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

NORTHWEST ALLOYS, INC. and MILLENNIUM BULK
TERMINALS-LONGVIEW, LLC,

Respondents/Cross-Appellants,

v.

STATE OF WASHINGTON DEPARTMENT OF NATURAL
RESOURCES, and THE HONORABLE HILARY S. FRANZ, and
COLUMBIA RIVERKEEPER, WASHINGTON ENVIRONMENTAL
COUNCIL, and SIERRA CLUB,

Appellants/Cross-Respondents.

**REPLY BRIEF OF APPELLANTS/CROSS-RESPONDENTS
STATE OF WASHINGTON DEPARTMENT OF NATURAL
RESOURCES AND THE HONORABLE HILARY S. FRANZ**

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I. INTRODUCTION

Respondents/Cross-Appellants Northwest Alloys, Inc. (NWA) and Millennium Bulk Terminals-Longview, LLC (Millennium) do not deny that Millennium lacks sufficient financial assets on its own to meet the requirements of the Lease. Br. of Respondents at 31. They also do not challenge the trial court's finding that the Department of Natural Resources' (DNR's) denial of their sublease request was based on "legitimate dollar concerns on the part of DNR." CP 17691. Unchallenged, the fact that DNR had legitimate concerns regarding Millennium's ability to perform as a subtenant under the Lease is a verity in this appeal.

Conceding that Millennium is completely dependent on outside infusions of money to function, that it did not have sufficient resources on its own to meet the requirements of the Lease, and that DNR had legitimate concerns about Millennium's financial viability and ability to perform under the Lease, NWA and Millennium nevertheless argue that any reasonable landlord would have readily accepted Millennium as a subtenant. Br. of Respondents at 23. Hemorrhaging cash, with a bankrupt corporate owner, and a lessee in NWA whose hands-off approach to a previous subtenant led to extensive damage of State property, no reasonable landlord would accept Millennium as a sublessee, let alone a landlord who

is responsible for protecting the public trust interest in the State's aquatic lands, as DNR is.

While the trial court correctly determined that the arbitrary and capricious standard of review is the applicable standard under RCW 79.02.030, it erroneously reversed DNR's denial of NWA's and Millennium's proposed sublease. DNR had legitimate reasons to deny the sublease request and, therefore, respectfully requests the Court reverse the trial court and reinstate the denial.

II. ARGUMENT

A. **Arbitrary and Capricious, Not Substantial Evidence, Is the Correct Standard of Review in This Matter Under RCW 79.02.030.**

Despite NWA's and Millennium's assertions to the contrary, "the appellate court stands in the same position as the trial court where the record consists only of affidavits, memoranda of law, and other documentary evidence." *Progressive Animal Welfare Soc'y v. Univ. of Wash.*, 125 Wn.2d 243, 252, 884 P.2d 592 (1994). *See also Dolan v. King Cty.*, 172 Wn.2d 299, 310-11, 258 P.3d 20 (2011). Here, the Court reviews DNR's record directly, and because the trial court did not weigh evidence or resolve issues of witness credibility, the substantial evidence standard does not apply. *Dolan*, 172 Wn.2d at 310-311.

Millennium and NWA rely on inapplicable case law to support their argument that this Court should apply the substantial evidence standard. Br. of Respondents at 20-21. Both *Hendrickson v. Department of Labor and Industries*, 2 Wn. App. 2d 343, 409 P.3d 1162 (2018), and *Groff v. Department of Labor and Industries*, 65 Wn.2d 35, 395 P.2d 633 (1964), involved L&I statutes and determinations of the Board of Industrial Insurance Appeals. The Board of Industrial Insurance Appeals acts in a judicial capacity under RCW Title 51 when it determines whether claimants are entitled to compensation. *Floyd v. Dep't of Labor & Indus.*, 44 Wn.2d 560, 578, 269 P.2d 563 (1954). Courts willingly accept a less deferential standard of review for quasi-judicial agency decisions because this would not violate any constitutional separation of powers. *Id.* (trial court authorized to conduct trial de novo of workers' compensation award). These decisions under Title 51 simply do not apply to the administrative functions DNR carries out in managing leases on state-owned aquatic lands. As discussed below, because DNR acted in an administrative, and not a quasi-judicial, capacity when it denied the sublease request, the arbitrary and capricious standard is the correct standard under RCW 79.02.030.

B. The Superior Court Applied the Correct Standard of Review Under RCW 79.02.030, But Reached the Wrong Conclusion Under That Standard.

In reviewing DNR's decision to deny the proposed consent to sublease, the superior court was correct that under RCW 79.02.030, DNR was performing an administrative proprietary function, and not a quasi-judicial function, when it considered NWA's request for the sublease. CP 17689. Based on this conclusion, the trial court determined that "[c]onsequently, the standard of review in this matter is whether DNR's actions were arbitrary, capricious, or contrary to law." CP 17689 (citing *Yaw v. Walla Walla Sch. Dist. No. 140*, 106 Wn.2d 408, 413-14, 722 P.2d 803 (1986)).¹

While RCW 79.02.030 provides for "de novo" review on the agency record, when courts have examined similar statutes, they have construed such "de novo" review language to mean "arbitrary, capricious, or contrary to law." *Household Fin. Corp. v. State*, 40 Wn.2d 451, 454-58, 244 P.2d 260 (1952) (statute granting court de novo trial on denial of license). Based on constitutional principles of separation of powers, courts will not substitute their own judgment for that of an administrative agency exercising legislative or executive functions, and the Legislature cannot

¹ DNR agrees that the four-part test of *Yaw* is the applicable test to determine whether an agency's actions are quasi-judicial or administrative for purposes of applying the correct standard of review.

impose non-judicial functions on the court. *Id.* at 455-57 (holding unconstitutional a statute granting the court de novo trial and review over banking supervisor's denial of a business license).

The subject matter or function of the administrative agency determines the scope of review. *Floyd*, 44 Wn.2d at 570. If the agency is performing a legislative or an administrative function, then the court uses the arbitrary, capricious, or contrary to law standard. *Id.* at 570-71. If the court determines the agency is fulfilling a judicial function, then de novo review provides for a less deferential review of the agency's decision. *Id.* A judicial function is the type of function that courts have historically performed. *Id.* at 571; *Francisco v. Bd. of Dir. of Bellevue Pub. Sch.*, 11 Wn. App. 763, 771, 525 P.2d 278 (1974) (determining employment rights inherently and historically a judicial function).

Exercising the discretion the Legislature vested in DNR to determine whether, and under what conditions, the use of state-owned aquatic lands should be authorized is an administrative function. *See, e.g., Hood Canal Sand & Gravel, LLC v. Goldmark*, 195 Wn. App. 284, 307-08, 381 P.3d 95 (2016) (DNR's issuance of easement was not quasi-judicial for purposes of statutory writ of review). While NWA and Millennium try to distinguish *Hood Canal Sand and Gravel* from the present case, Br. of Respondents at 46, *Hood Canal Sand and Gravel* specifically involved a

contract (an easement issued by DNR), and the rights under that contract. *Id.* at 304-06. Thus, the case is directly on point and demonstrates that DNR was not performing a judicial function when exercising its discretion about whether to approve a sublease and what information was necessary to evaluate the request. DNR's denial of NWA's sublease request was justified by the facts and authorized under the Lease.

Although the trial court applied the correct standard of review, it reached the wrong conclusion. As a preliminary matter, NWA and Millennium do not challenge the trial court's finding that after February 2015, Arch Coal, which held a 38 percent stake in Millennium, went into bankruptcy; Alcoa, the only source of revenue for the Longview facility, suspended its operation at Wenatchee Works; and that the coal market had been spiraling. CP at 17691 (Order on the Merits ¶ 9). Based on these facts, the trial court determined that "[t]hese events resulted in a changed situation since February of 2015 and raise legitimate dollar concerns on the part of DNR." *Id.* NWA and Millennium do not challenge these findings, and, as such, these unchallenged findings are verities in this appeal. *Fuller v. Emp't Sec. Dep't*, 52 Wn. App 603, 605, 762 P.2d 367 (1988). Because DNR's requests for financial and other business records were based on these legitimate concerns, they cannot be arbitrary and capricious under RCW 79.02.030. *See Hood Canal*, 195 Wn. App. at 307-08, (arbitrary and

capricious action means “willful and unreasonable action, without consideration and [in] disregard of facts or circumstances.”).

C. DNR’s Denial of NWA’s Sublease Request Was Justified by the Facts and Authorized Under the Lease.

NWA and Millennium do not dispute that a landlord has a legitimate interest in assessing the financial condition and business plans of a tenant’s proposed sublessee. *See Ernst Home Ctr. v. Sato*, 80 Wn. App. 473, 486, 910 P.2d 486 (1996). Moreover, NWA and Millennium do not deny that they failed to comply with DNR’s requests for financial statements and “any additional information [NWA] can provide to shed light on Millennium’s financial condition.” AR 001419. Instead, NWA and Millennium argue that DNR’s requests for financial information were arbitrary and unreasonable for two reasons. First, they argue that NWA would remain liable as tenant on the Lease and, therefore, “the subtenancy would have assured DNR of all the benefits it bargained for” when DNR entered into the Lease. Br. of Respondents at 23. Second, they argue that DNR knew Millennium was “a start-up entity with little revenue to cover its operating expenses,” and, therefore, DNR’s requests for financial statements would not have told DNR anything it did not already know. Br. of Respondents at 28. In support of these arguments, Millennium and NWA ask the Court to infer that DNR was biased against them based on the parties’ negotiations and DNR’s

actions in unrelated cases. Br. of Respondents at 8-11. NWA's arguments are factually incorrect and fail to justify NWA's and Millennium's refusal to comply with DNR's reasonable efforts at due diligence in this case.

First, NWA's and Millennium's arguments ignore DNR's express right under the Lease to consider the financial condition, business plans, and reputation of any proposed subtenant regardless of whether the proposed sublessee is a startup entity or the fact NWA will remain bound by the Lease. Second, even in the absence of the express provision of the Lease, DNR's efforts to evaluate Millennium's financial condition were commercially reasonable because a subtenant's financial condition is directly related to the subtenant's ability to perform. Third, NWA's and Millennium's effort to impugn DNR's motivations for denying their request are not supported by the record and ignore the overwhelming weight of evidence supporting DNR's need to review Millennium's financial condition. DNR has a legitimate interest in ensuring it has a financially sound subtenant, particularly where, as in this case, a default could damage the leased property, threaten public safety, and harm the environment. The facts of this case demonstrate that DNR's efforts to conduct due diligence were reasonable. NWA and Millennium's failure to comply with them fully justified DNR's decision to deny NWA's sublease request.

1. DNR Was Expressly Authorized Under the Lease to Consider Millennium's Financial Condition. DNR's Efforts to Do So Were Not Arbitrary.

In Washington, a landlord and tenant may agree to an absolute prohibition on assignments or subleases. *Johnson v. Yousoofian*, 84 Wn. App. 755, 759, 930 P.2d 921 (1996). It follows that the parties to a lease are also free to "negotiate lease terms to which this standard [of reasonableness] may or may not apply, as they wish." *Ernst*, 80 Wn. App. at 487. As such, even where the lease prohibits the landlord from unreasonably withholding consent, the lease may impose conditions that the tenant must meet to transfer an interest in the leasehold, regardless of whether those conditions are later deemed objectively reasonable. *Id.* (citing *Leonard, Street & Deinard v. Marquette Assocs.*, 353 N.W.2d 198 (Minn. App. 1984)). If the tenant fails to satisfy the conditions, the landlord may deny the request. *Id.*

In this case, the Lease defines what DNR may consider when confronted with a sublease request. Section 9.1(a) provides whenever a sublease or other transfer is proposed DNR may consider "the proposed transferee's financial condition, business reputation and experience, the nature of the proposed transferee's business . . ." in addition to any other factor that reasonably bears on the suitability of the subtenant. AR 001546. Because the express language of the Lease allows DNR to consider the financial condition of any proposed sublessee, DNR had the absolute right

to consider Millennium's financial condition prior to consenting to a sublease in this case.

DNR's right to consider Millennium's financial condition necessarily includes the right to request information to do so. As they must, NWA and Millennium concede that DNR may request financial information under the Lease. Response Br. at 31. DNR's requests for information to exercise its lease right were not arbitrary. To consider Millennium's financial condition, DNR asked for information that was specifically tailored to that purpose. DNR requested Millennium's financial statements as well as "any other information that would shed light on Millennium's financial condition." AR 001419. NWA and Millennium do not dispute that "the purpose of financial statements is to organize, summarize, and present to the public the financial performance and condition of an enterprise" as explained in DNR's Opening Brief. *See* DNR's Opening Br. at 33. Moreover, NWA and Millennium fail to address DNR's request for any information that would shed light on Millennium's financial condition.

NWA and Millennium do not address DNR's lease right to consider Millennium's financial condition. Instead, they argue that DNR's requests for financial information were unreasonable because NWA would remain bound by the Lease as the tenant, Br. of Respondents at 23, and Millennium was a startup company. Br. of Respondents at 28. Those arguments fail

because DNR has the right to consider the financial condition of *any* sublessee, assignee, or other transferee proposed under the Lease. AR 001546.

The Lease expressly contemplates that DNR may consider a subtenant's financial condition when NWA remains bound as tenant. Section 9.1(a) permits DNR to consider the financial condition of a proposed sublessee or assignee in every case. AR 001546. DNR's right to consider a subtenant's financial condition thus necessarily includes instances where NWA remains bound by the Lease. Under Section 9.1(c) of the Lease, NWA remains bound by the Lease following any assignment, sublease, or other transfer.² To have meaning, DNR's right to consider a proposed subtenant's financial condition in Section 9.1(a) must include instances where NWA will remain bound under Section 9.1(c). If DNR could not consider the financial condition of a proposed transferee when the tenant remains bound by the Lease, DNR's rights under Section 9.1(a) would never be effective.

Furthermore, nothing in Section 9 of the Lease limits DNR's ability to consider the financial condition of a proposed sublessee because it is a startup. AR 001546-48. The express language of Section 9.1(a) allows DNR

² The one exception identified in Section 9.1(c) involves a transfer to Chinook Ventures. AR 001547.

to consider a proposed subtenant's financial condition in any case. Courts must construe contract language in a manner that gives effect to the words used and does not render the chosen language meaningless. *MacLean Townhomes, L.L.C., v. Am. 1st Roofing & Builders, Inc.*, 133 Wn. App. 828, 831, 138 P.3d 155 (2006). To give effect to the language used here requires finding DNR had the express authority under the Lease to consider Millennium's financial condition, regardless if NWA remains bound by the Lease or Millennium is a startup entity.

DNR had the right to consider Millennium's financial condition under the Lease. Given the facts, DNR's requests for financial information to exercise its right to consider Millennium's financial condition were particularly valid. They were not arbitrary and capricious. NWA's and Millennium's failure to provide the financial information requested fully justified DNR's decision to deny the sublease request.

2. DNR's Efforts to Review Millennium's Financial Condition Were Commercially Reasonable.

Because DNR's denial of the sublease request was justified under DNR's express authority to consider Millennium's financial condition in Section 9.1(a) of the Lease, the Court need go no further to reverse the decision of the superior court. Even if the express language of Section 9.1(a)

is ignored, however, DNR's actions were commercially reasonable and fully support reversal as explained below.

The parties agree that to determine whether DNR acted reasonably in refusing consent to a sublease or assignment, the Court asks if a reasonably prudent person in the position of the landlord under the Lease would have refused consent. *Ernst Home Ctr.*, 80 Wn. App. at 484. There is no dispute that financial strength and responsibility of a proposed subtenant, as well as the nature and legality of its intended use and occupancy of the leased property, are among the commercially reasonable factors a landlord may consider in evaluating a sublease request. *See e.g., Ernst Home Ctr.*, 80 Wn. App. at 486. NWA and Millennium do not contest they have the burden to provide the information DNR needs to make a reasonable evaluation of their request here. *See* 1 Andrew R. Berman, *Friedman on Leases* § 7.3.4[D][3] at 7-58 (6th ed. 2016) (citing authorities). Nor do NWA and Millennium dispute that in the absence of such information, the landlord is justified in refusing to consent to a sublease request. *See, e.g., McKeon v. Williams*, 104 Or. App. 106, 110, 799 P.2d 198, 200 (1990).

To support their arguments, NWA and Millennium first urge the Court to ignore the fact that the land at issue is public land managed by DNR when applying the reasonable person standard, Br. of Respondents

at 23, 41, 49. NWA and Millennium then make two claims that DNR acted unreasonably: first, they argue DNR should have been satisfied with Millennium as subtenant because NWA would remain bound by the Lease as tenant, and second, they assert that, although DNR was entitled to request financial information to evaluate the sublease request, DNR did not ask for the right information. Br. of Respondents at 23, 28. NWA and Millennium are incorrect on all counts. In this case, the Court evaluates whether DNR's actions were reasonable from the position of DNR as the manager of the property. In addition to the fact the Lease expressly allows DNR to examine the financial condition of any proposed sublessee, the facts of this case show DNR's interest in Millennium's financial condition was not only reasonable, it was compelling, regardless of whether NWA remained bound by the Lease. Because Millennium's performance would directly affect DNR's interest in the leased property and Millennium would be responsible for building and operating a major new industrial facility on the Columbia River, DNR's requests for financial information appropriately focused on Millennium.

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3. DNR, as the Manager of the State’s Aquatic Lands, Has Unique Statutory and Constitutional Duties That This Court Must Consider in Evaluating DNR’s Actions Under the Lease.

As the manager of the State’s aquatic lands, “DNR executes its leasing authority with a view toward the State’s duty to protect the public trust.” *Pope Res. v. Wash. State Dep’t of Nat. Res.*, 190 Wn.2d 744, 754, 418 P.3d 90 (2018). The public trust doctrine is rooted in the constitution under art. XVII, § 1, and “protects public ownership interests in certain uses of navigable waters and underlying lands, including navigation, commerce, fisheries, recreation, and environmental quality.” *Id.*

Generally, a public trust impairment must be strictly construed in preservation of the public trust interest, and, as such, “[t]he general rule of construction applying to grants of public lands by a sovereignty to corporations or individuals is that the grant must be construed liberally as to the grantor and strictly as to the grantee, and that nothing shall be taken to pass by implication.” *Chelan Basin Conservancy v. GBI Holding Co.*, 190 Wn.2d 249, 262-263, 413 P.3d 549 (2018). Accordingly, because the Lease at issue here involves an interest in state-owned aquatic lands, the Court must construe the Lease terms liberally as to DNR and strictly as to NWA.

Where, as here, a lease provides that consent to sublet or assign will not be unreasonably withheld, the reviewing court determines “whether a reasonably prudent person *in the landlord’s position* would have refused consent.” *Ernst Home Ctr.*, 80 Wn. App. at 484 (emphasis added). NWA and Millennium argue that to determine what a reasonably prudent person in the position of the landlord would have done under the circumstances in this case, the Court should ignore that the landlord here is DNR. Br. of Respondents at 23, 41. For that proposition, they point to a case asserting the State, acting in its proprietary capacity, will “receive no better treatment than any two private individuals . . .” when applying principles of estoppel. *Id.* at 23 (citing *Metro. Park Dist. of Tacoma v. DNR*, 85 Wn.2d 821, 827, 539 P.2d 854 (1975)). Regardless of the merits of that proposition generally, it is not pertinent here. DNR is not seeking special treatment. All landlords must comply with the law that applies to them. Those legal obligations must be taken into account in applying the reasonably prudent person standard. Because DNR has legal responsibilities to consider environmental values in its leasing decisions under RCW 79.105.030 and RCW 79.105.210(3), for example, as well as under the public trust doctrine, the Court must take those obligations into consideration in determining whether DNR acted correctly under the Lease.

4. It Was Reasonable for DNR to Review Millennium's Financial Condition, Regardless of Whether NWA Remained Bound By the Lease.

There are several reasons why the fact NWA would remain DNR's tenant under the Lease does not render DNR's effort to examine Millennium's financial condition unreasonable. First, DNR has a legitimate interest in Millennium's financial condition because its activities as a subtenant would have a direct impact on DNR's interest in the property, particularly given its plans to build and operate a major new industrial facility. Second, Arch Coal's bankruptcy raised serious concerns and DNR has a legitimate interest in avoiding a bankruptcy by a subtenant, regardless of whether NWA remains the tenant. Third, to the extent NWA's continued tenancy under the Lease is relevant, DNR had reason to question its value as security for Lease compliance based on the Lease and NWA's history of lax oversight of its subtenants. For all of these reasons, DNR's effort to review Millennium's financial condition was entirely reasonable regardless of whether NWA would remain the tenant under the Lease.

"It is well settled that a lessor is entitled to weigh the financial responsibility of a proposed subtenant or assignee, in deciding whether to consent to a sublease or assignment." *Farhrenwald v. LaBonte*, 103 Idaho 751, 653 P.2d 806 (1982). This is true, although, as in this case, the tenant generally is not released from its obligations under the lease by either a

sublease or an assignment. 1 Berman § 7.3.4[D][3] at 7-68. Regardless of whether the tenant remains bound by the lease, a landlord has a legitimate interest in the financial condition of a proposed subtenant because of the effect a subtenant's activities may have on the landlord's interest in the property. *See, e.g., Popovic v. Florida Mech. Contractors, Inc.*, 358 So. 2d 880, 884-85 (Fla. Ct. App. 1978) (performance of lease covenants is directly related to "the dependability, solvency and stability of the actual occupant"); *Reget v. Dempsey-Tegler & Co.*, 70 Ill. App. 2d 32, 37, 216 N.E.2d 500, 503 (1966) ("the sublessee's credit is a meaningful factor").

The interest of the landlord in a subtenant's financial condition is particularly compelling where, as here, the subtenant will be responsible for fulfilling the tenant's duties under the Lease and the Lease calls for the tenant to do more than simply pay rent. *Popovic*, 358 So. 2d at 884-85 (landlord's interest in subtenant's financial condition particularly compelling in case of a "total performance lease"). In this case, NWA and Millennium do not dispute that NWA relies on its subtenants to fulfill all of its lease obligations and operate the facility on the leased property while it manages its business from Pittsburgh. AR 000452 (Millennium is NWA's "independent contractor" carrying out NWA's rights and obligations under the Lease); AR 001519 (Chinook sublease – NWA "delegates to Sublessee . . . all its obligations and duties of performance under the Lease"). As a

result, NWA's performance under the Lease, including its ability to cure defaults, is critically dependent on the financial condition and responsibility of its subtenants. *See Kazarinov v. L. B. Kaye Assocs.*, 111 Misc.2d 944, 951, 445 N.Y.S.2d 915, 920 (1981) (“[t]he great distance involved in the present situation exacerbates the tenant's ability to cure a default on the part of subtenant”).

When NWA's previous subtenant, Chinook Ventures, built unauthorized and unpermitted improvements that threatened human health and the environment, AR 005647, NWA took years to cure the default, relying exclusively on Chinook Ventures and then Millennium to complete the work. AR 00001-3 (initial notice), AR 000878 (cure notice). The Lease history here shows NWA depends entirely on its subtenants for performance and that curing defaults, particularly at an industrial site on a navigable river, can take a very long time. Accordingly, DNR has a significant interest in taking prudent steps to ensure NWA has a responsible subtenant and that defaults will not occur, regardless of whether NWA remains bound by the Lease, not the least because defaults at this site could threaten public safety and the environment.

The circumstances presented in the cases cited by NWA and Millennium are a far cry from those here, where the subtenant would be completely responsible for building and operating a major industrial facility

on a navigable river, and provide no support for the conclusion that DNR acted unreasonably in this case. The cases cited by NWA and Millennium present circumstances, such as the leasing of office space, where the landlord's primary interest is in prompt payment of rent. Response Br. at 23 (citing *Adams, Harkness & Hill, Inc., v. Ne. Realty Co.*, 281 N.E.2d 262 (Mass. 1972)); *Caplan v. Latter & Blum, Inc.*, 468 So. 2d 1188 (1985); *Ringwood Assocs. v. Jack's of Route 23, Inc.*, 153 N.J. Super. 294, 379 A.2d 508 (1977).³ Moreover, unlike here, where NWA and Millennium failed to provide any financial information after DNR requested it following the collapse of the coal market and the subsequent cascade of other factors demonstrating significant cause for concern, in the cases NWA and Millennium cite, evidence of financial responsibility was either provided, *Caplan*, 468 So. 2d at 1190; *Adams, Harkness & Hill*, 281 N.E.2d at 264, or was not a factor, *Ringwood Assocs.*, 379 A.2d at 512.

NWA and Millennium baldly assert that they were both financially sound, but can point to no authority or evidence in the record for support. Br. of Respondents at 24. They further argue that Lighthouse Resources'

³ Similarly, in *Vranas & Associates v. Family Pride Finer Foods*, 498 N.E.2d 333 (1986), Respondents Br. at 29, the landlord refused consent to an assignment of a lease where the proposed tenant would have simply continued the same grocery business operated under the lease. *Id.* at 340. Additionally, the proposed assignee provided significant evidence of its financial condition, including its \$25,000 in cash, and \$200,000 SBA-guaranteed loan, as well as the loan application, and the financial statements of its principal. *Id.* at 339-40. The case has no application here.

purchase of Arch Coal's interest in Millennium in bankruptcy somehow establishes Millennium's financial condition. *Id.* To the contrary, Lighthouse obtained Arch Coal's interest as a creditor in bankruptcy for next to nothing, which raised additional concerns regarding the value and viability of Millennium and its plans. AR 013767, 013780. The case NWA and Millennium cite in support of their argument, *224 Westlake, LLC v. Engstrom Properties, LLC*, 169 Wn. App. 700, 281 P.3d 693 (2012), involves a sale of real property pursuant to an option agreement where the purchaser paid what was required under the agreement and had in its bank accounts the amounts needed to close the sale. *Id.* at 720-21. The seller thus had all the information it needed to know the purchaser could close. *Id.* The case is inapposite here, because unlike a seller of real property who is "concerned primarily about the purchaser's financial ability to close," *id.*, a landlord is concerned about a subtenant's ability to perform all of the lease conditions over the entire term of the lease extending years into the future. That distinction is critical here, where Millennium plans to build and operate a major new industrial facility at a cost of hundreds of millions of dollars on public land over the term of the Lease.

DNR also has reason to question whether having NWA as the named tenant would provide a significant backstop for Lease defaults over the term of the Lease. According to Millennium's corporate parent, when

Millennium purchased the assets of Chinook, it also obtained an option to purchase NWA's upland property.⁴ AR 000415-16. That agreement is consistent with the Lease where NWA negotiated for a release from its obligations if it sold all of its interest in the leased property to Chinook. AR 001547 (Lease Section 9.1(c)). Given NWA's apparent willingness to dispose of the upland property, its major asset, NWA's continued liability under the Lease may be of significantly reduced value.⁵ Moreover, NWA has repeatedly refused to terminate Chinook as its sublessee, despite the fact that Chinook is "defunct." CP 15576. An apparent explanation for this is that NWA wishes to retain the possibility of shedding its Lease obligations as provided for under Section 9.1(c) of the Lease. AR 001547. While Millennium's obligations to NWA were reported to be guaranteed by a letter of credit, they never provided DNR with a copy of anything but a preliminary form letter of credit that failed to even identify the financial institution providing the letter. AR 000197. Without knowledge of the terms of the letter of credit, DNR could not determine whether the security would continue for the term of the Lease or whether it would even apply to the

⁴ Although DNR asked for a copy of the lease between NWA and Millennium, it was never provided. AR 001419; CP 15559 ("[NWA and Millennium] had had enough and chose not to respond").

⁵ Additionally, while NWA is a subsidiary of Alcoa, they are separate legal entities. Unlike at other properties, Alcoa has maintained a hands-off approach to the site owned by NWA. AR 001700-01.

leased property.⁶ It was unknown, for example, how a sale of NWA's interest in the upland property to Millennium would affect the letter of credit. As DNR noted in its June 2016 request for financial information, DNR had additional reasons for concern over the viability of the letter of credit. AR 001419-20. Under the purchase and sale agreement for Arch Coal's bankruptcy sale of its interest in Millennium, the letter of credit would be provided by the bankrupt Arch Coal through 2019, but the cost of maintaining the letter of credit was to be reimbursed by Millennium, which was then left with one corporate parent facing the same difficult economic conditions that drove Arch Coal to bankruptcy. AR 013766.

Because Millennium's planned facility is far larger than anything contemplated by the Lease and would significantly alter the use of the property, this is not a case in which approving a sublease would simply give DNR "the benefit of the bargain" it struck when the Lease was signed. Thus, the financial responsibility and capacity of Millennium to avoid default as the builder, operator, and maintainer of the facility is critical. NWA's and Millennium's arguments that DNR could have raised the bond amount under the Lease to address such risks miss the mark because DNR has a

⁶ As evidenced by the need for the letter of credit, the obligations of Millennium to NWA could be a significant factor affecting Millennium's financial condition. As a result, DNR requested a copy of the lease agreement between NWA and Millennium, but the lease was never provided. CP 15559.

legitimate interest in examining the financial condition of a subtenant to ensure defaults do not occur in the first place. *See, e.g., Nat'l Distillers & Chem. Corp. v. First Nat'l Bank of Highland Park*, 804 F.2d 978, 981 (7th Cir. 1986); *Kazarinov*, 445 N.Y.S.2d at 920. Additionally, it is unlikely that NWA and Millennium would have simply agreed to significant new bonding requirements, given their resistance to lease amendments. In fact, they disputed in negotiations with DNR that any increases in Lease obligations were even necessary. AR 001076-77. ("Lease already imposes sufficient obligations on Northwest Alloys, and provides sufficient safeguards to protect DNR's rights and interests . . ."). Instead, they insisted, "the proposed consent [to sublease] should contain the same Lease terms and conditions as currently exist." *Id.*

It is well settled that even under ordinary circumstances a landlord has a reasonable interest in a financially sound subtenant to avoid the potential for default and resulting litigation with the tenant. The landlord's need to ensure a proposed subtenant is financially sound is particularly compelling under a lease, such as the Lease presented, that requires the tenant to not only pay rent but also maintain the property and improvements; take necessary action to comply with laws and regulations; and pay all taxes, utilities, and other costs associated with occupancy. Where, as here, a proposed subtenant under such a lease has a corporate parent in bankruptcy

and plans to build, operate, and maintain a significant new facility dependent on an industry facing economic conditions so difficult that many of its largest firms were forced into bankruptcy, the landlord's interest in the subtenant's financial condition is overwhelming. Accordingly, DNR acted reasonably here, and the superior court's conclusion to the contrary is in error.

5. DNR's Requests Were Appropriately Focused on Millennium's Financial Condition, and Not That of Its Parent Company.

NWA and Millennium do not dispute that commercial landlords routinely request financial statements to review the financial condition of a proposed subtenant. In fact, NWA and Millennium have previously conceded that "in most situations, it is perfectly reasonable for a landlord to seek financial statements so that it can evaluate the financial condition of a prospective sublessee" CP 15725.

While they concede that ordinarily it is reasonable for a landlord to request financial statements to evaluate a proposed subtenant, NWA and Millennium argue that DNR should have focused on the financial condition of Millennium's parent, Lighthouse Resources, because Millennium is a startup company. Br. of Respondents at 29, 31. Their argument fails for multiple reasons. First, their argument ignores the express language of Section 9.1(a) which allows DNR to consider whether the proposed

subtenant itself is financially sound. AR 001546. Second, contrary to NWA's and Millennium's assertions, Millennium's financial statements would have provided valuable information concerning Millennium's financial condition at a time when DNR had significant cause for concern over the viability of Millennium and its plans. Third, NWA's and Millennium's assertion that DNR should have inquired about Lighthouse Resources' financial condition misses the mark because an examination of the financial condition of Millennium's parent company would do little to provide DNR with assurance of *Millennium's* financial ability to perform going forward, and NWA and Millennium had the burden of providing the information DNR needed to evaluate their sublease request. AR 001546-47.

DNR should not be denied the benefit of the bargain it made when it signed the Lease in 2008 because NWA later elected to propose a sublease to a newly formed limited liability company dependent on cash contributions provided by "substantial backers," who are strangers to the Lease. Br. of Respondents at 28. DNR had an express Lease right to consider the financial condition of Millennium itself. DNR is entitled to exercise that right in any case. NWA's and Millennium's argument that Millennium was completely dependent on "substantial backers" who are not obligated to perform under the Lease does not allow them to do an end run on DNR's right to consider Millennium's financial condition. If that were

so, NWA could render Section 9.1(a) of the Lease meaningless simply by proposing transfers of the Lease to newly formed LLCs in every case. That outcome would turn Section 9.1(a) on its head and prohibit DNR from considering the financial condition of an assignee or sublessee in the cases with greatest risk—those involving startup companies with no revenue and investors who have no obligation to perform.

The financial statements DNR requested would have provided key information to help DNR assess Millennium's financial condition. DNR requested Millennium provide "a balance sheet, income statement, and cash flow statement . . . that accurately states the current assets, liabilities, and capital of [Millennium] and its income and cash flow for the year ending June 30, 2016." AR 001419. Even assuming, for argument, that after five years of operating for NWA Millennium would have had no revenue,⁷ as NWA and Millennium argue, that fact says nothing about Millennium's assets and liabilities or how it spent the cash it received from

⁷ In addition to handling alumina for NWA, Millennium was NWA's contractor for cleanup of hazardous waste at the upland site adjacent to the Lease. AR 007185-86. Millennium was also engaged in other business activities unrelated to its work for NWA. Millennium brought in up to two weekly trainloads of coal by rail to the upland facilities adjacent to the Lease and unloaded it for Weyerhaeuser. *Id.* Millennium's substantial business activities for both NWA and Weyerhaeuser undercut its assertion that it was merely a startup company. DNR's requests for financial statements would have revealed what revenues Millennium's business activities were generating, how it was spending the revenue, what assets it had to support its activities, and what liabilities it was accruing as a result of them.

Arch Coal and Lighthouse Resources.⁸ The financial statements DNR requested would have answered these key questions regarding Millennium's financial condition.

Given Arch Coal's disclosure in bankruptcy that Millennium's capital needs were so great that Arch Coal's entire investment in Millennium, which it valued at \$38 million when the bankruptcy began, AR 013715, would have evaporated in a matter of weeks, DNR's concerns about Millennium's financial condition were particularly valid. AR 013766. The financial statements DNR requested would have provided insight into how the capital contributions of Arch and Lighthouse were spent, what debts Millennium was accruing, whether Millennium had any assets, their value, and to what degree they were encumbered. This information would have helped DNR make an informed judgment regarding whether Millennium's ship was sinking and, if so, how fast.

NWA's and Millennium's argument that DNR should have focused its inquires on the financial condition of Lighthouse instead of Millennium are off base. Br. of Respondents at 31. Because Lighthouse Resources is a separate legal entity from Millennium, it would have no duty to continue to

⁸ Millennium had represented to DNR, for example, that it had purchased the assets of Chinook Ventures and leased the underlying property in 2010. AR 000140. DNR's requests would have shown whether Millennium still owned these assets, their value, and the degree to which they were encumbered.

fund Millennium or meet Millennium's lease obligations beyond what it had already contributed to the company. *See, e.g., Jack Frost Sales, Inc., v. Harris Trust & Sav. Bank*, 104 Ill. App. 3d, 433 N.E.2d 941 (1982) ("One of the shareholders was wealthy but she was under no legal obligation to put any particular amount into the corporation. . ."). While Lighthouse Resources was a source of development capital for Millennium's plans, AR 013620, Lighthouse could be advancing that capital to Millennium in the form of loans, sending Millennium further into debt, with no obligation to continue funding Millennium's plans in the future. *See Jerome D. Whalen, Commercial Ground Leases* § 14.7 at 14-10, 11 (3d ed. 2013). Accordingly, DNR appropriately focused on Millennium to evaluate Millennium's financial condition as it was entitled to do under Section 9.1(a) of the Lease.

DNR had good reason to question whether Lighthouse Resources would continue to support Millennium following Arch Coal's bankruptcy, given the historically poor economic conditions in the coal industry. Curiously, NWA and Millennium argue that Arch Coal's bankruptcy improved Millennium's financial condition by leaving Millennium with a single corporate owner. Br. of Respondents at 26. To the contrary, Arch Coal's bankruptcy made it more likely, not less, that Lighthouse would abandon its investment in Millennium. Prior to Arch Coal's bankruptcy,

Millennium was a joint venture between Arch Coal and Lighthouse where both companies were obligated to each other to fund Millennium. AR 013765-66. After Lighthouse purchased Arch Coal's interest, Lighthouse no longer had an obligation to Arch Coal to fund Millennium and had the burden of satisfying Millennium's capital needs without the help of Arch. AR 013766-67; Br. of Respondents at 13.

At the time of Arch Coal's bankruptcy, the dim prospects for coal exports had already cast significant doubt on the viability of Millennium's plans. AR 013758. Arch Coal's bankruptcy further called into question the value of Millennium's project. Lighthouse purchased Arch Coal's share of Millennium for almost nothing—an option to purchase a small portion of the capacity of Millennium's planned export terminal if completed at market rate and little more. AR 013767, 013780. After the sale, Lighthouse was thus left paying more of Millennium's substantial capital needs for a project that, based on the bankruptcy sale, had little fair market value and faced significant economic headwinds. Given that Lighthouse had no obligation to continue to fund Millennium under the Lease, it would have made little sense for DNR to focus its attention on Lighthouse's financial condition.

Finally, Millennium's argument that DNR should have focused on the financial condition of Lighthouse fails because NWA had the duty to

provide the information necessary for DNR to evaluate the sublease request. AR 001546-47. In addition to requesting Millennium's financial statements, DNR requested "any information" that would shed light on Millennium's financial condition. AR 001419. DNR had no duty to use magic words so that NWA and Millennium would release the information DNR needed to evaluate their sublease request. NWA and Millennium do not dispute that NWA, as the tenant, had the duty to present the information DNR needed to evaluate the sublease request. AR 001546-47. As the trial court found, following the bankruptcy of Arch Coal, the closure of the Wenatchee Works, and precipitous downturn in the market for coal, DNR had legitimate concerns over Millennium's finances. CP 17691. This unchallenged finding is a verity in this appeal. Accordingly, if NWA and Millennium believed that Lighthouse Resources' financial information should have resolved DNR's concerns over Millennium's financial condition, they should have provided that information in response to DNR's request. Instead, Respondents stonewalled, ignoring the request altogether. CP 15559.

6. Because DNR's Actions Were Objectively Reasonable, NWA's and Millennium's Claims of Bias Fail.

Even under ordinary circumstances, it is reasonable for a landlord to seek information regarding a proposed subtenant's financial condition.

Following the dramatic downturn in the coal markets, Alcoa's closure of the Wenatchee Works, and the bankruptcy of Arch Coal, there was a significant change in circumstances that created a legitimate concern over Millennium's financial condition, as the superior court found. CP 17691. Given those facts, it would have been irresponsible for DNR not to enquire about Millennium's financial condition. Nonetheless, NWA and Millennium argue the facts should be cast aside because DNR acted differently under very different circumstances, and because Intervenors raised the facts as a concern in correspondence with DNR. Br. of Respondents at 8-11, 30. NWA's and Millennium's arguments amount to a claim that DNR arbitrarily requested financial statements based on bias. *Id.* The arguments fail. Given the circumstances presented, DNR's decision to seek financial statements and other information was not arbitrary. In fact, as explained thoroughly above, DNR's decision to request financial statements and other information was objectively reasonable.

Because DNR has authority to consider the financial condition of any proposed transferee under the Lease, NWA's and Millennium's claims of bias amount to a claim that DNR exercised its authority arbitrarily. *See Malmo v. Case*, 28 Wn.2d 828, 835, 184 P.2d 40 (1947) ("under the contracts, the Commissioner . . . had the power to grant, or refuse to grant, extensions. His refusal to do so was in entire good faith. He did not act

arbitrarily or capriciously”). A party seeking to demonstrate an agency acted arbitrarily bears a heavy burden. *Hood Canal*, 195 Wn. App. at 307. A disputed decision is not arbitrary and capricious so long as the decision is based on evidence. *Id.* Accordingly, DNR’s decision to request financial information that DNR did not request in other cases was not arbitrary, if DNR had a reason for it. *Id.*⁹

None of the documents in the record from the other unrelated leases present facts that are remotely similar to the facts of this case. Br. of Respondents at 11. In fact, the documents do not present any of the facts presented here. *Id.* None of the unrelated leases to which NWA and Millennium point appear to have involved new construction, bankruptcies, or any other issues of concern presented here.¹⁰ Because none of the unrelated transactions presents facts that are comparable, the unrelated transactions provide no support for NWA’s and Millennium’s claims of bias.

⁹ See also *Freeman v. Dep’t of Interior*, 37 F. Supp. 3d 313, 346 (D.D.C. 2014) (To show agency improperly treated claimant differently than others under the APA or equal protection clause, “parties must be prima facie identical in all relevant respects, or directly comparable in all material respects.”) (citation and punctuation omitted).

¹⁰ Nonetheless, DNR’s exchange with Intalco and Petrogas shows production of financial statements is routine. As part of its review of the proposed assignment, DNR requested documentation of Petrogas’ financial condition. AR 013784. From their response, it is clear that Alcoa and Petrogas understood that companies demonstrate their financial condition by providing financial statements. AR 013867.

Nor does it help NWA and Millennium here that Intervenors raised concerns about Millennium's financial condition in correspondence with DNR. Br. of Respondents at 10. That Intervenors called out the bankruptcy of Arch Coal and difficult conditions in the coal industry, among other things, in urging DNR to take action, does not make those facts less true. Because the facts support an objectively reasonable concern over Millennium's financial condition, DNR's decision to request financial information was not unreasonable, and it certainly was not arbitrary.

Nor does the record support NWA and Millennium's assertion that DNR "requested copious amounts of information and changed its position numerous times." Br. of Respondents at 8. Throughout its negotiations with NWA, DNR was consistent in its assertion that it could not issue a consent to sublease unless SEPA requirements were met. Nonetheless, DNR worked with NWA to meet its professed need for a sublease: "Northwest Alloy's sister facility in Wenatchee, which is a smelter, is critically dependent upon Millennium operating the dock . . . to load and transport alumina." AR 000437-38. Throughout those negotiations, DNR remained resolute that any action it took must comply with its environmental obligations under SEPA. *See, e.g.*, AR 014131, 001003, 001136-37. Millennium's arguments that DNR changed its position ignore the fact that Millennium, and

Millennium's proposal, and the economic circumstances they faced changed significantly.¹¹

The record here shows that what changed over the course of negotiations was not DNR's concern over environmental factors. DNR steadfastly maintained SEPA compliance was necessary, AR 014131, 001003, 001136-37, and reserved the right to consider environmental review of Millennium's plans to the end. AR 001003, 001136-37. What changed was economic conditions, which, in the coal industry, threw many of the nation's largest coal producers, including Millennium's corporate parent, into bankruptcy. AR 013795, 013758, 001260.

¹¹ For example Millennium and NWA argue that DNR requested lease amendments that would have blocked Millennium's coal export plans. Br. of Respondents at 8. The parties were discussing lease amendments in 2010 and 2011 to facilitate dredging, repair, and cure work while Millennium was also proposing plans for coal loading improvements on the existing dock. AR 000363, 014131. During that time, Millennium withdrew its applications for all that work after it came to light that Millennium had intentionally concealed its plans for a significantly larger coal export facility. AR 000406, 000401. When Millennium resubmitted its shoreline application for the work, it did not include coal handling facilities. AR 000486. At Millennium's request, Cowlitz County's October 2011 mitigated determination of non-significance (MDNS) for the new non-coal proposal contained a condition that prohibited coal export from the existing dock for a period of ten years but acknowledged Millennium could make "future permit applications for a new dock or docks . . . for the export of coal." AR 005645. Following issuance of the MDNS for Millennium's cure work, DNR re-initiated discussion of an approach to resolving Lease defaults, initially discussed in December 2010, AR 000363, that involved amendment of the Lease. AR 014131. Because each of the activities that Millennium was proposing—repairing the dock, dredging, and curing the default—required additional authorization from DNR, DNR suggested "the most expedient approach" was to amend the Lease to authorize the activities. *Id.* DNR also noted that if the Lease amendments were consistent with limitations on the use of the dock in Cowlitz County's MDNS for Millennium's proposed work, issued the week before, DNR could consider NWA's sublease request immediately, without concern over segmentation under SEPA. *Id.*

D. The Superior Court Erred by Concluding That the Proposed Expansion Is Allowed Under the Lease. DNR Properly Assigned Error to This Conclusion, and It Is Before the Court.

In its written findings, the trial court expressly construed the scope of the Lease as allowing Millennium's proposed coal terminal expansion. CP 17692 (Order on the Merits ¶ 12). As discussed in DNR's Opening Brief, this finding was in error, not supported by the record, and specifically not supported by the language in the Lease. *See* DNR Opening Br. at 39-45. NWA and Millennium agree that the scope of the permitted use was not before the trial court. Br. of Respondents at 35. As this issue was not before the trial court, the trial court should not have ruled on it, and the fact that it did so was erroneous.¹² DNR Opening Br. at 39-45. DNR assigned error to this finding, and it is therefore properly before the Court for consideration. DNR Opening Br. at 3-4.

In related litigation that is currently pending in the federal district court, Millennium is relying, in part, on the trial court's findings in this matter to support its various constitutional and preemption claims regarding the Lease against the Commissioner of Public Lands. *See Lighthouse Res.*,

¹² NWA and Millennium refer to the trial court's oral statements to assert that DNR's concerns regarding the scope of the trial court's order on the terminal expansion are baseless. Br. of Respondents at 35. However, the trial court's oral opinion "is no more than an expression of its informal opinion at the time it is rendered. It has no final or binding effect unless formally incorporated into the findings, conclusions, and judgment." *State v. Friedlund*, 182 Wn.2d 388, 394-95, 341 P.3d 280 (2015). Therefore, it is the content of the trial court's written order here that controls, not its oral statements.

Inc. v. Inslee, No. 3:18-cv-05005-RJB, Dkt. #1 at 33, ¶ 160 (W.D. Wash. filed January 3, 2018). Despite DNR's dismissal of the expansion request without prejudice, it is possible, if not likely, that Millennium will argue in the federal case that the trial court's findings in the present matter have a preclusive effect. Accordingly, the trial court's findings here are not mere dicta, as Millennium asserts, and its reliance on *ALLTEL Information Services, Inc. v. FDIC*, 194 F.3d 1036 (9th Cir. 1999), to support its position is therefore misplaced. *See* Br. of Respondents at 35.

Should this Court reverse the trial court, vacate its decision, and conclude that DNR properly denied NWA's and Millennium's request for a proposed sublease, it will not need to rule on the issue of whether Millennium's proposed coal terminal expansion is allowed under the Lease. However, should this Court uphold the trial court's ruling, it should specifically reverse the trial court's finding that the terminal expansion is allowed.

E. Even If the Court Finds DNR Acted Arbitrarily, Remand Is the Appropriate Remedy Under RCW 79.02.030.

The uncontested facts in this case show that DNR had legitimate concerns regarding Millennium's ability to perform as a subtenant under NWA's lease. CP 17691. Nevertheless, should this Court determine that DNR acted arbitrarily in denying the proposed sublease request, the

appropriate remedy is a remand to DNR. As the trial court correctly concluded, “the Court cannot substitute its judgment for that of the agency” under RCW 79.02.030. CP 17689. An interpretation of RCW 79.02.030 that would allow the Court to substitute its judgment on whether DNR should issue a sublease would render the statute unconstitutional on separation of powers principles. The Supreme Court discussed this point in *Household Finance Corporation*:

We are constrained to hold that the portion of Rem. Supp. 1941, § 8371-23, which purports to vest in the superior court for Thurston county the right to reverse on a trial *de novo* a decision of the supervisor with reference to the granting of such a license and, *in effect, to substitute its judgment for that of the supervisor as to whether or not a license should issue, is unconstitutional as an attempt to vest a nonjudicial power in a constitutionally created court.*

Household Fin. Corp., 40 Wn.2d at 456-57 (emphasis added). The Court should avoid a construction of the statute that would render it unconstitutional. *In re Personal Restraint of Matteson*, 142 Wn.2d 298, 307, 12 P.3d 585 (2000) (“Whenever possible, it is the duty of this court to construe a statute so as to uphold its constitutionality.”)

Despite the constitutional prohibition on judicial use of administrative discretion, NWA and Millennium argue that courts have interpreted RCW 79.02.030 to nevertheless allow courts to do exactly that. Br. of Respondents at 38. This argument conflates the power of the Court to review discretionary decisions under the arbitrary and capricious

standard and its power to review agency legal determinations de novo. Review of agency discretionary action under RCW 79.02.030 is limited to whether an agency acted arbitrarily and capriciously, regardless of whether the decision is made under a contract. *Malmo*, 28 Wn.2d at 835-36.¹³

NWA and Millennium cite to *Polson Logging Company v. Martin*, 195 Wash. 179, 80 P.2d 767 (1938), but that case does not advance their position. In *Polson*, “[t]he only question presented [was] whether the holding of the [timber] sale within the courthouse instead of without the front door rendered it invalid.” *Polson*, 195 Wash. at 181. The Court found the sale conducted inside the courthouse substantially complied with the statute requiring the sale to occur in front of the courthouse, and, therefore, the sale was not invalid. *Id.* at 185. At the time of the case, the timber at issue had been “sold to the Polson Logging Company at the appraised value.” *Id.* at 180. The issue of whether the sale was invalid was raised a week after the sale was completed. *Id.* The decision in *Polson* construing the sales statute thus simply confirmed that a sale already consummated was valid as a matter of law. Nothing in *Polson* suggests that

¹³ Although NWA and Millennium attempt to distinguish *Malmo*, Br. of Respondents at 46, *Malmo* explicitly looked at the Commissioner’s authority under an existing contract and applied the arbitrary and capricious standard. See *Malmo*, 28 Wn.2d at 835 (“we conclude that, under the contracts, the Commissioner of Public Lands had the power to grant, or refuse to grant, extensions. His refusal to do so was in entire good faith. He did not act arbitrarily or capriciously”).

RCW 79.02.030 gave the court the power to exercise administrative discretion to determine whether and under what conditions the timber should be sold.

The second case cited by NWA and Millennium, *Town of Ilwaco v. Ilwaco Railway & Navigation Company*, 17 Wash. 652, 50 P. 572 (1897), also presents a purely legal issue and does not help their argument.¹⁴ As stated by the court, “the disposition of the case [depended] on whether the tract in question was, at the time of purchase, within the limits of any public street of appellant town.” *Town of Ilwaco*, 17 Wash. at 657. In *Town of Ilwaco*, a railroad built a wharf on tidelands in front of the town in 1887. *Id.* at 653. In 1894, the town platted the tidelands. *Id.* In 1895, the railroad applied to purchase the tidelands on which the wharf was built “basing its right to purchase upon the fact of its having improved [the tidelands] prior to the 26th day of March 1890.” *Id.* at 654 (emphasis added). At the time *Town of Ilwaco* was decided, a party who had improved first-class tidelands prior to March 26, 1890, had an exclusive right to purchase the improved tidelands for 60 days after the tidelands were appraised. Laws of 1895, ch. 178, § 58. If no competing applications were filed during the 60-day period, the applicant was “deemed to have the right of purchase.”

¹⁴ The appeal in the case was made under a predecessor to RCW 79.02.030 found in the Laws of 1895, ch. 178, § 82.

Laws of 1895, ch. 178, § 61. Nonetheless, the State Board of Land Commissioners denied the railroad's application based on the conclusion that the tidelands in question were within a street on the plat. *Town of Ilwaco*, 17 Wash. at 654.

The Supreme Court resolved the case in favor of the railroad, holding that the town lacked legal authority to extend the street over the tidelands in question. *Id.* at 659. As a result of the Court's legal conclusion, the railroad was "deemed to have the right of purchase" by statute. Laws of 1895, ch. 178, §§ 61, 62. Nothing in *Town of Ilwaco* suggests that RCW 79.02.030, or its predecessor, could authorize the Court to exercise legislative or delegated administrative authority to determine whether, and under what conditions, public lands should be sold.

Washington courts have long recognized the distinction between judicial authority to determine legal issues de novo on appeal and discretionary administrative authority, which courts may not exercise. See *McNaught-Collins Imprv. Co. v. Atlantic Pac. Pile & Timber Preserving Co.*, 36 Wash. 669, 79 P. 484 (1905) (decision of the Board of State Land Commissioners not to resell harbor area lease "was executive and discretionary, and . . . is not appealable."); *Malmo*, 28 Wn.2d at 835-36 (review of Commissioner of Public Lands' discretionary contract decision under arbitrary and capricious standard). Even where a court finds that an

administrative agency failed to comply with a legal duty, the court may not exercise administrative discretion and direct the agency how to meet its duty. *See, e.g., Swinomish Indian Tribal Cmty. v. Island Cty.*, 87 Wn. App. 552, 562, 942 P.2d 1034 (1997).

In *Swinomish*, the court of appeals affirmed the superior court's holding that the County failed to protect the Tribe's cultural resources as required by the County's Shoreline Management Master Plan (SMMP). *Id.* at 561-62. The court of appeals found the superior court "exceeded its jurisdiction, however, when it prescribed the specific procedures the County must adopt [to protect the resources]." *Id.* The appellate court found that under the SMMP "the County has discretion to determine *how* it is going to implement the requirement . . .," and therefore, the court concluded it could not order the County to protect the cultural resources in a specific manner. *Id.* at 562 (emphasis in original). The court remanded the case to the superior court for an order directing the County to develop procedures to protect cultural resources as required by the SMMP. *Id.* at 563.

As these cases show, when an administrative decision involves the use of discretion, the Court may not, on appeal, substitute its judgment for that of the agency or direct the agency how to use its discretion. None of the cases cited by NWA and Millennium involve facts where the landlord

identified a legitimate concern regarding a proposed assignment or sublease. *See* Br. of Respondents at 38-41. Under Section 9.1 of the Lease, DNR has significant discretion to determine whether to consent to a sublease and to condition its consent upon amendments to the Lease, AR 001546, and it appropriately exercised that discretion in denying NWA's proposed sublease to Millennium.

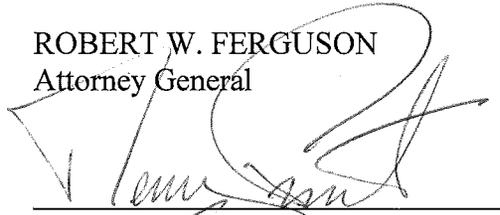
State-owned aquatic lands, such as the Columbia River bed leased by NWA, are a valuable natural resource that the State holds in trust for the benefit of the public. *See, e.g., Lake Union Drydock Co. v. Dep't of Nat. Res.*, 143 Wn. App. 644, 179 P.3d 844 (2008). As noted by the trial court, the history of subleasing under the Lease presents an object lesson illustrating what an unsound subtenant could do to those lands. CP 17691. Given that the Lease is for an industrial facility on the Columbia River, a financially unsound subtenant's operations may endanger the public, degrade the environment, and harm the property in ways that could take years to rectify, the Court should not lightly deem a sublease granted under these circumstances. Because DNR identified a legitimate concern regarding the viability of the sublease proposal, a fact that is unchallenged and thus a verity in this appeal, the proper remedy, should the Court conclude that DNR acted arbitrarily in denying the proposed consent to sublease, is a remand to DNR to address that concern.

III. CONCLUSION

For the foregoing reasons, DNR respectfully requests this Court reverse the superior court and reinstate DNR's denial of consent to NWA's proposed sublease to Millennium.

RESPECTFULLY SUBMITTED this 5th day of September, 2018.

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I certify that I caused a copy of the foregoing document to be served on all parties or their counsel of record on September 5, 2018, through the Washington State Appellate Courts' eFiling Portal.

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

DATED this 5th day of September, 2018, at Olympia, Washington.



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ATTORNEY GENERAL'S OFFICE - NATURAL RESOURCES DIVISION

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