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STATE OF WASHINGTON
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No. 40171-1-II

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION II

HENRY DRAGT and JANE DRAGT, husband and wife,

Appellants,

v.

DRAGT/DETRAY, L.L.C., a Washington limited liability;
and E. PAUL DETRAY and PHYLLIS DETRAY,
and their marital community,

Respondents.

**APPELLANTS' REPLY BRIEF REGARDING FUNDS HELD IN
THE REGISTRY OF THE COURT**

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I. INTRODUCTION

In his responding brief, DeTray concludes that RSC's security interest is unenforceable because the Dragts had no interest in the funds held in the registry of the court. His premise is that the funds were held in *custodia legis* and when funds are so held, the parties are divested of their rights therein.

DeTray's argument is wrong on several counts. First, not all funds deposited into court are held *in custodia legis* as DeTray contends. Second, the mere act of depositing funds into the registry of the court does not divest the owner of title thereto. Third, even if the funds were held in *custodia legis*, they were still subject to RSC's lien once this Court determined ownership of the funds and the purpose of depositing the funds was accomplished.

II. ANALYSIS

A. **DeTray's assumption that all funds deposited into court are held in *custodia legis* is unsupported and wrong.**

The first flaw in DeTray's argument is his assumption that all funds deposited into the registry of the court are necessarily placed in *custodia legis*. See Responding Brief at p. 8 (arguing that Washington law does not limit the application of *custodia legis* to particular situations).

This is simply not true. While a court may have custody over funds deposited into its registry, not all funds deposited are held in

custodia legis. Indeed, Washington law and the foreign law cited by DeTray unanimously impose limitations on the nature of funds held in *custodia legis*. As explained in Dragts' Opening Brief at 12, Washington courts have held that funds are held in *custodia legis* in limited circumstances, such as when property is repossessed under a writ of attachment or garnishment or when funds are paid to satisfy a judgment. Although DeTray cites to *Maybee v. Machart*, 110 Wn.2d 902, 757 P.2d 967 (1988), that case does not support his position; it merely reinforces that funds paid into court to satisfy a judgment are held in *custodia legis*. Contrary to DeTray's interpretation of the opinion, the majority held that funds deposited into court to satisfy a judgment are held in *custodia legis* while the dissent argued that the doctrine applies only when necessary to prevent jurisdictional conflicts with other courts. Neither situation exists here so the opinion does not support application of *custodia legis* in this case.

Likewise, DeTray's reliance on *Wilson v. Henkle*, 45 Wn. App. 162, 724 P.2d 1069 (1986) is misplaced. The court there did not rule that all funds deposited with a court are held in *custodia legis*. To the contrary, the court found that liens can attach to funds held in court and such liens would have priority over unsecured creditors' interests, although the lien

claimed in that case was invalid because it did not comply with the attorneys' lien statute. *Id.* at 169-70.

The foreign law relied upon by DeTray is consistent and, like Washington law, does not support his assumption that all funds deposited into a court are held in *custodia legis*. Rather, those cases emphasize the specific attributes of *custodia legis* and demonstrate why that doctrine is specifically inapplicable here. In *Davis v. Cox*, 356 F.3d 76 (1st Cir. 2004), for example, the court found the funds were being held in *custodia legis* because the order to escrow the funds was akin to a writ of attachment and court-appointed custodian of the funds was akin to a receiver, both of which are attributes of *custodia legis*. *Id.* at 93. In *Bank of Hawaii v. Benchwick*, 249 F.Supp. 74 (Ha. 1966), the court found that money deposited as bail in a criminal proceeding was held in *custodia legis*, and in *Arizona Land Corp. v. Sterling*, 5 Ariz. App. 4, 422 P.2d 734 (1967), the issue was whether money deposited as a supersedeas bond was held in *custodia legis*. None of the facts that made the doctrine of *custodia legis* applicable in those cases exist in the instant case.

B. DeTray's argument that the mere act of depositing funds into court divests one of title is equally wrong.

DeTray's assumption that all funds deposited into court are held in *custodia legis* appears to be based on his equally flawed conclusion that

merely depositing funds into court divests one of title. *See* Responding Brief, at p. 10 (“When a court orders funds to be deposited into the registry of court pending further order of the court, it divests the parties of legal title and title to the funds passes to the clerk as trustee”).

Again, this is simply not true. DeTray erroneously cites *Davis v. Cox*, 356 F.3d 76, in support of his proposition. The court there held that in a divorce proceeding under Maine law, when the court appoints a receiver to hold money in escrow pending determination of the spouses’ claims thereto, title to the money deposited vests in the receiver until ownership is determined. *Id.* at 93. The court did not say title to funds passes any time funds are deposited in the court’s registry.

The circumstances in which funds are held in *custodia legis* have one thing in common: a legal mechanism that divests the party’s rights to the funds. That mechanism can be, among other things, a writ of attachment issued by a court, the appointment of a receiver, or the deposit of funds into escrow, all of which legally divest a party of title to property. *See e.g., Davis v. Cox*, 356 F.3d at 93-94. But the mere act of depositing funds into the registry of a court does not divest a party of title.

C. Even if the funds at issue were held in *custodia legis*, RSC's security interest is still enforceable since it attached after the purpose of depositing the funds was accomplished.

Ultimately, whether or not the funds at issue here were held in *custodia legis* is not controlling since even if they were, RSC's security interest is still enforceable and superior to DeTray's claim. This is because of two important aspects of Washington law that DeTray fails to address.

First, in Washington, funds held in *custodia legis* can be attached or otherwise encumbered by creditors once the purpose behind depositing the funds has been accomplished. *State v. A.N.W. Seed Co.*, 54 Wn. App. 729, 733, 776 P.2d 143 (1989). In that case, proceeds from the sale of real property were deposited with the court to satisfy a judgment. A judgment creditor attached the funds and another party contended that the attachment was invalid because funds held in *custodia legis* could not be attached prior to a court order disbursing the funds. This argument was rejected. The court held that when the purpose of the custody of the law has been accomplished and ownership of the funds has been established, ownership of the funds vests without further court order. Once ownership vested, the only remaining decision was priority between the writ of attachment and other liens, which was decided in favor the former because it was "first in time." *Id.* at 733.

There is a subtle, but important, fact in the *A.N.W. Seed Co.* opinion that cannot be overlooked. In that case, funds were held pending disbursal by order of the court. Ownership of the funds was then determined by stipulation of the parties. In the court's view, once ownership vested, the custody of the law was accomplished, thereby triggering the parties' ability to attach or encumber the funds: "The parties' stipulation determined ownership of the funds. That ownership having been established, the property vested in the Kilthaus without further court decision." *A.N.W. Seed Co.*, 54 Wn. App. at 733. The parties did not have to wait for the court's disbursal order for the restrictions imposed by *custodia legis* to lift. Thus, to the extent DeTray argues that funds held in *custodia legis* cannot be attached or encumbered until the court enters a disbursal order, he is wrong; the funds are available to creditors once title vests and title vests as soon as the court determines title.

In the instant case, the purpose of depositing the funds – to secure the parties' conflicting claims to the Dragts' property – was accomplished when this Court decided *Dragt v. Dragt/DeTray, LLC* in 2007. The Court ruled that the Dragts owned the real property and that DeTray had no ownership interest. *Dragt v. Dragt/DeTray, LLC*, 139 Wn. App. 560, 573-74, 161 P.3d 473 (2007). With that decision, ownership of the property,

and the proceeds from the sale of the property, vested in the Dragts without further court order. Once ownership vested, the funds were subject to encumbrances. Thus, under Washington law, DeTray could have – but elected not to – attach the funds held in court at that time. Likewise, the Dragts were entitled to – and did – grant a security interest in the funds.

The second difference in Washington law concerns liens against funds held in *custodia legis*. While *custodia legis* funds are not subject to attachment or garnishment until ownership has vested, such funds are always subject to creditors' liens. This was confirmed by the Supreme Court in *Maybee v. Machart*, 110 Wn.2d 902. There, funds were held in *custodia legis* to satisfy a judgment. The judgment creditor garnished the funds after the debtor's attorney and healthcare provider had filed liens against the funds. While the court quashed the writ of garnishment because it was filed before ownership of the funds had been determined, the court recognized and enforced the liens even though they were also asserted prior to the determination of ownership. The court acknowledged the general rule that funds held in *custodia legis* were not subject to garnishment until the purpose of the custody of the law was accomplished. Nonetheless, the Court held that liens filed by the depositor's attorney and healthcare provider prior to judgment and prior to the purpose of custody

of the funds being accomplished, were valid and enforceable and superior to later garnishment rights. *Id.* at 968. Pursuant to that holding, the funds held in court were disbursed to the lien claimants instead of the judgment creditor. *Id.* at 968. Similarly, the court in *Wilson v. Henkle*, 45 Wn. App. at 170, acknowledged that court-held funds were subject to attorneys' liens and determined priority between the competing interests on a normal "first in time" basis. Finally, the Supreme Court in *A.N.W. Seed Co.*, 54 Wn. App. at 733, held that funds held in *custodia legis* were subject to attorneys' liens, although in that case the lien was subordinate to another creditor's attachment. Thus, based on these holdings, the Dragts could have encumbered the funds before ownership was decided.

Either way, the funds deposited into court were subject to RSC's security interest even if they were held in *custodia legis*. Consequently, the funds must be disbursed in accordance with RSC's priority lien. *Maybee v. Machart*, 110 Wn.2d at 905.

D. DeTray's other arguments are similarly flawed.

DeTray makes a related argument that the Dragts had only a contingent interest in the funds deposited into court. Responding Brief at 10-11. This argument is based on *Davis v. Cox*, 356 F.3d at 93, where the court said the depositor's interest was contingent on the court's determination of ownership. Applying this analysis here, the Dragts'

interest in the funds may have been contingent on the court's determination of title to the real property. But when this Court determined that the Dragts owned the real property and therefore the proceeds thereof, the contingency was removed and the Dragts' contingent interest ripened into a noncontingent interest.

Similarly, DeTray argues that the Clerk of the Court held the funds as "trustee." Responding Brief, at 10. If the clerk did hold the funds as trustee (and no Washington case so holds) the clerk was trustee only while title to the property was undetermined. Once DeTray's claim to title was extinguished, ownership of the funds became fully vested in the Dragts and the clerk's role as trustee necessarily evaporated.

Finally, one cannot overlook that DeTray's argument, if accepted, defeats any rights DeTray has to the funds. That is because DeTray, as a judgment creditor, can only enforce his judgment against assets owned by the Dragts. Accordingly, if the Dragts have no interest in the funds held by the court as DeTray claims, then DeTray cannot execute on those funds to satisfy his judgment. DeTray can execute upon the funds only if the Dragts have rights to those funds. But if the Dragts have rights to those funds, the security interest granted to RSC is enforceable.

III. CONCLUSION

As set out above, the funds deposited into court in this case were not held in *custodia legis*. And even if the funds were held in *custodia legis*, the funds were nonetheless subject to RSC's lien. In either event, the funds must be disbursed pursuant to RCW 4.44.480, which provides that court-held funds must be disbursed in accordance with "applicable principles of law." *See, Wilson v. Henkle*, 45 Wn. App. at 169.

Under "applicable" Washington law, RSC is a secured creditor with a valid, perfected lien against the funds. DeTray, on the other hand, is merely a judgment creditor and, as such, has no lien on the Dragts' personal property. Therefore, RSC's secured interest is prior and superior to DeTray's unsecured interest and the funds should be disbursed in accordance with the parties' respective rights.

Accordingly, the Dragts respectfully request that the Court reverse the trial court's November 19, 2010 order disbursing the funds held in court to DeTray and award such funds to the Dragts subject to the security interest granted to RSC.

Dated this 8th day of June, 2011.

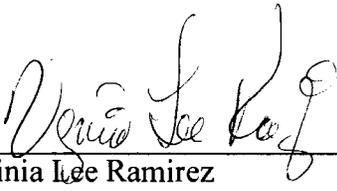
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DECLARATION OF SERVICE

I declare that on the 9th day of June, 2011, I caused to be served the foregoing document on counsel for Respondents, as noted, at the following addresses:

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Dated: June 9th, 2011

Place: Seattle, WA