp. v. MGM/UA Enter. Co., 106 Wn.2d 1, 13, 721 P.2d 1 (1986), also relied on by WaFed, the non-moving party failed to present any factual evidence as to the unconstitutionality of the state motion picture film distribution statute. Neither of these cases present any factual scenario similar to this case. That is, where concrete evidence disputing values is present in the record, even if the McNaughton's ultimate opinion of value is absent, summary judgment is not appropriate.

At a minimum, the McNaughtons have the right to rely on Horizon Bank's internal valuation of the properties at trial to establish fair value, even if they choose not to have their own appraisal done. After all, "the statute calls not for what the court would determine to be the Minimum value, but rather its Fair value." Nat'l Bank of Wash., 81 Wn.2d at 926.

D. Latecomer's Fees are not at Issue

Latecomer's fees are not an issue in this case, and it is odd that WaFed both complains that the McNaughtons do not discuss them and then argue that they are not relevant. Opp. at 31-32. Moreover, WaFed's appraiser never mentions latecomer's fees. Rather, he states:

> This appraisal does not attempt to establish the value of this lift station beyond recognizing the service that it provides to the plat that is the subject of this appraisal. We strongly recommend that the Client employ experts to establish the contributory value of this structure for properties that are located in the immediate area and would benefit from service provided by this station.

CP 1160 (emphasis in original); see also CP 1042.

The appraiser points out concerns about the value of the sewer lift station, not latecomers' fees. And nothing in the record establishes that WaFed hired any experts to "establish the contributory value" of the sewer lift station for the "properties that are located in the immediate area and would benefit" from its service. CP 1160. The appraiser's admission creates a material fact as to the viability and credibility of WaFed's conclusion of fair value.

V. CONCLUSION

The legal standard for evaluating fair value must be decided first; otherwise the parties have nothing against which to apply their facts to determine if that standard has been met. The trial court did not apply the correct standard for evaluating "fair value" when it granted WaFed's motion for summary judgment. On this basis alone the trial court's order may be reversed. But material factual conflicts also exist that should have prevented summary judgment in WaFed's favor.

The McNaughtons, in responding to WaFed's motion, do not dispute that they did not provide their own appraised value of the properties. But proving their own opinion of value will be their burden at trial. The McNaughtons' burden in responding to WaFed's motion for summary judgment was to demonstrate the existence of material issues of fact. They met this burden by demonstrating that (1) an important comparable sale had been ignored by WaFed's appraiser; (2) three other appraisals of property in the immediate vicinity of Sommerwood and King's Corner had concluded values that are higher than that reached by WaFed's appraiser; (3) Horizon's own internal documents valued the properties higher than WaFed's appraiser; and (4) WaFed's appraiser admits in the appraisals that it did not value the sewer lift station servicing

the properties. Because these facts contradict WaFed's assertion that its valuation is correct, summary judgment should have been denied.

DATED this 2nd day of July, 2013.

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CERTIFICATE OF SERVICE

I, Betty Lou Taylor, hereby certify that on the 2nd day of July, 2013, I caused to be served true and correct copies of the foregoing to the following person(s) in the manner indicated below:

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I certify under penalty of perjury under the laws of the United States and the state of Washington that the foregoing is true and correct.

EXECUTED this 2nd day of July, 2013, at Seattle, Washington.

Betty Lou Taylor