

No. 68978-9-I

DIVISION I, COURT OF APPEALS
OF THE STATE OF WASHINGTON

WASHINGTON FEDERAL SAVINGS AND LOAN ASSOCIATION,
a federal association,

Plaintiff-Appellant

v.

THE McNAUGHTON GROUP, a Washington limited liability company,
and SILVER LAKE WATER AND SEWER DISTRICT,

Defendants-Respondents

ON APPEAL FROM SNOHOMISH COUNTY SUPERIOR COURT
(Hon. Linda C. Krese)

REPLY BRIEF OF APPELLANT

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I. INTRODUCTION

TMG does not dispute that it borrowed over \$11 million from Horizon Bank secured by a deed of trust. TMG does not dispute that the deed of trust covered not only the Sommerwood Property, but also all existing or future improvements and fixtures constructed on the property, and all profits, rights and proceeds arising therefrom. TMG does not dispute that it used a portion of that loan to construct a \$3 million sewer facility on the Sommerwood Property. TMG does not dispute that it transferred the sewer facility to the District without Horizon Bank's consent and, in exchange, received a right to receive latecomers payments to reimburse the millions of dollars—taken from Horizon Bank's loan—that it cost to construct the facility. TMG does not dispute that after Horizon Bank foreclosed on the deed of trust, leaving a \$6 million deficiency on the loan, TMG refused to recognize Horizon Bank's interest in the latecomers payments and sought to keep those funds for itself.

TMG's effort to shield the payments from foreclosure was not only unjust, it was contrary to law. TMG asks this Court to ignore the plain language of the deed of trust in favor of an unexpressed intent that does not exist and, failing that, to equally ignore clear application of the UCC, the common law of fixtures and the Deed of Trust Act. For its part, the District asks this Court to adopt a novel and unnecessary public policy

exception to the black letter rule that, absent a lender's consent, property transferred to a public entity remains subject to an existing mortgage or security interest. This Court should refuse to do either. For the reasons stated in the opening brief and below, the trial court's judgment must be reversed and judgment entered in Washington Federal's favor.

II. ARGUMENT

A. **TMG Does Not Dispute That The Latecomers Payments Are "Rents And Profits" Of The Sommerwood Property.**

To the extent the latecomers payments are considered personal property, Horizon Bank had a valid security interest in that "collateral" under the UCC. *See* Section II.B. But the latecomers payments are also considered real property under Washington law. As Washington Federal explained, "[u]ntil paid, the rents and profits of real property constitute real property" subject to a deed of trust, which are "part of the bundle of rights passed to the new owner upon foreclosure." RCW 7.27.230(2); *Kezner v. Landover Corp.*, 87 Wn. App. 458, 464-65, 942 P.2d 1003 (1997). When Horizon Bank foreclosed on the Sommerwood Property, it not only acquired the real property, but also all future "rents and profits" thereof, including the latecomers payments. *See* Op. Br. at 30-31.

TMG apparently agrees, or at least has no argument or authority to the contrary; TMG does not address this issue in its brief, never once cites

RCW 7.28.230 or *Kezner*, and does not dispute that “profits” include any “benefit, advantage, or pecuniary gain accruing to the owner ... of land from its actual use.” *Id.* That term encompasses the latecomers payments. The payments are clearly a “benefit ... or pecuniary gain” that accrued to TMG by virtue of its ownership and use of the Sommerwood Property as a site for the Sewer Facilities; as TMG concedes, and the District confirms, only “owners” who agree to build sewer facilities on their land qualify for latecomers payments. *See* RCW 57.22.010 & .020. TMG used its land for precisely that purpose, and the latecomers payments are a “profit” of that use. The judgment below must be reversed for this reason alone.

B. The Deed Of Trust Gave Horizon Bank A Security Interest In The Latecomers Payments Under Article 9 Of The UCC.

1. The Parties’ Intent Must Be Derived From The Plain And Unambiguous Language Of The Deed Of Trust.

As it relates to the latecomers payments’ status as collateral under the UCC, the threshold issue is whether the Sewer Facilities were “improvements” or “fixtures,” both of which are categories of collateral identified in the Deed of Trust. CP 1269. As explained below, TMG effectively concedes that the facilities are “improvements” or “fixtures” under the common law definition and ordinary meaning of those terms. Instead, TMG tries to avoid the issue entirely, making the startling argument that “[w]hether an asset is included as collateral does not depend

on the categories that the parties specified in the security agreement,” but rather depends on the parties’ unexpressed intent. TMG Br. at 16-17. The law is, however, exactly the opposite. And, even if unexpressed intent mattered, there is no evidence that Horizon Bank intended to exclude the Sewer Facilities or latecomers payments from the Deed of Trust. It didn’t.

TMG agrees that security agreements are subject to the same rules of construction as ordinary contracts. *Parker Roofing Co. v. Pac. First Fed. Sav. Bank*, 59 Wn. App. 151, 155, 796 P.2d 732 (1990). Washington courts ascertain the parties’ intent “by focusing on the objective manifestations of the agreement, rather than on the unexpressed subjective intent of the parties.” *Hearst Commc’ns, Inc. v. Seattle Times Co.*, 154 Wn.2d 493, 503, 115 P.3d 262 (2005). Words used in a contract are given their ordinary, usual, and popular meaning unless the agreement clearly demonstrates a contrary intent. *Id.* Further, while Washington courts can examine extrinsic evidence where context may give meaning to the words used in an agreement, they cannot consider a party’s subjective intent or evidence that would vary, contradict or modify the written word. *Hollis v. Garwall, Inc.*, 137 Wn.2d 683, 695, 974 P.2d 836 (1999).

There simply is no evidence to suggest that the parties intended the terms “improvements” and “fixtures”—or the “all other rights ... relating to” language discussed below—to have anything other than their ordinary

and usual meaning. Testimony that the parties did not discuss the Sewer Facilities or latecomers payments when they executed the Deed of Trust—which is all the testimony shows—is not evidence that the parties had an objective intent to remove those assets from the scope of the Deed of Trust. CP 622-23 (Hall Depo at 21-22). Horizon Bank knew nothing about the Sewer Facilities at the time. CP 529 (*id.* at 36). It would be incredible to infer that Horizon Bank intended to exclude collateral—contrary to the plain terms of the Deed of Trust—that it did not even know existed. This is especially true where, as here, it is undisputed that the Deed of Trust expressly covered “all existing *or subsequently erected or affixed ... improvements and fixtures[.]*” CP 1274; CP 532 (*id.* at 39).

Washington courts have rejected the same argument TMG makes here. In *Parker Roofing*, the issue was whether an after-acquired property clause in a security agreement should be construed to cover a future cause of action. Like here, the debtor argued that the parties did not intend the security agreement to cover the cause of action because it “was not yet contemplated” and “did not exist at the time of the security agreement.” 59 Wn. App. at 154-155, 157. Like here, the debtor cited *In re Barton*, 37 B.R. 545 (E.D.Wash. 1984), for the proposition that evidence of purported intent could trump the language of the agreement. *Id.* at 159. Noting that *Barton* was correct only “so far as it goes,” the court held that intent must

be derived first and foremost “from the language of the agreement” and that the “wording of the agreement here manifests an intent to cover future causes of action.” *Id.*¹ The same reasoning applies with equal force here.

2. The UCC Does Not Require The Latecomers Payments To Be Specifically Identified In The Deed Of Trust.

Apparently recognizing that this Court cannot ignore the language of the Deed of Trust, TMG next asks the Court to demand a level of specificity not required by the UCC. TMG argues that the latecomers payments are not collateral because the Deed of Trust does not expressly refer to “reimbursement rights,” “development-related rights” or “general intangibles.” TMG Br. at 22-24. But, as Washington Federal pointed out, the UCC has long-since abandoned the notion that a security agreement must specifically identify collateral; “a description of ... property is sufficient, whether or not it is specific, if it reasonably identifies what is described.” RCW 62A.9A-108(a) & cmt. 2 (Article 9 “rejects any requirement that a description is insufficient unless it is exact and

¹ In any event, *Barton* did not hold that intent could only be determined from affidavits. Rather, the court examined the security agreement and inferred that the parties did not intend to include crop subsidies because the agreement included a list of farm-related property items, but conspicuously excluded “crops.” *Barton*, 37 B.R. at 545-48. The court recognized that “the factual conclusions assumed by the Court ... may have been unwarranted,” and invited the parties to file affidavits regarding their intent. *Id.* at 548. Context evidence was appropriate in *Barton* because, unlike *Parker Roofing* or here, the collateral at issue was not covered by the unambiguous language of the security agreement.

detailed”). Thus, while parties may describe collateral by specific listing, type or category, they may also use “any other method, if the identity of the collateral is objectively determinable.” RCW 62A.9A-108(b).

In any event, in focusing on whether the Deed of Trust identified the latecomers payments, TMG avoids the threshold issue of whether it identified the Sewer Facilities—because, if it did, Horizon Bank’s security interest *automatically* attached to all “proceeds” of the facilities. RCW 62A.9A-315(a)(2); RCW 62A.9A-203(f) (“a security interest in collateral gives the secured party the rights to proceeds”). The Deed of Trust did “reasonably identify” the Sewer Facilities and, indeed, did so by specific “category”—“improvements and fixtures”—as the UCC permits. RCW 62A.9A-108(b). Just as the Supreme Court held in *Rainier Nat’l Bank v. Bachman*, 111 Wn.2d 298, 757 P.3d 979 (1988), because the latecomers payments are “proceeds,” they do not need to be separately identified in the Deed of Trust as “general intangibles” or otherwise. *Id.* at 307-08. TMG has no answer to *Rainier* and, like much else, simply ignores it.

TMG’s reliance on *Stockton, Whatley, Davin & Co. v. C.I.T. Corp.*, 414 So.2d 606 (Fla. App. 1982), is misplaced. There, the creditor’s lien covered only “monthly sewer fees” and the issue was whether the limited scope of that lien applied to “sewage connection fees.” Not surprisingly, the court held that the two types of fees were different and,

thus, “the language of the lien ... [does] not include connection fees.” *Id.* at 608. The court did not analyze whether the fees were “proceeds” of the sewage treatment plant, or even whether the plant itself was subject to the lien as an “improvement,” “fixture” or otherwise. Similarly, there was no language in the lien, like there is here, giving the creditor a broad security interest in all “rights ... relating to” and “benefits derived from” the land. *Stockton* has nothing to do with UCC 9-108’s specificity requirements and, certainly, it does not stand for the proposition that the latecomers payments must be specifically identified.

3. The Sewer Facilities Are Both “Improvements” And “Fixtures” Covered By The Deed Of Trust.

There is no dispute that, under the UCC, this Court must look to Washington’s common law to determine whether the Sewer Facilities are “improvements” or “fixtures” within the scope of the Deed of Trust. RCW 62A.9A-102(41); *In re Logan*, 195 B.R. 769, 772 (E.D.Wash. 1996). Here too, TMG ignores the law entirely. Rather, without citation to any authority, TMG argues that the Sewer Facilities are not fixtures because, by statute and the terms of the extension agreements, TMG was required to convey them to the District upon completion. TMG Br. at 18-19. The District at least mentions the common law, but makes the same argument. Dist. Br. at 10-11, 13. The argument is wholly misplaced.

When determining whether a structure, machinery or equipment is an “improvement” or “fixture,” the issue is not whether the owner of the land intends to permanently retain title to the item, but whether the owner intends to permanently attach the item to the land. Here, TMG did.

TMG and the District apparently concede that the Sewer Facilities fit the definition of “improvements” in that they are a “valuable addition” to the Sommerwood Property, “intended to enhance its value ... or to adapt it for new or further purposes.” *Burgeson v. Columbia Producers, Inc.*, 60 Wn. App. 363, 367, 803 P.3d 838 (1991). Nevertheless, the District argues that improvements must be “permanent,” and that the Sewer Facilities do not qualify because TMG “contemplated ... that they would be transferred and conveyed to the District.” Dist. Br. at 10. The cases show, however, that this permanency factor relates solely to physical relationship between the item and the land, not to the permanency of ownership or title. *See Siegloch v. Iroquois Mining Co.*, 106 Wash. 632, 635, 181 Pac. 51 (1919) (“permanent in the sense that it can remain so attached and fixed until destroyed by the elements or worn out by use”).

The opinion in *Pinneo v. Stevens Pass, Inc.*, 14 Wn. App. 848, 545 P.2d 1207 (1976), cited by the District, proves the point. There, the issue was whether a ski lift was an “improvement.” The defendant did not own the land, but rather operated the ski lift under a special use permit that

“require[d] the permittee to remove all structures and improvements at the termination of the permit.” *Id.* at 850. Even though there was no unity of ownership between the land and the ski lift, and never would be, the Court easily concluded that the ski lift was an “improvement” because it “adds value to the property, is an amelioration of its condition, and enhances its use,” regardless of who owned it. *Id.* at 851-53. The same is true here. Regardless of who owns the Sewer Facilities, there is no dispute that they were permanently installed to enhance the value of the Sommerwood Property. Indeed, the facilities could not have been built anywhere else. CP 520-21 (Curran Depo at 86-87). Nothing more is required.

The analysis is similar for “fixtures.” The District does not dispute that the Sewer Facilities satisfy the first two prongs of the fixtures test and, instead, focuses on the third: “intent.” Dist. Br. at 13. Again, the District argues that “TMG did not have the intent to make the Sewer Facilities a permanent part of the Sommerwood property” because it planned to convey the facilities to the District. *Id.* TMG says the same thing. TMG Br. at 18. But as Washington Federal explained (Op. Br. at 20-21), the relevant “intent” has nothing to do whether the annexing party intends to permanently retain title to an item, but whether the party intended “to make a permanent accession to the freehold.” *Dep’t of Rev. v. Boeing Co.*, 85 Wn.2d 663, 667, 538 P.2d 505 (1975). Where, as here, a property

owner attaches an item to the land, the owner is presumed to have annexed it with the intention of enriching the freehold. *Western Ag. Land Partners v. Dep't of Rev.*, 43 Wn. App. 167, 173, 716 P.2d 310 (1986).

Neither TMG nor the District provide any authority to the contrary, or any reason why this presumption does not apply here. To be sure, there is no evidence to suggest that TMG installed the Sewer Facilities on the Sommerwood Property in a temporary manner or with the intent that they someday resume their character as personal property; it is undisputed that the facilities cannot be relocated. CP 512, 520-21 (Curran Depo at 52, 86-87). Indeed, “permanent” annexation was the whole point. TMG installed the Sewer Facilities on the Sommerwood Property for the same reason that any developer improves the land: to increase its marketability and value; without the facilities, there would be no plat approval and no residential development. The fact that TMG knew it would ultimately convey ownership and operation of the Sewer Facilities to the District did not make the manner of or reasons for installation any less “permanent.” The facilities were intended to be, and still are, a “permanent accession.”

4. Public Policy Did Not Prevent Horizon Bank’s Security Interest From Attaching To The Sewer Facilities.

The District additionally argues that—even if the Sewer Facilities are “improvements” and “fixtures” within the plain meaning of the Deed

of Trust—they should be excluded from the scope of Horizon Bank’s security interest as a matter of public policy. Dist. Br. at 7-8. The District fears that, if sewer facilities intended for public dedication and operation are considered collateral, creditors could seek to foreclose on them, “which would undermine the construction of public sewer and water facilities.” *Id.* The District provides no authority for this argument, which is contrary to the law, facts and practical considerations that control here.

The law makes no exceptions with respect to security interests on property transferred or dedicated to a public entity. It is axiomatic that a transferee of real property takes subject to a prior recorded deed of trust. 18 Wash. Prac., *Real Estate* § 18.9 (2d ed. 2012) (“mortgagor and grantee cannot ... between themselves release the mortgagee’s security.”). This same rule applies where the transferee is a municipality; “a dedication which is detrimental to the interests of a mortgagee cannot be made without the consent and cooperation of the mortgagee.” 26 C. J. S., *Dedication* § 8, at 276 (2011); also 23 Am.Jur.2d, *Dedication* §§ 14, 15, at 16-17 (2002); *Western Fertilizer and Cordage Co., Inc. v. BRG, Inc.*, 424 N.W.2d 588, 593 (Neb. 1988); *Lane Title & Trust Co. v. Brannan*, 440 P.2d 105, 110 (Ariz. 1968). And certainly, there are no exceptions for public dedication generally or sewer facility extensions specifically in the recording act (RCW 65.08.070), the plat subdivision statute (RCW 58.17

et seq.), the Deed of Trust Act (RCW 61.12 *et seq.*), the water/sewer district statutes (Title RCW 57) or the Snohomish County Code.²

Indeed, TMG's extension agreements with the District specifically contemplate that the Sewer Facilities may be subject to liens that must be removed by creditor consent prior to transfer. CP 347 (§ 5(e)(1): TMG warrants that facilities are "free and clear of all encumbrances and Developer has good right and authority to transfer title"). The RCW and Snohomish County Code contemplate the same thing when a subdivision is subject to public dedication. RCW 58.17.165 ("instrument of dedication shall be signed ... by all parties having any ownership interest in the lands subdivided"); Snohomish Cty. Code 30.41A.640(2) ("final plat shall be accompanied by an updated certificate of title showing the names of all persons, firms, or corporations whose consent is necessary to dedicate land for public usage, as well as any easements or other encumbrances"). If mortgages and security interests did not attach to land or property slated for public ownership, as a matter of public policy or otherwise, then these warranties and prior consent would be unnecessary.

² To the same effect, when a public entity *takes* private land through eminent domain, the mortgagee shares in the compensation awarded to the property owner in the condemnation proceedings. *See State v. Hemmingson*, 57 Wn.2d 635, 638, 359 P.2d 154 (1961) (mortgagee has an equitable lien in the compensation provided for mortgagor's property).

But security interests do attach and creditor consent is necessary. The District's fear that this process will impair the construction of sewer facilities is illusory—for creditors invariably consent. Creditors have no interest in foreclosing on a sewer facility because, as the District points out, they can be operated only by a public entity. WAC 173-240-104. At the same time, creditor consent allows a developer to transfer the facilities “free and clear,” thereby facilitating plat approval and increasing the value of the land still covered by the creditor's deed of trust. Simply put, creditors have little incentive to withhold consent or foreclose on public sewer facilities. What a creditor will do, however, to avoid the very kind of dispute that erupted here, is ask a developer to recognize the creditor's existing security interest in any latecomers payments that will arise from the transfer. Horizon Bank was never given that opportunity.

5. The Right To Receive Latecomers Payments Are “Proceeds” Of The Sewer Facilities.

TMG does not dispute that if the Sewer Facilities were collateral within the scope of the Deed of Trust (they were), then Horizon Bank's security interest automatically attached to all “proceeds” of that collateral. RCW 62A.9A-315(a)(2); RCW 62A.9A-203(f). TMG argues that this rule does not apply to the latecomers payments because it only received a “right to water and sewer service” when it conveyed the facilities to the

District, but not any “monetary proceeds.” TMG Br. at 25. But the UCC does not limit “proceeds” to monetary consideration, and the courts long ago abandoned any such precept. *Rainier Nat. Bank v. Bachmann*, 111 Wn.2d 298, 303, 757 P.2d 979 (1988) (definition “evidences an intent to include more than the usual cash proceeds received in a normal sale of the collateral”). Thus, the issue is whether TMG’s *right* to receive latecomers payments—above and apart from its right to receive water and sewer service—qualifies as proceeds of the Sewer Facilities. It does.³

Proceeds are defined, first and foremost, as “[w]hatever is acquired upon the ... disposition of collateral.” RCW 62A.9A-102(64)(A). As the Supreme Court has emphasized, this “all-encompassing” definition means “everything ... no matter what ... anything at all.” *Rainier*, 111 Wn.2d at 302-303; *Western Farm Serv., Inc. v. Olsen*, 151 Wn.2d 645, 648, 90 P.3d 1053 (2004). TMG received a right to latecomers payments only because it transferred the Sewer Facilities to the District. Under both state law and the extension agreements, TMG had no such right until that happened. RCW 57.22.010 & .020; CP 347, 351 (§§ 5(e), 18). Indeed, the District

³ TMG argues that it had standing to enter into the Latecomers Agreement with the District in October 2009 even though, by that time, Horizon Bank had already foreclosed on the Sommerwood Property. TMG Br. at 13-14. Washington Federal did not argue otherwise. The only issue here is whether TMG acquired the right to latecomers payments when it transferred the Sewer Facilities to the District. It did.

conceded it would not have signed the Latecomers Agreement absent a transfer. CP 412. Although TMG did not immediately acquire latecomers payments upon its transfer—because, as TMG points out, payments are made only when and if other property owners connect to the facilities—TMG did immediately acquire a *right* to receive the payments. That right is a proceed “acquired upon ... disposition” of the Sewer Facilities.

For the same reasons, the latecomers payments are also “[r]ights arising out of collateral”—a separate and more expansive definition of proceeds. RCW 62A.9A-102(64)(C). TMG makes the circular argument that the payments do not arise from “the collateral on the land, but rather the cost of construction.” TMG Br. at 27. Of course, without the “collateral,” *i.e.*, the Sewer Facilities, there would be no construction and, ultimately, no latecomers payments; the “cost of construction” merely establishes the amount to be paid as reimbursement for the collateral. RCW 57.22.030. That some of the sewer main and pipes extend onto a public right of way does not change the analysis.⁴ TMG does not dispute that it would have no right to latecomers payments at all had it not built

⁴ Indeed, even though the Deed of Trust was limited to the Sommerwood Property, Horizon Bank’s security interest in the Sewer Facilities would include those aspects of the facility that extended into the right of way. *See* RCW 62A.9A-336(a) & (c) (if collateral is physically united with other goods so that its identity is lost in a product or mass, then the security interest attaches to the entire “commingled goods”).

the Sewer Facilities on the Sommerwood Property; by law, latecomers payments are available only to an “owner” who constructs water or sewer facilities on private property within the District. RCW 57.22.020. The payments were “proceeds” for this reason as well.

6. The Latecomers Payments Are “Rights ... Relating To” The Sommerwood Property.

As Washington Federal explained, even if the latecomers payments are not proceeds, the payments were still covered by the Deed of Trust because they are “rights ... relating to” and “benefits derived from” the Sommerwood Property. Op. Br. at 25-27. Repeating its erroneous refrain that the Deed of Trust should have described the latecomers payments with specificity, TMG argues that the phrase “all other rights” is “too vague.” TMG Br. at 27. But TMG misquotes the Deed of Trust; it does not say “all other rights,” nor does it contain any other “supergeneric” description. RCW 62.9A-108(c). Rather, it “reasonably identifies” the collateral to include only rights and benefits “relating to” or “derived” from a specific and “objectively determinable” piece of land—the same land encumbered by the Deed of Trust. RCW 62.9A-108(a) & (b)(6). This language is far more descriptive than the catch-all phrase “general intangible”—which even TMG says would have been good enough.

TMG ignores the cases cited by Washington Federal that have found similar language sufficient. Op. Br. at 27. Instead, TMG cites *In re I.A. Durbin*, 46 B.R. 595 (S.D.Fla. 1995), but that case is distinguishable. There, the debtor signed a mortgage covering land and personal property located on the land and, separately, assigned certain contract rights. *Id.* at 597. The only issue was whether a financing statement—not a security agreement—sufficiently described the assigned contracts. The court held that it did not because the financing statement described the collateral only as the property rights “encumbered by the mortgage.” The mortgage, in turn, did not reference the contracts, nor did it contain language—like that found in the Deed of Trust—granting a security interest in “rights related to” the land. *Id.* at 597-601. On the contrary, the mortgage covered only equipment, fixtures and property “located” on the premises and “used or usable in connection” with the land. *Id.* at 597-98.

The Deed of Trust is far more expansive, and plainly gave Horizon Bank a security interest in the very kind of “intangible” personal property reflected by the latecomers payments. *Windstone v. JLM Fin. I, Ltd.*, 1997 WL 724878 (Tex. App. Nov. 20, 1997), is particularly instructive. There, like here, a developer entered into an agreement with a municipal utility district under which the developer would build water, sewer and drainage facilities on its land in exchange for reimbursement from the district. The

land and the right to reimbursement were later conveyed to the debtor who, in turn, executed a deed of trust in favor of the creditor. The creditor ultimately foreclosed on the property. Then, like here, both the creditor and debtor claimed the right to receive the “reimbursables.” *Id.* at *1.

One of the issues on appeal was whether the reimbursables were covered by the deed of trust. (Another issue was whether the water and sewer facilities were “fixtures”; the court concluded they were.) The court held that the creditor did have a security interest in the reimbursables:

The contractual right to the reimbursables was covered by the expansive language of the deed of trust and the substitute trustee’s deed, which included all the property conveyed in the deed of trust. Specifically, the deed of trust granted the trustee (1) ..., (2) all the estate, interest, right, title, and “other claims, or demands, which Grantor now has or may hereafter acquire or own in the Mortgaged Premises, and any Buildings and Improvements thereon,” and (3) “all other rights, titles, interests, estates, or other claims of every kind and character ... which Grantor now has or at any time hereinafter acquires in and to the Mortgaged Premises.

Id. at *6. The court also cited the parties’ security agreement, which covered “general intangibles” arising from ownership or operation of the land, but the opinion is clear that the “broad language of the deed of trust” alone was sufficient. *Id.* There is no meaningful distinction between the language of the deed of trust in *Windstone* and the language of the Deed of Trust here: just as the phrase “rights, titles, interests, estates, or other

claims ... in and to the Mortgaged Premises” covered the reimbursables in *Windstone*, the phrase “rights, royalties, and profits relating to the real property” covered the latecomers payments here.

C. The Terms Of The Trustee’s Deed Did Not Extinguish Horizon Bank’s Security Interest In The Latecomers Payments.

TMG argues that the trustee’s sale resulted in a conveyance of real property only, and the absence of any reference to “personal property” in the trustee’s deed “destroys WaFed’s claim to the security as part of Horizon’s collateral[.]” TMG Br. at 21. This argument fails on many levels. To begin with, as explained above, TMG does not dispute that the latecomers payments are “profits” of the Sommerwood Property and, thus, under RCW 7.27.230(2), they are “real property” under Washington law. Even if real property were the only thing sold at the trustee’s sale, and it wasn’t, the latecomers payments were “part of the bundle of rights passed to the [Horizon Bank] upon foreclosure.” *Kezner*, 87 Wn. App. at 464-65.

Moreover, even if considered “personal property,” Horizon Bank acquired the latecomers payments at the trustee’s sale. TMG does not dispute that where a security agreement covers both real and personal property, a creditor may foreclose on all the collateral under the Deed of Trust Act. RCW 62A.9A-604; RCW 61.24.020. The Act states:

When delivered to the purchaser, the trustee’s deed shall convey all of the right, title, and interest in the real and

personal property sold at the trustee's sale which the grantor had or had the power to convey at the time of the execution of the deed of trust and such as the grantor may have thereafter acquired.

RCW 61.24.050(1). In the case of a trustee's sale, then, the issue is not what the trustee's deed says, but what property was "sold at the trustee's sale." *Id.* Indeed, as Washington Federal pointed out (Op. Br. at 29 n. 10), and TMG ignores completely, the Supreme Court has recognized that, "[t]he trustee's delivery of the deed ... is a ministerial act." *Udall v. T.D. Escrow Serv. Inc.*, 159 Wn.2d 903, 911, 154 P.3d 882 (2007).

On the issue of what was "sold at the trustee's sale," there is no dispute; the sale included both the real *and personal property* secured by the Deed of Trust. The Notice of Trustee's Sale, which was both recorded and specifically referenced in the trustee's deed, stated expressly:

If the Deed of Trust grants the Beneficiary security interests in personal property located on the real property, ***said personal property will be included in the Trustee's Sale.*** ... Reference should be made to the Deed of Trust ... for a description of the personal property being sold.

CP 1301 (emphasis added). For the reasons explained in the opening brief and here, the Deed of Trust gave Horizon Bank a security interest in the latecomers payments, both as "proceeds" of "improvements and fixtures" on, and as "rights ... related to," the Sommerwood Property. Under the Deed of Trust Act, Horizon Bank acquired those rights when the trustee

accepted the bank's bid, finalizing the sale, *Udall*, 159 Wn.2d at 911-12, notwithstanding the description of property in the trustee's deed.

The UCC's enforcement provisions lead to the same result. Under the UCC, after default, a creditor can both dispose and purchase the debtor's collateral at public auction. RCW 62A.9A-610(a) & (c). When that occurs, the disposition of the collateral automatically "[t]ransfers to a transferee for value all of the debtor's rights in the collateral." RCW 62A.9A.617(a)(1). The transferor does not need to formally memorialize the transfer by way of deed, bill of sale, assignment or otherwise. *See Sky Technologies, LLC v. SAP A.G.*, 576 F.3d 1374, 1378-80 (Fed. Cir. 2009). Here, there is no dispute that the trustee's sale was commercially reasonable, and Horizon Bank was a transferee of the collateral for value. The description in the trustee's deed was irrelevant for this reason too.

Finally, even if the right to receive latecomers payments was not sold to Horizon Bank at the trustee's sale, the security interest in those payments was not "destroyed" as TMG asserts. The security interest in that collateral would still exist, and Washington Federal could foreclose on the collateral in the future. The Deed of Trust Act is unequivocal on this point: foreclosure "does not preclude" any "nonjudicial foreclosures of any ... other security interests or liens covering any real or personal property granted to secure the obligation that was secured by the deed of

trust foreclosed.” RCW 61.24.100(3)(b). TMG provides no authority to the contrary. In short, the lack of reference to “personal property” in the trustee’s deed does not limit the scope of collateral sold at the trustee’s sale, nor did it “destroy” the security interest in that collateral.

D. Washington Federal Filed A UCC Financing Statement To Protect Its Existing Right To The Latecomers Payments.

TMG suggests that Washington Federal “attempted to expand the scope of Horizon’s security interest” by filing a UCC financing statement that specifically referenced the latecomers payments. TMG Br. at 8 & 29. This argument is a classic red herring. Washington Federal has never contended that its June 2010 financing statement created a security interest in the latecomers payments. Financing statements do not create security interests; they “perfect” existing ones. RCW 62A.9A-310. In general, the first creditor to perfect a security interest has priority over other creditors with an interest in the same collateral. *Parker Roofing*, 59 Wn. App. at 155; RCW 62A.9A-322. Perfection, however, is irrelevant to the validity of the security interest between the parties to a security agreement. *Lojek v. Pedler*, 488 N.E.2d 864, 866 (Ohio 1986); *Farm Credit Servs. of America, Inc. v. Wilson*, 247 P.3d 1199, 1201 (Okla. App. 2010).

There is no dispute regarding the validity of the Deed of Trust and, as explained, there can be no reasonable dispute that it gave Horizon Bank

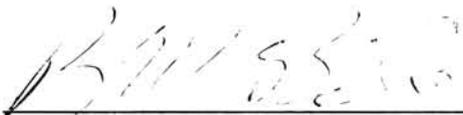
a security interest in the latecomers payments. Washington Federal filed the June 2010 financing statement solely to protect that interest. In the months following foreclosure, TMG refused to recognize Horizon Bank's (and, thereafter, Washington Federal's) right to the latecomers payments. CP 429-434. Even though it did not need to do so, Washington Federal filed the statement to give "fair warning" to TMG's other creditors and/or assignees of its superior interest in the payments. *Parker Roofing*, 59 Wn. App. at 160. That precautionary step has nothing to do with the validity or scope of the Deed of Trust, and everything to do with Washington Federal's effort to ensure that it could realize on its collateral to reduce the massive deficiency left by TMG on the Loan. That effort continues today.

III. CONCLUSION

When Horizon Bank foreclosed on the Deed of Trust, it acquired the right to receive latecomers payments and that right now belongs to Washington Federal. This Court should reverse the judgment below and direct the trial court to enter judgment in Washington Federal's favor.

RESPECTFULLY SUBMITTED this 14th day of January, 2013.

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By 

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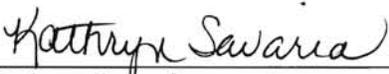
CERTIFICATE OF SERVICE

I hereby certify that on January 14, 2013, I caused to be served a copy of the foregoing **REPLY BRIEF OF APPELLANT** on the following person(s) in the manner indicated below at the following address(es):

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