No. 42811-3-II

COURT OF APPEALS
DIVISION II
OF THE STATE OF WASHINGTON

THE BERT KUTY REVOCABLE LIVING TRUST,
by its TRUSTEE DAVID NAKANO

Appellant (Plaintiff),

vs.

GERRY and JOHN DOE MULLEN, et al.

Respondents (Defendants)

APPELLANT'S OPENING BRIEF

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I. INTRODUCTION

This is a case involving the sale of real property that bears all the hallmarks of equity-stripping fraud, where the facts alleged by the Plaintiff, the Bert Kuty Revocable Trust, were particularly within the knowledge of the defendants, including Robert and Daniele Hayes and Columbia River Properties, Inc. This case should not have been resolved on summary judgment. The Trial Court erred in, on multiple motions for partial summary judgment, dismissing many of the Bert Kuty Trust's claims having made judgments as to credibility of witnesses based solely on declarations, having resolved disputes of material fact, and having ignored material undisputed facts. Further, the Trial Court erred in sanctioning the Bert Kuty Trust under CR 11 and RCW 4.84.185 when the lawsuit was both grounded in fact and warranted by existing law (or supported by a good faith argument for the extension of existing law), and when all the claims in the lawsuit had potential merit, and in failing to apply the lodestar analysis to the award of attorney fees against the Bert Kuty Trust.

This Court should reverse and remand for trial, where the credibility of witnesses and factual evidence may properly be weighed.

II. ASSIGNMENTS OF ERROR

Assignments of Error

1. The Trial Court Erred in Dismissing the Bert Kuty Trust's Claim for Accounting of the Proceeds of a Foreclosure Sale.

2. The Trial Court Erred in Dismissing the Bert Kuty Trust's Claims for Fraud and Civil Conspiracy With Prejudice, over the Bert Kuty Trust's Objection and Request that the Claims be Voluntarily Dismissed Without Prejudice.

3. The Trial Court Erred in Awarding Fees as Sanctions Against the Bert Kuty Trust under CR 11 and RCW 4.84.185.

4. The Trial Court Erred in Granting Columbia River Properties, Inc. Summary Judgment, and Denying the Bert Kuty Trust Summary Judgment, on Bert Kuty Trust's claim that Columbia River Properties was a Successor to DC Inc.

Issues Pertaining to Assignments of Error

1. If a note has a face value of $238,000, and no payments are made, what is it worth? *$238,000.*

2. If a note worth at least $238,000 is tendered in full as payment at a foreclosure sale, is the price paid at the sale at least $238,000? *Yes.*

3. If a holder of a note and deed of trust tenders in the deed of trust for its full face value and then, to avoid taxable profit, discharges the

note for a stated value less than its face value, is the foreclosure price retroactively reduced such that other secured parties cannot participate in the proceeds of the foreclosure sale? *No.*

4. If a claim becomes improbable, but not wholly lacking in evidentiary support (remains supported by at least a scintilla of evidence), should it be dismissed, with prejudice, on Summary Judgment over the Plaintiff's objection and request that it be voluntarily dismissed without prejudice subject to refilling if facts developed in subsequent discovery so warrant? *No.*

5. Are fees under CR 11 and RCW 4.84.185 appropriate for dismissal of claims for accounting and unjust enrichment when it appears that a foreclosing party purchased a fraudulently obtained note and deed of trust for 1/6 of its value, foreclosed on that note and deed of trust for its face value, and then accepted only the purchase price it paid for the note and deed of trust as the pay-off amount of the note of deed of trust, resulting in the stripping away of an inferior interest retained by the original seller of the property? *No.*

6. Are fees under CR 11 and RCW 4.84.185 appropriate for dismissal of a claim for equitable restitution when it appears that a foreclosing party purchased a fraudulently obtained note and deed of trust for 1/6 of its value, foreclosed on that note and deed of trust for its face value,

and then accepted only the purchase price it paid for the note and deed of trust as the pay-off amount of the note of deed of trust, resulting in the stripping away of an inferior interest retained by the original seller of the property? *No.*

7. Does an award of attorney's fees under CR 11 and RCW 4.84.185 need to be supported and justified by a lodestar analysis? *Yes.*

8. Does a Real Estate Brokerage succeed to the liabilities of another brokerage (which is ceasing operations) when it acquire the assets and pending contracts of the other brokerage, takes on the employees of the other brokerage, and when there is continuity of ownership between the brokerages, all with knowledge of the liabilities of the other brokerage, and then continues the business of the other brokerage? *Yes.*

III. STATEMENT OF THE CASE

The Bert Kuty Trust sold real property located in Lewis County to Defendant New Enterprise, LLC. New Enterprise did not come up with sufficient cash or financing to pay for the entire purchase price. (CP 79-80.) Bert Kuty Trust took a second deed of trust position and a promissory note of $56,000 to make up the difference between the pay-out amount and the purchase price. (CP 79-80, 94-95).

FACTS CONCERNING HAYES

New Enterprise had entered into a written "Speculative Construction Loan Agreement" with Le Grand Investments, LLC, in which Le Grand agreed to loan up to $238,000 to New Enterprise to construct a home for purposes of re-sale on the real property sold by the Bert Kuty Trust. (CP 119-163.) As part of the loan transaction New Enterprise executed a promissory note in the amount of $238,000 in favor of Le Grand and granted Le Grand a first position Deed of Trust on the property. Critically, the First Note and Deed of Trust were drafted with face values of $238,000 rather than language that allowed adjustment of the value based on amounts disbursed. (CP 145-153.) Despite this face value, Mr. and Mrs. Hayes were able to purchase those instruments from their original beneficiary for $40,000. (CP 120)

Prior to filing this action, the Bert Kuty Trust's counsel conducted a detailed month-and-a-half long investigation into the circumstances of this sale and the participants in the sale on the buyer's side. This investigation strongly suggested that this transaction was tainted by an intentional and elaborate scheme of equity stripping fraud. This scheme operates by purchasing property at a fractional value, inducing the seller to take a second-position to secure the balance of the purchase price. After the sale, the buyer defaults, allowing the seller's security interest to be scrubbed by a foreclosure of a friendly (insider) and over-stated first position interest. However, additional investigation required formal discovery, using the tools of discovery available litigation. On this factual and legal basis, the Bert Kuty Trust's counsel filed and served the complaint on behalf of the Trust. (CP 333-338.)

This initial investigation suggested that Defendant Robert Hayes was personally involved in the Endeavor scheme. Robert Hayes was the principal beneficiary of that scheme as it played out in this case. Robert Hayes purchased the note and first position deed of trust from Le Grand Investments for $40,000, despite its face value of nearly six times that amount. (CP 120; 283-284.) Based on that investment, Mr. Hayes ultimately received the Kuty property. (CP 120-121.)

The buyer, New Enterprise, failed to make any payments on the Hayes/Le Grand note and deed of trust. When New Enterprise failed to make any payments on either its obligation to Robert Hayes, Robert Hayes foreclosed on the property. (CP 120).

Mr. and Mrs. Hayes bid in their note and deed of trust as payment for the property at the foreclosure sale and purchased the property based on the tender of that note for whatever it was worth at the time of tender. (CP 280.) Based on this tender of the note "for what it was worth", the Bert Kuty Trust (unsuccessfully) argued to the Trial Court that the tender resulted in a foreclosure purchase price of $238,000 (the face value of the note). (CP 295-296.)

After the sale, Mr. and Mrs. Hayes's accepted $40,000 of the sale proceeds as a full pay-off of New Enterprise's obligations. The Bert Kuty Trust argued to the Trial Court (based on its unsuccessful theory about the valuation of the note) that this left $198,000 for payment of other obligations (including the Plaintiff's second position deed of trust), which overage was never paid or accounted for. (CP 296-298; 299-302.)

During the proceedings before the Trial Court, Hayes brought two Motions for Summary Judgment. The first Motion sought dismissal of the Plaintiffs' claims relating to the legality of the Hayes's note and deed of trust and to the alleged participation of Mr. and Mrs. Hayes in the equity stripping scheme. (CP 191-198.) The Court granted the motion with regard to the legality of the note, but denied it with regard to the scheme, and granted Plaintiff leave to amend to add its unjust enrichment claim. (CP 255-258.)

Hayes then moved for summary judgment a second time, seeking dismissal of Bert Kuty's claims for an accounting of the sale proceeds and allegations that Mr. and Mrs. Hayes were involved in the equity stripping scheme or, even if not involved, had been unjustly enrichment by it. (CP 281-288.) Based on newly discovered evidence, the Bert Kuty Trust conceded that point based on newly discovered evidence that tended to cast doubt on Hayes's role in the Endeavor scheme (at least during the transaction, which set it in motion), but requested that the dismissal be without prejudice because there were still unresolved evidentiary issues and discovery was not complete. (CP 292.) The Bert Kuty Trust resisted the motion to dismiss its accounting and unjust enrichment claims. (CP 289-298.) The Court granted the motion in full, dismissing Mr. and Mrs. Hayes from this litigation.(CP 310-312.)

After prevailing on the Second Summary Judgment, Defendant Hayes sought and received an award of sanctions in the form of attorney's fees under CR 11 and RCW 4.84.185. (CP 319-326; 340-344.)

FACTS CONCERNING COLUMBIA RIVER PROPERTIES

The Bert Kuty Trust also asserted claims against its real estate agent, Gerry Mullen, and the real estate agency (ultimately determined to be incorporated as D.C. Inc., identified in the Amended Complaint) for professional real estate malpractice. This claim was based on Gerry Mullen's failure to protect the Bert Kuty Trust from the fraudulent scheme involved in this case and from the risk of being in second position behind a development loan and on her recommending that and encouraging the Bert Kuty Trust sell the properties on the terms under which this sale occurred. (CP 345-353.) The Bert Kuty Trust obtained a default judgment against D.C. Inc. (CP 766-767), but has been unable to collect on that judgment as D.C. Inc. ceased operations under that name, reopening under Columbia River Property after a shift of its management structure (as outlined below).

Mr. Christopher Fry is a licensed real estate agent and a licensed real estate broker as well as holding positions, including ownership, officer, and directorship positions, in both D.C. Inc. and Columbia River Properties. Mr. Fry incorporated his own real estate brokerage in 1998, D.C. Inc., d/b/a Northwest Properties of Southwest Washington, located in Kelso, Washington. (CP 389-390, ll 23-1; CP 399, ll 23-24) When Mr. Fry started D.C. Inc., he was the only person working there, but within 6 weeks to 2 months, he started acquiring agents. (CP 390-391; ll 23-2.) Mr. Fry hired Gerry Mullen as an agent in late 1998, about 5-6 months after he opened. (CP 391, ll 17-25.) Michael Mullen, Gerry Mullen's husband, was also (for a time) an agent in Mr. Fry's brokerage. (CP 392, ll 3-6.)

By 2004, before Mr. Fry sold his interest in D.C. Inc., the brokerage had acquired 12-15 agents. (CP 392, ll. 12-15.) Even though Mr. Fry took pains to describe that real estate agents are independent contractors, not employees (CP 393, ll. 2-8), he also described his relationship with his agents in traditional boss-worker terminology: "Gerry worked as an agent for me." (CP 290, l. 16.) Mr. Fry also stated:

"I'm responsible for their [the agents'] work so, you know, if anything goes kapooey, the state or any other interests would hold the broker responsible typically." Mr. Fry explained that there is only one designated broker permitted per company. (CP 394, ll. 17-18.)

While Mr. Fry was the designated broker for D.C. Inc., his agents worked as both buyers' agents and sellers' agents. Mr. Fry also started a property management division, whereby D.C. Inc. managed property for others, including collecting rents and coordinating maintenance. (CP 395, ll. 14-18.) Mr. Fry estimated that the property management division represented about 20-25 percent of D.C. Inc.'s gross income, and that the remainder of the gross income was real estate sales commissions. (CP 395-396, ll. 19-4.)

During the time that Mr. Fry was the designated broker for D.C. Inc., his agent, Gerry Mullen, entered into multiple exclusive sale and listing agreements with plaintiff, the Bert Kuty Trust, through its trustee, David Nakano. (CP 449-474.) The majority of these listing agreements were entered into in late 2004, right before Mr. Fry sold his interest in D.C. Inc. to Michael and Gerry Mullen. One of these listing agreements was for Lot D in the Country Acres subdivision, the sale of which to New Enterprise, LLC, forms the subject matter of this lawsuit.

Mr. Fry sold his interest in D.C. Inc. to the Mullens on December 31, 2004, when he left Kelso and moved to California with his wife, who had found a job down there. (CP 365; 397-398, ll. 22-6.) Mr. Fry sold D.C. Inc. to the Mullens for $105,000. (CP 396, ll. 19-22.) This represented an agreed-on price between a willing buyer and a willing seller.

> Q. And how did you come up with that figure [$105,000]?
> A. That's what we agreed on.
> Q. Mm-hmm. And was it based on the physical plant? Was it based on a book of clients, the property management division? Was it based on a book of clients in terms of buyers and seller? What went into that – what did you think about when you were coming up with a figure?
> A. Well, I wanted to leave. They were willing to pay that.

(CP 396-397, ll. 23-5.) After Mr. Fry left, Michael Mullen became the designated broker for D.C. Inc. (CP 403, l. 22.)

During the time that Mr. Fry was away, Michael and Gerry Mullen did not run D.C. Inc. very well. After returning, Mr. Fry felt that the company was headed "in the wrong direction." (CP 404, ll 1-7.) For example, the property manager that D.C. Inc. had working for it quit and left, taking with him a "bunch" of D.C. Inc.'s property management portfolio. (CP 410, ll. 18-21.) Out of the 12-15 real estate agents that had worked for Mr. Fry at the time he sold his interest to D.C. Inc., most had left. Besides Michael Mullen, the broker, there were only three agents remaining: Gerry Mullen and Larry and Janie McVicker. (CP 417-418, ll. 21-7.) Also during this time period, Gerry Mullen and the brokerage of D.C. Inc., doing business as Northwest Properties of SW Washington, committed the professional malpractice vis-a-vis the Bert Kuty Trust that forms part of the basis for the allegations in this lawsuit.[1] Finally, Mr. Fry, upon moving back up to Kelso from California, observed that D.C. Inc. had "far more debts than income could support." Fry Dep., p. 24, ll. 9-10.

Nonetheless, Mr. Fry re-joined D.C. Inc. when he returned from California to Kelso. Even though the former property manager had left and taken a bunch of clients or customers with him, a substantial amount of clients remained. Mr. Fry became the new property manager for D.C. Inc. (CP 400-401, ll. 9-11.) Mr. Fry, who had once been president of D.C. Inc., became a corporate officer again. He became D.C. Inc.'s Secretary. (CP 401, ll. 14-18.) He became the Secretary so that he could run the business while the Mullens were traveling. (CP 401, ll. 19-23.)

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[1]The plaintiff, Bert Kuty Trust, filed this lawsuit on July 2, 2008. At the time, knowing that the brokerage was called "Northwest Properties of SW Washington" (recall that D.C. Inc. did business as "Northwest Properties of SW Washington"), plaintiff erroneously named another company owned by the Mullens as a defendant, NWREP, Inc. After learning that NWREP, Inc, was not the correct company, plaintiff made a motion to dismiss NWREP from the case and to amend the complaint to name D.C. Inc. and its successor company, Columbia River Properties, Inc. The 2nd Amended Complaint naming D.C. Inc. as a defendant was filed April 19, 2010.

Mr. Fry was also a signatory on D.C. Inc.'s bank account, and it was he who signed all the payroll checks. (CP 403, ll. 1-9.) In addition to the agents – Gerry Mullen, Larry and Janie McVicker – D.C. Inc. also employed Chris Williams as a bookkeeper and Sandra Moen as a maintenance coordinator. (CP 417-418, ll. 19-4.)

Mr. Fry was aware that "creditors were continuously calling looking for money." (CP 404, ll. 13-14.) He also knew that D.C. Inc. was having "trouble meeting payroll." He also knew about this instant lawsuit. The Mullens told him about it. (CP 416-417, ll. 25-11.) The Mullens told him about it not long after he re-joined D.C. Inc., in 2009. (CP 427, ll. 6-9.)

> A. Could you restate your question again? Was I worried that your client was going to sue DC Inc.?
> Q. Yeah.
> A. It was my understanding they already had.

(CP 428, ll. 1-4.)

After returning to Kelso from California, and rejoining D.C. Inc. in his capacity as corporate officer (Secretary), the person who ran the company while the Mullens were away, property manager, and signatory on D.C. Inc.'s bank account, Mr. Fry – perhaps understandably, given his new-found knowledge of D.C. Inc.'s problems with its creditors, its difficulty meeting payroll, and the lawsuit with Bert Kuty Trust (Mr. Fry thought D.C. Inc. had already been sued), decided to start his own brokerage. (CP 404, ll. 16-18.) Mr. Fry started Columbia River Properties, Inc. (CP 404. ll. 21-22.) When Mr. Fry filled out the incorporation forms for the Secretary of State's office, he listed D.C. Inc.'s physical address as 107 Church Street in Kelso, the business address for Columbia River Properties. (CP 423-424, ll. 15-5.)

On August 1, 2009, when Columbia River Properties opened its doors, it opened them in a new location, 111 North Pacific Avenue in Kelso. (CP 405, ll. 4-6.) From the moment that Columbia River Properties started doing business, D.C. Inc. stopped doing business. Out of the three real estate agents that were working for D.C. Inc., Gerry Mullen, Larry and Janie McVickers, all three of them immediately started work at Columbia River Properties. (CP 407-408, ll. 21-13; CP 412, ll. 10-16.) There were no other agents working for Columbia River Properties when it opened its doors (during the year and five months between its incorporation and Mr. Fry's deposition, Columbia River Properties hired some other agents, at least one of whom is still working there) other than the ones from D.C. Inc. Likewise, D.C. Inc.'s bookkeeper, Chris Williams, and Sandra Moen, its maintenance coordinator, came straight from D.C. Inc. to Columbia River Properties.

(CP 417-418, ll. 16-7.) Columbia River Properties got D.C. Inc.'s old phone number and its old fax number. (CP 421-422, ll. 7-15.) Columbia River Properties also got D.C. Inc.'s old website. Save for the address change and the name change, the two websites are virtually identical. (CP 430-435.)

Not only were the agents the same, the employees the same, the phone number the same, the fax number the same, and the website the same, but a large portion of the business was the same. Mr. Fry testified that the former property manager who had left D.C. Inc. before Mr. Fry rejoined it had taken with him a "bunch" of the properties that D.C. Inc. had managed. (CP 410, l. 18.) At the time that Mr. Fry had sold his interest in D.C. Inc. to the Mullens, there were approximately 70 property management customers or clients. (CP 409-410, ll. 24-1.) During the Mullens' tenure, their property manager left and took with him a "bunch." When Mr. Fry opened up his new brokerage, Columbia River Properties, he acquired about 30 of the property management customers or clients that remained after the old property manager had taken his "bunch." (CP 411, ll. 7-13.) "The clients that came over from DC Inc., the majority of the ones that came over here were clients I had initially when I started DC Inc." (CP 419-420, ll. 23-1.) In addition to the book of property management clients or customers that he got from D.C. Inc., Mr. Fry also took the existing listings associated with the agents who had been at D.C. Inc. and had moved to Columbia River Properties. While Mr. Fry took pains, during his deposition, to emphasize how small the number of active listings there existed at D.C. Inc., and thus carried over to Columbia River Properties, he admitted that there were at least one or two active listing that he re-signed, as designated broker for Columbia River Properties. (CP 414, ll. 20-21.)

Even though Columbia River Properties took all of D.C. Inc.'s agents, D.C. Inc.'s employees, D.C. Inc.'s phone number, D.C. Inc.'s fax number, D.C. Inc.'s website, 30 of the remaining property management clients or customers (after D.C. Inc.'s former property manager made off with a "bunch" of them), and re-signed the existing listings associated with the agents who had worked for D.C. Inc., Columbia River Properties did not pay one single cent for any of these assets. (CP 419, ll. 20-21.) The Mullens had purchased Mr. Fry's interest in D.C. Inc. for $105,000. Even though the assets of D.C. Inc. had been reduced by the Mullens' tenure, they were not worth nothing, even if successorship liability is recognized.

Even though Mr. Fry was a corporate officer, a Secretary, at D.C. Inc., he testified that he took no interest nor was involved in D.C. Inc.'s winding-up procedures. (CP 405, ll. 7-21.) As Secretary, he signed no articles of dissolution. He did not learn of the disposition of corporate assets. (CP 405-406, ll. 24-1.) He did not receive copies of any articles of dissolution. (CP 406, ll. 2-4.) Mr. Fry, as corporate Secretary, simply did not undertake or involve himself in the winding-up procedures. (CP 406, ll. 8-20.) Even though Mr. Fry knew that there were creditors and claimants, he did not work on making sure that they all got paid. (CP 407-408, ll. 21-7.)

In declaration, Mr. Fry declared: "When I sold all my shares of D.C., Inc. to Michael and Gerry Mullen in 2004, they gave me a promissory note in payment. A substantial amount remained due on that note when they were discharged in bankruptcy in July of 2009." (CP 365, ¶ 9.) Mr. Fry also declared: "In early 2009, I returned to Washington and was hired by D.C., Inc. to run their real property management operation. I was an at-will employee and did not acquire any ownership interest in D.C., Inc." (CP 365, ¶ 10.)

Michael and Gerry Mullen filed bankruptcy on March 23, 2009. Their case, Re Michael L. Mullen and Geraldine R. Mullen, No. 09-41903-PBS (Bankr. W.D. Wash. Nov. 5, 2009), is viewable online on the CM/ECF system (requires a login and password) of the U.S. Bankruptcy Court for the Western District of Washington. Both Michael and Gerry Mullen were discharged in bankruptcy on July 2, 2009. Before that, on April 16, 2009, Michael and Gerry Mullen filed their "Debtor's Balance of Schedules," Docket Number 12 in the Mullen bankruptcy case. (CP 536-542). At CP 542, the Mullens electronically signed the Statement of Financial Affairs. At CP 538, the Mullens were asked: "**5. Repossessions, foreclosures and returns:** List all property that has been repossessed by a creditor, sold at a foreclosure sale, transferred through a deed in lieu of foreclosure or returned to the seller, within **one year** immediately preceding the commencement of this case." The Mullens answered, "NAME AND ADDRESS OF CREDITOR OR SELLER: Chris Fry, 107 Church Street, Kelso, WA, 98626; DATE OF REPOSSESSION, FORECLOSURE SALE, TRANSFER OR RETURN: 01/15/09; DESCRIPTION AND VALUE OF PROPERTY: Northwest Properties Inc." Recall that D.C. Inc. did business as "Northwest Properties of SW Washington." Therefore, the Mullens, as of January 15, 2009, returned to Mr. Fry all the ownership interest in D.C. Inc. that he had sold to them in 2004.

Mr. Fry thus possessed complete ownership of D.C. Inc. when D.C. Inc. transferred its assets for zero consideration to Mr. Fry's new company (which he also wholly owns), Columbia River Properties, which opened its doors on August 1, 2009.

IV. SUMMARY OF ARGUMENT

The Bert Kuty Revocable Living Trust sold an undeveloped piece of residential real property to New Enterprise, LLC, for a total purchase price of $80,000 accepting a partial cash payment and a promissory note secured by a second position deed of trust for the remainder. It was represented to the Bert Kuty Trust that the only way New Enterprise could get financing to develop the property was by getting a "Speculative Construction Loan Agreement," from LeGrand Investments, LLC, secured by a first position deed of trust, for an amount -- $238,000 -- that far exceeded the total purchase price of the property. After the deal was concluded, and after making an initial $40,000 disbursement under the agreement, LeGrand Investments immediately sold their note and deed of trust to a couple named Robert and Daniele Hayes for that same $40,000. When the buyer defaulted on the note, Mr. and Mrs. Hayes foreclosed and caused the property to be sold at trustee's sale. Mr. and Mrs. Hayes bid in their note and deed of trust, which both had a face value of $238,000, at the sale and ended up purchasing the property for $238,000 but with only having actually paid $40,000 for a property worth $80,000. The Bert Kuty Trust, holding the second position deed of trust, was left with nothing, since Mr. and Mrs. Hayes did not account for the $238,000 that they bid at the sale, only for the $40,000 with which they bought the note and deed of trust from LeGrand.

Meanwhile, the Bert Kuty Trust had filed this lawsuit, alleging an equity stripping scheme, and adding, in a subsequent complaint, an unjust enrichment claim. Mr. and Mrs. Hayes brought two motions for partial summary judgment. The Trial Court granted both motions, dismissing all of the Bert Kuty Trust's claims as to Mr. and Mrs. Hayes. These were not claims and this was not a case that was amenable to summary judgment, since many of the facts alleged were particularly within the knowledge of the defendants, and it was error for the Trial Court to grant summary judgment here. Further, the Trial Court ignored the undisputed evidence of the face value of the note and first position deed of trust. Finally, the Trial Court awarded sanctions of attorney fees against the Bert Kuty Trust under CR 11 and RCW 4.84.185, even though there was a basis in fact and law for the Bert Kuty Trust's claims, and awarded the fees without conducting a lodestar analysis. This was error.

The Bert Kuty Trust had also named its real estate brokerage, D.C. Inc. d/b/a Northwest Properties of SW Washington, as a defendant, since its real estate agent, Gerry Mullen, had committed professional malpractice in encouraging and recommending that the Bert Kuty Trust accept the financing arrangement and the second position deed of trust. The Bert Kuty Trust obtained an order of default against D.C. Inc., and then, at trial, a default judgment. However, this victory was hollow in that D.C. Inc. had closed its doors and then reopened them as an entity called Columbia River Properties, Inc. The Bert Kuty Trust amended its complaint to allege successor liability against Columbia River Properties. In response to Columbia River Properties' motion for summary judgment, the Bert Kuty Trust showed that Columbia River properties had acquired the assets and pending contracts of D.C. Inc., had paid no consideration, had taken on the employees of D.C. Inc., had continuity of ownership with D.C. Inc., had continued the business of D.C. Inc., and had actual knowledge of the Bert Kuty Trust's claims, but the Trial Court granted summary judgment to Columbia River Properties, ignoring caselaw and binding precedent. This, too, was error.

V. ARGUMENT

A. **The Standard of Review is de Novo**

When reviewing an order granting summary judgment, the Court of Appeals engages in the same inquiry as the Trial Court. Failor's Pharmacy v. DSHS, 125 Wn.2d 488 at 493, 886 P.2d 147 (1994). The Court of Appeals will affirm the summary judgment only if there are no genuine issues of material fact between the parties and only if, on the undisputed facts, the moving party is entitled to judgment as a matter of law. Id. All facts and all reasonable inferences from those facts are considered in the light most favorable to the party resisting summary judgment. Id. The burden is on the party moving for summary judgment to demonstrate that there is no genuine dispute as to any material fact. Morris v. McNicol, 83 Wn.2d 491 at 494, 519 P.2d 7 (1974). Summary judgment is sustainable on review only if reasonable minds could reach but one conclusion from the evidence, and only if the conclusion thus reached entitles the moving party to a judgment in its favor. Failor's Pharmacy at 493.

"When a trial court rules as a matter of law, it must accept the [non moving party's] evidence as true, and determine whether or not the [non-moving party] has a prima facie case." Spring v. Department of Labor and Industries, 96 Wn.2d 914, 918, 640 P.2d 1 (1982). The trial court should not make factual determinations or evaluate the non-moving party's evidence, except as may be necessary to favorably resolve conflicts appearing therein. *See* Spring v. Dept. L&I, 96 Wn.2d at 918.

"If affidavits and counter-affidavits submitted by the parties conflict on material facts, the court is essentially presented with an issue of credibility, and summary judgment will be denied." Tegland and Ende, *Washington Handbook on Civil Procedure*, § 69.16, p. 428 (2004 ed.). "[T]he court should not grant summary judgment when there is some question on the credibility of a witness whose statements are critical to an important issue in the case." *See* Id., *citing to* Powell v. Viking Insurance Col, 44 Wn. App. 495, 722 P.2d 1343 (1986).

There is almost never a case in which the actions of a party are so unambiguous that reasonable persons could reach only one conclusion as to that party's knowledge, intent or motivations.

> Where intent is the primary issue, summary judgment is generally inappropriate. Drawing inferences favorably to the nonmoving party, summary judgment will be granted only if all reasonable inferences defeat the plaintiff's claims. The moving party's burden is therefore a heavy one.

Admiralty Fund v. Tabor, 677 F.2d 1297 at 1298 (Ninth Cir. 1982).

Summary judgment is not appropriate "where a trial, with its opportunity for cross-examination and testing the credibility of witnesses, might disclose a picture substantially different from that given by the affidavits." United States v. Perry, 431 F.2d 1020 at 1023 (Ninth Cir. 1970).

This principle has been thoroughly and articulately explained in a series of cases from the Second Circuit:

> Summary judgment has been found to be notoriously inappropriate in cases such as this one in which judgment is sought "on the basis of 'the inferences which the parties seek to have drawn [as to] questions of motive, intent, and subjective feelings and reactions.

Litton Industries Credit v. Plaza Super of Malta, 503 F. Supp. 83 at 86 (N. D. NY 1980).

The rationale is that "[d]ealving into the internal workings of the parties' minds and making credibility assessments is within the special province of the trier of fact." First Amercan Title Co. v. Politano, 932 F. Supp. 631 at 635 (1996). "[I]ntent can rarely be established by direct evidence, and must often be proven circumstantially and by inference. Intent is therefore peculiarly inappropriate to be decided on a motion for summary judgment." Zilg v. Prentice-Hall, 515 F. Supp. 716 at 719 (S. D. NY 1981). "Leaving issues of assessing credibility to juries or fact-finders is particularly important when conflicting inferences about a party's knowledge can be deduced from the evidence." Politano, at 635.

> It is obvious that this evidence must come largely from the defendants. This case illustrates the danger of founding a judgment in favor of one party upon his own version of the facts within his sole knowledge as set forth in affidavits prepared *ex parte*. Cross-examination of the party and a reasonable examination of his records by the other party frequently bring forth further facts which place a very different light upon the picture. This is not the kind of case that can be settled on summary judgment. It is peculiarly the kind of case where the triers of fact whose business is not only to hear what men say but to search for and find the roots from which the sayings spring, should be afforded full opportunity to determine the truth and integrity of the case.

Subin v. Goldsmith, 224 F.2d 753 (Second Cir. 1955) (citations omitted).

With regard to a party's knowledge or intent, it is usually the case that the nonmoving party need not even file counter affidavits disputing moving party's allegations. Subin, at 759. The other facts of the case, even without restatement in affidavit form, almost always support a wide range of inferences regarding knowledge and intent. This Federal analysis has been specifically cited and adopted in Washington. Percival v. Bruun, 28 Wn. App. 291, 293-94, 622 P.2d 413 (1991).

This rule about mental states is an extension of a more general limitation on summary judgments. Courts, at summary judgment hearings, should not resolve issues of credibility, and if such an issue is present the motion should be denied. Hudesman v. Foley, 73 Wn.2d 880, 887, 441 P.2d 532 (1968). "We are reluctant to grant summary judgment when "material facts are particularly within the knowledge of the moving party." Riley v. Andres, 107 Wn. App. 391, 395, 27 P.3d 618 (2001). In such cases, the matter should proceed to trial "in order that the opponent may be allowed to disprove such facts by cross-examination and by the demeanor of the moving party while testifying." Mich. Nat'l Bank v. Olson, 44 Wn. App. 898, 905, 723 P.2d 438 (1986)." Arnold v. Saberhagen Holdings, Inc., 157 Wn. App. 649, 661-62, 240 P.3d 162 (2010) *review denied*, 171 Wn.2d 1012, 249 P.3d 1029 (2011).

On these principles, the summary judgment orders under appeal here are improper and should be reversed by this Court with a remand for such further proceedings as are necessary.

B. **There is a Triable Case on the Bert Kuty Trust's Accounting Claim.**

Regardless of any defense Hayes has to the Bert Kuty Trust's claims against him (for participation in the civil conspiracy), and regardless of any defense Hayes has to the Bert Kuty Trust's claim seeking restoration of title (after voiding of the fraudulent transaction), Hayes has an obligation to account for the proceeds of the foreclosure sale and to pay over any amount left after payment of the costs of sale and the note secured by its first position deed of trust.

In this case, the foreclosure price was the face amount of the first deed of trust ($238,000). Additionally, the foreclosure was based on the tender of the deed of trust (not the underlying promissory note). Thus, the price realized at the foreclosure sale was $238,000, which Mr. Hayes promised to pay. He intended that this entire amount go to him to discharge the obligation he was owed. However, he was only owed $40,000, so a full tender of the auction price would have resulted in a surplus of nearly $200,000, more than enough to pay the Bert Kuty Trust deed of trust.

This surplus should have been accounted for and paid to the county clerk for payment on to the Bert Kuty Trust. It was not. This is a separate defect in the sale, arising from the sale. As a right that arose only at and after the foreclosure sale, Bert Kuty has not waived its right to assert a claim to the surplus proceeds of the sale merely because it did not seek to enjoin the sale.

The Value of the Note

Promissory notes can be set up in two ways. Either the note indicates an indebtedness of a specified amount, or it represents an open-ended account.

If it represents an open-ended account, its terms must reflect that by stating that the amount of the debt is "whatever amount may be advanced to debtor from time to time." Such an open-ended account may also state an upper limit of the indebtedness, such as a credit card limit. These notes are worth whatever has been advanced and have no face value.

Other notes represent specific amounts due, and state the amount of the note as a principal sum. These notes have a face value, which is shown on the face of the note. These amounts can be reduced when paid down, but remains as the stated value of the note unless paid down.

The note in this case has a face value of $238,000, which appears on its face. On its own terms, "FOR VALUE RECEIVED, the undersigned New Enterprise, LLC (a Washington Limited Liability Company) ("Makers") promise to pay in lawful money of the United States of America, to the order of Legrand Investments, LLC ("Lender") [Hayes's predecessor in interest], the principal sum of Two Hundred Thirty Eight Thousand & 00/100 Dollars ($238,000), with interest on the unpaid principal balance at a rate of Twenty percent (20%) per annum ..." (CP 146.) These terms state an absolute obligation to pay the full sum of the note – and do not set or purport to set an upper limit on an unfunded open account.

This note is secured by a deed of trust, which on its terms reiterates the face amount of the note as an absolute present obligation, rather than as the upper limit of an open account. "This deed is for the purpose of securing performance of each agreement of the grantor herein contained, and payment of the Sum of $238,000 (Two Hundred Thirty Eight Thousand and 00/100 dollars) with interest, in accordance with the promissory note of even date herewith…" (CP 149.)

The note represents an absolute obligation to pay $238,000 plus interest. No payments were made. Therefore, the note and deed of trust were worth at least $238,000 when tendered as payment at the foreclosure sale.

The Price at the Foreclosure Sale

Hayes and his counsel admit that "[a]lthough the Hayes's had no obligation to do so, they directed that the entire outstanding balance be credited as their initial bid at the sale." (CP 278.) Thus, the amount paid at the foreclosure sale was the outstanding balance on the note. The outstanding balance on the note was its stated value ($238,000) plus interest and penalties, because no payments had been made on the note.

As observed by Hayes's counsel, Mr. and Mrs. Hayes could have tendered a cash payment less than the value of the note (which would have resulted in a payment to Hayes of the full foreclosure price, leaving Hayes with a balance due on the note). Alternatively, Hayes could have tendered in part of the indebtedness, purchasing the property in exchange for a partial satisfaction of the note. However, Hayes did neither thing. Rather, Hayes tendered in the note for its full value – resulting in a foreclosure price of more than $238,000.

Post-Sale Apportionment of Proceeds

After the sale, essentially as a book-entry, Hayes accounted for just over $48,000 of the $238,000 purchase price, leaving $198,000 in sale proceeds unaccounted for. (CP 168-172; CP 284; CP 301.) Hayes repaid himself the amount he paid for the note, but did not otherwise account for any of the remaining value of the note, which he tendered in full as the consideration at the foreclosure sale. Mr. and Mrs. Hayes, through their agent and trustee Michael Johns, has an obligation to account for all the proceeds of the foreclosure sale and to pay over any amount left after payment of the costs of sale and the note secured by its first position deed of trust.

RCW 61.24.080 sets forth the trustee's duties in regard to distributing any surplus funds after the nonjudicial foreclosure sale. The trustee first applies the funds to satisfy the expenses of the foreclosure. RCW 61.24.080(1). The trustee then satisfies the obligation secured by the foreclosing deed of trust. RCW 61.24.080(2). After that, the trustee must deposit any surplus in the clerk's registry of the superior court in the county where the foreclosure sale occurred. RCW 61.24.080(3). The trustee is required to provide notice of the remaining surplus to "each party to whom the notice of trustee's sale was sent pursuant to RCW 61.24.040(1)." RCW 61.24.080(3). The trustee is additionally required to record the notice and provide a copy to the court clerk. RCW 61.24.080(3).

After the trustee deposits the surplus, the court clerk indexes it under the grantor's name and may not disburse any funds absent a superior court order. RCW 61.24.080(3). Although the Act does not outline the procedure to obtain such an order, it does specify that, "[i]nterests in, or liens or claims of liens against the property eliminated by sale under this section shall attach to the surplus in the order of priority that it had attached to the property." RCW 61.24.080(3). This plain language states that the priority liens on the property attach to the surplus in the same priority order they attached to the property. This process was not followed here.

In this case, the foreclosure price was the face amount of the first deed of trust ($238,000) plus interest. Hayes "directed that the entire outstanding balance be credited as their initial bid at the sale." (See Declaration of Michael Johns in support of the Hayes's second Motion for Summary Judgment, dated 12/25/08.) Thus, the price realized at the foreclosure sale was $238,000. However, the amount claimed as due in the advertisement, including interest and other charges, was only $63,724.62 (of which only $48,775.57 was claimed as principal debt plus ordinary interest). (CP 169-172.) This left a substantial surplus that has yet to be accounted for or disbursed, and which, if accounted for and disbursed, would pay the debt owed to the Bert Kuty Trust.

This surplus should have been accounted for and paid to the county clerk for payment on to the Bert Kuty Trust. It was not. This Court should rule as a matter of law that the foreclosure sale price was at least $238,000, on Hayes's own admission, of which only $63,734.62 has been accounted for. Then this Court remand this case to the Trial Court for Trial on Bert Kuty's claim for an accounting of the remaining $198,000 in foreclosure proceeds.

C. <u>**There is a Triable Case on Bert Kuty Trust's Unjust Enrichment Claim.**</u>

Bert Kuty's Trust claim primarily involves the fraudulent transaction by which it was induced to sell the property to New Enterprise. The Bert Kuty Trust sought damages under a theory of "civil conspiracy." Civil conspiracy requires proof that (1) two or more people combined to accomplish an unlawful purpose or to accomplish an unlawful purpose by lawful means, and (2) the conspirators entered into an agreement to accomplish the conspiracy. <u>Newton Ins. Agency & Brokerage, Inc. v. Caledonian Ins. Group, Inc.,</u> 114 Wn. App. 151 at 160, 52 P.3d 30 (2002) (citing to <u>Allstar Gas, Inc. v. Bechard</u>, 100 Wn. App. 732 at 740, 998 P.2d 367 (2000). This claim would provide for joint and several liability among all defendants shown to have been involved in the civil conspiracy. <u>Sterling</u>

Business Forms, Inc. v. Thorpe, 82 Wn. App. 446 at 454, 918 P.2d 531 (1996).

The specific civil conspiracy claimed in this case involves an equity stripping scheme. In the context of home sales, such schemes are specifically prohibited by statute. RCW 61.34. The mechanism and harm of such schemes is well described in the Legislative Finding to support the Act.

> The legislature finds that persons are engaging in patterns of conduct which defraud innocent homeowners of their equity interest or other value in residential dwellings under the guise of a purchase of the owner's residence but which is in fact a device to convert the owner's equity interest or other value in the residence to an equity skimmer, who fails to make payments, diverts the equity or other value to the skimmer's benefit, and leaves the innocent homeowner with a resulting financial loss or debt.

RCW 61.34.010.

Civil conspiracy claims are generally not appropriately resolved on summary judgment.

> To establish liability for conspiracy, it is sufficient if the proof shows concert of action or other facts and circumstances from which the natural inference arises that the unlawful overt act was committed in furtherance of a common design, intention, and purpose of the alleged conspirators. In other words, circumstantial evidence is competent to prove conspiracy. Lyle v. Haskins, 24 Wn.2d 883, 899, 168 P.2d 797 (1946) (quoting 11 Am.Jur. 585 § 56). See also Accurate Products, Inc. v. Snow, 67 Wn.2d 416, 425, 408 P.2d 1 (1965). Since direct evidence of a conspiracy is ordinarily in the possession and control of the alleged conspirators and is seldom attainable, a conspiracy

> is usually susceptible of no other proof than that of circumstantial evidence. Lyle, 24 Wn.2d at 900, 168 P.2d 797.
>
> The liability of conspirators is joint and several. That is, each is liable for all acts committed by any of the other parties, either before or after their entrance, in furtherance of the common design. Id. at 900, 168 P.2d 797. Here, the entire alleged conspiracy should be placed before the finder of fact, because although the finder of fact must base its decision on clear and convincing evidence, it could find that [the Defendant] participated in a conspiracy. That determination will require weighing of the evidence, credibility determinations and the drawing of legitimate inferences from the facts.

Sterling Bus., 82 Wn.App. at 454.

Bert Kuty Trust's cause of action arose during the original sale. The foreclosure of the property establishes damages (by computing the harm to the Bert Kuty Trust that was set up by the original fraudulent inducement in the original transaction), but does not otherwise operate in the Bert Kuty Trust's claim. Because liability (as opposed to damages) is unrelated to and predates the foreclosure on the first deed of trust held by Defendant Hayes, that claim is not waived or otherwise invalidated by the foreclosure.

However, after denial of Hayes' first Motion for Summary Judgment seeking dismissal of the civil conspiracy claim, but before the second motion, two critical litigation events occurred. First, the Bert Kuty Trust amended its Complaint to add a fall-back, unjust enrichment theory against the Hayes. Second, the Bert Kuty Trust learned new information that cast in doubt (but did not disprove or rebut) the assertion that the Hayes were active participants in the equity stripping scheme.

The elements of unjust enrichment are: "(1) the defendant receives a benefit, (2) the received benefit is at the plaintiff's expense, and (3) the circumstances make it unjust for the defendant to retain the benefit without payment." Young v. Young, 164 Wn.2d 477 at 484-485, 483, 191 P.3d 1258 (2008). "Unjust enrichment occurs when one retains money or benefits which in justice and equity belong to another." Young, 164 Wn.2d at 484, *quoting* Bailie Commc'ns, Ltd. v. Trend Bus. Sys., Inc., 61 Wn. App. 151, 160, 810 P.2d 12 (1991). The Unjust Enrichment claim is based on the same accounting arithmetic as the Accounting claim. The Hayes received an asset (the property) which the Bert Kuty Trust lost through a fraud, and the Hayes received that asset for $40,000 despite its being worth more than six times that amount.

As with the Accounting claim, this claim presents triable issues distinct from the underlying fraud. An innocent person who receives a windfall as a result of a third-party's fraud still receives an ill-gotten windfall and has been unjustly enriched. Such a person is not entitled to benefit at the expense of another and must disgorge the gain.

D. The Court Erred in Awarding Fees.

> The signature (on a pleading or other filed document) of a party or of an attorney constitutes a certificate by the party

> or attorney that the party or attorney has read the pleading, motion, or legal memorandum; that to the best of the party's or attorney's knowledge, information, and belief, formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. .... If a pleading, motion, or legal memorandum is signed in violation of this rule, the court, upon motion or upon its own initiative, may impose upon the person who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the pleading, motion, or legal memorandum, including a reasonable attorney fee.

CR 11, *in* relevant part.

> In any civil action, the court having jurisdiction may, upon written findings by the judge that the action, counterclaim, cross-claim, third party claim, or defense was frivolous and advanced without reasonable cause, require the nonprevailing party to pay the prevailing party the reasonable expenses, including fees of attorneys, incurred in opposing such action, counterclaim, cross-claim, third party claim, or defense.

RCW 4.84.185

The basic standard under both these rules is substantially identical. A legal action is frivolous if a reasonable inquiry would show that the action is it is not "well grounded in fact and is [not] warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, [or] that it is [] interposed for any improper purpose."

"The purpose behind CR 11 is to deter baseless filings and curb abuses of the judicial system." Bryant v. Joseph Tree, Inc., 119 Wn. 2d 210, 219, 829 P.2d 1099 (1992.) "Complaints which are 'grounded in fact' and 'warranted by existing law of a good faith argument for the extension, modification, or reversal of existing law' are not 'baseless' claim, and are therefore not the proper subject of CR 11 sanctions." Joseph Tree at 219-220. CR 11 "is not intended to chill an attorney's enthusiasm or creativity in pursuing factual or legal theories." Joseph Tree at 219. Indeed, an imposition of CR 11 sanctions is "not a judgment on the merits of the action," but rather "the determination of a collateral issue: whether the attorney has abused the judicial process." Biggs v. Vail, 124 Wn2d 193, 197, 876 P.2d 448 (1994) (Biggs II), quoting Cooter & Gell v. Hartmax Corp., 496 U.S. 384 at 396, 110 S. Ct. 2447, 110 L.Ed.2d 359 (1990). Washington courts reserve CR 11 sanctions "for egregious conduct" and prohibit sanctions from being used "as simply another weapon in a litigator's arsenal." Biggs II, 124 Wn.2d 193 at 198, n.2.

RCW 4.84.185 operates similarly to CR 11, but with an additional limitation. The Washington Supreme Court has held that "[t]he lawsuit ..., *in its entirety*, must be determined to be frivolous and to be advanced without a reasonable cuase before an award of attorney's fees may be made pursuant to the frivolous lawsuit statute, RCW 4.84.185." Biggs v. Vail, 119 Wn.2d 129, 133, 830 P.2d 350 (1992) (Biggs I). In any claim in a lawsuit has potential merit, the action may not be deemed frivolous.

Tiger Oil Corp v. Dept of Licensing, 88 Wn. App. 925, 938, 946 P.2d 1235 (1997).

Civil conspiracy and fraud are recognized causes of action in the State of Washington. Fraud is an intentional tort, which provides for joint and several liability of all participants. Civil conspiracy allows the Court to spread responsibility to key participants in the fraud even if those participants did not have "face-time" with their victim. Civil conspiracy requires proof that (1) two or more people combined to accomplish an unlawful purpose or to accomplish an unlawful purpose by lawful means, and (2) the conspirators entered into an agreement to accomplish the conspiracy. Newton Ins.,114 Wn. App. at 160, (citing to Allstar Gas, 100 Wn. App. at 740. A claim for civil conspiracy would provide for joint and several liability among all defendants. Sterling Bus., 82 Wn. App. at 454.

Similarly, Bert Kuty's claims for accounting and unjust enrichment (as argued above) are well-recognized causes of action in Washington under these circumstances. Again, as argued above, far from being frivolous, these claims are meritorious, triable claims and should be reinstated on remand for trial.

Finally, Hayes asserts that Bert Kuty Trust's final claim against the Hayes – for a writ of rescission returning the property to the Bert Kuty Trust is frivolous, even if no other claims are, because the Bert Kuty Trust did not act to enjoin the foreclosure and therefore the rescission claim was legally barred upon the completion of the foreclosure sale under CHD, Inc. v. Boyles, 138 Wn. App. 131 at 137, 157 P.3d 415 (2007). However, this argument fails to account for the timing of the Complaint, which was filed *before* the foreclosure sale (filed July 2, 2008; CP 1-8) while the foreclosure sale did not occur until July 25, 2008 (CP 166). Because the foreclosure sale had not occurred at the time the Complaint was filed, it could not have the effect of making that Complaint frivolous.

Even if the foreclosure sale had such retroactive effect, Bert Kuty had a fair argument for the modification of existing law. This case involves a fraud in the form of an equity stripping scheme. The Legislature has weighed in on such schemes in the residential home context and has provided specific remedies in such context. The Bert Kuty trust claim was based on the argument that the equities and injustices recognized by the Legislature in the situation of equity stripping from a home apply equally outside the personal residence context, and that these equities support a modification, even a reversal, of the law prohibiting parties from contesting their loss of real property following a foreclosure sale. This is a fair argument for modification of the existing law. Even if the Bert Kuty Trust were ultimately unsuccessful, it should not be penalized for the attempt to extend the prohibition of equity skimming fraud beyond the home-owner context (here, the lot was undeveloped residential property).

Further, Bert Kuty's counsel carried out an elaborate pre-filing investigation of this matter before filing the Complaint. The details of that investigation, and the facts revealed in the investigation, are set forth in the Declaration of Ben Cushman in Opposition to the Motion for Fees (CP 333-338). Those facts sustain a probable, nonfrivolous claim against all the defendants, including the Hayes, at the time the complaint was filed. While it is true that additional evidence, which tended to cast doubt on the liability of Mr. Hayes as a participant in the fraud and civil conspiracy came to light after the filing of this case, that evidence cannot retroactively make a nonfrivolous claim into a frivolous one, especially as the Bert Kuty Trust acted promptly to modify the lawsuit in light of the new information. (CP 337.)

E. Lack of Proper Lodestar Analysis

Washington's Supreme Court set forth the process by which trial judges may set reasonable attorneys' fees. Bowers v. Transamerica Title Ins. Co., 100 Wn.2d 581, 675 P.2d 193 (1983). This process, the "lodestar method," incorporates the twelve factors that are based on guidelines for private fee arrangements set forth in the Model Rules of Processional Conduct (1982). 100 Wn.2d at 595-96. These factors are:

> (1) the time and labor required; (2) the novelty and difficulty of the questions; (3) the skill requisite to perform the legal services properly; (4) the preclusion of other employment; (5) the customary fee in the community for similar work; (6) the fixed or contingent nature of the fee; (7) time limitations imposed by the client or the circumstances; (8) the amount involved and results obtained; (9) the experience, reputation, and ability of the attorneys; (10) the undesirability of the case; (11) the nature and length of the professional relationship with the client; and (12) awards in similar cases.
>
> *Id.* at 596.

The lodestar method incorporates these twelve factors into an analytical framework that "can be easily applied by trial judges and that will make possible meaningful appellate review." *Id.*

The application of the lodestar method necessarily begins with a lodestar figure – the number of hours reasonably expended in the litigation. 100 Wn.2d at 597. "The Court must limit the lodestar to hours reasonably expended, and should therefore discount hours spent on unsuccessful claims, duplicated effort, or otherwise unproductive time." *Id.* Next, the Court multiplies this lodestar figure by a reasonable hourly rate of compensation. In calculating the reasonably hourly rate, the Court may consider, in addition to the attorney's usual billing rate, relevant factors enumerated above. *See id.* at 596, 597. Finally, after multiplying a reasonable number of hours by a reasonable hourly rate, the court may consider adjusting the dollar amount to reflect either or both of two broad categories: the contingent nature of success and the quality of work performed. *Id.* at 597. (Here, the attorneys have not indicted in their declarations that they had entered into contingent fee agreements with their clients. "The contingent nature of success" is therefore likely inapplicable.)

This analysis should be done by the party seeking fees, and should be accepted, rejected, or modified by the Court after argument.

In this case, neither the Hayes in their moving papers, nor the Trial Court, in its ruling and subsequent order, used a lodestar analysis. The moving papers merely recite the amount of fees charged, attaching billings, without providing any back-up lodestar analysis. (CP 313-326) The Order Granting Fees (CP 340-344) does not evaluate the amount of fees incurred, the reasonableness of those fees, or provide any other reviewable analysis. This was error. Even if Mr. and Mrs. Hayes were entitled to an award of fees, which they are not, they are not entitled to an award of fees unless there is a reviewable analysis supporting the amount of fees awarded.

F. The Court Erred in Dismissing Successorship Claims Against Columbia River Properties

D.C. Inc., the real estate brokerage company where real estate agent Gerry Mullen worked and committed her professional malpractice against Bert Kuty Trust, has closed its doors. When D.C. Inc. was in its winding-up period, it failed to make provision for the claims of the Bert Kuty Trust. Instead, it divested itself of all its assets – its business good-will, its internet website, its book of property management clients or customers, its real estate agents, the existing listings at the time of the transfer of assets, its telephone number and its fax number – to Columbia River Properties, who knew about the Bert Kuty Trust claims, for no consideration. Therefore, the exceptions that exist for the protection of creditors like the Bert Kuty Trust apply: Columbia River Properties is *not* a bone fide purchaser who gives adequate consideration and who lacks notice of prior claims against the property. *See* Hall v. Armstrong Cork, Inc., 103 Wn.2d 258, 261, 692 P.2d 787 (1984). This Court should impose successor liability on Columbia River Properties.

As a general rule, a corporation purchasing the assets of another corporation does not, by reason of the purchase of assets, become liable for the debts and liabilities of the selling corporation. *See* Hall, 103 Wn.2d at 261. "The courts have recognized, however, that the traditional rule allows a transferring corporation, under certain circumstances, to effectively avoid its obligations to the detriment of *creditors* and minority *shareholders*." Martin v. Abbott Laboratories, 102 Wn.2d 581, 609, 689 P.2d 368 (1984) (emphasis in original). (Here, the Bert Kuty Trust is in the position of one of D.C. Inc.'s creditors. The Bert Kuty Trust has obtained a default judgment against D.C. Inc. for the professional malpractice of its real estate agent, Gerry Mullen.)

However, there are four exceptions to the traditional rule that exist for the protection of creditors like the Bert Kuty Trust: "(1) the purchaser expressly or impliedly agrees to assume liability; (2) the purchase is a *de facto* merger or consolidation; (3) the purchaser is a mere continuation of the seller; or (4) the transfer of assets is for the fraudulent purpose of escaping liability." Hall, 103 Wn.2d at 262; Martin, 102 Wn.2d at 609. "The basis of this traditional corporate law doctrine is that a sale of corporate assets transfers an interest separable from the corporate entity and does not result in a transfer of unbargained-for liabilities from the seller to the purchaser. Rather, the purchasing corporation receives the protection accorded any purchaser of property: the bona fide purchaser *who gives adequate consideration and who lacks notice of prior claims against the property acquires no liability for those claims*." Hall, 103 Wn.2d at 262. Here, D.C. Inc. has given all its assets – its business good-will, its internet website, its book of property management clients or customers, its real estate agents, the existing listings at the time of the transfer of assets, its telephone number and its fax number – to Columbia River Properties for *no* consideration. Further, here Columbia River Properties knew of the liabilities of D.C. Inc. when it took on D.C. Inc.'s assets and took over and continued D.C. Inc.'s business operations.

Columbia River Properties is a mere continuation of D.C. Inc. This Court has adopted a relatively simple test for determining whether one business entity is a "mere continuation" of another: (1) common identity of the officers, directors, and stockholders in the selling and purchasing companies and (2) whether there is sufficient consideration running to the seller. Eagle Pacific Ins. Co. v. Christensen Motor Yacht Corp., 85 Wn. App. 695, 706, 934 P.2d 715 (1997).

Here, before Michael and Gerry Mullen filed for bankruptcy, Chris Fry – the man who had sold the Mullens his interest in D.C. Inc. – repossessed the interest in D.C. Inc. that the Mullens had purchased from him on a promissory note. Mr. Fry was therefore the sole shareholder of D.C. Inc. after repossessing the company (Mr. Fry's testimony that he did not re-acquire shares in D.C. Inc. when he returned to Washington is simply not credible, in light of the Mullens' bankruptcy filing). Likewise, Mr. Fry is the sole shareholder of Columbia River Properties. Mr. Fry was the Secretary of D.C. Inc. and is the President of Columbia River Properties. Mr. Fry, who testified that he was running D.C. Inc. while the Mullens were away, was a "director" of D.C. Inc. (Black's defines "director" as "one who manages, guides, or orders; a chief administrator"). Mr. Fry is also the director of Columbia River Properties. There is therefore common identity of the officers, directors, and stockholders in D.C. Inc. and Columbia River Properties. The first element of the this Court's two-factor test is fulfilled.

The second element is whether there was sufficient consideration. Here, Mr. Fry testified that he sold his interest in D.C. Inc. to the Mullens for $105,000, but that he paid nothing – zero – for the assets of D.C. Inc. (its business good-will, its internet website, its book of property management clients or customers, its real estate agents, the existing listings at the time of the transfer of assets, its telephone number and its fax number) that were transferred to Columbia River Properties in 2009. Now, in Columbia River Properties' There was no consideration at all, let alone *sufficient* consideration. The second element is fulfilled.

Because Columbia River Properties is a mere continuation of D.C. Inc., and D.C. Inc. is liable to the Bert Kuty Trust, the Trial Court erred in excusing Columbia River Properties from that liability. This Court should reverse and remand this matter to the Trial Court with direction that the Trial Court enter judgment against Columbia River Properties as co-debtor on the judgment against its predecessor, D.C. Inc.

VI. CONCLUSION

This is a case where the Bert Kuty Trust deserved to have its claims tried by the trier of fact, not dismissed on summary judgment. The facts that were undisputed supported the Bert Kuty Trust's claims; the facts that were disputed were particularly within the knowledge of the various defendants, requiring that an assessment of credibility and demeanor be made. This Court should reverse and remand the case for trial.

SUBMITTED this 23rd day of April, 2012.

CUSHMAN LAW OFFICES, P.S.

Ben D. Cushman, WSBA #26358
Attorney for Appellant

CERTIFICATE OF SERVICE

I declare under penalty of perjury according to the laws of the State of Washington, that on the date signed below, I caused the foregoing document to be filed with this Court, and emailed and mailed to opposing counsel indentified below:

DATED this 23rd day of April, 2012.

Jennifer Harkins, Legal Assistant

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BY ______ DEPUTY

Mon 4/23/2012 3:52 PM

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