No. 681788-I

DIVISION I, COURT OF APPEALS
OF THE STATE OF WASHINGTON

WASHINGTON FEDERAL SAVINGS & LOAN ASSOCIATION, a federal association,

Plaintiff-Respondent

v.

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

Defendants-Appellants

ON APPEAL FROM SNOHOMISH COUNTY SUPERIOR COURT
(Hon. Thomas J. Wynne)

BRIEF OF RESPONDENT

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I. INTRODUCTION

Appellants Mark and Marna McNaughton ("the McNaughtons") do not dispute that they guaranteed a commercial loan made to their company. They do not dispute that they breached that guaranty when their company defaulted on the loan and they failed to satisfy the debt. They do not dispute that they are liable to Respondent Washington Federal (f/k/a Washington Federal Savings & Loan) for the deficiency left on that debt following a trustee's sale of the company's property. The only issue is whether the McNaughtons are liable for the full amount of the deficiency or something less. The Deed of Trust Act allows a guarantor to claim, as an affirmative defense, that the "fair value" of the foreclosed property was higher than the sale price and, if proven, to receive a corresponding reduction in the amount of the deficiency judgment. RCW 61.24.100(5).

Washington Federal was surprised by the McNaughtons' claim that the property's "fair value" was greater than its $6 million sale price. After all, the sale price exceeded the property's appraised value by nearly $1 million. In discovery, Washington Federal asked the McNaughtons to identify the alleged "fair value," and to produce evidence that this value was more than $6 million. They did neither. When Washington Federal moved for summary judgment, the McNaughtons hired an expert and asked for a CR 56(f) continuance to give him time to appraise the

property. The court agreed, but the McNaughtons still did nothing. At his deposition, the expert admitted that—in the five months since he had been hired—he had not appraised the property, and had no idea whether the $6 million sale price was higher or lower than the property's "fair value."

Washington Federal moved for summary judgment a second time and, yet again, the McNaughtons failed to submit any evidence to show the alleged "fair value" of the property—no lay testimony, no appraisal, no expert report or opinion. The trial court properly granted Washington Federal's motion, concluding that it was not enough for the McNaughtons to simply criticize Washington Federal's appraisals or to speculate that, if different methodology was used, "fair value" might exceed $6 million. Rather, because "fair value" is an affirmative defense for which the McNaughtons bore the burden of proof, to survive summary judgment, they had to make out a prima facie case concerning that essential element of their claim. It is undisputed that they failed to do so. This Court can and should affirm for this reason alone. The McNaughtons' arguments on appeal are ultimately irrelevant and, in any event, equally without merit.

II. STATEMENT OF THE ISSUES

The McNaughtons' opening brief does not get off to a good start. It contains no assignments of error or statement of issues. RAP 10.3(a)(4). It is clear enough, however, that the McNaughtons challenge the trial

court's order granting Washington Federal summary judgment. CP 1-3. Washington Federal submits that the issues on appeal are as follows:

1. Did the trial court properly conclude that the McNaughtons failed to satisfy their burden on summary judgment of demonstrating a genuine issue of material fact when:

   a. The McNaughtons conceded that they personally guaranteed the bank's loan to their company, they defaulted on the guaranty, and they were liable for a deficiency judgment following the bank's non-judicial foreclosure of the company's property;

   b. The McNaughtons sought to reduce their liability based on an allegation that the "fair value" of the property was greater than the $6 million paid for it at the trustee's sale;

   c. A guarantor's right to limit liability for a deficiency judgment based on a property's "fair value" is an affirmative defense for which the guarantor bears the burden of proof; and

   d. Despite receiving a CR 56(f) continuance, neither the McNaughtons nor their expert offered any facts or opinion regarding the alleged "fair value" of the property in opposition to Washington Federal's motion for summary judgment?

2. Does "fair value," as used in RCW 61.24.100(5) and defined in RCW 61.24.005(6), require a court to value property based on

market conditions existing on the date of the trustee's sale and, if so, was the "fair value" of the property less than the $6 million sale price?

3. Does the "fair value" of the property exclude the value of sewer facilities and/or related latecomers' fees that the McNaughtons argued—and another trial court determined—were not part of the property that Washington Federal acquired at the trustee's sale?

III. COUNTERSTATEMENT OF THE CASE

The McNaughtons' "Statement of Facts" is replete with argument, omits reference to key facts, and is devoid of any discussion regarding the procedural background leading up to summary judgment. RAP 10.3(a)(5) (brief of appellant must contain a fair statement of the facts and procedure relevant to the issues without argument). The last defect is particularly glaring since this appeal can and should be decided solely based on the McNaughtons' failure to oppose summary judgment with any evidence concerning the one and only essential element of their affirmative defense: "fair value." The following undisputed facts are dispositive of this appeal.

A. Factual Background

In March 2005, Horizon Bank loaned The McNaughton Group, LLC ("TMG") $11,700,000 pursuant to a business loan agreement and promissory note. CP 695-702; CP 704-07. To secure the loan, TMG granted Horizon Bank a deed of trust on two parcels of real property in

Snohomish County, referred to as the Sommerwood Property and King's Corner Property. CP 690 (McKenzie Decl.), ¶ 4. In addition, Mark and Marna McNaughton, the owners of TMG, each executed a Commercial Guaranty, in which they personally, absolutely and unconditionally guaranteed payment of TMG's indebtedness on the loan. CP 709-14.

TMG agreed to make monthly payments and to pay the remaining balance on the loan plus all accrued interest and other charges on or before a July 31, 2009 maturity date. CP 690 (McKenzie Decl.), ¶ 5; CP 704-07. TMG failed to make the November 2008 installment, and paid nothing thereafter. *Id.*, ¶ 7; CP 1283 (Answer, ¶ 4.1 (admitting TMG's default)). The McNaughtons likewise defaulted on the guaranties, paying nothing toward TMG's debt. *Id.*, ¶ 8; CP 1283 (Answer, ¶ 4.2 (admitting the McNaughtons' default)). As of September 2009, the balance of principal and interest owing on the loan and guaranty was over $12 million. *Id.*

Horizon Bank thereafter initiated the process for the non-judicial foreclosure of the Sommerwood and King's Corner Properties. *Id.*, ¶ 9. The McNaughtons received notice of the trustee's sale, which informed them that they "may be liable for a deficiency judgment to the extent the sale price obtained at the trustee's sale is less than the debt secured by the deed of trust." CP 716-19; CP 1283 (Answer, ¶ 5.2). The McNaughtons still did not cure the default. CP 691 (McKenzie Decl.), ¶ 9. Around the

same time, in preparation for the sale, Horizon Bank had the Sommerwood and King's Corner Properties appraised at a combined market value of $5,045,000. CP 367-68 (Bryan Decl.), ¶¶ 2-3; CP 371-478 (April 2009 Sommerwood); CP 489-598 (June 2009 King's Corner).

The trustee's sale was held on September 18, 2009. CP 691 (McKenzie Decl.), ¶ 10. Horizon Bank was the successful bidder at the sale with a credit bid of $6,000,000—nearly a million dollars more than the appraised value of the Sommerwood and King's Corner Properties. *Id.*; *also* CP 368 (Bryan Decl.), ¶ 4; CP 721-25 (trustee's deed). After applying a credit in the amount of the successful bid, over $6 million still remained owing on the loan and guaranties. *Id.* Shortly thereafter, the FDIC assigned all of Horizon Bank's interest in the loan documents and guaranties to Washington Federal. CP 690 (McKenzie Decl.), ¶ 6.

B. Procedural Background

Washington Federal's First Motion for Summary Judgment. In May 2010, Washington Federal sued the McNaughtons to enforce the guaranties in the amount of the deficiency. CP 1289-1314; *see* RCW 61.24.100(3)(c) (permitting deficiency judgments against guarantors of commercial loans after non-judicial foreclosure). The McNaughtons answered and admitted that they defaulted on the guaranties, but asserted as an affirmative defense a request "that the Court determine the fair value

for the property sold at the trustee's sale, pursuant to RCW 61.24.100(5)." CP 1281-86. As explained in greater detail below, under the Deed of Trust Act, if a guarantor proves that the "fair value" of the foreclosed property is greater than the price paid at the trustee's sale, the guarantor's liability for a deficiency judgment is limited to the difference between the indebtedness and that "fair value." RCW 61.24.100(5).

In an effort to understand the basis for this "fair value" defense, Washington Federal served discovery asking the McNaughtons to identify the "fair value" of the Sommerwood and King's Corner Properties. CP 738-39. The McNaughtons failed to produce any information regarding value, stating only that they were "in the process of identifying an expert witness" on the issue. *Id.* Washington Federal's counsel followed up with a letter, noting the McNaughtons' failure to identify the alleged value of the properties and insisting that it was critical that they supplement their discovery responses "given that the alleged value of the property is your clients' primary defense." CP 754. The McNaughtons replied, but they still made no reference to valuation whatsoever. CP 726 (Fox Decl.), ¶ 3.

On August 12, 2011, Washington Federal moved for summary judgment. CP 1268-76. Washington Federal's motion established that the McNaughtons admitted default on the guaranties; that it purchased the Sommerwood and King's Corner Properties for nearly $1 million more

than the properties' market value; and that the McNaughtons failed to produce any evidence of a greater (or even different) "fair value" under RCW 61.24.100(5). CP 1268-76. Washington Federal also submitted a more recent appraisal, prepared in June 2010, that identified the then-current market value of the properties at $5.1 million—still $900,000 less than what Washington Federal paid for the properties nine months earlier. CP 1030 (McMahon Decl.), ¶ 4; CP 1150-1238 (June 2010 appraisal).

The McNaughton's Motion for a Continuance. In response, the McNaughtons asked for more time under CR 56(f). CP 1015-28. They argued that their recently hired expert, Anthony Gibbons, had not yet had time to prepare a report or complete his analysis. CP 1020; CP 970-71 (Newton Decl.), ¶ 6. The McNaughtons submitted a 3-page declaration from Gibbons in which he summarized his "preliminary opinion" that the 2009 appraisal did "not accurately value the Property as of the date of the trustee's sale." CP 1011-12 (Gibbons Decl.), ¶ 5. Among other things, he stated that the sale price "may not represent the 'Fair Value' of the Property under 'normal' market conditions due to the extraordinary economic conditions beginning in late 2008 and continuing into 2009." *Id.* Gibbons did not, however, conclude that the value of the property was more than $6 million on the date of the sale, nor did he provide any "fair value" appraisal of his own. *Id.* Instead, he wrote that he would "need to

conduct additional analysis and data gathering ... in order to provide a final opinion." *Id.*, ¶ 6. As discussed below, there was no final opinion.

The McNaughtons also argued that Washington Federal's motion was premature because liability could not be determined until a separate lawsuit between Washington Federal and TMG was resolved. CP 1025-26. The other suit, the so-called "Latecomers' Lawsuit," stemmed from TMG's transfer of sewer facilities built on the Sommerwood Property to a local sewer district. In return for the transfer, TMG obtained a right to receive "latecomers' fees" that the district will collect from other property owners who connect to the facilities in the future. CP 42-43 (McNaughton Decl.), ¶¶ 15-17. The fees are intended to reimburse a property owner for the cost of constructing and transferring sewer facilities. RCW 57.22.020. Washington Federal claimed that it owned the right to the latecomers' fees by virtue of its foreclosure, and ownership, of the Sommerwood Property. CP 976-97. In the Latecomers' Lawsuit, the McNaughtons were steadfast that the fees belonged to them (or, more accurately, belonged to TMG), but in this case, they argued that "the deficiency in this action will depend

on the extent to which the court in the Latecomers' Lawsuit determines WaFed is entitled to the Latecomers' Fees." CP 1026.[1]

The trial court refused to delay the proceedings pending the outcome of the Latecomers' Lawsuit, but agreed to continue Washington Federal's motion until December 2011 to give Gibbons time to conduct an analysis and/or appraisal regarding the "fair value" of the Sommerwood and King's Corner Properties. CP 1333-34. Yet no such analysis was forthcoming. When Washington Federal asked the McNaughtons to produce Gibbons' expert report or appraisal, and to supplement their prior discovery responses, the McNaughtons did not respond. CP 727 (Fox Decl.), ¶ 5; CP 771-72. Washington Federal then noted the deposition of Gibbons, and asked the McNaughtons to produce his report in advance of the deposition. The McNaughtons' counsel responded that there was no report and, notwithstanding the December 2011 hearing date, the report "likely won't be completed before the 1st of the year." CP 776.

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[1] The trial court in the Latecomers' Lawsuit ultimately granted TMG summary judgment, concluding that Washington Federal had no right to the latecomers' fees. Washington Federal appealed that judgment, and the appeal is pending. *See Washington Federal Savings & Loan Assoc. v. The McNaughton Group*, Appellate Case No. 68978-9-I. As explained below, the outcome of that appeal will have no effect on this case. The judgment specifically provides that, in the event Washington Federal prevails in the Latecomers' Lawsuit, the amount of the deficiency judgment against the McNaughtons will be reduced by the amount of any latecomers' fees it receives in the future. CP 2-3.

Washington Federal went forward with Gibbons' deposition on November 3, 2011. Gibbons testified that he had been hired in June 2011 and asked to prepare an appraisal of the Sommerwood and King's Corner Properties, but had been "too busy" to do so. CP 249-50 (Gibbons Depo at 31-32). Not only had he not yet prepared an appraisal, he had not done any work on the case since August, when he did the "initial review" summarized in his 3-page CR 56(f) declaration. CP 252, 279 (*id.* at 34, 61). He repeatedly conceded that he had undertaken no effort to appraise the value the properties, and had no idea what their value was on the date of the trustee's sale or any other time. CP 253, 271, 273, 283, 299-300, 310-311, 315, 317-18 (*id.* at 35, 53, 55, 65, 81-82, 92-93, 97, 99-100). Finally, and critically, Gibbons could not and would not testify that Washington Federal's $6 million credit bid was less than the properties' "fair value" on the date of the sale. CP 318-19 (*id.* at 100-101).

Washington Federal's Second Motion for Summary Judgment. Washington Federal then filed an amended motion for summary judgment. Once again, the McNaughton's liability for a deficiency judgment was undisputed; the only issue was the affirmative defense of "fair value" under RCW 61.24.100(5). Mustering both existing and additional evidence, Washington Federal demonstrated that:

- The Sommerwood and King's Corner Properties were thoroughly appraised according to industry standards just months before the September 2009 trustee's sale at a market value of $5,045,000—approximately $1 million less than Washington Federal's credit bid. CP 367-68 (Bryan Decl.), ¶¶ 2, 3; CP 371-598.

- It was the appraiser's expert opinion that the market value of the properties had not materially changed between the date of the appraisals and the date of the trustee's sale, and was less than the $6 million sale price. CP 368 (Bryan Decl.), ¶ 4.

- The Sommerwood and King's Corner Properties were appraised nine months after the trustee's sale in June 2010 at a combined market value of $5.1 million—still $900,000 less than the sale price. *Id.*, ¶ 5; CP 600-88.

- It was the appraiser's expert opinion that the "fair value" definition contained in RCW 61.24.005(5) is consistent with the market value definition in the two appraisals of the properties. CP 4 (Bryan Decl.), ¶ 2.

- Following the foreclosure sale, Washington Federal had received several third-party offers for the property ranging from $3,858,260 to $5,250,00—all less than the $6 million sale price. CP 692 (McKenzie Decl.), ¶ 12.

- Washington Federal had sold the Summerwood Property for $4 million in 2011—less than its pre- and post-foreclosure appraised value. *Id.*, ¶ 13.

- The McNaughtons had failed—despite a CR 56(f) continuance—to produce any evidence, information, appraisal or expert report identifying the purported "fair value" of the properties on the date of the trustee's sale.

- The McNaughtons' own expert had not undertaken an analysis of the properties' value, had not done any work on the case in months, had no opinion on the issue of "fair value," and could not state that the $6 million sales price was more or less than "fair value."

CP 786-805. Regarding the Latecomers' Lawsuit, Washington Federal showed that it was the McNaughtons' position that the latecomers' fees were not part of Washington Federal's collateral and, thus, had no basis to complain that the $6 million sale price did not include the value of those fees. CP 794-95; CP 727 (Fox Decl.), ¶ 8. Washington Federal further noted that the court could, in any event, simply order the McNaughtons' deficiency judgment set-off in the amount of any latecomers' fees Washington Federal might receive in the future. CP 799-800.

The McNaughtons opposed Washington Federal's motion, arguing that the $6 million sale price did not reflect the "fair value" of the Sommerwood and King's Corner Properties and repeating their earlier arguments regarding the Latecomers' Lawsuit. CP 15-35. Amazingly, the McNaughtons still did not offer any evidence to show what the purported "fair value" was—no expert declaration or report; no appraisal; nothing. *Id.* Instead, they pointed to Gibbons' prior CR 56(f) declaration and deposition testimony criticizing Horizon Bank's appraisals (but offering no opinion on "fair value"), and a declaration from Mark McNaughton attaching appraisals of unrelated properties in Snohomish County which, they argued, might be relevant to the "fair value" of the Sommerwood and King's Corner Properties. CP 39-41 (McNaughton Decl.), ¶¶ 9-12.

The trial court would have none of it. On December 7, 2011, the court granted Washington Federal's motion for summary judgment. CP 1-3. The court granted Washington Federal judgment (for the deficiency plus prejudgment interest) in the amount of $7,204,045. *Id.* In the event that Washington Federal prevailed in the Latecomers' Lawsuit (which had not yet been decided) and received latecomers' fees in the future, to avoid the possibility of double recovery, the court ordered that "Washington Federal's judgment shall be reduced by any amounts unconditionally paid to Washington Federal ... pursuant to that certain Latecomers Agreement[.]" CP 2-3. The McNaughtons appealed. CP 1315-18.[2]

IV. ARGUMENT

A. Standard of Review

The standard of review drives the outcome of this appeal. This Court reviews de novo a trial court's order granting summary judgment. *Boguch v. Landover Corp.*, 153 Wn. App. 595, 608, 224 P.3d 795 (2009). The Court undertakes the same analysis as the trial court. *Id.* Summary judgment is appropriate when the pleadings, depositions, and admissions in the record, together with any affidavits, show that there is no genuine

[2] Shortly after filing the notice of the appeal, the McNaughtons filed for bankruptcy, automatically staying the appeal. The bankruptcy court lifted the stay in January 2013 after the McNaughtons agreed to waive the discharge of personal liability on the guaranties.

issue as to any material fact and that the moving party is entitled to judgment as a matter of law. CR 56(c); *Young v. Key Pharms., Inc.*, 112 Wn.2d 216, 225, 770 P.2d 182 (1989). The purpose of summary judgment is to avoid an unnecessary trial. *Young*, 112 Wn.2d at 226.

The moving party has an initial burden of showing no genuine issue of material fact, which can be met by pointing out that there is no evidence to support the other party's claim (or, in this case, affirmative defense). *Id.* at 225 & n.1. The burden then shifts to the nonmoving party to make out a prima facie case concerning the essential elements of his claim. *Id.* If, at this point, the nonmoving party "fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial," the trial court must grant the motion. *Id.* (quoting *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986)). Summary judgment is warranted because "a complete failure of proof concerning an essential element of the nonmoving party's case necessarily renders all other facts immaterial." *Id.*

B. The Trial Court Properly Granted Washington Federal Summary Judgment Because The McNaughtons Failed To Establish An Essential Element Of Their Affirmative Defense.

The McNaughtons' appeal is based on a faulty assumption: that it was Washington Federal's burden to prove that the $6 million sale price for the Sommerwood and King's Corner Properties reflected the "fair

value" of the properties. *See* Opening Br. at 1 ("WaFed seeks to prove that Horizon Bank's credit bid at the trustee's sale of $6 million represents 'fair value' of the property."). The McNaughtons have it backwards. "Fair value" is not an element Washington Federal's claim; it is an element of the McNaughtons' affirmative defense. Thus, as the trial court recognized, when faced with Washington Federal's motion for summary judgment, the McNaughtons could not simply challenge the bank's valuation of the properties; they had to present facts to establish a prima facie case regarding "fair value"—which they failed to do.

1. "Fair Value" Is An Affirmative Defense For Which The McNaughtons Bear The Burden Of Proof.

The Deed of Trust Act generally forbids creditors from seeking a deficiency judgment against borrowers, grantors and guarantors following the non-judicial foreclosure of property secured by a deed of trust. RCW 61.24.100(1). The Act creates an exception where, as here, a deed of trust secures a "commercial loan." In that case, a creditor may bring "an action for a deficiency judgment against a guarantor" if the guarantor is given timely notice of the default, trustee's sale and foreclosure. RCW 61.24.100(3)(c). Although the Act does not define deficiency judgment, "the difference between the sale price and debt is commonly referred to as a 'deficiency.'" *Gardner v. First Heritage Bank,* --- P.3d ---, 2013 WL

2250438, *3 (Wn. App. Mar. 25, 2013) (citation omitted). The Act describes a deficiency judgment against a guarantor in those terms as well. *See* RCW 61.24.042 ("judgment to the extent the sale price obtained at the trustee's sale is less than the debt secured by the deed of trust.").

If a guarantor believes that the sale price was too low (thereby increasing his liability for a deficiency judgment), the Deed of Trust Act gives him the right ask the trial court to determine the deficiency amount in light of the "fair value" of the property, if greater than the sale price:

> In any action against a guarantor following a trustee's sale under a deed of trust securing a commercial loan, the guarantor may request the court or other appropriate adjudicator to determine ... the fair value of the property sold at the sale and the deficiency judgment against the guarantor shall be for an amount equal to the sum of the total amount owed to the beneficiary by the guarantor as of the date of the trustee's sale, less the fair value of the property sold at the trustee's sale or the sale price paid at the trustee's sale, whichever is greater, plus interest on the amount of the deficiency ... and any costs, expenses, and fees that are provided for in any contract evidencing the guarantor's liability for such a judgment. ...

RCW 61.24.100(5). As discussed in detail below, the Act defines "fair value" as the probable price that would have been paid for the property on the date of the trustee's sale assuming the buyer and seller each acted "prudently, knowledgeably, and for self-interest." RCW 61.24.005(6).

Because a "fair value" determination may operate to reduce a guarantor's liability, it is an affirmative defense for which the guarantor,

not the creditor, bears the burden of proof. *Locke v. City of Seattle*, 133 Wn. App. 696, 713, 137 P.3d 52 (2006) ("burden of proof is ... placed upon the party asserting the avoidance"). Indeed, the Deed of Trust Act expressly places the burden of proving "fair value" on the guarantor:

> ... in any action for a deficiency, *the guarantor will have the right to establish the fair value of the property* as of the date of the trustee's sale, less prior liens and encumbrances, *and to limit its liability for a deficiency* to the difference between the debt and the greater of such fair value or the sale price paid at the trustee's sale, plus interest and costs.

RCW 61.24.042 (emphasis added); *cf. Asplundh Tree Expert Co. v. Dept. of Labor and Indus.*, 145 Wn. App. 52, 61, 185 P.3d 646 (2008) (where a statute expressly places the burden of proof on the defendant, it is an affirmative defense, and the defendant must prove all essential elements). Not surprisingly, when the McNaughtons answered Washington Federal's complaint, they specifically plead "fair value" as an affirmative defense (CP 1284), as they were required to do. CR 8(c) (defendant must plead "any matter constituting an avoidance or affirmative defense").

2. Washington Federal Satisfied Its Burden On Summary Judgment Of Establishing The McNaughtons' Liability And The Absence Of Evidence Regarding Fair Value.

It was Washington Federal's burden on summary judgment to demonstrate that there was no genuine issue of material fact on the elements of its claim. The trial court properly concluded that Washington Federal made that showing; the McNaughtons did not—and still do not—

challenge any aspect of Washington Federal's prima facie case. The McNaughtons did not dispute they defaulted on the guaranties. CP 1283 (¶ 4.2: "the McNaughtons admit they defaulted on the terms of the Guarantees"). They did not dispute they received the requisite notice of the trustee's sale. *Id.* (¶ 5.2). They did not dispute Washington Federal's calculation of the "deficiency" based on the difference between the "sale price obtained at the trustee's sale" and "the debt secured by the deed of trust." RCW 61.24.042; *see* CP 691-692 (McKenzie Decl.), ¶ 10.

Washington Federal also easily satisfied its burden regarding "fair value." Because the McNaughtons were required to prove "fair value" at trial, Washington Federal's only burden on summary judgment was to point out the lack of evidence on the issue. *Young*, 112 Wn.2d at 225 n. 1. Washington Federal did just that. CP 793-94. It is undisputed that—despite a CR 56(f) continuance—the McNaughtons never identified the alleged "fair value" of the Sommerwood and King's Corner Properties in any discovery response, appraisal or expert report. CP 726-27 (Fox Decl.), ¶¶ 3, 5; CP 738-39; CP 754; CP 771-72; CP 776. It is likewise undisputed that the McNaughtons' own expert—despite five months on the job—testified that he had made no effort to appraise the properties, had no opinion on their value, and did not know whether the $6 million

sale price was higher or lower than the properties' "fair value." CP 249-253, 299, 310-311, 315-319 (Gibbons Depo at 31-35, 81, 92-93, 97-101).

Indeed, even though Washington Federal had no burden to present facts regarding "fair value," it did so anyway. Washington Federal's expert appraiser testified that the definition of market value contained in the 2009 and 2010 appraisals of the Sommerwood and King's Corner Properties was entirely consistent with the definition of "fair value" contained in RCW 61.24.005(6), and that the value of the properties on the date of the trustee's sale was less than the $6 million sale price. CP 4 (Bryan Decl.), ¶ 2; CP 368 (Bryan Decl.), ¶ 4. Not only was the appraised value of the properties—both before and after foreclosure—nearly one million dollars less than the $6 million sale price, none of the third-party offers Washington Federal received for the properties in the months after the foreclosure even came close to reaching $6 million. CP 367-68 (Bryan Decl.), ¶¶ 2, 3 & 5; CP 692 (McKenzie Decl.), ¶ 12.

3. The McNaughtons Failed To Satisfy Their Burden On Summary Judgment Because They Did Not Present Any Evidence To Show The "Fair Value" Of The Propery.

In the face of Washington Federal's showing, to survive summary judgment the McNaughtons had to "make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." *Young*, 112 Wn.2d at 225.

They couldn't and didn't. Ignoring the burden of proof, the McNaughtons blithely argued that they "need not provide an appraisal of their own or prove the fair value of the Property." CP 30. While they did not need to *prove* fair value on summary judgment, they did need to *present evidence* "to establish the fair value of the property," RCW 61.24.042, and they failed to do so. No where did the McNaughtons once identify the alleged "fair value." CP 15-35. Their brief on appeal is similarly devoid of any such reference. Amazingly, the McNaughtons still did not ask their expert Gibbons to analyze "fair value" or prepare his long-promised appraisal—even though they received a CR 56(f) continuance for that very purpose. They provided no report or new declaration from Gibbons whatsoever.

Rather, as they do on appeal, the McNaughtons simply challenged Washington Federal's appraisals and the sale price, arguing that they may not reflect the "fair value" of the properties. But the McNaughtons cannot create a genuine issue of fact by attacking Washington Federal's evidence on an issue for which it had no burden of proof. Washington Federal's only burden was to prove liability and the amount of the deficiency, which it undisputedly did. To reduce that deficiency, it was the McNaughtons' burden to prove the $6 million sale price was less than "fair value" and, if so, by how much. Without an iota of evidence to show what the alleged "fair value" was, much less that it was greater than the sale price, the court

had to grant Washington Federal's motion. *Young*, 112 Wn.2d at 225 (court must grant summary judgment where there is "a complete failure of proof concerning an essential element of the nonmoving party's case.").

The closest the McNaughtons come to identifying an alleged "fair value" is back-of-the-napkin math based on two unrelated appraisals; they argue that if the per-lot value of the Sommerwood and King's Corner Properties was the same as the per-lot value used in these appraisals, then the properties' value was "potentially" higher than $6 million. Opening Br. at 17-18, 29. It's pure speculation. The appraisals concern *different* land, valued by a *different* appraiser, working for a *different* bank, on *different* dates. There is no evidence that these appraisals are relevant to the value of Sommerwood and King's Corner: the McNaughtons' expert had no opinion, nor did Mark McNaughton testify on the issue; he simply attached the unauthenticated and hearsay appraisals to his declaration. CP 40-41 (McNaughton Decl.), ¶¶ 10-11; CP 45-156. Indeed, even though an owner may give lay opinion on the value of his or her own property, *Port of Seattle v. Equitable Capital Group, Inc.*, 127 Wn.2d 202, 211-12, 898 P.2d 275 (1995), the McNaughtons never even bothered to offer any self-

serving opinion on "fair value" (or market value).[3] This Court can and should affirm based solely on the failure of proof regarding "fair value."

C. There Is No Genuine Issue Of Material Fact That The "Fair Value" Of The Property Was Less Than $6 Million.

The McNaughtons' inability to present evidence regarding the "fair value" of the Sommerwood and King's Corner Properties renders their other arguments on appeal irrelevant. Simply put, it doesn't matter whether Washington Federal used the wrong definition of "fair value" or should have included the value of the sewer facilities; even if the McNaughtons were right on both counts, they made no effort to show that these alleged flaws resulted in a sale price that was less than "fair value," as was their burden. The McNaughtons' arguments are without merit in any event. Even if the Court considers these issues, it must conclude that there are no genuine issues of fact to preclude summary judgment.

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[3] This Court can similarly reject the McNaughtons' suggestion that the 2009 appraisal was flawed because it did not consider the price the McNaughtons allegedly received for the sale of yet-another unrelated property. Opening Br. at 15-16. Here too, there is no evidence linking the price of this property to the "fair value" of the Sommerwood or King's Corner Properties. Mark McNaughton merely recites the alleged sale price in his declaration, and the McNaughtons' expert testified that he did not know if it was a proper comparable. CP 39-40 (McNaughton Decl.), ¶ 9; CP 281-82 (Gibbons Depo at 63-64). In fact, the only evidence on the issue was submitted by Washington Federal, whose expert appraiser testified that the sale was not a valid comparable because, unlike the Sommerwood and King's Corner Properties, the property at issue was not intended for residential development. CP 5 (Bryan Decl.), ¶ 5.

1. "Fair Value" Under RCW 61.24.005(6) Is Not The Same As "Upset Price;" The $6 Million Washington Federal Paid For The Property At The Trustee's Sale Was Far More Than The Property's "Fair Value."

The McNaughtons' primary contention is that the $6 million sale price for the Sommerwood and King's Corner Properties may not reflect "fair value" because it was based on a market value appraisal that took into account the distressed economic conditions in the real estate market present at the time of the trustee's sale. Opening Br. at 3-11, 20-27. In essence, the McNaughtons ask the Court to construe RCW 61.24.005(6), which defines "fair value" in the context of non-judicial foreclosures, to mean the same thing as "upset price" described in RCW 61.12.060, which applies in the context of judicial foreclosures. *Id.* They claim that, if "fair value" is viewed as an "upset price," then Washington Federal would have valued the properties higher for purposes of the trustee's sale—although, as discussed above, neither the McNaughtons nor their expert made any effort to identify what that alleged correct "fair value" would have been.

The McNaughtons' effort to link the concept of "fair value" and "upset price" defies the plain meaning of the statutes. The legislature elected *not* to equate "fair value" with "upset price." Judicial discretion to set an "upset price" is exclusive to the *judicial* foreclosure process set forth in RCW 61.12 *et seq.* *See* RCW 61.12.060. In contrast, the concept

of "fair value," as used in RCW 61.24.100(5) and defined in RCW 61.24.005(6), is exclusive to the *non-judicial* foreclosure process set forth in RCW 61.24 *et seq.* *See Thompson v. Smith*, 58 Wn. App. 361, 365, 793 P.2d 449 (1990) (in non-judicial foreclosures, debtors "relinquished a right ... to a judicially imposed upset price"). Notably, the legislature did not incorporate the concept of "upset price" in RCW 61.24 *et seq.* It did just the opposite: "This section is *in lieu of any right* any guarantor would otherwise have *to establish an upset price* pursuant to RCW 61.12.060 prior to a trustee's sale." RCW 61.24.100(5) (emphasis added). The McNaughtons' extended discussion of "upset price" is wholly inapposite.

The legislature also used different language when defining "upset price" and "fair value," and the latter does not support the McNaughtons' claim that a court is required to ignore current market conditions when valuing the property. The *judicial* foreclosure statute expressly permits courts, when setting an "upset price," to "take judicial notice of economic conditions ...." RCW 61.12.060. This unique statutory language has been construed to give a court discretion in limited circumstances to consider "the state of the economy and local economic conditions," and to fix a minimum "upset price" based on "normal" economic conditions. *Nat'l Bank of Wash. v. Equity Investors*, 81 Wn.2d 886, 926, 506 P.2d 20 (1973). The McNaughtons argue that Washington Federal's appraisals

and/or the sale price erroneously failed to follow this inapposite "upset price" convention of valuing property based on "normal" conditions.

Unlike RCW 61.12.060's description of "upset price," however, RCW 61.24.005(6)'s definition of "fair value" contains no reference to "economic conditions." Nor can the McNaughtons identify any language in RCW 61.24.005(6) that would allow a court to value the property with reference to "normal" or ideal economic conditions. On the contrary, the statute unambiguously requires a court to determine "fair value" based on actual market conditions existing "as of the date of the trustee's sale":

> This value shall be determined by the court or other appropriate adjudicator by reference to the most probable price, *as of the date of the trustee's sale,* which would be paid in cash or other immediately available funds, after deduction of prior liens and encumbrances with interest to the date of the trustee's sale, *for which the property would sell on such date after reasonable exposure in the market under conditions requisite to a fair sale*, with the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under duress.

RCW 61.24.005(6) (emphasis added). The point of the statute 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, *i.e.*, foreclosure. The statute, therefore, requires the court to determine value based on a hypothetical price for the property in an arms-length transaction between self-interested parties. The statute expressly pegs the relevant date for this hypothetical

price as the date of the trustee's sale—not some remote date in the past or future when "normal" economic conditions may exist. *Id.*

To be sure, no prudent, knowledgeable and self-interested buyer—the hypothetical buyer described in RCW 61.24.005(6)—would pay more for a property on "the date of the trustee's sale" than current market conditions dictate. Washington Federal's appraisers recognized this, and they properly appraised the Sommerwood and King's Corner Properties using a "market value" methodology, which they defined as follows:

> Market value means the most probable price that a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, and knowledgeably, and assuming the price is not affected by unique stimulus. Implicit in this definition is the consummation of a sale ... under conditions whereby
>
> 1. Buyer and seller are typically motivated
>
> 2. Both parties are well informed or well advised, and both acting in what they consider their own best interest
>
> 3. A reasonable time is allowed for exposure in the open market
>
> 4. Payment is made in terms of cash in U.S. dollars ...
>
> 5. The price reflects normal consideration for the property sold unaffected by special or creative financing ...

CP 390-91 (citing 12 CFR Part 34, Subpart C, 34.42). This definition practically mirrors the definition of "fair value" in RCW 61.24.005(6), and Washington Federal's expert appraiser testified that the two definitions are entirely consistent. CP 4 (Bryan Decl.), ¶ 2. Indeed, the McNaughtons' own expert conceded that the two definitions were largely the same; when pressed on how they differed, the only thing he could point to was the notion that "fair value" should be construed like "upset price," and value determined with an eye toward "normal" market conditions. CP 267-68, 276-79 (Gibbons Depo at 49-50, 58-61). As explained above, that notion finds no support in the text of the statute or any other authority.

Thus, even putting aside the relevant burdens of proof, there is no genuine issue of material fact on "fair value." The Sommerwood and King's Corner Properties were appraised shortly before foreclosure at a value of $5,045,000. CP 368 (Bryan Decl.), ¶ 3. That valuation satisfied the definition of "fair value" in RCW 61.24.005(6), and was properly based on current market conditions—not "normal" market conditions. The properties' value did not change between the date of the appraisal and the date of trustee's sale. *Id.*, ¶ 4. Thus, the $6 million Washington Federal paid for the properties was nearly a $1 million more than the properties' "fair value." The post-foreclosure appraisal of the properties ($5,100,000), subsequent purchase offers (between $3,858,260 and

$5,250,000) and re-sale price ($4,000,000 for Sommerwood) all confirm that the "fair value" of the properties on the date of the trustee's sale was far less than $6 million. *Id.*, ¶ 5; CP 692 (McKenzie Decl.), ¶¶ 12, 13.

Finally, even if—implausibly—the definition of "fair value" under RCW 61.24.005(6) did require the trial court to ignore current market conditions, it still properly granted summary judgment. It is undisputed the McNaughtons presented no evidence whatsoever regarding the value of the properties under "normal" market conditions, whatever that means, much less that this supposed fair value exceeded the $6 million sale price. When the McNaughtons asked for a CR 56(f) continuance, they told the court that "fair value ... is an issue that requires specific knowledge and expertise." CP 1022. The McNaughtons got their continuance, yet when deposed months later, their expert, Gibbons, candidly admitted:

> Q. Are you able to state at this time that it is probable that the $6 million credit bid at the foreclosure sale was greater than the fair value of the property in September of 2009?
>
> A. Again, I don't know until I've done the work.

CP 319 (Gibbons Depo at 101). As noted, Gibbons never did the work; never appraised the properties; never gave an opinion on "fair value." A nonmoving party may not defeat summary judgment with speculation or argumentative assertions that unresolved factual issues remain. *Seven Gables v. MGM/UA Entm't*, 106 Wn.2d 1, 13, 721 P.2d 1 (1986). But that

is all there is. Washington Federal's evidence of "fair value" is the *only* evidence of value in the record. Regardless of how "fair value" is defined, the McNaughtons failed to raise a genuine issue of material fact.

2. The "Fair Value" Of The Property Does Not Include The Value Of The Sewer Facilities And/Or Latecomers' Fees, And, Even If It Does, The McNaughtons Will Receive A Set-Off In The Amount Of That Value.

This Court must likewise reject the McNaughtons' argument that Washington Federal's appraisal was flawed because it did not include the value of the sewer facilities on the Sommerwood Property. Opening Br. at 11-15, 28-29. There is no dispute that Washington Federal's appraisal did not value the facilities or related right to the "latecomers' fees." *See* CP 381. But as discussed below, the "fair value" of the Sommerwood Property, however defined, cannot include the value of sewer facilities and/or latecomers' fees given the McNaughtons' position (and judgment) in the Latecomers' Lawsuit and, in any event, the issue is moot given the trial court's ruling that the McNaughtons are entitled to a set-off in the amount of any latecomers' fees Washington Federal receives in the future.

To begin with, the McNaughtons' myopic focus on the value of the actual, physical, sewer facilities built on the Sommerwood Property is a red herring. It is undisputed that the McNaughtons (or, more accurately, their company TMG) purported to convey the sewer facilities to the Silver

Lake Water & Sewer District by bill of sale in February 2009—more than six months *before* the September 2009 trustee's sale. CP 42 (McNaughton Decl.), ¶ 15. At that point, according to the McNaughtons, the facilities belonged to the district and were no longer part of the property. Thus, not only was it appropriate to exclude the value of the facilities from the price paid at the trustee's sale, it is necessarily irrelevant to a "fair value" determination "as of the date of the trustee's sale." RCW 61.24.005(6). The only value that matters—as the McNaughtons recognized below (CP 1025-26; CP 1011 (Gibbons Decl.), ¶ 5(c)), but conspicuously ignore on appeal—is the value of the right to receive future latecomers' fees, which TMG acquired a proceeds when it transferred the facilities to the district.

On that issue, the McNaughton's brief is silent (it does not mention the latecomers' fees even once). Because the McNaughtons do not argue that the property's "fair value" includes the right to receive these fees, that issue is waived. *Cowiche Canyon Conservancy v. Bosley*, 118 Wn.2d 801, 809, 828 P.2d 549 (1992). The reason for the McNaughtons' silence is transparent. In the Latecomers' Lawsuit—which they also ignore—the McNaughtons argued that the latecomers' fees belonged to them, and that Washington Federal acquired no right to the fees at the trustee's sale. CP 727 (Fox Decl.), ¶ 8; CP 42-43 (McNaughton Decl.), ¶¶ 15-17. The trial court in the Latecomers' Lawsuit agreed. It denied Washington Federal's

motion for summary judgment (CP 1007-08), and, while this case was on appeal, granted judgment to TMG—holding that Washington Federal "has no security interest in or other claim to Latecomer's Fees." Appendix A.[4] Now that the McNaughtons have won the Latecomers' Lawsuit (at least for the time being), they know they cannot have it both ways.

Regardless, even had the McNaughtons raised the issue of the value of the latecomers' fees on appeal, summary judgment was still proper. Once again, regardless of who had the ultimate burden of proof, the McNaughtons failed to raise a genuine issue of fact because they presented no evidence at all regarding the alleged value of the latecomers' fees and, more importantly, no evidence to show whether that value, when added to the "fair value" of the real estate (however defined), exceeded the properties' $6 million sale price. Like everything else it seems, the

[4] A copy of the judgment in the Latecomers' Lawsuit is attached as Appendix A. This Court can take judicial notice of that judgment, which was entered after entry of judgment, and the filing of the notice of appeal, in this case. ER 201(f); *Ensley v. Pitcher*, 152 Wn. App. 891, 901-902 & n. 9, 222 P.3d 99 (2009) (taking judicial notice of subsequent judgment entered in related case and appeal thereof); *see also* RAP 9.11(a) (appellate court may consider additional evidence on review if, among other things, "additional proof of facts is needed to fairly resolve the issues on review" and "it is equitable to excuse a party's failure to present the evidence to the trial court"). As noted, Washington Federal has appealed that judgment, *see Washington Federal Savings & Loan Assoc. v. The McNaughton Group*, Appellate Case No. 68978-9-I.

McNaughtons' expert Gibbons refused to offer an opinion on the value of the latecomers' fees. CP 289-90 (Gibbons Depo at 71-72).[5]

In the end, however, it simply does not matter whether the latecomers' fees were properly excluded from the appraisal or sale price and/or should be considered part of the property's "fair value." The trial court recognized that it did not have to decide the issue, and this Court doesn't either. In its order of summary judgment, the court ruled:

> Washington Federal's judgment shall be reduced by any amounts unconditionally paid to Washington Federal by the Silver Lake Water and Sewer District (the "District") pursuant to that certain Latecomers Agreement between the District and The McNaughton Group, LLC, date October 7, 2009, and Plaintiff will file a partial satisfaction of judgment reflecting receipt of any such payments.

CP 2-3. In other words, if the latecomers' fees are later determined to belong to Washington Federal, then the McNaughtons' liability will be reduced, dollar-for-dollar, in the amount of any fees Washington Federal actually receives. There is no risk that Washington Federal will receive

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[5] Notably, the McNaughtons cite to documents estimating that the sewer facilities cost $2 million to install and had an as-built value of $3 million, but those documents relate only to the physical facilities, not the value of the contingent right to receive latecomers' fees. Opening Br. at 13-14, 28-29 (citing CP 349-54). As noted, the McNaughtons conveyed the facilities to the district *before* the trustee's sale and, in return, received as proceeds the right to collect latecomers' fees in the future. There is no evidence in the record regarding the value of those fees—the amount of which is uncertain and will not be known until and unless surrounding property owners connect to the facilities and pay the fees.

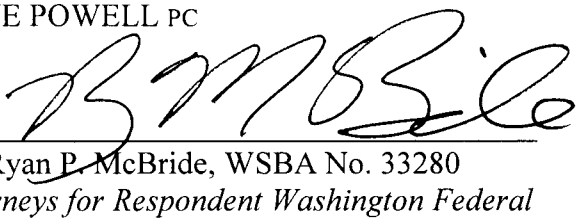
value it did not pay for—even if Washington Federal prevails in the appeal of the Latecomers' Lawsuit. The McNaughtons will get exactly what they want: a credit for the value of the sewer facilities/latecomers' fees.

V. CONCLUSION

It was the McNaughtons' burden to prove that the $6 million sale price was lower that the properties' "fair value" under RCW 61.24.100(5). The McNaughtons had nearly a year and a half, including a CR 56(f) continuance, to muster some evidence on the issue. They couldn't. This Court should affirm the trial court's grant of summary judgment.

RESPECTFULLY SUBMITTED this 4th day of June, 2013.

LANE POWELL PC

By 

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Attorneys for Respondent Washington Federal

CERTIFICATE OF SERVICE

I hereby certify that on June 4, 2013, I caused to be served a copy of the foregoing **BRIEF OF RESPONDENT** on the following person(s) in the manner indicated below at the following address(es):

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- ☐ by **Facsimile Transmission**
- ☐ by **First Class Mail**
- ☑ by **Hand Delivery**
- ☐ by **Overnight Delivery**

Kathryn Savaria

Kathryn Savaria

APPENDIX A

Civil Judge's Calendar
Noted for Hearing: May 22, 2012 at 9:30 a.m.
With Oral Argument
Moving Party

IN THE SUPERIOR COURT FOR THE STATE OF WASHINGTON
IN AND FOR SNOHOMISH COUNTY

WASHINGTON FEDERAL SAVINGS & LOAN ASSOCIATION, a federal association,

Plaintiff,

v.

THE MCNAUGHTON GROUP LLC and SILVER LAKE WATER AND SEWER DISTRICT,

Defendants.

NO. 10-2-10927-5

ORDER GRANTING THE McNAUGHTON GROUP, LLC'S MOTION FOR SUMMARY JUDGMENT AND DENYING WASHINGTON FEDERAL SAVINGS & LOAN ASSOCIATION'S MOTION FOR SUMMARY JUDGMENT

THIS MATTER came before the Court on May 22, 2012 with oral argument on two motions for summary judgment. The first entitled Motion for Summary Judgment by Defendant The McNaughton Group LLC and the second entitled Washington Federal's Second Motion for Summary Judgment. The Court has heard the parties' oral arguments and has considered the following submissions:

1. Defendant The McNaughton Group LLC's Motion for Summary Judgment;

2. Declaration of Christopher I. Brain in Support of Defendant The McNaughton Group LLC's Motion for Summary Judgment;

3. Declaration of Dick Buss in Support of Defendant The McNaughton Group LLC's Motion for Summary Judgment;

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EXHIBIT A

4. Washington Federal's Opposition to The McNaughton Group LLC's Motion for Summary Judgment;

5. Defendant Silver Lake Water and Sewer District's Response to Washington Federal Savings & Loan Association's and the McNaughton Group, LLC's Motions for Summary Judgment;

6. Defendant The McNaughton Group LLC's Reply in Support of Motion for Summary Judgment;

7. Declaration of Brian L. Holtzclaw in Support of Defendant The McNaughton Group LLC's Reply to Motion for Summary Judgment;

8. Washington Federal's Second Motion for Summary Judgment;

9. Declaration of Michael A. Nesteroff in Support of Plaintiff Washington Federal's Motion for Summary Judgment;

10. Declaration of Ronald McKenzie in Support of Motion for Summary Judgment of Washington Federal Savings and Loan Association (Dkt. #12);

11. Defendant The McNaughton Group LLC's Opposition to Plaintiff Washington Federal's Second Motion for Summary Judgment;

12. Declaration of Mary B. Reiten in Support of Defendant The McNaughton Group LLC's Opposition to Plaintiff Washington Federal's Second Motion for Summary Judgment,

13. Declaration of Mark McNaughton (Dkt. #26);

14. Declaration of Ben Giddings (Dkt. #27); and

15. Reply in Support of Washington Federal's Motion for Summary Judgment; and

16. Praecipe to Declaration of Michael A. Nesteroff.

Based on the foregoing and the arguments presented, NOW, THEREFORE,

IT IS HEREBY ORDERED as follows:

1. Defendant The McNaughton Group LLC's Motion for Summary Judgment is **GRANTED**;

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2. Washington Federal's Second Motion for Summary Judgment is **DENIED;**

3. Plaintiff Washington Federal Savings & Loan Association has no security interest in or other claim to the Latecomer's Fees that Defendant The McNaughton Group LLC is entitled to receive under its Latecomer's Agreement with Defendant Silver Lake Water and Sewer District.

ENTERED this _____ day of MAY 31 2012, 2012.

LINDA C. KRESE

_____
Judge, Snohomish County Superior Court

Presented by:

TOUSLEY BRAIN STEPHENS PLLC

By: _____
Christopher I. Brain, WSBA #5054
Mary B. Reiten, WSBA #33623
Attorneys for Defendant, The McNaughton Group LLC

Copy Received; Notice of Presentation Waived:

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By: _____
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By: Eric C. Frimodt

John W. Milne, WSBA #10697
Eric C. Frimodt, WSBA #21938
Attorneys for Defendant Silver Lake Water and Sewer District

ORDER GRANTING THE MCNAUGHTON GROUP, LLC'S MOTION FOR SUMMARY JUDGMENT AND DENYING WASHINGTON FEDERAL SAVINGS & LOAN ASSOCIATION'S MOTION FOR SUMMARY JUDGMENT - 4
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