No. 43043-6-II

COURT OF APPEALS, DIVISION II,
FOR THE STATE OF WASHINGTON

RICHARD APPLEGATE and KAREN APPLEGATE, husband and wife,

Appellants/Cross-Respondents,

v.

WASHINGTON FEDERAL, INC., d/b/a WASHINGTON FEDERAL SAVINGS, a Washington Corporation and Federal Savings and Loan; KITSAP BANK, a Washington Financial Institution; HARBOR HOME DESIGN, INC., a Washington Corporation; CHARLES BUCHER and JANE DOE BUCHER, husband and wife, and the marital community comprised thereof; OHIO CASUALTY INSURANCE CO., Bond No. 3620699,

Respondents/Cross-Appellants.

REPLY BRIEF OF APPELLANTS/CROSS-RESPONDENTS RICHARD AND KAREN APPLEGATE

Philip A. Talmadge, WSBA #6973
Sidney Tribe, WSBA #33160
Talmadge/Fitzpatrick
18010 Southcenter Parkway
Tukwila, WA 98188-4630
(206) 574-6661

Justin Bristol, WSBA #29820
Gourley | Bristol | Hembree
1002 10th Street
Snohomish, WA 98290
(360) 568-5065
Attorneys for Richard and Karen Applegate

TABLE OF CONTENTS

Page

A. INTRODUCTION 1

B. REPLY ON STATEMENT OF THE CASE 1

(1) Reply To Statement of the Case by Respondent WFS 1

(2) Reply To Statement of the Case by Respondents HHD/Bucher 3

C. SUMMARY OF ARGUMENT IN REPLY 4

D. ARGUMENT IN REPLY TO RESPONDENT-CROSS APPELLANT WSF 5

(1) WFS' Argument That the Jury Verdict In Favor of HHD/Bucher Necessitates a Verdict for WFS Is Applicable Only If the Verdict Against HHD/Bucher Is Not Reversed 6

(2) This Case Is Not Controlled by *Tokarz*, Which Did Not Involve a Complex Progressive Construction Loan, But Is Instead an Issue of First Impression for Washington Courts 7

(3) The Independent Duty Doctrine Does Act to Dissolve a Pre-Existing Duty 12

(4) Regarding the Applegates' Contract Claim Against WFS, the Single Most Critical Question on the Verdict Form Was Confusing and Misleading, a Fatal Flaw That Could Not Be Cured By the Jury Instructions 15

E. ARGUMENT IN RESPONSE TO WFS' CROSS-APPEAL 17

(1) Standard of Review 17

(2) WFS, the Drafter of Its Contract, Could Have Written It to Encompass an Action Like the Applegates' and Unambiguously Did Not 19

(3) Even If This Court Concludes the Contract Is Ambiguous, Any Ambiguity Must Be Construed Against WFS 22

F. ARGUMENT IN REPLY TO RESPONDENTS HHD/BUCHER 23

(1) HHD/Bucher's Claim that Floberg Was Not Disclosed in Accordance With the Case Schedule and that a Summary of Floberg's Opinion Is Incorrect, His Exclusion Was Improper 24

(2) The Improper Exclusion of Diana Behrens Testimony Eliminated the Applegates' Ability to Prove HHD/Bucher's Lack of Mistake 27

G. CONCLUSION 29

TABLE OF AUTHORITIES

Page

Table of Cases

Washington Cases

Absher Constr. Co. v. Kent School District No. 415, 77 Wn. App. 137, 890 P.2d 1071 (1995) 18
Affiliated FM Ins. Co. v. LTK Consulting Services, Inc., 170 Wn.2d 442, 243 P.3d 521 (2010) 13, 14, 15
Am. Legion Post No. 32 v. City of Walla Walla, 116 Wn.2d 1, 802 P.2d 784 (1991) 20
Brown v. State, 130 Wn.2d 430, 924 P.2d 908 (1996) 23, 29
Burnet v. Spokane Ambulance, 131 Wn.2d 484, 933 P.2d 1036 (1997) 26
Capers v. Bon Marche, Div. of Allied Stores, 91 Wash. App. 138, 955 P.2d 822, 823 (1998) 16
Corbray v. Stevenson, 98 Wn.2d 410, 656 P.2d 473 (1982) 19
Denny's Restaurants, Inc. v. Security Union Title Ins. Co., 71 Wn. App. 194, 859 P.2d 619 (1993) 18
Elcon Const., Inc. v. E. Washington Univ., 174 Wn.2d 157, 273 P.3d 965 (2012) 13
Guy Stickney, Inc. v. Underwood, 67 Wn.2d 824, 410 P.2d 7 (1966) 23
Hue v. Farmboy Spray, 127 Wn.2d 67, 896 P.2d 682 (1995) 15
Hunsley v. Giard, 87 Wn.2d 424, 553 P.2d 1096 (1976) 15
Hutson v. Wenatchee Fed. Sav. & Loan Ass'n, 22 Wn. App. 91, 588 P.2d 1192 (1978) 10, 11
In re Marriage of Boisen, 87 Wn. App. 912, 943 P.2d 682 (1997) 19
Interstate Prod. Credit Assoc. v. MacHugh, 90 Wn. App. 650, 953 P.2d 812 (1998) 18
Knipschield v. C–J Recreation, Inc., 74 Wn. App. 212, 872 P.2d 1102 (1994) 18
Lancaster v. Perry, 127 Wn. App. 826, 113 P.3d 1 (2005) 24, 25
Mayer v. Pierce County Med. Bureau, 80 Wn. App. 416, 909 P.2d 1323 (1995) 22
Petersen-Gonzales v. Garcia, 120 Wn. App. 624, 86 P.3d 210 (2004) 20
Scoccolo Const., Inc. ex rel. Curb One, Inc. v. City of Renton, 158 Wn.2d 506, 145 P.3d 371 (2006) 21, 22

Shafer v. Board of Trustees of Sandy Hook Yacht Club Estates, Inc., 76 Wn. App. 267, 883 P.2d 1387 (1994), *review denied*, 127 Wn.2d 1003, 898 P.2d 308 (1995) 19
Snyder v. Med. Serv. Corp. of E. Wash., 145 Wn.2d 233, 35 P.3d 1158 (2001) 14
State v. Bisson, 156 Wn.2d 507, 130 P.3d 820 (2006) 23
State v. Brown, 113 Wn.2d 520, 782 P.2d 1013 (1989), *opinion corrected*, 787 P.2d 906 (1990) 28
Stender v. Twin City Foods, Inc., 82 Wn.2d 250, 510 P.2d 221 (1973) 23
Taylor v. Stevens County, 111 Wn.2d 159, 759 P.2d 447 (1988) 15
Tokarz v. Frontier Fed. Sav. & Loan Ass'n, 33 Wn. App. 456, 656 P.2d 1089 (1983) 7, 8, 9, 10
Wachovia SBA Lending, Inc. v. Kraft, 165 Wn.2d 481, 200 P.3d 683 (2009) 21

Other Cases

Daniels v. Army Nat'l Bank, 249 Kan. 654, 822 P.2d 39 (1991) 11
Harden v. Akridge, 193 Ga. App. 736, 389 S.E.2d 6 (1989) 11
Sobi v. First S. Bank, Inc., 946 So. 2d 615 (Fla. Dist. Ct. App. 2007) 11

Statutes

RCW 4.84.330 ..... *passim*

Rules and Regulations

CR 35 ..... 24, 25
ER 403 ..... 27, 28
ER 404(b) 28, 29
PCLR 26(d)(3) 26
RAP 10.3(a)(5) 2

Other Authorities

Random House Dictionary 644 (2d ed. 1987) 20
W. Page Keeton, et al., Prosser and Keeton on Torts § 53 (5th ed. 1984) 15
Webster's Third New International Dictionary 751 (1986) 20
Webster's Third New International Dictionary 591 (1993) 20

A. INTRODUCTION

This case demonstrates why it is no longer acceptable, given modern banking practices, for courts to treat complex progressive construction loans as mere "arm's-length transactions" akin to withdrawals from a saving account. The outdated notion that a bank, having assured its customer of its expertise and cautious practices, can wash its hands of a contractor's wrongdoing should be abolished.

Instead, this Court should set a new standard for these transactions, holding that there is a duty for banks who profit from them to discharge their duties with reasonable care. In so doing, this Court will uphold Washington's long tradition of protecting consumers and holding large financial institutions accountable for violations of the fiduciary duties they undertake.

The question of whether these banks have a duty is not merely academic. Here, had the trial court's exclusion of key evidence not prejudiced Richard and Karen Applegate's ("the Applegates") case, it would have been claim that Washington Federal Savings ("WFS") could have prevented the harm caused by Harbor Home Design and its owner, Charles Bucher ("HHD/Bucher").

B. REPLY ON STATEMENT OF THE CASE

(1) Reply To Statement of the Case by Respondent WFS

WFS offers a long recitation of the facts that unsurprisingly differs from the Applegates' statement of the case. Br. of Resp't WFS at 5-17. In many respects, it violates RAP 10.3(a)(5), which requires a statement of the case to recite facts "without argument." For example, WFS describes the provisions of its adhesion loan contract as "insulat[ing] WF[S] from liability for issues that sometimes arise between an owners and a builder...." Br. of Resp't WFS at 6.

WFS' view of the facts is largely irrelevant, because the Applegates have challenged the trial court's summary judgment ruling, which requires this Court to view the facts in the light most favorable to them. However, some clarifications are warranted.

WFS concedes that this was a "complicated construction project" and that "issues...sometimes arise." Br. of Resp't WFS at 6. WFS also admits that it has a "right" to inspect a project, but insists it does not have a duty to ensure that funds it disburses are legitimately earned. *Id.* at 7.

WFS does not deny, and therefore also concedes, that its loan officer made specific *repeated* representations to the Applegates regarding WFS' policies and actions, reassuring them that the Applegates would be protected from improper disbursements. CP 299, 389.

WFS chastises the Applegates for failing to provide their own written verdict form, Br. of Resp't WFS at 16, but concedes that the

Applegates properly objected to the verdict form and offered their own alternative language to the trial court. Br. of Resp't WFS at 33-37. WFS does not argue that the Applegates have waived their objection. Thus, it is unclear how their failure to provide a written verdict form is relevant to the issues on appeal.

(2) Reply To Statement of the Case by Respondents HHD/Bucher

HHD/Bucher state that their contract with the Applegates "provided for a twenty percent profit," but "does not state that construction payments will be based upon what the builder paid to various subcontractors." Br. of Resp'ts HHD/Bucher at 3. Presumably, they mean to establish a rationale for the fact that they demanded from WFS amounts due to subcontractors that were greater than what those subcontractors charged them. CP 389, 649-50, 652-54.

However HHD/Bucher do not explain how, if their profit was meant to be twenty percent over the underlying costs, inflating those underlying costs did not also constitute an improperly inflated profit.

HHD/Bucher claim that the Applegates withheld payments regarding "some shadows on a ceiling." Br. of Resp'ts HHD/Bucher at 5. HHD/Bucher do not cite to the record in support of this statement. *Id.*

In reality, the Applegates terminated their business with HHD/Bucher over serious concerns about deception, fraud, and misappropriation of their loan funds. CP 390, 624, 626, 649-50, 652-54. The $52,000 the Applegates had deposited with Bucher, was supposed to be credited toward construction costs and deducted from the first WFS draw request. CP 624. It was not, and Bucher later admitted that fact. CP 626. Bucher was claiming to have completed certain items and requesting draws that were higher than the invoice submitted by the subcontractor, such as the foundation and framing. CP 649-50, 652-54. They also noticed that Bucher had billed higher for certain items, such as their deck, than the budgeted amount. CP 389. When the Applegates discovered Bucher had forged Richard Applegate's signature on a draw check for $108,000. CP 390. Bucher did not deny forging the signature on the check. CP 2260. He claimed that Richard Applegate's signature on the CJP confirmed that Applegate had given Bucher permission to sign the check in his name. *Id.* However, Applegate also had not signed the CJP. CP 689. After that, they fired HHD/Bucher.

C. SUMMARY OF ARGUMENT IN REPLY

This Court should establish that banks who profit from complex, progressive construction loans in which they dispense large amounts of their customers' money to third parties have a duty to do so with

reasonable care. This is particularly true where, as here, bank employees made specific, repeated assurances to their customers that reasonable care would be taken. WFS' argument, that these kinds of loans are merely "arm's length transactions," in which the duty of care falls solely on their customers, does not reflect the reality of how these complex loans are controlled and administered.

Regarding WFS' cross-appeal, the trial court properly concluded that WFS' adhesion contract did not, by its own terms, provide for an award of attorney fees to either party. The WFS contract is ambiguous at best, and that ambiguity must be construed against WFS as the drafter of the document. This case does *not* implicate RCW 4.84.330, because the question is not whether an applicable attorney fee clause is reciprocal.

The trial court abused its discretion in excluding two critical witnesses that would have allowed the Applegates to contest HHD/Bucher's central trial defenses: that forgery, fraud and conversion were merely mistakes, misunderstandings, or miscommunications between the parties.

D. ARGUMENT IN REPLY TO RESPONDENT-CROSS APPELLANT WFS

In their opening brief, the Applegates argued that the trial court improperly dismissed on summary judgment their negligence and breach of fiduciary duty claims against WFS. Br. of Appellant at 10-23.

WFS' response is threefold. First, it argues the verdict in favor of HHD/Bucher means that the Applegates were not damaged, and is essentially a harmless error argument. Br. of Resp't WFS at 19-20. Second, it argues that Washington should create a *per se* rule that a bank never has a tort or fiduciary duty in dispensing this kind of complex progressive construction loan, where payments are made directly to the contractor in stages conditioned upon adequate completion of the project. *Id.* at 21-29. Third, it argues that the independent duty doctrine bars any tort claim against it.

In its cross-appeal, WFS argues it should be awarded attorney fees at trial and on appeal based on an attorney fee provision in its contract with the Applegates.

(1) WFS' Argument That the Jury Verdict In Favor of HHD/Bucher Necessitates a Verdict for WFS Is Applicable Only If the Verdict Against HHD/Bucher Is Not Reversed

WFS first argues that the jury's verdict in favor of HHD/Bucher means that even if this Court believes it did have a fiduciary or tort duty in dispensing the Applegates' progressive construction loan, there are no damages because the jury found in favor of HHD/Bucher. Br. of Resp't

WFS at 19-20. In WFS' view, because HHD/Bucher did nothing wrong, any breach of WFS' duty to properly dispense the loan is harmless, and judgment can be affirmed "on that basis alone." *Id.*

What WFS fails to acknowledge are the serious defects in the litigation between the Applegates and HHD/Bucher that have also been appealed. If the Applegates had only appealed the judgment as to WFS, these arguments might hold sway. That is not the case.

This Court is considering verdicts against both defendants, and if it concludes that a new trial is warranted as to HHD/Bucher, then it must also consider the question of whether Washington banks should take reasonable care in dispensing progressive constructions loans.

(2) This Case Is Not Controlled by *Tokarz*, Which Did Not Involve a Complex Progressive Construction Loan, But Is Instead an Issue of First Impression for Washington Courts

In their opening brief, the Applegates argued that the modern practice of dispensing complex progressive construction loans should be considered, at least in some cases if not all, "special circumstances" that create a fiduciary and/or tort duty for banks. Br. of Appellant at 14-19. They argued that, unlike a typical loan where the money is simply handed over to the borrower in one transaction, progressive construction loans involve a complex relationship where the bank dispenses funds directly to

third parties, giving rise to the possibility of malfeasance or negligence. *Id.*

WFS responds by relying entirely on *Tokarz v. Frontier Fed. Sav. & Loan Ass'n,* 33 Wn. App. 456, 458-59, 656 P.2d 1089 (1983). WFS takes an expansive view of *Tokarz,* describing the holding of that case as "no fiduciary relationship exists between a commercial lender and a borrower because the parties deal at arm's length." Br. of Resp't WFS at 22. WFS claims that the Applegates have asked this Court to "change" what WFS calls "this deep rooted tenet of Washington law." *Id.*

WFS has failed to apprehend the Applegates' argument, which does not seek to "change" any Washington law. Rather, the Applegates ask this Court to consider a question of first impression: whether the "special circumstances" test from *Tokarz* – the very authority WFS trumpets – should apply to modern progressive construction loans where banks are actively involved in the ongoing fiscal dealings of their borrowers.

Contrary to WFS' claim, a critical fact in *Tokarz* was the nature of the claimed duty: it was not a claim that the bank negligently handled the disbursement process, but that the bank should have told Tokarz that the contractor was having financial difficulties unrelated to the Tokarz project. *Id.* at 461. The *Tokarz* court did not rule that lenders never have a duty to

borrowers, but rather specifically addressed "whether there was a special relationship between the plaintiff borrower and defendant bank such *as to create a duty to disclose to Tokarz the financial instability* of the builder/contractor." *Id.* Upon that narrow question, Division III of this Court concluded that no evidence of a special relationship existed.

There was no evidence in *Tokarz* of any assurances or guarantees that would have led the borrower to conclude that the lender would keep him informed about the financial health of the contractor. *Id.* at 462-63. The *Tokarz* court suggests that if there had been assurances, special circumstances may have arisen. *Id.*

Here, WFS did make verbal and written representations that it would look out for their interests, and take special care to make sure that their funds were not misused. CP 297-99, 397. This fact alone takes this case out of the realm of *Tokarz.* WFS's "Policies and Procedures" afforded WFS significant control over the disbursement of funds, stated that WFS would "not advance money" for items not installed, and said WFS would have the right to stop work if it was unsatisfactory. CP 397. The Applegates justifiably believed that WFS policies meant that at least, when they complained about potential problems with HHD/Bucher, WFS would investigate. CP 251. When Richard Applegate explained that he and Karen had "never built a house before" and had no idea what they

were doing, CP 389, Cross assured them that they could rely on her "experience and expertise" and that WFS would be "looking out for their interests" and "representing [the Applegates] in the process." *Id.* WFS took on extra services beyond merely lending money. WFS' own policy manual established that WFS assumed extensive control and responsibility over the disbursement process, including on-site progress inspections. CP 397.

WFS claims that all of this evidence is "scant," and that summary judgment was still justified. However, it is not the function of the trial court considering summary judgment to weigh evidence. The issue is whether the evidence is sufficient to create a disputed issue of material fact. Under *Tokarz,* and the rest of the case law in this area, it is.

WFS dismisses the remaining authority the Applegates cite, including *Hutson v. Wenatchee Fed. Sav. & Loan Ass'n,* 22 Wn. App. 91, 588 P.2d 1192 (1978) and several foreign cases that are closely analogous to this case. Br. of Resp't WFS at 27-29. With respect to *Hutson,* WFS argues that this Court should not seek guidance from that decision because it is "limited to its facts." *Id.* at 28. Regarding the foreign cases, WFS first disdains them as "unpersuasive" because they "represent the laws and policies of other states," and then immediately cites cases from other jurisdictions that support WFS' own position. *Id.*

Hutson should not be ignored simply because it is "limited to its facts." It is arguable that every case is limited to its facts, and is only useful precedent insofar as the facts of the present case are analogous to the facts of the cited case. In *Hutson,* particular assurances by a lender to a borrower created an issue of fact as to whether a special relationship existed. *Hutson,* 22 Wn. App. at 105. Here, as explained *supra,* such assurances also created a fact issue for the jury.

Regarding the foreign authority WFS cites in support of its own position, it does nothing more than prove that the issue the Applegates raise is a difficult issue of first impression. Both parties have cited foreign authority dealing with these questions, and this Court is free to adopt or reject the reasoning of other states as it sees fit.

It is notable, however, that none of the cases WFS cites involve the kind of express assurances WFS made to the Applegates, nor do they support the notion that summary judgment was proper here. In *Sobi v. First S. Bank, Inc.*, 946 So. 2d 615, 616 (Fla. Dist. Ct. App. 2007), the plaintiff borrowers actually received a trial on their negligence claims. In *Harden v. Akridge*, 193 Ga. App. 736, 389 S.E.2d 6 (1989) and *Daniels v. Army Nat'l Bank*, 249 Kan. 654, 655, 822 P.2d 39, 41 (1991), the borrowers tried to hold the lender responsible for the contractor's shoddy work, but did not claim (as is claimed here) that the lender had made any

express assurance or negligently made disbursements under false and fraudulent pretenses.

WFS's written policies, combined with the express representations and assurances of its employee, create an issue of material fact as to whether WFS took reasonable care to inform the Applegates and/or take action with respect to critical matters involving the administration of their progressive construction loan, and whether the Applegates reasonably relied upon those policies and assurances.

(3) The Independent Duty Doctrine Does Act to Dissolve a Pre-Existing Duty

Potential negligence in the field of progressive construction loans is an issue of great public import that supports the finding of a duty. Borrowers are essentially entrusting lenders to oversee the disbursal of an amount of money that is, for most people, the largest financial obligation of their lives. Borrowers cede control of the payment of their funds to a professional, who in turn should have a duty to avoid disbursing those funds in a negligent manner. The independent duty doctrine should not bar tort claims such as those brought here, even if the parties' relationship was initially contractual.

The Applegates argued in their opening brief that the trial court erred in applying the independent duty doctrine to bar their claims,

because a special relationship existed. Br. of Appellant at 23. They noted that the doctrine is merely a tool to discern whether a duty exists, and if there is no question that a duty already clearly exists in law, then application of the doctrine is irrelevant. *Id.* Thus, if this Court concludes that a duty exists under the special relationship exception, the independent duty doctrine will not apply. *Id.*

WFS first responds by arguing that because this is a case of first impression, and no Washington court has yet found a duty by a construction lender under the special relationship exception, none can exist. Br. of Resp't WFS at 31. WFS does not respond to the Applegates' argument that, if this Court concludes a special relationship existed, the independent duty doctrine is irrelevant.

WFS' circular logic should be rejected, and its concession accepted. Just because no Washington court has had the chance to consider the issues raised in this appeal, is not a reason to find against the Applegates on the issue of duty. If this Court does so find, then the independent duty doctrine is not at issue. *Elcon Const., Inc. v. E. Washington Univ.*, 174 Wn.2d 157, 165, 273 P.3d 965, 969 (2012); *Affiliated FM Ins. Co. v. LTK Consulting Services, Inc.*, 170 Wn.2d 442, 448-49, 243 P.3d 521, 525 (2010).

WFS next argues that *Affiliated* is distinguishable because it is limited to activities of engineers that may endanger the public. Br. of Resp't WFS at 32.

Again, WFS misapprehends the Applegates' argument. Their reference to *Affiliated* notes that it is a good description of the contours of the independent duty doctrine, not that the facts of this case are identical to the facts of that case. Br. of Appellant at 25.

Affiliated is helpful guidance regarding proper application of the independent duty doctrine, but this Court must apply the doctrine to the facts here to determine if it is relevant. The doctrine is a focusing tool that requires courts to ascertain if a tort duty is actually a contract duty in disguise. Here, if a special relationship between WFS and the Applegates created a duty at law, then the analysis is simple: the doctrine does not dissolve the pre-existing tort duty.

This Court has the opportunity to speak to the issue of whether, in complex progressive construction loans such as the one at issue, particularly when assurances of reasonable care are made, the independent duty doctrine should allow certain tort claims after weighing considerations of "logic, common sense, justice, policy, and precedent." *Snyder v. Med. Serv. Corp. of E. Wash.*, 145 Wn.2d 233, 243, 35 P.3d 1158 (2001). The concept of duty is a reflection of all those

considerations of public policy which lead the law to conclude that a plaintiff's interests are entitled to legal protection against the defendant's conduct. *Taylor v. Stevens County,* 111 Wn.2d 159, 168, 759 P.2d 447 (1988) (citing W. Page Keeton, et al., Prosser and Keeton on Torts § 53 at 357 (5th ed.1984)). Using judgment, courts balance the interests at stake. *Affiliated FM,* 170 Wn.2d at 450; s*ee also, Hunsley v. Giard,* 87 Wn.2d 424, 435, 553 P.2d 1096 (1976) (balancing the interests and holding that the defendant owed the plaintiff "a duty to avoid the negligent infliction of mental distress").

(4) Regarding the Applegates' Contract Claim Against WFS, the Single Most Critical Question on the Verdict Form Was Confusing and Misleading, a Fatal Flaw That Could Not Be Cured By the Jury Instructions[1]

The Applegates argued in their opening brief that the first question on the special verdict form – the only question the jury answered with respect to WFS – was misleading, confusing, and prejudicial to the Applegates' case. Br. of Appellant at 26-28. Despite the fact that the Applegates theory of the case was whether WFS breached its contract improperly administering and disbursing the Applegates' construction loan, the special verdict form asked the jury whether WFS "breached its

[1] WFS correctly notes that the applicable standard of review is abuse of discretion, rather than *de novo.* Br. of Resp't WFS at 34. Counsel for the Applegates cited *Hue v. Farmboy Spray,* 127 Wn.2d 67, 92, 896 P.2d 682 (1995). The issue in *Hue* appeared to be the specific wording of the instruction, but the Court clarified that it was dealing with a claimed misstatement of the law. *Id.*

contract *to provide* a loan...." CP 2739. Because it was undisputed that WFS provided the loan, this confusing wording clouded the issues and likely prejudiced the verdict.

Specifically, the Applegates pointed out that *even when jury instructions are correct,* this Court has set an additional test for special verdict forms that applies even if the jury instructions are legally correct:

> Notwithstanding the legal sufficiency of the instructions, we must find these instructions insufficient *if they are misleading or if the special verdict form clouds the jury's vantage point* of the contested issues.

Capers v. Bon Marche, Div. of Allied Stores, 91 Wash. App. 138, 143, 955 P.2d 822, 823 (1998). This test, specific to special verdict forms, is what this Court must apply. *Id.*

WFS nevertheless argues that the jury instructions, when read as a whole, somehow cured the insufficiency in the verdict form. Br. of Resp't WFS at 35-36. It distinguishes the facts of *Capers,* without actually applying the legal principles announced therein to the special verdict form at issue here. *Id.* It claims that Instruction No. 2 cures any deficiency in the special verdict form.

The special verdict form was in fact misleading and clouded the issues presented to the jury. It suggested that if the jury concluded WFS "provide[d] a loan" to the Applegates – a fact which was not in dispute –

then it did not breach its contract. WFS' reliance on Instruction No. 2 is misplaced because when a special verdict form contradicts a jury instruction it is *more* confusing, not less.

As WFS concedes, the trial court was presented with an exceedingly simple alternative that would have unclouded the issue: the Applegates requested that the special verdict form omit the "to provide a loan" language and simply ask whether WFS breached its contract. Br. of Resp't WFS at 33; VRP 10/31/11 at 393. That was in fact the issue at trial.

Given the Applegates' suggestion of a straightforward and uncontroversial fix to the special verdict form, and the risk of compromising the result of a long and expensive trial, the trial court's refusal to offer a clear, simple, unclouded jury instruction was an abuse of discretion. Because the misleading form likely prejudiced the verdict, it should be reversed.

E. ARGUMENT IN RESPONSE TO WFS' CROSS-APPEAL

WFS cross-appeals on the issue of attorney fees, which the trial court denied. Br. of Resp't WFS at 38-45. WFS claims that the attorney fee provision in its loan agreement warrants an award of fees in this action. *Id.*

(1) Standard of Review

WFS challenges the trial court's interpretation of the attorney fee provision in the WFS contract, and asserts that the standard of review is *de novo*. Br. of Resp't WFS at 41.

However, the standard of review here is complicated. If this Court concludes that the contractual language is unambiguous, then WFS is correct that the standard of review is *de novo*. *Absher Constr. Co. v. Kent School District No. 415,* 77 Wn. App. 137, 141, 890 P.2d 1071 (1995). Also, the trial court's determination of the legal consequences flowing from a contract term involves a question of law. *Denny's Restaurants, Inc. v. Security Union Title Ins. Co.,* 71 Wn. App. 194, 201, 859 P.2d 619 (1993). Such questions of law are reviewed *de novo*. *Knipschield v. C–J Recreation, Inc.,* 74 Wn. App. 212, 215, 872 P.2d 1102 (1994).

However, if this Court concludes that the provision is ambiguous, then the trial court's interpretation is reviewed for substantial evidence. Determining a contractual term's meaning involves a question of fact and examination of objective manifestations of the parties' intent. *Denny's,* 71 Wn. App. at 201. If only one reasonable meaning can be ascribed to the agreement when viewed in context, that meaning necessarily reflects the parties' intent; if two or more meanings are reasonable, a question of fact is presented. *Interstate Prod. Credit Assoc. v. MacHugh,* 90 Wn. App. 650, 654, 953 P.2d 812 (1998). When a question of fact exists as to

meaning, the trial court must identify and adopt the meaning that reflects the parties' intent; the appellate court reviews the trial court's decision for substantial evidence. *In re Marriage of Boisen,* 87 Wn. App. 912, 920, 943 P.2d 682 (1997).[2]

(2) WFS, the Drafter of Its Contract, Could Have Written It to Encompass an Action Like the Applegates' and Unambiguously Did Not

Words in a contract should be given their ordinary meaning. *Corbray v. Stevenson,* 98 Wn.2d 410, 415, 656 P.2d 473 (1982). Courts should not make another or different contract for the parties under guise of construction. *Id.* A contract is not ambiguous simply because the parties each ascribe different meanings. *Shafer v. Board of Trustees of Sandy Hook Yacht Club Estates, Inc.,* 76 Wn. App. 267, 275, 883 P.2d 1387 (1994), *review denied,* 127 Wn.2d 1003, 898 P.2d 308 (1995).

WFS' contract states in relevant part that WFS may recover attorney fees from the Applegates "If the Lender seeks the services of an attorney ... to enforce any of the provisions of this Agreement...." CP 3774.

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[2] The statutory standard of review WFS cites is irrelevant here. Br. of Resp't WFS at 41-42. Although WFS claims to be challenging the trial court's interpretation of RCW 4.84.330, Br. of Resp't WFS at 42, it is not. The trial court did not conclude that WFS was not the prevailing party, nor did the trial court conclude that it had discretion to deny attorney fees under the statute. CP 3837-38. Had it done so, then interpretation of the statute would be at issue. Instead, the trial court interpreted the language of WFS' own contract and concluded it did not encompass the Applegates' claims. *Id.*

The critical term in WFS attorney fee clause is "enforce any provisions of this Agreement." CP 3774. The ordinary meaning of that term, according to our Supreme Court is "to put or keep in force, compel obedience to," or "to give force to." *Am. Legion Post No. 32 v. City of Walla Walla*, 116 Wn.2d 1, 10, 802 P.2d 784, 788 (1991) (citing *Random House Dictionary* 644 (2d ed. 1987); *Webster's Third New International Dictionary* 751 (1986)).

As the trial court noted, WFS specifically did not contemplate an award of attorney fees to "defend" against any action:

> If they wanted to receive attorney's fees for defending an action against them, they should have clearly put in the clause "enforce and/or defend against any claim brought against Washington Federal." If Washington Federal wishes to put people on notice that their customers are going to be held for large sums of attorney's fees if they have to defend against an action that they brought, I think that should be clearly spelled out in the clause.

CP 3837-38, Appendix A.

The trial court's observation that WFS omitted the term "defend" is notable because "defend" is precisely what WFS did here. "Defend" means "to deny or oppose the right of a plaintiff in regard to (a suit or a wrong charged): controvert: oppose, resist <—a claim at law>: contest <—a suit>." *Petersen-Gonzales v. Garcia*, 120 Wn. App. 624, 631, 86 P.3d 210, 213 (2004), quoting *Webster's Third New International*

Dictionary 591 (1993). WFS opposed and resisted the Applegates' claims, it did not enforce the provisions of the contract.

The contract language unambiguously did not envision an award of fees to WFS for defending against the Applegates' action. The trial court's interpretation thus employed the ordinary meaning of the term "enforce," which WFS chose. WFS rejected myriad options for much broader language that could have encompassed the Applegates' action. In addition to including fees for having to "enforce or defend" the contract, as the trial court suggested, it could have asked for fees in any action "arising from" the contract, an exceedingly broad term that is often employed. *See, e.g., Wachovia SBA Lending, Inc. v. Kraft*, 165 Wn.2d 481, 485, 200 P.3d 683, 685 (2009). WFS also could have used the phrase "any action on the contract," which is the language used in RCW 4.84.330.

WFS' appeal to *Scoccolo Const., Inc. ex rel. Curb One, Inc. v. City of Renton*, 158 Wn.2d 506, 145 P.3d 371, 378 (2006), is unavailing. In that case, a contractor sued the City for breach of contract. The relevant attorney fee provision awarded fees *from the contractor to the City* "*in the enforcement* of any of the covenants, provisions, and agreements hereunder." *Scoccolo,* 158 Wn.2d at 520. Our Supreme Court correctly ruled that this clause, despite only facially applying to the City, was

applicable under RCW 4.84.330 to the contractor's action to enforce the contract. *Id.* at 521. *Scoccolo* was thus a straightforward question of statutory construction, not contract interpretation.

However, *Scoccolo* says nothing about whether the proper interpretation of the contract was to award fees for a successful defense, which was not at issue. The *Scoccolo* court never dealt with the question of whether the contract envisioned or intended to encompass fees for a successful defense. It is inapposite.

WFS cannot rewrite this action as an action to "enforce" the agreement by arguing that it had to refer to the agreement's provisions to defend against or rebut the Applegates' claims. WFS defended the action, as that term is ordinarily defined. Attorney fees are not available.

(3) Even If This Court Concludes the Contract Is Ambiguous, Any Ambiguity Must Be Construed Against WFS

"A contract provision is ambiguous when its terms are uncertain or when its terms are capable of being understood as having more than one meaning." *Mayer v. Pierce County Med. Bureau,* 80 Wn. App. 416, 421, 909 P.2d 1323 (1995). When the terms of a contract are ambiguous, the court must look for the intent of the parties by considering the subject matter and objective of the contract, the circumstances surrounding its making, the subsequent acts and conduct of the parties to the contract, and

the reasonableness of the respective interpretations advocated by the parties. *Stender v. Twin City Foods, Inc.,* 82 Wn.2d 250, 254, 510 P.2d 221 (1973).

Contract language is to be interpreted most strongly against the party who drafted the contract. *State v. Bisson,* 156 Wn.2d 507, 522, 130 P.3d 820, 827 (2006); *Guy Stickney, Inc. v. Underwood,* 67 Wn.2d 824, 827, 410 P.2d 7 (1966). This is particularly true when the contract is a preprinted contract, rather than a truly negotiated agreement between equally powerful parties. *Brown v. State*, 130 Wn.2d 430, 457, 924 P.2d 908, 922 (1996).

Even if this Court concludes that the attorney fee provision is ambiguous, that ambiguity should be resolved in favor of the Applegates, and attorney fees to WFS should be denied.[3]

F. ARGUMENT IN REPLY TO RESPONDENTS HHD/BUCHER

In their appeal of the verdict in favor of HHD/Bucher, the Applegates challenge the exclusion of two critical witnesses. Br. of Appellant at 29-34. They argue that the trial court improperly excluded Robert Floberg and Diana Behrens, and that those exclusions likely prejudiced the verdict. *Id.*

[3] As the Applegates argued in their opening brief, if this Court concludes that the attorney fee provision does apply but concludes they, not WFS are the prevailing party, they are entitled to attorney fees at trial and on appeal. Br. of Appellant at 36; RCW 4.84.330.

HHD/Bucher respond that the witnesses were properly excluded, or at least that their exclusion was not manifestly unreasonable. Br. of Resp'ts HHD/Bucher at 14.

(1) HHD/Bucher's Claim that Floberg Was Not Disclosed in Accordance With the Case Schedule and that a Summary of Floberg's Opinion Is Incorrect. His Exclusion Was Improper

HHD/Bucher argue that the Applegates failed to timely disclose a summary of Floberg's expert opinion, and thus his exclusion was proper. In support, they cite *Lancaster v. Perry*, 127 Wn. App. 826, 829, 113 P.3d 1 (2005).

The pertinent facts in *Lancaster* make clear that that case is inapposite here. In that tort case, Lancaster sued Perry for personal injuries arising from an automobile collision. The Case Scheduling Order required the disclosure of expert witnesses on or before September 8, 2003. On September 4, 2003, Perry set forth his disclosure of expert witnesses "those healthcare professionals who will conduct a CR 35 examination of the Plaintiff. This CR 35 examination has not been scheduled at this time and, accordingly, defendants cannot identify those professionals who may conduct the examinations." *Lancaster,* 127 Wn. App. at 829. Perry failed to request CR 35 examinations. Then, Perry disclosed his planned rebuttal witness list, on October 20, 2003, and

identified his experts in the same manner as above. *Id.* By November 10, 2003 unsuccessfully. Perry had yet to request CR 35 examinations. With a trial impending, Lancaster sought to exclude all "unidentified" expert and fact witnesses. *Id.*

The *Lancaster* court excluded all "unidentified" expert witnesses. Court of Appeals noted that Perry had not actually identified a witness:

> Here, Perry failed to even name his expert witness. Perry points out he gave the names of three possible witnesses in his rebuttal witness disclosure. This, however, is not helpful. If the specific witness is identified, the opposing party may at least seek to depose the witness. Here, no CR 35 examination, which would serve as the basis for the expert's testimony, had even been requested or ordered, let alone conducted.

Id. at 832. The *Lancaster* court pointed out a second salient fact not at issue here:

> More importantly, Perry did not have the right to call this witness absent court order. CR 35 is not self-executing; in order to conduct a CR 35 examination a party must obtain the agreement of opposing counsel or must obtain a court order.

Id. at 832. Thus in *Lancaster,* there was no opportunity for the opposing party to depose the witness, and thus no chance for proper discovery.

This case resembles *Lancaster* neither factually *nor* legally. Here, Robert Floberg was timely disclosed, identified, and, the substance of his expected testimony provided within the proper deadline. CP 3525. He was not named in order to conduct a CR 35 examination, he was named in

order to opine on whether certain signatures were forgeries. *Id.* The Applegates did not need to seek a court order to obtain his opinions, and in fact under the rules were not even required to submit a written summary of his opinion. PCLR 26(d)(3). It is HHD/Bucher, not the Applegates, who cancelled his deposition on the improper grounds that Floberg voluntarily submitted a one-page opinion letter a week before the deposition. CP 3495. It is HHD/Bucher, not the Applegates, who falsely claimed that they were ignorant of the claim that the CJP was forged, despite Richard Applegate's assertion in his declaration *10 months before trial*: "I do not doubt Mr. Bucher forged my name on the March 2008 CJP as well." CP 573.

Excluding an expert witness is a severe sanction, and should be exercised when a party's conduct is "egregious." *Burnet v. Spokane Ambulance*, 131 Wn.2d 484, 498, 933 P.2d 1036, 1042 (1997). As HHD/Bucher note, PCLR 26(d)(3) provided the trial court with other options short of exclusion.

In these circumstances, it was manifestly unreasonable for the trial court to exclude such a crucial witness. The nature and substance of Floberg's testimony was timely disclosed, and was frankly not complicated. There was no prejudice to HHD/Bucher's ability to prepare

when his one-page opinion letter was disclosed a full week before his deposition (which was scheduled after the discovery cutoff).

The exclusion of Floberg was prejudicial. He was prepared to testify that, in his expert opinion, both the endorsement on a $108,000 check and on the CJP were forgeries. Bucher claimed at trial that Mr. Applegate signed the CJP. Floberg would have seriously undermined Bucher's credibility in a case where his credibility was a central issue. The trial court abused its discretion, and reversal is warranted.

(2) The Improper Exclusion of Diana Behrens Testimony Eliminated the Applegates' Ability to Prove HHD/Bucher's Lack of Mistake

The Applegates argued in their opening brief that the trial court abused its discretion by refusing to admit the testimony of Diana Behrens. Br. of Appellant at 35-36. They averred that the trial court mistakenly categorized Behrens' testimony as inadmissible character evidence, when it was actually offered to show lack of mistake or accident and was therefore admissible.

In response, HHD/Bucher incorrectly claim that the Applegates' argument "faults the trial court for failing to conduct" the balancing test of ER 403, that is, whether the potential prejudice of the evidence outweighs its probative value. Br. of Resp'ts HHD/Bucher at 22. HHD/Bucher ignore the Applegates' argument on appeal, instead referring this Court to

the legal arguments made below, which they claim lacked "analysis." *Id.* at 21-22.

Regardless of how well HHD/Bucher thinks the Applegates' articulated their argument below, the analysis before this Court on appeal has drawn no substantive response from HHD/Bucher.

The Applegates' argument is not about the balancing test under ER 403, it is about the trial court's characterization of Behrens' testimony as "character evidence" excludable under ER 404(b), and the fact that the trial court focused on the Applegates' motives, rather than the defenses HHD/Bucher raised.

Our Supreme Court has held that the key inquiry under ER 404(b) is whether the defendant is claiming its behavior toward the plaintiff was the result of mistakes or accidents, rather than intent. *State v. Brown*, 113 Wn.2d 520, 527, 782 P.2d 1013, 1019 (1989), *opinion corrected*, 787 P.2d 906 (1990). If a plaintiff claims fraud and the defendant responds by claiming a mere mistake, then prior instances of fraud are appropriate evidence for the jury to consider, with proper limiting instructions. *Id.*

HHD/Bucher argued to the jury that any misdeeds with respect to how they obtained funds improperly were merely mistakes and omissions, rather than fraud or conversion. CP 932. Behrens had direct knowledge

that controverted the notion that the fraud and conversion were mere mistakes or misunderstanding. CP 787-89.

Nevertheless, the trial court made no reference to HHD/Bucher's defenses when it excluded Behrens' testimony was propensity evidence under ER 404(b). Instead, the court focused on the nature of the Applegates' claims, which is error under *Brown.*

Exclusion of Behrens was an abuse of discretion that undermined the Applegates' ability to respond to HHD/Bucher's defense at trial, and likely prejudiced the outcome of the case.

G. CONCLUSION

Summary judgment dismissal of the Applegates' negligence and breach of fiduciary duty claims against WFS was improper. The banking practice of releasing funds over time through a progressive construction loan involves much more than the mere arm's length bank transaction where the borrower signs a paper and the bank hands over the funds. It is a complex relationship where the bank may only release funds based upon work completed, and where builders may try to swindle borrowers by relying on a bank's indifference. The special circumstances test should apply to such loans, and place a duty of reasonable care upon the bank to ensure that funds are not looted, wasted, or converted. That is particularly true when the bank assures customers it is protecting their interests.

The special verdict form here misled the jury into believing the Applegates had no breach of contract claim unless WFS failed to provide a loan. This confusing form, which contradicted the Applegates' theory of the case and the jury instructions, likely affected the verdict.

The Applegates' fraud and conversion claims were eviscerated by the exclusion of key witnesses. HHD/Bucher's offer little in response to the trial court's ruling, other than to rely on the trial court's power of discretion.

These critical errors necessitate a reversal and remand for a new trial. Should the Applegates prevail and attorney fees become awardable, they should be awarded both at trial and on appeal.

DATED this 11th day of March, 2013.

Respectfully submitted,

Philip A. Talmadge, WSBA #6973
Sidney Tribe, WSBA #33160
Talmadge/Fitzpatrick
18010 Southcenter Parkway
Tukwila, WA 98188-4630
(206) 574-6661

Justin Bristol, WSBA #29820
Gourley | Bristol | Hembree
1002 10th Street
Snohomish, WA 98290
(360) 568-5065
Attorneys for Richard and Karen Applegate

APPENDIX A

case, Your Honor. And there is no argument with respect to the amount of the fees or the amount of the costs. It's appropriate to enter a judgment and enter an order for those fees and costs in accordance with the agreement.

MR. BRISTOL: Your Honor, I request --

THE COURT: I'm through. I am ready to rule. I looked at this entire agreement and what its purpose was and what the purpose of this attorney's fees clause was, and I don't think there's anything ambiguous about this clause at all in the respect that this was a clause that was inserted that if the bank had to enforce any portion of this agreement, i.e., the borrower breached any of this agreement, went into default, failed to comply with payments, et cetera, that if they took an action and prevailed, they would be awarded attorney's fees. If they wanted to receive attorney's fees for defending an action against them, they should have clearly put in the clause "enforce and/or defend against any claim brought against Washington Federal." And they did not include the word "defend."

I don't see enforcement as -- there was no counterclaim. There was no allegation that these people breached the agreement. There were affirmative

defenses raised by the bank, but I don't think they did anything to enforce this agreement. They defended against the agreement. If Washington Federal wishes to put people on notice that their customers are going to be held for large sums of attorney's fees if they have to defend against an action that they brought, I think that should clearly be spelled out in the clause.

And I look at this as simply an attorney's fees clause that if Washington Federal initiated a suit and they were successful in enforcing the terms of their contract, they would be awarded attorney's fees. So I respectfully disagree with the interpretation by Washington Federal, although they are entitled to their costs that they would have incurred from the date of offer of judgment that they made. I don't know if there were any costs, but I think that they are clearly entitled to costs from the date that they gave the offer of judgment.

MR. WAKEFIELD: Your Honor, I think it would -- I'm not sure that there were any costs actually incurred that would be recoverable the way the costs are, but I did prepare a judgment that awards statutory attorney's fees in the amount of $200. I'll provide a copy of that to counsel here and hand it to Ms. Mangus for the Court's consideration. Obviously

DECLARATION OF SERVICE

On said day below I emailed a courtesy copy and deposited in the U.S. Postal Service for service a true and accurate copy of the Reply Brief of Appellants/Cross-Respondents Richard and Karen Applegate in Court of Appeals Cause No. 43043-6-II to the following:

Justin Bristol
Gourley Bristol Hembree
1002 10th Street
Snohomish, WA 98290

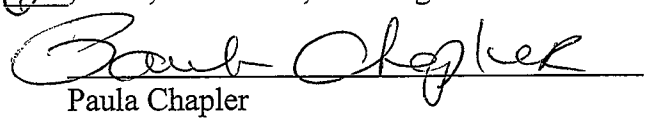
Pamela Andrews
Jennifer Lauren
Andrews Skinner PS
645 Elliott Avenue W., Suite 350
Seattle, WA 98119

Scott C. Wakefield
Todd & Wakefield
1501 4th Avenue, Suite 1700
Seattle, WA 98101-3660

Original efiled with:
Court of Appeals, Division II
Clerk's Office
930 Broadway, Suite 300
Tacoma, WA 98402-4427

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

DATED: March 20, 2013, at Tukwila, Washington.



Paula Chapler
Talmadge/Fitzpatrick

TALMADGE FITZPATRICK LAW

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