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NO. 87174-4  
SUPREME COURT  
OF THE STATE OF WASHINGTON

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COLUMBIA COMMUNITY BANK,

Respondent/Cross Appellant

v.

NEWMAN PARK, LLC,

Appellant/Cross Respondent.

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SUPPLEMENTAL BRIEF

---

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## INTRODUCTION

The Supreme Court last addressed the issue of equitable subrogation in *Bank of America, N.A. v. Prestance Corporation*, 160 Wn.2d 560, 160 P.3d 17 (2007). In general terms, the Court adopted the formulation of the doctrine contained in Restatement (Third) *Property* §7.6. The Court's holding was limited, however, in the following language:

The only issue before us is a legal one: should we adopt section 7.6 of Restatement (Third) to hold a refinancing mortgagee's actual or constructive knowledge of intervening liens does not automatically preclude a court from applying equitable subrogation.

160 Wn.2d at 564. The Court did not address the primary question presented here—whether equitable subrogation applies when there is no unjust enrichment.

The formulation of equitable subrogation in Restatement (Third) *Property* §7.6 states that equitable subrogation is only available to prevent unjust enrichment. Under Washington law, a party who is a volunteer cannot rely on the doctrine of unjust enrichment. Columbia Community Bank (CCB) was unquestionably a volunteer. It loaned money to Trinity Development-Northwest, LLC (Trinity). It made the loan for the express purpose of establishing what it believed would be a profitable and

continuing banking relationship with Joseph Sturtevant. It took property belonging to Newman Park, LLC (Newman Park) as security. Trinity had no interest in the property or in Newman Park. Since CCB is a volunteer, it cannot take advantage of equitable subrogation.

### FACTS

Newman Park is a Washington limited liability company. In 2004, it purchased real property in Thurston County, Washington. A portion of the purchase price came from a loan from Hometown National Bank (Hometown) in the amount of \$393,100.00. Hometown took a Deed of Trust on the property as security for the loan. (CP 668-685)

Newman Park had twelve members at all material times. These included eleven individuals (the Individual Members) who held 61% of the ownership interest in the company. Landmark Development Ventures, Inc. held the remaining 39%. Joseph Sturtevant was its sole shareholder, director, and officer while relevant events were occurring. Newman Park's Operating Agreement identified Mr. Sturtevant as the company's "manager" and/or "managing member." (CP 471-475)

Newman Park's Operating Agreement contained limitations on borrowing. Specifically:

The Members shall not cause the Company to do any of the following without the consent of Members holding an eighty percent interest:

- (1) Mortgage, pledge, or grant a security interest (collectively, the "pledge") in any Company property to the extent that the secured indebtedness from such pledge would exceed \$50,000 in the aggregate.
- (2) Incur or refinance any indebtedness for money borrowed by the Company, if after such financing, the aggregate indebtedness of the company would exceed \$50,000.00.

Trinity is another Washington limited liability company. It was formed in October of 2007. (CP 540) Mr. Sturtevant held a 95% membership interest in Trinity. (CP 550) No Individual Member ever had any interest in Trinity. (CP 464, 597-616)

CCB is an Oregon state chartered bank. Bradley Volchok was an assistant vice-president of CCB in 2007. His duties included marketing, which involved securing deposits for the Bank. The Bank sought to make a profit by loaning the money it received as deposits at a higher rate than the interest it paid its depositors. (CP 243-244, 255-256)

Mr. Sturtevant approached CCB and Mr. Volchok to obtain a loan in late 2007. (CP 272) Mr. Volchok was interested in having the Bank begin a relationship with Mr. Sturtevant. He considered Mr. Sturtevant to be a prime client. Mr. Sturtevant appeared to have a lot of connections

that could result in referrals that would yield additional business for the Bank. CCB's president and executive vice-president were also interested in cultivating Mr. Sturtevant. They met with him to discuss his projects and to begin an ongoing banking relationship. (CP 247, 250-251, 272)

CCB was interested in loaning Mr. Sturtevant money but it wanted Newman Park's property to serve as security. It knew about Hometown's Deed of Trust on the Newman Park property. Mr. Volchok told Mr. Sturtevant that CCB was considering loaning Trinity between \$2 million and \$2.4 million. The amount of the loan would depend on whether Hometown's loan was paid off as part of the transaction. The amount loaned would be smaller if CCB was in second position behind Hometown because CCB would then bear the risk of paying the Hometown loan to Newman Park if Trinity defaulted. (CP 252)

Mr. Volchok sent a commitment letter to Mr. Sturtevant outlining several options for a loan to Trinity. One of the terms of the letter was CCB receiving a first Deed of Trust on Newman Park's property as security for the loan. (CP 254, 288-291) The letter also discussed deposits that Mr. Sturtevant would make in the following terms:

Primary deposit relationship with Columbia Community Bank for Sturtevant, Golemo & Associates, PLLC (Mr. Sturtevant's architectural and engineering firm) and Trinity Development-Northwest, LLC would be required.

Additionally, we would appreciate the opportunity for the deposit relationship with Landmark Development Ventures, Inc. and other entities plus your personal deposit relationship.

(CP 290) This language was placed into the commitment letter to bring more money into the Bank that in turn would fund other loans.

(CP 256-257)

The commitment letter also stated that the amount of the loan would be no more than 65% of the appraised value of Newman Park's property plus 80% of the appraised value on Mr. Sturtevant's residence.

(CP 288) CCB obtained an appraisal that put the value of Newman Park's property at \$4.2 million. (CP 317-320) This placed the loan to value at approximately 25% since the maximum value of the lien on Newman Park's property wound up being \$1,040,000.00. (CP 509)

CCB asked for and obtained a copy of Newman Park's Operating Agreement. Mr. Sturtevant produced a document that was altered in that it made no mention of the Individual Members. (CP 305-306) CCB never asked for a copy of Newman Park's tax return. Had it done so, it would have learned that Newman Park had members other than Landmark. (CP 551-579) CCB states that it would not have consummated the loan had it known of the Individual Members. (CP 270).

The loan transaction closed on or about February 8, 2008. Mr. Sturtevant, on behalf of Trinity, executed a Promissory Note in favor of CCB in the amount of \$1.5 million. It required payment of all interest and principal by no later than February 28, 2009. (CP 482-484) Mr. Sturtevant, as president and secretary of Landmark, signed a Deed of Trust pledging Newman Park's property with CCB as beneficiary. As indicated, the Deed of Trust stated that its lien would not exceed \$1,040,000.00. The proceeds of the loan were used to pay off the obligation to Hometown in the amount of \$430,127.60 and real property taxes in the amount of \$8,356.11. (CP 551, 553) This was done so that CCB would be in first position on Newman Park's property — a requirement of the commitment letter. The proceeds of the loan were also used to pay a premium on a policy of lender's title insurance coverage for the benefit of CCB. (CP 811-813)

CCB prepared and sought the execution of a raft of documents in connection with the loan. (CP 483-528) One of these was Limited Liability Company Resolution to Grant Collateral. This document was executed in the same fashion as all others requiring signature on behalf of Newman Park. Landmark was the signatory as a member of Newman Park, and Mr. Sturtevant signed as president and secretary of Landmark. The document stated that Landmark was authorized to execute it. It was

created from a template. The second page contains the following language which is part of the template:

NOTE: If the member signing this Resolution is designated by the foregoing document as one of the members authorized to act on the Company's behalf, it is advisable to have this Resolution signed by at least one non-authorized member of the Company.

(CP 499-500)

Trinity did not repay the loan. The Individual Members knew nothing of the transaction until June of 2009 when the loan was already in default. (CP 464, 597-616)

CCB began nonjudicial foreclosure proceedings. Newman Park and CCB ultimately filed complaints for declaratory relief to determine the enforceability of CCB's Deed of Trust. The trial court ruled that the Deed of Trust was invalid. It granted CCB judgment, however, against Newman Park in the amount of the obligations paid through the loan proceeds. It also imposed an equitable lien on Newman Park's property in that amount. The trial court denied Newman Park's motion for attorney's fees opining that there was no prevailing party since each side had prevailed on substantial issues. (CP 72-73, 409-411, 412-417, 435-439) Newman Park appealed, and CCB cross-appealed. The Court of Appeals affirmed the trial court on all issues. The Supreme Court granted review to consider

only the equitable subrogation issue and CCB's judgment against Newman Park.

### ISSUES PRESENTED

1. Does the doctrine of equitable subrogation apply when there is no unjust enrichment?
2. Is unjust enrichment absent because CCB is a volunteer?
3. Under all the circumstances of this case, should the doctrine of equitable subrogation apply?

### ARGUMENT

#### I. CCB Is Not Entitled to Equitable Subrogation Relief Because It Is a Volunteer.

The doctrine of equitable subrogation contained in Restatement (Third) *Property* §7.6 states and adopted in *Bank of America, N.A. v. Prestance Corporation, supra*, states as follows in pertinent part:

One who fully performs an obligation of another, secured by a mortgage, becomes by subrogation the owner of the obligation and the mortgage to the extent necessary to prevent unjust enrichment. Even though the performance would otherwise discharge the obligation and the mortgage, they are preserved and the mortgage retains its priority in the hands of the subrogee.

(Emphasis added.) This statement of the rule is in harmony with the conclusion that a party cannot obtain the benefits of equitable subrogation

simply by paying off an existing loan. Equitable subrogation is an equitable doctrine and will be applied only to prevent unjust enrichment. What is unjust enrichment depends on the circumstances of each case. *Kim v. Lee*, 145 Wn.2d 79, 88-89, 331 P.3d 665 (2001).

There is no unjust enrichment when the person making payment is a volunteer. *Lynch v. Deaconess Medical Center*, 113 Wn.2d 162, 165, 775 P.2d 681 (1989), cited with favor in *Young v. Young*, 164 Wn.2d 477, 484, 191 P.3d 1258 (2008); *Ellenburg v. Larson Fruit Co.*, 66 Wn.App. 246, 835 P.2d 225 (1992). Furthermore, a person who is a volunteer cannot take advantage of the doctrine of equitable subrogation. *In re Farmers' & Merchants' State Bank of Nooksack*, 175 Wash. 78, 88, 26 P.2d 631 (1933); *BNC Mortgage, Inc., v. Tax Pros, Inc.*, 111 Wn.App. 238, 46 P.3d 812 (2002). This rule arises from the notion that equity will not aid a volunteer. *Falconer v. Stevenson*, 184 Wash. 438, 442, 51 P.2d 618 (1935); *Norris v. Tebrich*, 65 Wn.2d 238, 241, 396 P.2d 637 (1964).

A volunteer is a person who, acting upon his or her own initiative, pays the debt of another without invitation, compulsion, or necessity of self-protection. *In re Farmers' & Merchants' State Bank of Nooksack, supra*, 175 Wash. at 88. A person is under "duty or compulsion" if he or she acts to fulfill his or her own legal duty, to protect his or her own rights or to save his or her own property, or in some other way that he or she

does not voluntarily choose. *Murray v. O'Brien*, 56 Wash. 361, 372, 105 P. 840 (1909); *BNC Mortgage, Inc., v. Tax Pros, Inc.*, 111 Wn.App. at 253-254.

Under this test, CCB was clearly a volunteer. It was under no compulsion or duty to make the loan to Trinity and to take Newman Park's property as security. It also was not required as part of the transaction to pay off the loan to Hometown or the taxes levied on the property. It chose to do so to secure its position in the property.

As indicated, whether a person is a volunteer is determined in light of all the surrounding circumstances. These include whether the benefits were conferred at the request of the party benefitted; whether the party benefitted knew of the payment but stood back and let the party make the payment; and whether the benefits were necessary to protect the interests of the party who conferred the benefit or the party who benefitted thereby. *Ellenburg v. Larson Fruit Co., supra*, 66 Wn.app. at 251-52

Under this test, CCB is clearly a volunteer. First of all, Newman Park did not ask CCB to pay taxes on the property or the loan to Hometown. The loan was made at the request of Trinity, not Newman Park. In order for Newman Park to give approval, 80% of its membership had to approve as its operating agreement states. This never happened. Secondly, Newman Park didn't stand back and let the payment be made.

Its Individual Members—the individuals whose agreement would be necessary to reach the 80% threshold to pledge the property for the loan to Trinity—knew nothing of the transaction. Mr. Sturtevant’s knowledge cannot be attributed to Newman Park because he was clearly acting adversely to its interests in connection with this transaction. Restatement (Second) *Agency* §§280, 282. Finally, the payment of outstanding property taxes or the loan to Hometown was not necessary to protect any interest that CCB had. CCB was not required to loan any money to Trinity. It did so to make a profit. It expected Mr. Sturtevant to make substantial deposits in the future that it could use to fund other loans.

Persons who make loans when not otherwise compelled to do so have been held to be volunteers. In *Ellenburg v. Larson Fruit Co., supra*, the trial court found that the lender was not required to make the loan and therefore a volunteer who could not claim unjust enrichment. In *Bank of America, N.A. v. Wells Fargo Bank, N.A.*, 126 Wn.App. 710, 723, 109 P.3d 863 (2005), reversed on other grounds *sub nom. Bank of America, N.A. v. Prestance Corporation, supra*, the Court held that a lender who made a loan for profit and, in the process, paid a prior loan could not claim unjust enrichment because it was a volunteer based upon the factors set out in *Ellenburg v. Larson Fruit Co., supra*. The Court of Appeals in *BNC Mortgage, Inc., v. Tax Pros, Inc., supra*, came to the same conclusion. In

ruling that BNC Mortgage, Inc. was not entitled to equitable subrogation relief, it stated:

BNC was a volunteer here. It was not under any duty or compulsion to loan money to . . . It had no interest . . . that it needed to protect. It did not act under any other duty or compulsion, but instead chose freely and voluntarily to avail itself of a business opportunity. Its hopes were to achieve a profit and, quite understandably, to secure itself against loss. That it may not realize those hopes is not by itself sufficient to warrant a judicial alteration of Washington's long-settled scheme of lien priorities.

111 Wn.App. at 254-55. In the same way, CCB made the loan to make a profit and also to establish an ongoing and continuously profitable relationship with Mr. Sturtevant. It is not entitled to equitable relief when its expectations were not fulfilled.

Reasonable minds could reach only one conclusion here. Under all of these tests, CCB is a volunteer. The doctrine of unjust enrichment is not available to it for that reason. Equitable subrogation is also unavailable because it can only be applied to prevent unjust enrichment.

## II. The Equities Do Not Favor CCB.

Equitable subrogation is, obviously, an equitable doctrine. Equity aids the diligent. It will not help those who fail to discover material facts. *Teeter v. Brown*, 130 Wash. 506, 228 P. 291 (1924); *see also, Morgan Guaranty Trust Co. of New York v. American Savings and Loan*

*Association*, 804 F.2d 1487, 1986 (9<sup>th</sup> Cir. 1986) — equity will not aid someone who deliberately foregoes an opportunity to discover materials facts. And, equitable subrogation will not be applied to benefit a title company that negligently failed to discover an intervening judgment, *Kim v. Lee, supra*.

CCB would not have made the loan had it known of the Individual Members. It could have discovered their existence easily but failed to do so. The operating agreement Mr. Sturtevant presented showed that Landmark was Newman Park's only member. But it also contained provisions restricting action—such as pledging company property—without agreement of members holding 80% of the membership interests. Such a provision would only be necessary if the company had members other than Landmark. CCB apparently did not notice this or saw it and failed to make any inquiry about it. CCB could also have asked for Newman Park's tax returns, a common piece of due diligence for lenders. Had it taken either of these steps, it would have learned that there were other members and, as it has conceded, not made the loan in the first place.

This failure is all the more critical because of the notation on the template CCB used to formulate the Limited Liability Company Resolution to Grant Collateral. The template stated that it was advisable

to get the signature of someone other than the member authorized to sign, in this case Landmark.

CCB rebut this argument by claiming that it was defrauded by Mr. Sturtevant. A person cannot claim fraud when he or she has the means of discovering the truth but simply does not do so. *Oates v. Taylor*, 31 Wn.2d 898, 904, 199 P.2d 924 (1949); *Tokarz v. Frontier Federal Savings and Loan*, 33 Wn.App. 456, 464, 656 P.2d 1089 (1982). CCB had the means of obtaining information. The operating agreement provided, altered though it was, provided at least inquiry notice that Newman Park had members other than Landmark. And CCB could have required virtually anything from Mr. Sturtevant—such as Newman Park's tax returns. Since CCB had information and the opportunity to obtain more, it cannot claim that the equities run in its favor.

Jurisdictions other than Washington recognize that the negligence of a party claiming equitable subrogation will eliminate that party's claim. For example, in *State, Department of Taxation v. Jones*, 61 Ohio St.2d 99, 399 N.E.2d 1215 (1980), the lender made a loan, took a mortgage on real estate as security, but delayed the recording of the mortgage for several months. In the interim, the Department of Taxation filed a lien for unpaid taxes. The lender paid encumbrances prior to lien filed by the Department of Taxation and claimed priority over the Department of Taxation on the

basis of equitable subrogation. The Court held that the lender was not entitled to relief and priority based upon that doctrine because of its own negligence in not promptly recording its mortgage.

Our case is no different. CCB was given documents that would have shown it that it should not have made the loan and taken Newman Park's property as security. It cannot take advantage of equitable subrogation when it failed to recognize what the facts indicated.

III. Illustration 28 from Restatement (Third) Property §7.6 Is Not Apt and Is at Odds with Washington Law.

The Court of Appeals chose to rely on Illustration 28 to Restatement (Third) *Property* §7.6, which reads as follows:

28. Blackacre is owned by A and B, subject to a mortgage held by Mortgagee-1 securing a debt of \$100,000. A and B are tenants in common. A approaches Mortgagee-2 and induces it to make a loan of \$150,000, of which \$100,000 is used to pay off the first mortgage in full. The remaining \$50,000 is used by A for other purposes. B is not a party to this transaction, but A forges B's name on the note and mortgage to Mortgagee-2. Mortgagee-2 is subrogated to the first mortgage to the extent of \$100,000, and can enforce it against B's interest in Blackacre. Mortgagee-2 is not entitled to subrogation with respect to the remaining \$50,000.

The applicability of this illustration to our case is subject to significant question. Most importantly, the loan in the illustration was taken out by and presumably benefited one of the owners of the property.

That is not true in our case. Trinity secured the loan, and no Individual Member of Newman Park had any interest in Trinity. Equitable subrogation simply should not apply when a stranger to the property convinces a lender to take the property as security for a loan made to that stranger.

More importantly, the illustration does not account for Washington law on the doctrine of unjust enrichment. Unjust enrichment might be present under Washington law because one of the property's owners requested the loan and also stood by while Mortgagee-1 was paid off. *See Ellenburg v. Larson Fruit Co. supra*. As noted above, that is not the case here. For these reasons, Illustration 28 is not helpful.

#### IV. Disallowing Equitable Subrogation to CCB Is Sensible Given Current Lending Practices.

This case represents a template for current commercial lending practices. Lenders require security and personal guarantees. The amount of the loan will only be a percentage of the value of the security—65% in this case. If the security has existing encumbrances, lenders insist on applying loan proceeds to pay off those encumbrances so that the lender will be in first position. Lenders may also seek subordination of the interest of a senior lienholder. In other words, lenders don't rely on the doctrine of equitable subrogation to secure their positions when they make

loans. They account for and eliminate any claim senior to theirs as part of the loan transaction.

Lenders also secure lender's title insurance policies much as CCB did here. Among other things, these policies protect the insured from loss due to any invalidity or unenforceability of the lien of the insured mortgage upon the title. 1 *Title Insurance Law* §5:14. In other words, these policies protect lenders from just the sort of problem CCB has experienced in this case.<sup>1</sup>

V. CCB Is Not Entitled to an Equitable Lien on Newman Park's Property.

At CCB's request, the trial court imposed an equitable lien on Newman Park's property. That relief is not warranted, however, when the creditor can sue the debtor on an obligation that is enforceable. Whether the creditor can ultimately collect doesn't matter. *Sorensen v. Pyeatt*, 158 Wn.2d 523, 536-38, 146 P.3d 1172 (2006). Trinity executed a promissory note in favor of CCB. That note is enforceable. That means that CCB is not entitled to an equitable lien on Newman Park's property.

The existence of these practices raises the question of whether the doctrine of equitable subrogation has any utility at all where commercial

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<sup>1</sup> Parenthetically, a title insurer who contracts to insure a risk cannot take advantage of equitable subrogation. *Kim v. Lee, supra*.

lenders are concerned. The comments of the Court of Appeals in *BNC Mortgage, Inc., v. Tax Pros, Inc., supra*, set out on p. 11 above become apt. Lenders who loan for profit have no complaint when their expectations are frustrated. This is nothing more than a simple business risk.

The Court in *Bank of America, N.A., v. Prestance Corporation, supra*, expressed concern that equitable subrogation is necessary to insure refinancing of homeowner loans because of the reduction of title insurance premiums. 160 Wn.2d at 581-82. The situation presented in this case is obviously not a refinance of a home loan. It is dissimilar to the normal refinancing process in one other critical respect. When a homeowner wants a refinance, that homeowner contacts a lender or mortgage broker to arrange the refinance. In our case, that did not happen. Newman Park's operating agreement required approval of 80% of membership interests before any obligation could be refinanced. That approval never happened. For these reasons, not allowing equitable subrogation in our case should have no effect on the ability of a homeowner to refinance his or her home loan.

#### VI. Newman Park Is Entitled to Attorney's Fees.

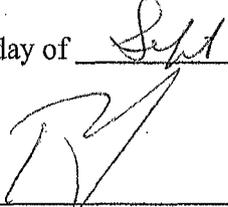
Newman Park has sought to invalidate a deed of trust that contains a provision allowing attorney's fees to the prevailing party in the event of any suit. (CP 514) It is therefore entitled to an award of attorney's fees

both at trial court level and on appeal since it has invalidated CCB's deed of trust and since CCB should not have received equitable subrogation relief. Contrary to the statement of the Court of Appeals, Slip Opinion, p. 18 fn. 5, Newman Park made extensive argument on the attorney's fee question. (Brief of Appellant, pps. 29-34)

### CONCLUSION

This matter was decided in the trial court on motions for summary judgment. That method of resolving the case was appropriate because there is no genuine issue of material fact and reasonable minds could reach only one conclusion. *Wilson v. Steinbach*, 98 Wn.2d 434, 437, 656 P.2d 1030 (1982). The conclusion the trial court reached, however, was incorrect. CCB is obviously a volunteer and a lender for profit. It failed to discover the true facts. Therefore, it is not entitled to equitable subrogation relief. It is also not entitled to an equitable lien on Newman Park's property. The Supreme Court should so hold and should order that Newman Park receive its attorney's fees both at trial and on appeal.

DATED this 13 day of Sept., 2012.

  
\_\_\_\_\_  
BEN SHAFTON, WSB #6280  
Of Attorneys for Newman Park

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NO. 41470-8-II  
IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON  
DIVISION II

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COLUMBIA COMMUNITY BANK,

Respondent/Cross Appellant

v.

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Appellant/Cross Respondent.

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Please find attached Newman Park's Supplemental Brief along with an Affidavit of Mailing for filing. Thank you for your attention to this matter.

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