70004-9

70004-9

No. 70004-9-I

DIVISION I, COURT OF APPEALS
OF THE STATE OF WASHINGTON

WASHINGTON FEDERAL, a federally chartered savings association,

Plaintiff-Appellant,

v.

KENDALL D. GENTRY and NANCY GENTRY, individually and the marital community comprised of thereof,

Defendants-Respondents.

ON APPEAL FROM SKAGIT COUNTY SUPERIOR COURT
(Hon. Dave Needy)

REPLY BRIEF

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I. INTRODUCTION

The Gentrys' construction of RCW 61.24.100 and the deeds of trust is flawed for the same basic reason. The Gentrys read a single word or provision in isolation, and give it a strained meaning that conflicts with the language and context of the statute or contracts as a whole. The Gentrys don't even bother arguing that their interpretation is what the legislature or parties actually intended; they can't. There is no legislative history, secondary authority or extrinsic evidence to support their theory. Rather, the Guaranties clearly manifest the parties' intent that the Gentrys unconditionally satisfy any deficiency that remains after the non-judicial foreclosure of their companies' property, and RCW 61.24.100(3)(c) clearly manifests the legislature's intent to permit Washington Federal to obtain a deficiency judgment if the Gentrys refuse to do so.

This Court must reject the Gentrys' myopic reading of RCW 61.24.100(10) and "Related Documents" term, and construe the entirety of the statute and parties' agreements according to their plain meaning and commercial reasonableness. RCW 61.24.100 permits a lender to obtain an unlimited deficiency judgment against a guarantor unless the guarantor grants a deed of trust on his own property—which the Gentrys did not do. The deeds of trust did not secure the Gentrys' Guaranties in any event; any

doubt on that issue was laid to rest by the modified deed of trust, which not only omits the "Related Documents" term, but confirms that the deeds secured only the obligations of a borrower and grantor—not a guarantor. Finally, if the Gentrys had any anti-deficiency rights, they waived them; enforcing a sophisticated guarantor's knowing waiver of any such right in the context of a commercial loan does not offend the public good.

II. ARGUMENT

A. The Deed Of Trust Act Permits Washington Federal To Obtain A Deficiency Judgment Against The Gentrys; RCW 61.24.100(10) Has Nothing To Do With Deficiency Judgments.

The Gentrys go out of their way to avoid any reference to RCW 61.24.100(3)(c), but do not dispute that section (3)(c) allows a lender to obtain an unlimited deficiency judgment against a guarantor of a commercial loan, subject only to a "fair value" defense. Resp. Br. at 8; RCW 61.24.100(3)(c) & (5). That right is curtailed where the guarantor grants a deed of trust on his own property, in which case section (6) limits the deficiency judgment to waste and wrongful retention of rents. RCW 61.24.100(6). In this way, section (6) mirrors section (3)(a)(i), which likewise limits a deficiency judgment against a "borrower or grantor" to waste and wrongful retention of rents when the guarantor is, in effect, a grantor. RCW 61.24.100(3)(a)(i). Neither of these limitations apply to the Gentrys, however; they concede they were not the borrowers or the

grantors of the deeds of trust. On its face, then, section (3)(c) allows Washington Federal to obtain an unlimited deficiency judgment.

Into this perfectly symmetrical scheme, the Gentrys try to inject RCW 61.24.100(10). Worse yet, the Gentrys would interpret section (10) to give them an absolute anti-deficiency defense the Deed of Trust Act affords no other category of obligor. Even the Gentrys would concede that an unsecured guarantor is liable for an unlimited deficiency judgment. RCW 61.24.100(3)(c). Similarly, there is no dispute that a borrower, grantor or guarantor who grants a deed of trust on his own property is also subject to deficiency judgment, albeit one limited to waste and wrongful retention of rents. RCW 61.24.100(3)(a)(i) & (6). Yet, under the Gentrys' implausible interpretation of section (10), a commercial guarantor who doesn't encumber his own property with a deed of trust, but whose guaranty is deemed secured by the borrower's or grantor's deed of trust, would be totally immune from a deficiency judgment.

Why would the legislature treat that kind of guarantor differently than an unsecured guarantor? In both cases, the guarantor has not encumbered his own property to secure the debt or his guaranty; unlike a borrower-grantor or a guarantor-grantor, he's contributed nothing toward the "quid pro quo" inherent in a non-judicial foreclosure. *Donovick v. Seattle-First Nat'l Bank*, 111 Wn.2d 413, 416, 757 P.2d 1378 (1988).

Even more inexplicably, why would the legislature give that guarantor immunity from a deficiency judgment when the borrower and grantor are still on the line for a limited deficiency judgment? It simply makes no sense. In passing, the Gentrys cite RCW 61.24.100(6) to suggest that a deficiency judgment would still be available for waste and rents in that situation (Resp. Br. at 19), but on its face, RCW 61.24.100(6) applies only where the guarantor is the "grantor" of the foreclosed deed of trust.[1]

The Gentrys don't suggest that the legislature actually intended the absurd result they seek and, unlike Washington Federal, which supported its interpretation with both legislative history and secondary materials (*see* Opening Br. at 18-19, 21-23), the Gentrys find no authority for their interpretation. All they can do is point to the dictionary, and argue that the words "enforce any obligation" used in RCW 61.24.100(10) could encompass an action for a deficiency judgment. But a dictionary

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[1] It is entirely unclear how the Gentrys construe section (10). First they say it would "extinguish" a lender's right to a deficiency judgment if the guaranty is secured by the foreclosed deed of trust. Resp. Br. at 15. But then they say that a deficiency judgment would still be available for waste. *Id.* at 19. The trial court adopted the latter position, citing not RCW 61.24.100(10), but RCW 61.24.100(3)(c). CP 766. As Washington Federal explained, the trial court's interpretation is contradicted by the express terms of RCW 6.24.100(3)(a), (3)(c) and (6), which limit a lender's right to obtain a deficiency judgment to waste against a guarantor only where a "guarantor grant[s] a deed of trust to secure its guaranty." Opening Br. at 14-16 (citing RCW 61.24.100(6)). The Gentrys cannot seriously argue that section (6) applies here; they were not grantors.

definition does not control where, as here, the statute as a whole demonstrates a different legislative intent. *Am. Legion Post No. 32 v. City of Walla Walla*, 116 Wn.2d 1, 8, 802 P.2d 784 (1991). As Washington Federal explained, the legislature was careful to use the specific term "deficiency judgment" in the sections of the statue that address a lender's right to such a judgment following non-judicial foreclosure, and it chose not to use that term in section (10). *See* RCW 61.24.100(1), (3)(a), (3)(c), (5) & (6). Section (10) must, therefore, refer to something else.[2]

It is the Gentrys who ignore the plain meaning of section (10); that is, foreclosure does not preclude a lender from enforcing an "obligation" that is separate or carved-out from the commercial loan at issue. Opening Br. at 18-19. They argue that this interpretation creates contradictory meanings, such that "guarantors could still be pursued for deficiency judgments, but borrowers could not." Resp. Br. at 2, 17. But section (10) has nothing to do with deficiency judgments, nor does it mean different things for "borrowers" and "guarantors." Both can owe obligations that are separate from the commercial loan, such as environmental indemnity

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[2] Notably, RCW 61.24.100(4) creates a one year statute of limitations on "any action referred to in subsection (3)(a) and (c) of this section"—*i.e.*, "an action for a deficiency judgment." If RCW 61.24.100(10) also encompassed actions for a deficiency judgment, as the Gentrys claim, then why doesn't RCW 61.24.100(4) also refer to section (10)? The Gentrys don't say. The reason, of course, is that section (10) has nothing to do with actions for deficiency judgments.

agreements and, as noted below, completion and performance guaranties. Section (10) confirms that foreclosure of a deed of trust securing a commercial loan does not prevent a lender from enforcing these unrelated or otherwise separate obligations. Indeed, the Gentrys fail to explain where in RCW 61.24.100 this right is preserved—if not section (10).

The Gentrys also ignore the conflict their interpretation creates between sections (3)(a)(i) and (6), on the one hand, and section (10), on the other. As noted, and the Gentrys do not dispute, sections (3)(a)(i) and (6) permit a lender to obtain a limited deficiency judgment against a borrower or a guarantor who grants a deed of trust on his own property. RCW 61.24.100(3)(a)(i) & (6). If section (10)'s reference to an action to "enforce any obligation" truly meant the same thing as an action "for a deficiency judgment," then read literally, section (10) would bar any kind of deficiency judgment against a "borrower or guarantor"—even those deficiency judgments permitted by sections (3)(a)(i) and (6). After all, unlike the general anti-deficiency rule in RCW 61.24.100(1), which contains an express exception for deficiency judgments on commercial loans as set forth in sections (3) and (6), RCW 61.24.100(10) is absolute in its terms; it provides for no exceptions. Under the Gentrys' interpretation, section (10) would prohibit exactly what sections (3)(a) and (6) permit.

This Court should reject the Gentrys' flawed interpretation, and give RCW 61.24.100 its common sense meaning: section (3)(c) allows a lender to obtain an unlimited deficiency judgment against a guarantor of a commercial loan, except when the guarantor is a "grantor" of the deed of trust, in which case section (6) limits the scope of the deficiency judgment to waste and wrongful retention of rents. Section (3)(c) applies here; section (6) does not. Section (10) has nothing to do with a "deficiency judgment." This Court should not stretch the statute's plain meaning to reach a result that even the Gentrys concede would frustrate the Deed of Trust Act's goal of promoting "efficient and cost-effective" non-judicial foreclosures. *Cox v. Helenius*, 103 Wn.2d 383, 387, 693 P.2d 683 (1985). The Act manifests the legislature's clear intent that guarantors like the Gentrys—who are not party to and contribute nothing toward the quid pro quo represented by the deed of trust—have no anti-deficiency protection, other than a "fair value" defense. This Court should uphold that intent.

B. The Original Deeds Of Trust Did Not Secure The Gentrys' Guaranties; The Deeds Secured Only The Notes And "Related Documents" Of The Borrowers And Grantors.

The Gentrys concede that their construction of the original deeds of trust, like the trial court's, is based entirely on the boilerplate definition of the term "Related Documents." The argument goes like this: because the deeds of trust say they were intended to secure the "Indebtedness," and

term "Indebtedness" is defined to include the term "Related Documents," and the term "Related Documents" is, in turn, defined to include the word "guaranties," then—the Gentrys argue—the deeds of trust secured their Guaranties. Resp. Br. at 5-6, 9-13. The Gentrys do not argue that this was what the parties actually intended, or even that this was their belief at the time. It wasn't. Fortunately, the plain language of the agreements, as well as their context, reflect the parties' actual intent. The deeds of trust—to which the Gentrys were not even a party—were intended to secure only the borrowers' and grantors' obligations under the loans, not the Gentrys' independent obligations under the Guaranties. The modification of the Little Mountain Deed of Trust, discussed below, confirms that intent.

The Gentrys give lip service to the context rule (Resp. Br. at 9-10), but then ignore all other language in the deeds of trust, the other loan documents, the circumstances giving rise to the deeds and Guaranties and, notably, any concept of commercial reasonableness. The context rule, however, requires consideration of all these things. *Berg v. Hudesman*, 15 Wn.2d 657, 667-669, 801 P.2d 222 (1990); *Wilson Court Ltd. P'ship v. Tony Maroni's, Inc.*, 134 Wn.2d 692, 705, 952 P.2d 590 (1998) ("[w]here two commercial entities sign a commercial agreement, [courts] will give such an agreement a commercially reasonable construction"). Washington Federal showed that, when the language of the deeds of trust is construed

in its entirety, and the term "Related Documents" is read in context with the "Payment and Performance" and other provisions, it is clear that the parties intended the deeds to secure only the obligations of the "Borrower and Grantor"—not a "Guarantor" like the Gentrys. Opening Br. 25-28.

That intent is further shown by the Guaranties, which—unlike the borrowers' promissory notes—do not identify the deeds of trust as security. *Id.* at 29; *compare* CP 93 (note) with CP 118-123 (guaranty). It is implausible to believe the Gentrys would agree to personally guarantee millions of dollars of debt, relying exclusively on a generic definition in a deed of trust, to which they were not even party, to identify the purported collateral for the guaranty—while omitting any reference to the collateral in the Guaranties themselves. Indeed, the Guaranties say just the opposite: the Guaranties unambiguously manifest the Gentrys' intent to "absolutely and unconditionally" guarantee the borrowers' indebtedness without limit. CP 118. The Gentrys fail to point to any other provision in the deeds of trust, the Guaranties, the notes or extrinsic evidence to support their sequestered interpretation of "Related Documents." There is nothing.[3]

[3] The Gentrys cite to the parol evidence rule in a transparent effort to pass off their inability to present any evidence—even a self-serving declaration from the Gentrys themselves—to show the parties actually intended the deeds of trust to secure the Guaranties. Resp. Br. at 9-10. In any event, the Gentrys do not and cannot argue that the parol evidence rule bars the Court from considering the parties' related and contemporaneous

Instead, the Gentrys argue the generic word "guaranties" in the definition of "Related Documents" must mean their Guaranties, because a "borrower cannot be [his] own surety." Resp. Br. at 12. But even putting aside the fact that the Gentrys' Guaranties are separately defined as "Guaranty," and that word is not included in the definition of "Related Documents," *see* Opening Br. at 27-28 & n. 4, the word "guaranties" can encompass far more than a third-party guaranty of the borrower's debt; it includes guaranties commonly given in connection with commercial loans, such as completion guaranties, validity guaranties and performance guaranties. *See Turnberry Residential Ltd. Part., L.P. v. Wilmington Trust FSB*, 99 A.D.3d 176, 950 N.Y.S.2d 362 (2012) (completion guaranty); *In re Charlotte Commercial Group, Inc.*, 2002 WL 31770866 (Bankr. M.D.N.C. Dec. 9, 2002) (validity guaranty); *In re Kaiser Group Intern. Inc.*, 399 F.3d 558 (3d Cir. 2005) (performance guaranty). In short, there is nothing about the word "guaranties" that is exclusive to the Gentrys' Guaranties or that changes the meaning of the deeds of trust as a whole.

The Gentrys' construction also flies in the face of commercial reasonableness. It simply would make no sense for the parties to agree to have the deeds of trust secure the borrower's loan and a guaranty of that

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loan documents to ascertain the meaning of the deeds of trust, whether or not they were "integrated" or ambiguous. *See Berg*, 15 Wn.2d at 667-669.

loan. As Washington Federal explained, no party—not the lender, not the borrower or grantor, not the guarantor—receives a benefit from doing so. Opening Br. at 29-30. The Gentrys do not argue otherwise. Ironically, if the Gentrys' interpretation of RCW 61.24.100(10) is correct, their construction of the deeds of trust becomes even more untenable. Why would a sophisticated commercial lender insist on having a deed of trust secure a guaranty of the borrower's debt when doing so would render the guaranty meaningless in the very situation it was intended to apply most, *i.e.*, where a deficiency remained after a non-judicial foreclosure of the deed of trust? Here too, the Gentrys don't say. This Court should reject the Gentrys' strained construction of the "Related Documents" term to avoid an absurd result the parties plainly did not intend.[4]

Wilson Court, *supra*, is instructive. There, the landlord agreed to enter into a commercial lease with a corporate tenant, Tony Maroni's. As an inducement, Tony Maroni's president, Riviera, executed a commercial

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[4] This Court can reject the Gentrys' suggestion that, if the deeds of trust are ambiguous, they must be construed against Washington Federal as the "drafter." Resp. Br. at 12. Washington Federal was not the "drafter" of the deeds of trust (Horizon Bank was) and the Gentrys were not a party to the deeds of trust (their various limited liability companies were) and, thus, the Gentrys cannot invoke the rule against Washington Federal. In any event, the rule applies only if an ambiguity remains after the court construes the contract in light of its circumstances, objective and reasonableness of the parties' interpretations. *See Roberts, Jackson & Assoc. v. Pier 66 Corp.*, 41 Wn. App. 64, 69, 702 P.2d 137 (1985). Here, proper construction of the deeds of trust reveals no ambiguity.

guaranty. When he signed the guaranty, however, Riviera wrote the word "president" after his name. The issue was whether the parties intended Riviera to sign the guaranty as a corporate officer, or in a personal capacity. 134 Wn.2d at 696-98. In rejecting Riviera's argument that the parties did not intend personal liability, the Supreme Court recognized:

> As an inducement to the execution of the Lease, the Guaranty should be reasonably interpreted in such a way as to give it effect. Riviera's asserted position renders the entire Guaranty meaningless, hardly an inducement to anything, and is contrary to established rules of contract construction.

Id. at 706-07. The Court found that "it would make no sense for Tony Maroni's to guarantee obligations it had already promised to undertake in the Lease," especially given the "commercial sophistication of the parties" and "the circumstances under which the Guaranty was entered into." *Id.* at 709-10. This Court should likewise refuse to give the deeds of trust an unreasonable construction that makes no sense and that would, if Gentrys are right about RCW 61.24.100(10), render the Guaranties meaningless following a non-judicial foreclosure of the deeds of trust.

C. The Little Mountain Deed Of Trust Was Modified So That It No Longer Secured "Related Documents;" Even Under The Gentrys' Theory, Washington Federal Is Entitled To A Deficiency Judgment On Two Of The Guaranties.

The Gentrys omit any reference to the modification of the Little Mountain Deed of Trust in their Statement of Facts, and give the issue

short-shrift in their argument—for good reason. They do not dispute that the modified Little Mountain Deed of Trust was the only deed of trust securing the Blackburn Southeast and Gentry Family loans. CP 178-197. Thus, even if the Gentrys' interpretation of RCW 61.24.100(10) is correct (it's not) and the original deeds of trust secured the Guaranties by virtue of the "Related Documents" term (they don't), the Gentrys are still liable for a deficiency judgment for those two loans unless the modified Little Mountain Deed of Trust also secured the Guaranties. It didn't. As Washington Federal explained, as modified, the Little Mountain Deed of Trust omits any reference to the "Related Documents" as among those debts and obligations secured by the deed. *See* Opening Br. at 30-32.

The Gentrys argue that because the modified Little Mountain Deed of Trust did not re-define the term "Related Documents" to exclude the "guaranties" generally or their Guaranties specifically, it continued to secure the Guaranties to the same extent as the original deeds of trust. Resp. Br. at 13-14. The Gentrys deliberately miss the point. "Related Documents" is simply one of many defined terms in the deed of trust; it does not have any independent function. CP 185. As the Gentrys' own argument shows, the term is relevant only because it is incorporated into the section of the original deed of trust that describes the scope of the secured indebtedness. CP 179. What matters, then, is not whether the

modified deed of trust changed the definition of "Related Documents," but whether it changed the section describing what the deed secured. It did.

The original deed of trust provided that it secured "payment of the Indebtedness and ... performance of any and all obligations under the Note, the Related Documents, and the Deed of Trust." CP 179 (emphasis added). The Modified Little Mountain Deed of Trust provided, instead, that it secured "the Note, this Deed of Trust ... [and] all obligations, debts and liabilities ... of either Grantor or Borrower." CP 192. In the clearest of terms, the modification no longer incorporated "Related Documents" in its description of the secured indebtedness, and clarified the parties' intent to secure only the debts of the "Grantor or Borrower"—not a Guarantor. *Id.* Thus, even if this Court accepts the Gentrys' construction of the Deed of Trust Act and "Related Documents" term, the Modified Little Mountain Deed of Trust did not secure the Guaranties of the Blackburn Southeast and Gentry Family loans. At the very minimum, Washington Federal is entitled to a deficiency judgment on those two Guaranties.

D. The Gentrys' Waiver Is Enforceable.

The Gentrys fail to offer even one reason why a commercial guarantor's knowing waiver of anti-deficiency defenses is "against the public good" or "injurious to the public"—which is the standard they must satisfy. *Scott v. Cingular Wireless*, 160 Wn.2d 843, 851, 161 P.3d 1000

(2007). Indeed, the Deed of Trust Act clearly reflects the legislature's intent to allow deficiency judgments against commercial guarantors. RCW 61.24.100(3)(c). There is no dispute that, under section (3)(c), a lender has a right to an unlimited deficiency judgment against an unsecured guarantor, subject only to a "fair value" defense. Even if the Gentrys' implausible interpretation of RCW 61.24.100(10) is accepted, and that right is curtailed where the guaranty is secured by the borrower's deed of trust, what possible "public good" is injured by allowing the parties to agree to give the lender the same rights it otherwise would have against an unsecured guarantor under section (3)(c)? None, of course.

Rather, the Gentrys argue, without authority, that the Deed of Trust Act is "consumer protection legislation ... that cannot be waived by contract." Resp. Br. at 22-23. The Deed of Trust Act is not consumer protection legislation; it creates a process for non-judicial foreclosure that benefits both lenders and borrowers. The "quid pro quo" works both ways. *Donovick*, 111 Wn.2d at 416. Notably, the Act expressly identifies those acts—such as collusive bidding—that *per se* violate the Consumer Protection Act. RCW 61.24.135. That statute says that it is not an unfair or deceptive act for the "beneficiary ... to reach any good faith agreement with the borrower, grantor, any guarantor, or any junior lienholder." *Id.* The Gentrys' promise to unconditionally guarantee the loans and to waive

anti-deficiency defenses, if any, is such a "good faith agreement." To be sure, the Gentrys never claimed they did not read, understand and voluntarily agree to the Guaranties' express waiver clause. They did.

Nor is there any merit to the Gentrys' predictable and misplaced reliance on *Schroeder v. Excelsior Mgmt. Group LLC*, --- Wn.2d ---, 297 P.3d 677 (Feb. 28, 2013). That case has nothing to do with the Deed of Trust Act's anti-deficiency provisions and, more to the point, does not hold that a borrower or guarantor "cannot waive the protections of the Deed of Trust Act." Resp. Br. at 22, 23. On the contrary, the Supreme Court expressly recognized that "[m]ost rights can be waived by ... contract," and specifically noted that its opinion should not be construed to preclude parties from agreeing to modify or waive "rights and privileges" created by the Act, as opposed to "mandated requisites" and "procedures" to a trustee's sale. 297 P.3d at 683 & n.7. The Court's earlier decision in *Bain v. Metro. Mortg. Group, Inc.*, 175 Wn.2d 83, 285 P.3d 34 (2012), says the same thing. *Id.* at 108 ("We find no indication the legislature intended to allow the parties to vary *these procedures* by contract.").

A guarantor's anti-deficiency defenses are precisely the kind of "rights and privileges" that can be waived. As Washington Federal explained, unlike procedural requisites to a trustee's sale (notice of sale, opportunity to cure, etc.), which are statutory limits on trustee's power to

conduct a sale without judicial supervision, the Deed of Trust Act's anti-deficiency rights arise only after a sale, and they affect no one but the parties to the loan and/or guaranty. *See* Opening Br. at 36-37. In short, to the extent the Act gives a guarantor an anti-deficiency defense, it is a right unrelated to the trustee's power to sell the property. The Gentrys do not dispute that, at common law, no principle of public policy prevented a guarantor from contractually waiving similar defenses. *See* Opening Br. at 33. The same is true here. Even if there were public policy reasons to limit a borrower's ability to waive that right in the context of a residential loan, those concerns do not exist in the case of a commercial loan—especially for a guarantor, who is not even party to the deed of trust.

By the same token, there is no merit to the Gentrys' slippery-slope argument that enforcing their Guaranties would "eliminate the protective nature of the statute." Resp. Br. at 23. This Court need only decide the validity of a guarantor's waiver of anti-deficiency rights in the context of a commercial loan; nothing more. A waiver executed by a sophisticated commercial guarantor—to induce a lender to loan millions of dollars to the guarantor's companies—implicates none of the concerns that arise from a borrower's waiver of anti-deficiency rights in the context of a residential loan. To be sure, enforcing a commercial guarantor's waiver does nothing to upset the Deed of Trust Act's "quid pro quo between

lenders and borrowers." *Donovick*, 111 Wn.2d at 416. The borrower still receives all the anti-deficiency protections of the Act, and the lender and guarantor get what they mutually bargained for. That is exactly what the legislature intended when it enacted RCW 61.24.100(3)(c).

III. CONCLUSION

The trial court's construction of the Deed of Trust and Deed of Trust Act were erroneous as a matter of law, as was its refusal to enforce the Gentrys' waiver. This Court should reverse, hold the Gentrys to the unambiguous terms of their absolute Guaranties, and remand the case for further proceedings on their "fair value" defense.

RESPECTFULLY SUBMITTED this 20th day of June, 2013.

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CERTIFICATE OF SERVICE

I, Kathryn Savaria, hereby certify under penalty of perjury of the laws of the State of Washington that on June 20, 2013, I caused to be served a copy of the attached document to the following person(s) in the manner indicated below at the following address(es):

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