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NO. 77708-0

SUPREME COURT
OF THE STATE OF WASHINGTON

Court of Appeals No. 22764-2-III

Court of Appeals No. 23239-5-III

Cashmere Valley Bank, a Washington corporation,

Respondent

v.

Terry B. Brender, a single man,

Petitioner

SUPPLEMENTAL BRIEF OF RESPONDENT
CASHMERE VALLEY BANK

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I. ASSIGNMENT OF ERROR

Whether the Court of Appeals correctly affirmed Chelan County Superior Court's dismissal of Terry B. Brender's ("Brender") Truth in Lending Act ("TILA") counterclaim and affirmative defense.

II. STATEMENT OF CASE

Cashmere Valley Bank's (the "Bank") Statement of the Case set forth in its Briefs in Court of Appeal's Cases No. 22764-2-III and No. 23239-5-III, and in its Answer to Petition for Review previously filed with this Court, are incorporated herein by this reference.

III. ARGUMENT

The TILA applies only to a loan made **primarily** for personal, family, or household purposes. 15 U.S.C § 1602(h). The TILA does not apply to a loan made for business or commercial purposes. 15 U.S.C § 1603(1).

Based on the undisputed facts, this Court may find, as a matter of law, that the 1993 Loan was for business or commercial purposes, and a transaction excluded from the TILA. The 1993 Loan was not primarily for personal, family, or household, regardless of whether the Quantitative Test, the Original Purpose Test, or the All Circumstances Test is applied. Further, the Court of Appeals correctly applied the Quantitative Test to Brender's hybrid loan.

A. Quantitative Test

Under the Quantitative Test, a loan is excluded from the TILA when the majority of the loan's proceeds are used for a business or commercial purpose. Kurtis A. Kemper, Annotation, What Constitutes "Business or Commercial" Purposes Within Meaning Of § 104(1) Truth In Lending Act, 54 ALR Fed. 491, §3; Consumer and Borrower Protection, 17 Am. Jur.2d §14; and Stillman v. First National Bank of North Idaho, 791 P.2d 23 (Idaho App. 1990).

It is undisputed that Brender used the majority of the proceeds of the 1993 Loan for the business or commercial purpose of satisfying the Defaulted Business Loans and settling the Bank's commercial lawsuit against Brender on those business debts. Of the 1993 Loan's approximately \$350,000 in proceeds, Brender used about \$200,000 to satisfy the Defaulted Business Loans and to settle the Bank's commercial lawsuit against him. Brender used the remaining \$150,000 to remove his soon-to-be ex-wife's interests in the properties the Bank required Brender pledge as collateral to secure the 1993 Loan. The Bank would not have made the 1993 Loan unless Brender pledged these properties free and clear of his ex-wife's interests.

Applying the Quantitative Test adopted by the Court of Appeals in Cashmere Valley Bank v. Brender, 128 Wn. App. 497 (Div. III 2005), the

Bank is entitled to the dismissal of Brender's TILA claims, as a matter of law.

B. Original Purpose Test

Under the Original Purpose Test, the purpose of a loan transaction is determined by the use to which the proceeds are originally placed and maintained. Toy Nat. Bank of Sioux City v. McGarr, 286 N.W.2d 376 (Iowa 1979).

The Bank's original loans to Brender were the Defaulted Business Loans. It is undisputed that these loans were for business and commercial purposes. It is also undisputed that the 1993 Loan refinanced the Defaulted Business Loans, and settled the Bank's commercial lawsuit against Brender on those pre-existing business debts.

Applying the Original Purpose Test to Brender's case, the 1993 Loan was, as a matter of law, for business or commercial purposes and, therefore, excluded from the TILA.

C. All Circumstances Test

Pursuant to the All Circumstances Test, whether a loan is for personal or business purposes is answered by evaluating all the circumstances surround the loan transaction. Conrad v. Smith, 42 Wn. App. 559 (Div. III 1986). Despite the All Circumstances Test's factual inquiry, a court may decide, as a matter of law, that a loan was not

primarily for personal, family, or household purposes, "when reasonable minds could reach but one conclusion". Id. at 564.

In Brender's case, reasonable minds could only conclude that the 1993 Loan was not primarily for personal, family, or household purposes. Brender does not dispute that the 1993 Loan satisfied Brender's Defaulted Business Loans, and settled the Bank's commercial lawsuit against Brender on those defaulted business debts. Brender's deposition testimony is as follows:

Question: So it's your testimony that all those loans that got refinanced were related to the orchard operations or to the mill operation?

Answer: Yes.

Question: Because I think at the time of the 1993 loan there was about \$200,000 you owed Cashmere Valley Bank; does that sound about right?

Answer: Yes.

Question: So it's your testimony that \$200,000 that was being refinanced was due to loans the bank had made on your businesses; the orchard and the mill?

Answer: Yes.

Question: Now, the bank also gave you \$150,000 cashier's check at the time of that 1993 loan, right?

Answer: Not me.

Question: Who did they give the check to?

Answer: Apparently to John Hotchkiss because I never saw it.

Question: Hotchkiss was your attorney?

Answer: Yes.

Question: He was representing you in your divorce?

Answer: Correct. Yes.

Question: And it's your understanding that - - that those funds were going to be -- were going to your --were going to Brenda, your soon-to-be ex-wife?

Answer: Yes.

Question: And it's my understanding that the -- that the purpose for that \$150,000, as you testified to earlier, was to -- was to go towards securing from her a quit claim deed on the orchard and the mill and your home and then you said "everything"; is that correct?

Answer: Basically, the lady only wanted money.

Question: So you -- the \$150,000 went to her to primarily pay off -- pay her off so you could keep all the interest in the orchards and the mill?

Answer: Yes.

Question: And the orchards and the mill are your primary income source? That was your business back in August of 1993?

Answer: Yes. It's always been.

(CP 293-335).

The deposition testimony of Brender's loan officer at the Bank, Jim Geary, further explains that Brender's pledging of collateral was the settlement of Brender's defaults on the Defaulted Business Loans:

Question. Alright. Is one of the reasons that you extended this loan [the 1993 Loan] to Brender was so that you could get some security?

Answer: Yes.

Question. Okay. Because the Bank was kind of unsecured out there on the \$230,000?

Answer: Yes.

...

Question: Okay. And so, in order to better the Bank's position by giving them the \$353,000 loan, isn't it true that the Bank got security when it didn't have security before?

Answer: Yes.

(CP 380-482).

The Bank's Memorandum to Credit File made at the time of the 1993 Loan further establishes the business and commercial purpose of the 1993 Loan. It reads: "These new funds and *the restructuring of our*

present debt would put the bank in a fully secured and amortizing position.” (CP 65).

Brender also admitted the business and commercial purpose of the 1993 Loan when he signed a Disbursement Agreement and Authorization, in which Brender represented and warranted to the Bank that the 1993 Loan was for business and commercial purposes. (CP 336-357).

Based on the undisputed facts, summary judgment in favor of the Bank is appropriate. Brender admits the 1993 Loan satisfied the Defaulted Business Loans, and settled the Bank’s commercial lawsuit against him on those business debts. Brender further admits that the \$150,000 in 1993 Loan Proceeds were needed to secure the 1993 Loan. Brender needed the \$150,000 to acquire his soon-to-be ex-wife’s interests in the properties the Bank required Brender pledge to secure the 1993 Loan. The Bank conditioned the 1993 Loan on Brender’s pledge of these properties free and clear of his ex-wife’s interests. The pledge included Brender’s orchard and cedar shake mill, the operations of which provided Brender’s income. Without Brender’s pledge of these business assets, the Bank would not have made the 1993 Loan and would have continued with its commercial collection action against Brender on the Defaulted Business Loans.

D. Quantitative Test is Appropriate Approach for Hybrid Loans

The Quantitative Test is the appropriate approach for hybrid loans, such as the 1993 Loan. Hybrid loans involve a loan made for both consumer and business purposes. The TILA does not apply to a hybrid loan, unless the hybrid loan was primarily for personal, family, or household purposes.

The application of the Quantitative Approach to hybrid loans is perhaps best explained in Stillman v. First Nat. Bank of North Idaho, 791 P.2d 23 (Idaho App. 1990). The Stillman Court stated:

A single loan may have both exempt and non-exempt purposes. In deciding how such a loan should be characterized, the courts have adopted a quantitative approach. Where more than half the money loaned is for an exempt purpose, such as to fund a business, the disclosure requirements are deemed not to apply. See Federal Land Bank of Jackson v. Kennedy, 662 F. Supp. 787 (N.D. Miss. 1987) (loan is "primarily" for an exempt purpose, and therefore totally exempt from the requirements of the Truth in Lending Act, where more than half the proceeds were devoted to the exempt purpose). Accord, Bokros v. Associates Finance, Inc., 607 F.Supp. 869, 871-72 (D.C.Ill.1984); In re Klutzaritz, 46 B.R. 368, 370 (Bankr. E. D. Pa 1985).

Stillman, at 25.

Courts use the Quantitative Test for hybrid loans, because of the Test's simplicity and objectivity. As the Court of Appeals correctly stated in Cashmere Valley Bank v. Brender.

The quantitative approach is the easiest to apply and it will promote certainty in the commercial marketplace. Conversely, a test for hybrid loans that examines all relevant circumstances will promote uncertainty and litigation. As already noted, the majority of the loan proceeds here were used for commercial purposes and, consequently, the loan is exempt from the application of the TILA for a business loan.

Brender, 116 P.3d at 426.

For non-hybrid loans (such as the loan at issue in Conrad v. Smith), the quantitative approach is not appropriate. There is only one loan purpose. The question is whether the non-hybrid loan's single purpose was primarily consumer. The All Circumstance Test used by the Court of Appeals to analyze the non-hybrid loan at issue in Conrad v. Smith is appropriate. The Conrad Court considered all the circumstances surrounding the loan transaction, and determined the TILA did not apply as a matter of law because the Conrads secured the loan to refinance a pre-existing business debt.

Since the 1993 Loan is a hybrid loan, the Court of Appeals and Chelan County Superior Court correctly applied the Quantitative Test and

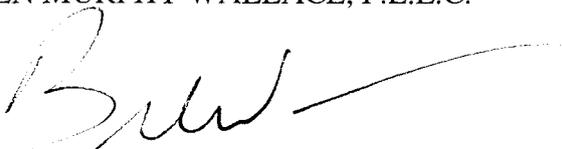
found the 1993 Loan excluded from the TILA. The Bank respectfully requests that this Court affirm these prior decisions, and rule that the Quantitative Test is the correct approach to apply to hybrid loans.

IV. CONCLUSION

Based on the foregoing, the Bank respectfully requests this Court affirm the Court of Appeal's decision in Cashmere Valley Bank v. Brender, 128 Wash. App. 497 (Div. III 2005).

RESPECTFULLY SUBMITTED this 28th day of June, 2006.

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