



No. 331920

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

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FIRST BANK OF LINCOLN,

Plaintiff/Appellant,

v.

DONALD C. TUSCHOFF and JANE DOE TUSCHOFF; BANANA  
BELT GAMING, LLC; JOHN DOES 1-IV, and all parties claiming  
right, title, or interest in the subject real property in Asotin County,  
Washington,

Defendants/Respondents.

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Appeal from the Superior Court for Asotin County  
Cause No. 14-2-00105-9

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BRIEF OF RESPONDENT BANANA BELT GAMING, LLC

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## I. INTRODUCTION

Under Washington law, full payment of the obligation secured by a deed of trust extinguishes the lien because the lien cannot exist independent of an obligation. This appeal asks whether the collateral assignment of a deed of trust creates an exception to this rule and makes the deed of trust enforceable beyond full payment of the obligation the deed of trust secured. The trial court correctly found that the deed of trust became a “nullity” upon full payment of the obligation and should be affirmed.

First Bank of Lincoln (“First Bank”) wants to foreclose an extinguished deed of trust that secured a debt - now paid in full - that Gene M. Schwab and his partners (“Schwab” collectively) owed to Defendant Donald C. Tuschoff (“Tuschoff”). The Tuschoff/Schwab Deed of Trust covered real property now owned by Banana Belt Gaming, LLC (“Banana Belt”) in Asotin County, Washington (the “Property”). The extinguished Tuschoff/Schwab Deed of Trust did *not* secure payment of Tuschoff’s debt to First Bank (“Montana Note”). Tuschoff’s debt to First Bank was secured by a deed of trust on property located in Lincoln, Montana and a *collateral* assignment of Tuschoff’s beneficial rights in the Tuschoff/Schwab Deed of Trust.

Banana Belt purchased the Property from Schwab in June 2013 for \$1,350,000.00. At closing, \$359,271.82 of the proceeds was paid to fully satisfy Schwab's debt to Tuschoff and extinguish the lien on the Property. First Bank's interest flowed through, and was limited in scope to, Tuschoff's interest in the Tuschoff/Schwab Deed of Trust. Accordingly, First Bank's interest was extinguished when Tuschoff's interest was extinguished.

Likewise, Tuschoff's debt to First Bank ("Montana Note") was extinguished as a matter of Montana law when First Bank non-judicially foreclosed on the Lincoln, Montana property and purchased that property with a credit bid of the full debt amount. First Bank fails to explain how it can foreclose the Tuschoff/Schwab Deed of Trust when the debt it secured has been satisfied and Tuschoff's debt to First Bank was satisfied by First Bank's non-judicial foreclosure of the Lincoln, Montana property.

Despite the fact that no debt to Tuschoff or First Bank remains, First Bank wants Banana Belt to pay twice for the Property or face foreclosure. First Bank erroneously claims that it, not Tuschoff, should have received the final Tuschoff/Schwab payment at the closing of Banana Belt's purchase of the Property.

Tuschoff assigned First Bank a security interest in his beneficial interest in the Tuschoff/Schwab Deed of Trust on January 27, 2011. Between January 27, 2011 and June 30, 2013, Schwab made twenty-nine (29) monthly principal interest payments, totaling **\$283,957.85**, directly to Tuschoff. Tellingly, First Bank claims no entitlement to those payments - because it cannot - just as First Bank had no right to the final payment to Tuschoff. First Bank President Kenneth Martin testified that the Bank knew in May of 2013 that Tuschoff may not be able to satisfy his obligation to First Bank, but made no attempt to seek direct payments from Schwab.

Although there are a number of transactions involved, the issue here is simple. This case requires a distinction between an absolute assignment and a collateral assignment. An absolute assignment immediately transfers the assignor's rights and interests under a contract to the assignee. *Uni-Com Nw., Ltd. v. Argus Publ'g Co.*, 47 Wn. App. 787, 794 (1987). Under a collateral assignment, by contrast, the assignor retains its rights and interests unless it defaults on a separate obligation to the assignee. *Id.* The transfer of rights and interests under a collateral assignment is thus contingent upon the assignor's default. *Id.*

First Bank seeks to avoid this distinction by suggesting that it owned “all right, title and interest” in the Tuschoff/Schwab Deed of Trust. Likewise, the cases it cites address absolute assignments, not collateral assignments. However, First Bank admits that it took a *collateral* assignment of Tuschoff’s beneficial interest in the Tuschoff/Schwab Deed of Trust and acknowledged that Tuschoff, not First Bank, was the owner of the Tuschoff/Schwab Note and Deed of Trust. First Bank President Kenneth Martin referred to the payments on the Tuschoff/Schwab Note as “Mr. Tuschoff’s revenue.” Consequently, the transfer of Tuschoff’s beneficial interest in the Tuschoff/Schwab Deed of Trust (the right to foreclose on the Property in the event of a default by Schwab) was contingent on Tuschoff defaulting on his separate obligation to First Bank. Tuschoff retained the right to collect payment on the Note, as evidenced by the fact that he collected all 29 principal and interest payments—a total of \$283,957.85—before Banana Belt purchased the Property.

Despite allowing Tuschoff to collect almost \$300,000.00 from Schwab, First Bank insists that it, rather than Tuschoff, was entitled to the final payoff of the Tuschoff/Schwab Note at closing. However, First Bank has presented no evidence that Tuschoff was in default at

that time under the Montana Note. As such, First Bank's representation that it owned "all right, title and interest" in the Tuschoff/Schwab Note and Deed of Trust fails as a matter of law. Given that Tuschoff was not in default, First Bank had no right to enforce its security interest in the Tuschoff/Schwab Deed of Trust, and Tuschoff was entitled to the final payoff. First Bank does not have a "lien" on the Property, because a lien cannot exist independently of a legally enforceable obligation. First Bank cannot foreclose a deed of trust where the obligation it secured has been satisfied.

Even if First Bank had suggested, let alone proven, that Tuschoff was in default, its claims fail for three additional reasons. First, the bank never issued a direct payment demand to Schwab. As a result, payment of the funds to Tuschoff extinguished Schwab's remaining obligation on the Tuschoff/Schwab Note. RCW 65.08.120. Second, First Bank bid the full amount of Tuschoff's obligation to First Bank at a Trustee's sale of the Lincoln, Montana property. Third, First Bank's action is barred by Montana's anti-deficiency statute. Given that First Bank non-judicially foreclosed on the Lincoln, Montana property in August 2014, it cannot pursue a second

foreclosure to satisfy any remaining deficiency (if any deficiency in fact remains) on the Montana Note. Mont. Code Ann. § 71-1-317.

The Court should affirm the judgment of the trial court and award Banana Belt its fees and costs.

## **II. ASSIGNMENTS OF ERROR**

Banana Belt makes no assignments of error.

## **III. ISSUES ON APPEAL**

1. Is the holder of a collateral assignment of a note and deed of trust entitled to direct payment on the note when the assignor has not defaulted on the obligation for which the assignment was given as collateral?
2. Does the collateral assignment of a deed of trust create an exception to the rule that a lien is extinguished upon satisfaction of the underlying debt?
3. Is the holder of a collateral assignment of a note and deed of trust entitled to direct payment in the absence of a demand for direct payment issued to the obligor?
4. Is a debt satisfied when the deed of trust beneficiary bids the full debt amount at a Trustee's sale following a non-judicial foreclosure of the deed of trust securing the debt?

5. Does the non-judicial foreclosure of a deed of trust bar the foreclosing party from seeking a deficiency under Montana law?

#### **IV. STATEMENT OF THE CASE**

First Bank took a *collateral* assignment of the deed of trust it now seeks to foreclose. Contrary to First Bank's assertions, this assignment did not vest First Bank with "all right, title, and interest" under the Tuschoff/Schwab Note and Deed of Trust. First Bank acquired only a *contingent* right to step into Tuschoff's shoes if Tuschoff defaulted on his separate obligation to First Bank; and even then First Bank could only foreclose if Schwab defaulted on the Tuschoff/Schwab Note. Regardless of the interest First Bank obtained from Tuschoff, there will never be a default by Schwab because the debt to Tuschoff has been paid in full. Since there can be no default, the Tuschoff/Schwab Deed of Trust cannot be foreclosed. The Court should reject First Bank's attempts to foreclose a lien it never held to satisfy a debt that has been paid in full.

##### **A. The 1998 Tuschoff/Schwab Transaction**

In 1998, Tuschoff sold the Property, currently owned by Banana Belt, to Gene M. Schwab, Ladene Schwab, James R. Schwab,

Dianney T. Huffaker, David C. Prall, Kathy Prall, and David Shawn Prall (collectively "Schwab"). CP 394. Tuschoff agreed to finance the sale in return for Schwab executing an installment note in the amount of \$1,100,000.00. CP 394, 396-99. To secure Schwab's obligation on the Tuschoff/Schwab Note, Schwab executed the Tuschoff/Schwab Deed of Trust. CP 396-99. The Tuschoff/Schwab Deed of Trust identified Tuschoff as the Beneficiary and stated:

This deed is for the purpose of securing performance of each agreement of Grantor [Schwab] herein contained, and payment of the sum of One Million One Hundred Thousand and No/100 Dollars (\$1,100,000.00) with interest, in accordance with the terms of a promissory note of even date herewith payable to Beneficiary or order, and made by Grantor, and all renewals, modifications and extensions thereof, and also such further sums as may be advanced or loaned by Beneficiary to Grantor, or any of their successors or assigns, together with interest thereon at such rate as shall be agreed upon.

CP 396-99 (emphasis added). Nothing in the Tuschoff/Schwab Deed of Trust indicated that the Property was being pledged to secure Tuschoff's separate obligations to a third-party. *Id.* Nor did the Tuschoff/Schwab Deed of Trust grant Tuschoff the right to pledge the Property as collateral for his own obligations to a third-party. *Id.* The Tuschoff/Schwab Deed of Trust was recorded November 2, 1998, as Instrument No. 237362, in Asotin County, Washington. CP 396.

On October 26, 1998, Tuschoff executed a Request for Reconveyance authorizing the named Trustee, Alliance Title & Escrow Corp., to execute a reconveyance upon receipt of the original promissory note marked "PAID IN FULL" and the original recorded deed of trust. CP 401, 496.

The original Tuschoff/Schwab Deed of Trust and original Tuschoff/Schwab Note were placed into escrow with Land Title of Nez Perce County ("Land Title") (formerly "Fidelity Escrow"). CP 403-05. Land Title held the original loan documents, collected Schwab's payments, and disbursed those payments to Tuschoff. CP 411, 525-26. First Bank never notified anyone that payments on the Tuschoff/Schwab Note should be sent directly to First Bank.

**B. First Bank's 2011 Loan to Tuschoff ("Montana Note")**

Approximately thirteen years later, on January 27, 2011, Tuschoff signed a promissory note ("Montana Note") in the amount of \$440,000.00 to First Bank to purchase a property known as the Hotel Lincoln in Lewis and Clark County, Montana ("Hotel Lincoln"). CP 423-27. In addition to a deed of trust on the Montana property, Tuschoff gave First Bank a collateral assignment of his beneficial interest in the Tuschoff/Schwab Deed of Trust to partially

secure his obligation to First Bank. CP 440-41. Tuschoff assigned only his rights as a beneficiary under the Tuschoff/Schwab Deed of Trust. CP 440-41; *see also* 398 (Mutual Agreements ¶ 8). The collateral assignment acknowledged that the Tuschoff/Schwab Deed of Trust was “given to secure payment” of the Tuschoff/Schwab Promissory Note. CP 440-41. There is no document showing that the Property itself was pledged to secure Tuschoff’s obligation to First Bank on the Montana Note.

First Bank cannot dispute that the assignment was a collateral, not absolute, assignment. First Bank admits that the assignment was “given for collateral purposes only.” CP 410. The UCC Financing Statement Tuschoff signed in favor of First Bank listed the Tuschoff/Schwab Deed of Trust as collateral Tuschoff “own[ed],” CP 447. First Bank President Kenneth Martin signed a Subordination Agreement that acknowledged that Tuschoff owned the note secured by the Tuschoff/Schwab Deed of Trust and referenced the payments on the Tuschoff/Schwab Note as “Mr. Tuschoff’s revenue” in his declaration testimony. CP 449-50; 64 at ¶ 12.

Following the collateral assignment, First Bank never sent notice to anyone that payments on the Tuschoff/Schwab loan should

be sent to First Bank rather than Tuschoff. CP 412, 528-29. Accordingly, Schwab made twenty-nine (29) principal and interest payments totaling \$283,957.85, directly to Tuschoff (via Land Title) between the January 27, 2011 collateral assignment and the June 2013 sale to Banana Belt. CP 452-60, 554.

Likewise, Land Title retained possession of the original Tuschoff/Schwab loan documents. CP 412, 518-19. First Bank never notified Land Title that it had a collateral assignment of the Tuschoff/Schwab Deed of Trust and never requested that Land Title hold the original Tuschoff/Schwab loan documents as a custodian for First Bank. CP 414, 524-25.

First Bank recorded the collateral assignment in the real property records of Asotin County, Washington, and filed a UCC Financing Statement in Washington State. CP 440-41, 443-47.

First Bank President Kenneth Martin testified that First Bank knew in May of 2013 that Tuschoff would not be able to satisfy his obligation from the Hotel Lincoln's income alone. CP 064 ¶ 12. However, the Bank made no demand for direct payment on the Tuschoff/Schwab Note and waited until January 29, 2014, to make any attempt to check the status of its collateral. CP 64 ¶ 13.

### **C. Schwab's 2013 Sale to Banana Belt**

In 2013, Banana Belt agreed to purchase the Property from Schwab for \$1,350,000.00. CP 361-64. A May 31, 2013 title commitment on the Property listed the Tuschoff/Schwab Deed of Trust and the Humphrey/Tuschoff Deed of Trust.<sup>1</sup> CP 470-71. Banana Belt's lender, Columbia Bank, demanded a first lien position on the Property and conditioned the loan to Banana Belt on release of the two existing deeds of trust. CP 462-75, 477-78.

First American was the closing agent on the Banana Belt purchase of the Property. CP 535. On April 10, 2013, in preparation for closing the transaction, First American asked Land Title for a full payoff amount for the Tuschoff/Schwab Note. CP 480-85. That same day, Tonja Hatcher from First American<sup>2</sup> sent an email to Rita Johnson at Land Title. CP 480. The email asked Ms. Johnson to confirm that she had "all of the release documents required to release

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<sup>1</sup> The Humphrey/Schwab Deed of Trust was dated July 22, 1994, and secured a debt Tuschoff owed to Rex Humphrey and Helen Humphrey. CP 484. The Humphrey/Schwab Deed of Trust was eliminated in the sale to Banana Belt and is not at issue in this case. CP 512-13.

<sup>2</sup> Title Financial Corporation is the reconveyance department of First American. CP 550.

paragraphs 21 and 23 from the title commitment.” CP 480. The email attached the pages of the title commitment listing the Humphrey/Tuschoff Deed of Trust at paragraph 21 and the Tuschoff/Schwab Deed of Trust at paragraph 23. CP 484-85.

On April 15, 2013, Ms. Hatcher sent a follow-up email to Ms. Johnson requesting confirmation of the payoff of the Tuschoff/Schwab Deed of Trust, so “I can guarantee clear title to the buyer and buyer’s lender.” Ms. Johnson responded “This is a wrap and both Deeds of Trust will be paid.” CP 487.

On June 21, 2013, Land Title provided a final payoff quote showing \$359,271.82 outstanding on the Tuschoff/Schwab Note. CP 489-90.

On June 26, 2013, First American sent Land Title an Outgoing Payoff Letter enclosing a check for \$359,271.82 to Land Title. CP 492-94. The Outgoing Payoff Letter stated “These funds are tendered in exchange for a release of the original Promissory Note and original Deed of Trust/ Mortgage recorded November 02, 1998, as Instrument No. 237362 recorded in Asotin County, Washington [the Tuschoff/Schwab Deed of Trust].” CP 492 (emphasis added). The First American Outgoing Payoff Letter further stated that “Our check

in the amount \$359,271.82 and any additional interest or fees that may apply representing full payoff of the [Tuschoff/Schwab] loan, negotiation of said check constitutes your agreement to issue a full Reconveyance of the Deed of Trust securing said loan.” CP 493 (emphasis added).

Land Title negotiated the check from First American on July 1, 2013, and disbursed those funds to Tuschoff the same day. CP 512-14. Accordingly, Schwab’s obligation to Tuschoff was paid in full that day. CP 452-60. However, Land Title did not facilitate the reconveyance of the Tuschoff/Schwab Deed of Trust. CP 520-22.

On June, 26, 2013, Schwab conveyed the Property to Banana Belt via Statutory Warranty Deed. CP 366-67.

**D. First Bank Files this Action Seeking to Foreclose the Tuschoff/Schwab Deed of Trust**

On April 24, 2014, almost a year after Banana Belt’s purchase closed, First Bank filed this action seeking declaratory judgment that the 2011 assignment of Tuschoff’s beneficial interest in the Tuschoff/Schwab Deed of Trust remains a valid, enforceable lien on the Property.

On May 30, 2014, Banana Belt filed its answer with cross claims for relief against Tuschoff and counterclaims against First

Bank. CP 10-30. Banana Belt's counterclaims requested declaratory judgment that the Tuschoff/Schwab Deed of Trust is invalid and unenforceable because the debt it secured was paid in full and asked the trial court to quiet title in Banana Belt. CP 14-15. First Bank never answered Banana Belt's counterclaims.

**E. First Bank Non-Judicially Forecloses on its Montana Deed of Trust**

First Bank has proffered no evidence that explains how or when Tuschoff defaulted on the Montana Note. Nonetheless, First Bank non-judicially foreclosed on the Hotel Lincoln property on August 25, 2014. CP 66. First Bank was the only bidder at the Trustee's sale and took title to the Property. CP 66. Based on the Notice of Trustee's Sale, the outstanding principal balance on the Montana Note was \$400,430.42. CP 639. Despite numerous requests by Banana Belt's counsel, First Bank refused to disclose the amount it bid for the Property at the sale. CP 632 ¶ 3. However, First Bank has never denied that it bid the full amount due. *Id.* Based on First Bank's failure to aver otherwise, it presumably bid the full outstanding balance on the Montana Note.

**F. The Trial Court Grants Banana Belt's Cross-Motion for Summary Judgment**

On October 24, 2014, Banana Belt moved for summary judgment and an order to quiet title and reconvey the Tuschoff/Schwab Deed of Trust on the basis that the payment to Tuschoff satisfied Schwab's debt to Tuschoff and extinguished the Tuschoff/Schwab Deed of Trust. CP 332-56. First Bank cross-moved for summary judgment on its claims. CP 36-37. The trial court heard the parties' cross-motions for summary judgment on December 5, 2014. On February 10, 2015, the trial court issued its Summary Judgment and Order to Quiet Title and Reconvey granting Banana Belt's motion and denying First Bank's cross-motion. CP 732. In granting Banana Belt's summary judgment, the court found that Tuschoff's assignment of the Tuschoff/Schwab Deed of Trust:

...was simply an assignment of Mr. Tuschoff's *beneficial interest* in and to the deed of trust, he remained legally entitled to receive all payments made on the Schwab promissory note. There is no indication in the record that at the time the note was paid in full, that Mr. Tuschoff was under any legal disability to receive that payment. Once the funds were received by Tuschoff, the deed of trust became a nullity. Tuschoff did not fulfill his obligation to First Bank of Lincoln. Banana Belt Gaming, had no duty or obligation, thru its agent or otherwise, to First Bank of Lincoln. Banana

Belt Gaming, having already purchased the property once, will not be required to purchase it a second time.

CP 730-31 (emphasis in original).

On appeal, First Bank again fails to establish or point to anything in the record demonstrating “that Mr. Tuschoff was under any legal disability to receive [the final] payment.” Instead, it faults Banana Belt and its agents for failing to direct that payment to First Bank. There is no fault, because First Bank had no legal right to that payment. Accordingly, the Tuschoff/Schwab Deed of Trust is a nullity and the trial court should be affirmed.

#### **G. Summary Timeline of Relevant Transactions**

For the Court’s convenience, Banana Belt provides the following summary of the relevant transactions:

**October 1998:** Schwab purchased the Property from Tuschoff. The purchase was financed by the Tuschoff/Schwab Note in the amount of \$1,100,000.00, payable to Tuschoff. Schwab executed the Tuschoff/Schwab Deed of Trust, listing Tuschoff as the beneficiary, to secure Schwab’s obligation on the Tuschoff/Schwab Note.

**January 2011:** Tuschoff purchased the Hotel Lincoln in Lincoln, Montana. To finance the purchase, Tuschoff executed a \$440,000.00 promissory note in favor of First Bank (“Montana Note”). As security for this obligation, Tuschoff gave the following: (1) a deed of trust to the Hotel Lincoln property listing First Bank as the beneficiary; and (2) a collateral assignment of his beneficial interest in the Tuschoff/Schwab Deed of Trust.

**June/July 2013:** Banana Belt purchased the Property from Schwab for \$1,350,000.00. At closing, \$359,271.82 of the purchase price was applied to paying off the remaining balance on the Tuschoff/Schwab Note and to release the Tuschoff/Schwab Deed of Trust. These funds were paid to Land Title, the escrow agent responsible for collecting all payments on the Tuschoff/Schwab Note. Land Title subsequently disbursed the funds to Tuschoff.

**August 2014:** First Bank non-judicially foreclosed on the Hotel Lincoln property in Lincoln, Montana. First Bank was the successful bidder at the Trustee’s sale, presumably bidding the full amount due on the Montana Note.

## V. ARGUMENT

### A. **First Bank's claims that it was entitled to direct payment fail as a matter of law because Tuschoff was not in default when the payment was made.**

First Bank claims that it owned "all right, title and interest" in the Tuschoff/Schwab Note and Deed of Trust. Opening Brief at 11. This is not true and completely contradicts First Bank's actions, admission, and documents. If First Bank owned "all right, title and interest" in the Tuschoff/Schwab Note and deed of trust, it would not have allowed Tuschoff to collect 29 payments totaling \$283,957.85 on that Note.

First Bank knew in May 2013 that Tuschoff could not satisfy his obligation to First Bank. CP 064 ¶ 12. Nonetheless, it waited until January 29, 2014, days before Tuschoff's loan was set to mature on February 1, 2014, to make any attempt to even inquire about the status of the Tuschoff/Schwab Note and Deed of Trust. CP 64 ¶¶ 12-13. This demonstrates that First Bank knew it had no right to demand direct payment from Schwab until Tuschoff's obligation to the Bank matured and he ultimately defaulted.

First Bank took a *collateral* assignment of Tuschoff's beneficial interest in the Tuschoff/Schwab Deed of Trust as security

for the Montana Note. First Bank admits that this assignment was given “for collateral purposes only.” CP 410. Its own documents listed Tuschoff as the owner of the Tuschoff/Schwab Deed of Trust and Note. Since this was a collateral assignment—as distinguished from an absolute assignment—Tuschoff retained the right to receive payment on the Tuschoff/Schwab Note unless he defaulted on the Montana Note. The law on this point is clear:

An absolute assignment divests the assignor of all control and right to a cause of action against the original debtor; the assignee is entitled to control and to receive the benefits of the contract between the original debtor and the assignor. On the other hand, an assignment for security [*i.e.*, a collateral assignment] *conditions transfer of title upon the assignor's default*.

*See Uni-Com Nw., Ltd. v. Argus Pub'g Co.*, 47 Wn. App. 787, 794 (1987) (emphasis added).

First Bank's claims fail as a matter of law. There is no evidence that Tuschoff was in default when Banana Belt purchased the Property from Schwab. Indeed, First Bank has never even suggested that Tuschoff was in default at that time. In the absence of a default, First Bank had no right to direct payment of the final payoff of the Tuschoff/Schwab Note at closing. *Uni-Com Nw.*, 47 Wn. App. at 794. The final payoff belonged to Tuschoff, just like the 29

principal and interest payments that preceded it. The final payoff satisfied the debt to Tuschoff and extinguished Tuschoff's and First Bank's right to foreclose the Tuschoff/Schwab Deed of Trust.

First Bank attempts to complicate this straightforward analysis by arguing that Banana Belt was not a bona fide purchaser. *See, e.g.*, Opening Brief at 14 (“Banana Belt is not a bona fide purchaser because it and its agent had knowledge of the assigned interest.”). Banana Belt never alleged the bona fide purchaser defense, nor did the trial court grant summary judgment on that basis. First Bank's bona fide purchaser argument is inapplicable in this case. First Bank had a collateral assignment of Tuschoff's beneficial interest in the Tuschoff/Schwab Deed of Trust. First Bank's interest, if any, in the Property did not exist independently of the Tuschoff/Schwab Deed of Trust. First Bank's claim, and rights in the Tuschoff/Schwab Deed of Trust, flowed from Tuschoff's claim and rights in the Tuschoff/Schwab Deed of Trust. Accordingly, when the final payoff satisfied Schwab's debt to Tuschoff, the Tuschoff/Schwab Deed of Trust was extinguished, and so was First Bank's purported lien.

Additionally, First Bank's bona fide purchaser argument is based on the unsubstantiated claim that First American was Banana

Belt's agent, so Banana Belt is responsible for the purported "failure" to direct the payoff funds to First Bank instead of Tuschoff. However, the closing agent owes a fiduciary duty to both the seller and the purchaser. *Stryrk v. Cornerstone Inv., Inc.*, 61 Wn. App. 463, 472, 810 P.2d 1366, 1377 (1991). First Bank has cited no cases holding a purchaser vicariously liable for the actions of a closing agent in a real estate transaction. To the extent that First American or Land Title acted improperly, Banana Belt bears no liability for those improper actions.

Finally, First Bank's bona fide purchaser argument fails because it relies on the unsubstantiated premise that First Bank had a superior claim to the final payoff. First Bank had *no* claim to the final payoff, much less a superior claim. It is undisputed that Tuschoff collected each and every principal and interest payment on the Tuschoff/Schwab Note—29 payments totaling \$283,957.85—between Tuschoff's collateral assignment to First Bank and Banana Belt's purchase of the Property. CP 452-60. First Bank knew that Tuschoff was receiving these payments and never once objected. The fact that First Bank allowed Tuschoff to collect these payments is unmistakable evidence of the *conditional* nature of the assignment.

First Bank's failure to demand direct payment in May 2013 when it knew Tuschoff could not satisfy his obligation to First Bank demonstrates First Bank knew it had *no* right to payment until Tuschoff defaulted. Had First Bank believed that it owned "all right, title, and interest" in the Tuschoff/Schwab Note and Deed of Trust as it now contends, it would not have allowed Tuschoff to pocket more than a quarter of a million dollars in principal and interest payments.

The conditional nature of the assignment is further confirmed by the testimony of First Bank President Kenneth Martin. Specifically, Mr. Martin testified that First Bank allowed Tuschoff to pledge his "stream of reliable income" from the Tuschoff/Schwab Note as collateral for the Montana Note:

The purpose of [First Bank's] loan to Mr. Tuschoff and Ms. Parks was to enable them to purchase the Hotel Lincoln. . . . Mr. Tuschoff offered as security the Bowling Alley / Casino property located at 1250 Bridge Street, Clarkston, Washington[,] that he sold on contract to Gene Schwab, et al. . . . As reflected on Mr. Tuschoff's balance sheet[,] the outstanding sum due on the Schwab contract at the time of [Tuschoff] applying for the loan was \$566,486. Mr. Tuschoff also provided First Bank of Lincoln a copy of the \$1,100,000 Promissory Note that Gene Schwab et al. [had] signed in his favor together with the Deed of Trust securing the Promissory Note and encumbering the [Property]. .

Given that [First Bank] did not have financial statements reflecting the cash flows from the Lincoln Hotel, but [that] Mr. Tuschoff had a stream of reliable income secured by a recorded Deed of Trust, First Bank of Lincoln elected to take the offered assignment in the [Tuschoff/Schwab] Deed of Trust.

\* \* \*

First Bank of Lincoln always depended on Mr. Tuschoff's stream of revenue from the Schwab/Tuschoff Note secured by the Deed of Trust to make the payments on the loan First Bank of Lincoln extended to Mr. Tuschoff.

CP 61-63 (emphasis added).

This testimony makes clear that First Bank understood Tuschoff was entitled to the payments from Schwab. First Bank had a security interest in Tuschoff's right to receive payment on the Tuschoff/Schwab Note. To protect that interest, it also took a collateral assignment of the Tuschoff/Schwab Deed of Trust. But this collateral assignment did not vest First Bank with an unconditional right to receive payment on the Tuschoff/Schwab Note. To the contrary, as evidenced by Mr. Martin's testimony, all future payments—including any final payoff—belonged to Tuschoff. *Uni-Com Nw.*, 47 Wn. App. at 794. The sole purpose of the collateral assignment was to grant First Bank the same right that *Tuschoff* enjoyed as the beneficiary of the Tuschoff/Schwab Deed of Trust—

namely, the right to foreclose on the Property in the event that Schwab defaulted on the Tuschoff/Schwab Note. But that right, like the right to enforce its security interest, was contingent upon Tuschoff defaulting on the Montana Note.

The fact that Tuschoff retained all rights under the Tuschoff/Schwab Note is further confirmed by the Subordination Agreement between Tuschoff and First Bank. Tellingly, the Subordination Agreement refers to Tuschoff as the “owner” of the Tuschoff/Schwab Note and to First Bank as the “owner and holder of an assignment” of the Tuschoff/Schwab Deed of Trust. CP 449-50. This language cannot be squared with First Bank’s present claims that Tuschoff made an *absolute* assignment of both the promissory note and deed of trust, vesting it with “all right, title and interest” under both agreements. The Subordination Agreement clearly reflects that the parties intended for Tuschoff to retain ownership of the Tuschoff/Schwab Note, to grant First Bank a UCC Article 9 security interest in payments made thereon, and to conditionally assign his beneficial interest in the Tuschoff/Schwab Deed of Trust, so that First Bank could foreclose on the Property *if* Tuschoff defaulted on his

obligations to First Bank and *if* Schwab defaulted on his obligations to Tuschoff.

Against this backdrop—and without having produced a shred of evidence that Tuschoff was in default—First Bank insists that *it* was entitled to the final \$359,271.82 payoff rather than Tuschoff. However, First Bank fails to show the basis for its entitlement to the final payoff. All First Bank can say is that it recorded the collateral assignment with the Asotin County Auditor, thus giving notice to all the world of its “interest.” But the act of recording the collateral assignment did not change the character of the assignment itself. The act of recording simply put the world on notice that First Bank had a *contingent* right to foreclose on the Property. It did not magically transform First Bank into a “senior lienholder” with an interest in the Property superior to Tuschoff’s.

First Bank’s rights under the collateral assignment were contingent on Tuschoff defaulting on the Hotel Lincoln loan. Since Tuschoff had not defaulted, Tuschoff was entitled to the final payoff. That is who was paid at the closing when Banana Belt bought the Property. There is no further analysis required. The Court should affirm the award of summary judgment to Banana Belt.

**B. Payment to Tuschoff fully discharged Schwab's remaining obligation on the Tuschoff/Schwab Note.**

For the reasons noted above, First Bank's failure to establish that Tuschoff was in default is fatal to its claims. But, even assuming *arguendo* that Tuschoff had been in default on the Montana Note, First Bank's claims would still fail.

A security interest cannot exist independent of an obligation. William B. Stoebuck and John W. Weaver, 18 *Washington Practice* § 17.1 (2d ed. 2004) ("An obligation may exist without security, but not security without obligation."). The purpose of the Tuschoff/Schwab Deed of Trust was to secure "payment of the sum of One Million One Hundred Thousand and No/100 Dollars (\$1,100,000.00), with interest, in accordance with the terms of a promissory note of even date herewith payable to Beneficiary [Donald C. and Meredith<sup>3</sup> B. Tuschoff.]" CP 396. The Tuschoff/Schwab Deed of Trust was granted to secure Schwab's debt to Tuschoff; it was not granted to First Bank to secure Tuschoff's separate obligation to First Bank under the Montana Note. *See* CP 396-99. The only collateral, related to the Property, securing Tuschoff's debt to First Bank is Tuschoff's assignment of his beneficial interest in the

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<sup>3</sup> Meredith Tuschoff assigned her interest in the Tuschoff/Schwab Deed of Trust to Donald Tuschoff on February 4, 2011. CP 554.

Tuschoff/Schwab Deed of Trust. Schwab's obligation to Tuschoff was satisfied during the closing of Banana Belt's purchase of the Property. Since the obligation no longer exists, the security is extinguished.

The Tuschoff/Schwab debt was paid in full during the closing of Banana Belt's purchase of the Property. In Washington, the rules of mortgage law also apply to deeds of trust. RCW 61.24.020; *see also* CP 398 (Mutual Agreements ¶ 6) (allowing foreclosure of the deed of trust as a mortgage). First Bank recorded Tuschoff's collateral assignment of his beneficial interest in the Real Property Records in Asotin County. CP 440. However, the "recording of an assignment of a mortgage is not in itself notice to the mortgagor, his or her heirs, *assigns* or personal representatives, to invalidate a payment made by any of them to a prior holder of the mortgage." RCW 65.08.120 (emphasis added). First Bank never demanded possession of the original Tuschoff/Schwab loan documents and never demanded that Schwab's payments be sent directly to First Bank.

Land Title collected and disbursed Schwab's monthly payments on the Tuschoff/Schwab Note during the entire life of that loan—including the period between Tuschoff's January 2011 Collateral Assignment of his beneficial interest to First Bank and the June 2013 payoff of the Tuschoff/Schwab Note. CP 452-60. No

payments were ever sent to First Bank. On June 26, 2013, First American sent Land Title a check for \$359,271.82 “representing full payoff of the” Tuschoff/Schwab Note. CP 492-94. Just as it had with every other payment on the Tuschoff/Schwab Note, Land Title cashed the payoff check and disbursed the funds to Tuschoff. CP 496, 512 (35:6-22), 514-15 (37:18-38:3). About six months later, on January 29, 2014, First Bank contacted Land Title, claiming for the very first time that First Bank should have been paid directly from the payments on the Tuschoff/Schwab Note. CP 496.

Tuschoff’s obligation to pay First Bank was independent of, and has no bearing on, the fact that the Tuschoff/Schwab debt has been paid in full. *See* RCW 65.08.120. First Bank’s recording of the collateral assignment did not invalidate the final payoff payment and the outstanding balance on the Tuschoff/Schwab Note is \$0.00. *Id.*; CP 452-60. The satisfaction of Schwab’s obligation to Tuschoff immediately extinguished the Tuschoff/Schwab Deed of Trust.

First Bank relies on the inapplicable 1886 New York case, *Brewster v. Carnes*, 9 N.E. 323, 103 N.Y. 556 (N.Y. 1886), for the premise that RCW 65.08.120 does not apply because Banana Belt, rather than Schwab, paid the final payment to Tuschoff. Opening Brief at 19-20. First, this argument fails technically, because Banana Belt provided the money to Schwab for the payoff - the payment at

closing to Schwab was reduced by the amount paid to Tuschoff. Second, *Brewster* also does not apply because the New York statute it analyzed protected only the “mortgagor, his heirs or personal representatives.” *Brewster*, 9 N.E. 323, 103 N.Y. at 561 (citing 1 R.S. 763, § 41). The Washington statute, by contrast, also protects the mortgagor’s assigns. RCW 65.08.120 (“mortgagor, his or her heirs, assigns or personal representatives”). In addition, the “purchaser” in *Brewster* purchased the “equity of redemption” rather than the Property, and continued to make payments on the obligation after the purchase. *Id.* at 561-62. Here, a portion of the purchase price was directed to pay off Schwab’s obligation to Tuschoff. Accordingly, the *Brewster* case is factually and substantively inapplicable.

It is undisputed that First Bank never delivered a demand for direct payment to Schwab. CP 412-14, 528-29. As such, even if Tuschoff had been in default on the Montana Note, the payment of the remaining obligation to Tuschoff at closing fully discharged Schwab’s obligation. RCW 65.08.120. Accordingly, First Bank has no cause of action against Banana Belt. Its sole remedy is to obtain the funds from Tuschoff.

**C. First Bank's attempts to foreclose on the Property are barred by Montana law.**

Even if First Bank had established that Tuschoff was in default on the Montana Note, its claims would fail for yet another reason: it non-judicially foreclosed on the Hotel Lincoln property, triggering Montana's anti-deficiency statute. Just as the debt to Tuschoff has been satisfied and the related liens extinguished, Tuschoff's debt to First Bank is extinguished as a matter of law by First Bank's non-judicial foreclosure. Like Washington, Montana limits a creditor's ability to pursue a deficiency remaining after a non-judicial foreclosure on a deed of trust. Mont. Code Ann. § 71-1-317 (2009). The anti-deficiency statute provides:

When a trust indenture<sup>4</sup> executed in conformity with this part is foreclosed *by advertisement and sale*, other or further action, suit, or proceedings may not be taken or judgment entered for any deficiency against the grantor or the grantor's surety, guarantor, or successor in interest, if any, on the note, bond, or other obligation secured by the trust indenture or against any other person obligated on the note, bond, or other obligation.

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<sup>4</sup> A "trust indenture" is the equivalent of a deed of trust in Washington. See Mont. Code Ann. § 71-1-303(6) ("Trust indenture" means an indenture executed in conformity with this part and conveying real property to a trustee in trust to secure the performance of an obligation of the grantor or other person named in the indenture to a beneficiary.").

Mont. Code Ann. § 71-1-317 (2009) (emphasis added).

By operation of this statute, “the creditor possessing the foreclosed note and trust indenture is prohibited from seeking a deficiency judgment or *maintaining any other action for amounts still owing on the secured note.*” *First Interstate Bank of Kalispell, N.A. v. Wann*, 765 P.2d 749, 750 (Mont. 1988) (emphasis added). Unlike its Washington analogue, the Montana statute does not contain an exception for deeds of trust securing commercial loans. *Compare* RCW 61.24.100(3)(b) (exception for deeds of trusts securing commercial loans), *with* Mont. Code Ann. § 71-1-317 (containing no such exception). Also, unlike the Washington statute, the Montana statute does not contain an exception allowing successive foreclosures. *Id.*

First Bank non-judicially foreclosed on the Hotel Lincoln property on August 25, 2014. CR 66. First Bank was the only bidder at the Trustee’s sale and successfully purchased the Property. CR 66, 642-43. Throughout these proceedings, First Bank has never denied that it bid the full amount of the debt at the Trustee’s sale. CP 632 ¶ 3, 636. On October 31, 2015, Banana Belt’s counsel sent an email to First Bank’s counsel requesting the amount of First Bank’s credit bid,

and stating that it would assume First Bank bid the full debt amount unless First Bank informed him otherwise. CP 632 ¶ 3, 636. First Bank never disputed that it bid the full amount owing on the Montana Note. CP 632 ¶ 3. Accordingly, this fact is undisputed.

Since First Bank bid the full debt amount owing, there is no deficiency presently owing on the Montana Note and First Bank lacks a good-faith basis for continuing to pursue its claims against Banana Belt.

On the other hand, if First Bank did not bid the full debt amount, then it is barred from bringing “any other action” to recover the deficiency. Mont. Code Ann. § 71-1-317 (2009); *Wann*, 765 P.2d at 750. The statute’s prohibition on maintaining “any other action” extends to *this* action. Having already foreclosed on the First Bank/Tuschoff Deed of Trust, First Bank now seeks to foreclose on different property to satisfy that same debt. That is precisely the type of action that Mont. Code Ann. § 71-1-317 expressly forbids.

First Bank may argue that the anti-deficiency statute does not bar this action because the statute does not apply to commercial loans. In support of that argument, First Bank may point to an order entered in First Bank’s lawsuit against Tuschoff in Montana in which the

court ruled that Montana's anti-deficiency statute "does not apply to commercial transactions." CP 716. However, the Montana court failed to recognize that the exception to the anti-deficiency statute for commercial loans only applies in *judicial* foreclosure proceedings. *First State Bank of Forsyth v. Chunkapura*, 734 P.2d 1203, 1211 (Mont. 1987); *see also First Western Fed. Savings Bank v. Lence*, 839 P.2d 1277, 1279-80 (Mont. 1992) (summarizing cases addressing the availability of deficiency following a *judicial*, rather than non-judicial, foreclosure). Montana law is clear that when a creditor forecloses *non-judicially*, the creditor is barred from pursuing any remaining deficiency, regardless of whether the loan is residential or commercial in nature. *Chunkapura*, 734 P.2d at 1205 ("It is certain that when a *trustee* conducts a foreclosure sale, a deficiency judgment is not allowed.") (emphasis added); *id.* at 1206 ("it is clear that in cases of *trustee sales* under trust deeds ... the lender under a trustee's sale has *no right to a deficiency judgment*") (emphasis added). Accordingly, the Court should hold that Montana law bars this action and affirm the judgment of the trial court.<sup>5</sup>

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<sup>5</sup> In addition to this action and the non-judicial foreclosure of the Montana property, First Bank also sued Tuschoff, Laurie Parks, Lancer Enterprises, Inc., and Lincoln Hotel Limited seeking the same

First Bank may also argue, as it did below, that its non-judicial foreclosure of the Hotel Lincoln property must be invalidated because it failed to give proper notice of the Trustee's sale to a junior lienholder named Richard D. Porterfield Trust ("Porterfield"). Contrary to First Bank's assertions, the lack of notice to Porterfield does not invalidate the foreclosure sale. Instead, the lack of notice renders the sale null and void *only* as to Porterfield. *Terry L. Bell Generations Trust v. Flathead Bank of Bigfork*, 302 P.3d 390, 394 (Mont. 2013). As a result, the Trustee is now required to conduct a second sale at which Porterfield will have the opportunity to purchase the Property. *Id.* ("When the notice requirements are not followed, the only recourse is a second trustee's sale where each interest holder who did not previously receive notice receives appropriate notice and has an opportunity to purchase the subject property.").

**D. The Court should award Banana Belt reasonable attorney's fees and costs incurred in defending against First Bank's frivolous appeal.**

Banana Belt moves for an award of attorney's fees and costs pursuant to RCW 4.84.185. That statute allows an appellate court to

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amount it seeks to collect here through the foreclosure on the property. CP 645-51. On June 11, 2014 First Bank obtained a pre-judgment attachment, for the amount it seeks in this case, on the bank

order a non-prevailing party to pay attorney's fees and costs incurred by the prevailing party in responding to claims that were "frivolous and advanced without reasonable cause." RCW 4.84.185. First Bank's claims easily meet that standard. First Bank is attempting to "foreclose" on a debt it never owned and that has been fully satisfied. It has also chosen to completely ignore the most obvious issue presented: whether it had a lawful claim to the final payoff given that Tuschoff was not in default. Since First Bank has not even *attempted* to address this issue, the Court should award Banana Belt its attorney's fees and costs.

## VI. CONCLUSION

First Bank took a *collateral* assignment of the Tuschoff/Schwab Deed of Trust. Its rights under this assignment were contingent upon Tuschoff defaulting on the Montana Note. There is no evidence that Tuschoff was in default when Banana Belt purchased the Property. Accordingly, First Bank's claims fail as a matter of law. Tuschoff, having not defaulted on the Montana Note, was entitled to the final payoff of the Tuschoff/Schwab Note at closing just as he was entitled to the 29 principal and interest

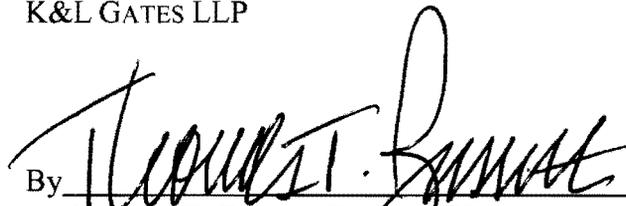
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accounts of those defendants. CP 653-54.

payments which preceded it. Tuschoff properly received the final payment. First Bank had no claim to the funds and therefore could not have had a "lien" on the Property. The Court should affirm the award of summary judgment to Banana Belt. The Court should also award Banana Belt its reasonable attorney's fees and costs on appeal.

RESPECTFULLY SUBMITTED this 19th day of June, 2015.

K&L GATES LLP

By 

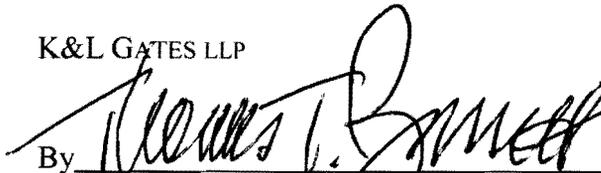
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**CERTIFICATE OF SERVICE**

I certify that on June 19, 2015, I caused to be served the foregoing RESPONDENT BANANA BELT GAMING, LLC'S BRIEF on the following and in the manner described below:

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ERIKA BALAZS ATTORNEY AT LAW 3206 WEST CONNAUGHT DRIVE SPOKANE, WA 99208 <i>Attorney for Appellant</i>	<input checked="" type="checkbox"/> U.S. Mail, Postage Prepaid <input type="checkbox"/> Federal Express Overnight <input type="checkbox"/> UPS 2 Day Shipping <input type="checkbox"/> E-mail per Agreement <input type="checkbox"/> Courier (hand delivery)
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