

63331-7

63331-7

No. 63331-7-I

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

GMAC, a Delaware corporation,

Appellant,

v.

EVERETT CHEVROLET, INC., a Delaware corporation,
JOHN REGGANS, AND JANE DOE REGGANS,

Respondents.

APPELLANT'S REPLY APPELLATE BRIEF

John E. Glowney, WSBA No. 12652
STOEL RIVES LLP
600 University Street, Suite 3600
Seattle, WA 98101
206-624-0900
Attorneys for Appellant GMAC

FILED
MAR 21 10 4:34
STOEL RIVES LLP
JOHN E. GLOWNEY

TABLE OF CONTENTS

	Page(s)
I. ARGUMENT	1
A. Introduction.....	1
B. The Relevant Financial Facts and GMAC’s Contract Rights Were Ignored by the Trial Court	1
C. The Trial Court Failed to Apply Controlling Precedent Governing the Duty of Good Faith.	8
1. Badgett: The Duty of Good Faith Applies Only to Specific Contract Terms	8
2. Badgett: The Duty of Good Faith Does Not Apply to Restructuring Negotiations	10
3. Badgett: GMAC Had No Duty to Provide EC with Details of Its Financial Analysis; No False Targets Were Given to or Expected of EC	13
4. EC Relies upon Inapposite Case Authority	15
D. GMAC’s Wholesale Security Agreement Contained a “Demand Obligation.”	16
E. GMAC’s Remedies Against Its Collateral Were Conditioned upon a Default; GMAC’s Right to Make Demand Was Not; <i>Coffee</i> Supports GMAC’s Argument	19
F. EC’s Brief Contains Misleading and Exaggerated Factual Assertions.....	21
1. GMAC Audits.....	21
2. GMAC’s Curtailment Demands/Audit Charges	22
3. GMAC Used EC’s Own Records to Determine Sales Dates and “Out of Trust” Sales	24
4. Unsupported Assertions by the Trial Court	25
G. GMAC Properly Exercised Its Remedies Against GM’s Open Account and EC’s Retail Banks.....	28

H.	Ex Parte Injunctive Relief Was Necessary to Halt EC's and Reggans' Conversion	29
I.	Equitable Principles Are Not Applicable and Were Not Argued.....	31
J.	The Trial Court's Award of Fees to EC Was Error	32
K.	The Motion to Amend the Complaint Should Have Been Granted	33
L.	An Award of Attorneys' Fees Under the Contract Is Premature	34
II.	CONCLUSION.....	34

TABLE OF AUTHORITIES

	Page(s)
FEDERAL CASES	
<i>Bank of Am. N.T. & S.A. v. McMahon</i> , 8 F.3d 25, 1993 WL 366663 (9th Cir. 1993)	11
<i>Brown v. AVEMCO Inv. Corp.</i> , 603 F.2d 1367 (9th Cir. 1979)	15, 31
<i>Coffee v. GMAC</i> , 5 F. Supp. 2d 1365 (S.D. Ga. 1998).....	19, 20
<i>Fasolino Foods Co. v. Banca Nazionale Del Lavoro</i> , 961 F.2d 1052 (2nd Cir.1992).....	12
<i>Gen. Ins. Co. of Am. v. Lowry</i> , 570 F.2d 120 (6th Cir. 1978)	31
<i>K.M.C. Co. v. Irving Trust Co.</i> , 757 F.2d 752 (6th Cir. 1985)	15, 16
<i>Kham & Nate’s Shoes No. 2, Inc. v. First Bank of Whiting</i> , 908 F.2d 1351 (7th Cir.1990)	12
<i>Reid v. Key Bank of S. Me., Inc.</i> , 821 F.2d 9 (1st Cir. 1987).....	15, 16
<i>Rosemark Gardens Funeral Chapel-Cemetery, Inc. v. Trustmark Nat’l Bank</i> , 330 F. Supp. 2d 801 (S.D. Miss. 2004).....	10, 11
STATE CASES	
<i>Allied Sheet Metal Fabricators, Inc. v. Peoples National Bank of Washington</i> , 10 Wn. App. 530, 518 P.2d 734, review denied, 83 Wn.2d 1013, cert. denied, 419 U.S. 967 (1974).....	7, 8, 17, 28, 34

<i>Ameriquest Mortgage Co. v. Attorney Gen.</i> , 148 Wn. App. 145, 199 P.3d 468 (2009).....	30
<i>Badgett v. Sec. State Bank</i> , 116 Wn.2d 563, 807 P.2d 356 (1991).....	passim
<i>Bowen v. Danna</i> , 276 Ark. 528, 637 S.W.2d 560 (1982).....	31
<i>Carney v. Shawmut Bank, N.A.</i> , No. 07-P-858, 2008 Mass. App. Unpub. LEXIS 458 (Mass. App. Ct. Sept. 19, 2008).....	11
<i>Glenfed Financial Corp., Commercial Finance Div. v. Penick Corp.</i> , 276 N.J. Super. 163, 647 A.2d 852 (N.J. Super. A.D. 1994)	11, 12, 17, 19
<i>Knox v. Phoenix Leasing Inc.</i> , 29 Cal. App. 4th 1357, 35 Cal. Rptr. 2d 141 (1994).....	32
<i>Lane v. John Deere Co.</i> , 767 S.W.2d 138 (Tenn. 1989).....	31
<i>Liebergessell v. Evans</i> , 93 Wn.2d 881, 613 P.2d 1170 (1980).....	13
<i>Nat'l Bank of N. N.Y. v. Shaad</i> , 60 A.D.2d 774, 400 N.Y.S.2d 965 (1977)	31
<i>Price v. Wells Fargo Bank</i> , 213 Cal. App. 3d 465, 261 Cal. Rptr. 735 (1989).....	11, 12
<i>Seattle-First Nat'l Bank v. Westlake Park Assocs.</i> , 42 Wn. App. 269, 711 P.2d 361 (1985).....	21
<i>Shallcross v. Cmty. State Bank & Trust Co.</i> , 180 N.J. Super. 273, 434 A.2d 671 (Law Div. 1981).....	31
<i>Solar Motors, Inc. v. First Nat'l Bank of Chadron</i> , 4 Neb. App. 1, 537 N.W.2d 527 (1995), <i>aff'd</i> , 545 N.W.2d 714 (1996).....	15, 16

<i>Urdang v. Muse</i> , 114 N.J. Super. 372, 276 A.2d 397 (Essex County Ct. 1971)	31
--	----

STATE STATUTES

RCW 4.84.330	34
RCW 62A.1-103	31
RCW 62A.1-203	9
RCW 62A.1-208	17, 18
RCW 62A.9A-102(2).....	28
RCW 62A.9A-102(42).....	28
RCW 62A.9A-201(a).....	18
RCW 62A.9A-406	28, 29
RCW 62A.9A-607	6,28
UCC Article 1	17, 18
UCC Article 3	18
UCC Article 9	18, 19, 32
UCC § 1-208.....	17
UCC § 1-309.....	17, 18
UCC § 3-102.....	18
UCC § 3-104.....	18
Uniform Commercial Code.....	passim

OTHER AUTHORITIES

American Law Institute.....17
Banking Law Journal vol. 113, No. 8, 81518
National Conference of Commissioners on Uniform State Laws.....17

I. ARGUMENT

A. Introduction

The record in this case is clear. GMAC¹ acted in good faith. Throughout 2008, Everett Chevrolet's (EC) financial condition seriously deteriorated in the face of a severe sales recession engulfing the auto industry. In response, GMAC took the ordinary, reasonable, and prudent steps a lender takes when faced with a financially troubled borrower.² Everett Chevrolet's Respondent's Brief (EC Brief), like the trial court's opinion, asserts unsupported legal theories, and contains numerous misleading factual assertions. The trial judge failed to apply the duty of good faith correctly and failed to enforce clear contractual language. The trial court's orders should be reversed.

B. The Relevant Financial Facts and GMAC's Contract Rights Were Ignored by the Trial Court.

EC's argument centers on assertions that GMAC set out with a hidden agenda to pressure EC out of business and manufactured a default by EC so that GMAC could make demand.³ EC's argument that GMAC's conduct caused EC's financial problems is nothing more than

¹ Everett Chevrolet's motion to dismiss based on GMAC's name has been dismissed by the Commissioner.

² EC's debt to GMAC was \$6,367,294.89 when GMAC made demand in December 2008. R Ex. 77.

³ The trial court's ruling included unsupported assertions that GMAC was conducting a "working capital assault" and had "false targets." EC Brief at 22-23.

argumentative rhetoric without support in the record, and is contradicted by EC's own financial records and the testimony of John Reggans and other EC employees. EC's recitation of its success prior to 2008, while not disputed, is simply irrelevant to its ability to pay its debts in 2008. EC Brief at 1-3. GMAC's July 31 letter, containing GMAC's proposals for a financial strengthening of its borrower and restructuring of the security for the loan, was a response to EC's deteriorating financial condition.⁴

Despite obtaining a substantial increase to its revolving line of credit from GMAC in November 2007,⁵ EC entered the year 2008 suffering operating losses⁶ and without sufficient working capital to see it through a severe sales recession engulfing the auto industry.⁷ Those substantial losses accelerated through 2008.⁸

⁴ EC's annual profit shrank from \$700,000 in 2006 to \$28,000 in 2007. RP Vol. X 100:1-7. Mr. Reggans admitted that he had observed the auto market declining in 2006 and had begun "proactively" trying to address EC's financial distress in July 2007 *even before* GMAC raised the issue with EC in early 2008. Mr. Reggans asked GMAC to provide 100% financing for his real estate purchase. RP Vol. X 103:17-23; RP Vol. XIII 100:1-25, 118:5-16. RP Vol. XIII 100:18-101:3;

⁵ In November 2007, GMAC increased EC's line of credit limit by \$300,000 to an \$800,000 maximum. RP Vol. I 18:17 – 20:16.

⁶ EC had serious problems paying numerous bills in late 2007, early 2008, according to Rebecca Iverson, EC's long-time controller (1996-Sept. 2008). RP Vol. III 4:23-25, 7:19-8:2, 10:2-12, 12:4-13:3, 18:1-15.

⁷ The U.S. auto sales industry suffered a substantial downturn in 2007 and "went off a cliff" in 2008 (Reggans' testimony). RP Vol. X 103:19-21, 99:7-100:13.

⁸ EC's monthly financial statements contain a year-to-date monthly profit or loss summary. RP Vol. I 25:16-26:9; *see, e.g.*, R Exs. 60, 64, 79. EC had two slightly profitable months to start 2008, January (\$11,496) and February (\$41,370), but then the

The result was predictable. By May 2008, EC had used virtually all of GMAC's \$300,000 increase on the RLCA to pay bills, increasing EC's outstanding balance on the RLCA to \$786,000. RP Vol. I 18:17-20:16. Even before GMAC sent its July 31 letter, EC's financial records showed that EC had a severe cash shortage due to operating losses; EC's July 2008 year-to-date losses already totaled \$415,706.

On July 31 (or on any date), GMAC had the contractual right to make demand (with or without reason) for full payment of the approximately \$6.4 million EC owed. GMAC's Opening Appellate Brief (GMAC Brief) at 18-20. (Certainly EC's financial condition on July 31 gave GMAC "reason" enough, if a reason were needed, to have made demand then and there.)

Although GMAC's financing contract gave GMAC the right to demand payment at any time, GMAC instead proposed to restructure and strengthen the borrowers financial condition and the loan's security. In June, GMAC notified EC that it needed to increase working capital and provide a personal guaranty in order for GMAC to continue the lending

losses accelerated dramatically. (R Ex. 79) in March (\$111,899), April (\$104,010), May (\$78,218), June (\$87,405), and July (\$87,040).

relationship.⁹ GMAC's July 31 letter gave EC until October 31 (ultimately until December) to meet those terms. R Ex. 1. The July 31 letter was clear and direct about GMAC's source of concerns, its requests, and the consequences if EC could not meet those requests.¹⁰

Based on an analysis of the Dealership's operating trends, repayment capacity, and available security, GMAC is unable to increase the limit of the Dealership's Revolving Line of Credit or extend a working capital loan to the Dealership.

Further, the deteriorating operating trends and credit base of the Dealership and its poor wholesale performance increase GMAC's credit risk associated with the Dealership's account. In order to continue the financing arrangement between the Dealership and GMAC and to help mitigate GMAC's credit risk, GMAC requires, at a minimum, the following: [the letter lists requests for an \$800,000 unencumbered capital injection, a personal guaranty from Mr. Reggans, and faithful and prompt payment for vehicles upon sale, and sets a deadline of October 31, 2008].

If the Dealership is unwilling or unable to comply with the above requirements, GMAC may suspend or terminate the Dealership's wholesale credit lines.

⁹ GMAC became seriously concerned with EC's deteriorating financial condition from its review of EC's April financial statement. RP Vol. I 24:13-32:25, 140:7-141:10. Jerry Vick, GMAC's branch manager, first discussed GMAC's concerns with Mr. Reggans in telephone calls and then in a meeting in early June 2008. *Id.*

¹⁰ In other words, GMAC met the UCC or common law standard of good faith and rebuts EC's allegations that GMAC did not act honestly with EC. There is no doubt that Mr. Reggans, an experienced auto dealer with 19 years' experience in the industry, including 12 years operating the EC dealership, fully understood the July 31 letter. R Ex. 100; RP Vol. X 63:2-64:6. GMAC then acted as it stated it would.

R Ex. 1 (emphases added).¹¹ After the July 31 letter, EC's losses continued unabated.¹² GMAC extended its deadline from October 31 to November 30, but EC was still unable to meet the July 31 restructure terms. The financial records showed that EC's severe cash shortage that Ms. Iverson identified as existing in late 2007 or early 2008 due to monthly operating losses¹³ had worsened throughout all of 2008. By December 2008, EC's cash shortage was beyond the crisis stage, *even after* receiving \$500,000 in October from Motors Holdings.¹⁴ EC's year-to-date November operating losses increased to \$717,552. R Ex. 79.

Inevitably, in late November and early December, EC repeatedly went "out of trust," *i.e.*, EC failed to pay GMAC the "floor plan" amount for vehicles EC sold. GMAC Brief at 12-14. Even then, GMAC did not

¹¹ This letter contained GMAC's first request to EC to pay \$10,000 per month on the RLCA, as provided by the contract, and to pay audit costs of \$500 per inventory audit. GMAC conducted a total of 23 audits in the first 11 months of 2008, or approximately two per month on average. R Ex. 97. Nine audits were conducted in October, and three in November.

¹² August (\$73,095), September (\$78,413), October (\$96,291), and November (\$94,068). Ms. Iverson, EC's long-time controller, quit in September over her concern about personal liability for unpaid state taxes. RP Vol. III 15:18-17:10.

¹³ EC's claims about the impact of GMAC's audits and requests for payment on EC are misleading and exaggerated. *See infra* Section F (1) and (2).

¹⁴ The \$500,000 only paid some of EC's overdue bills to GMAC and others and could not provide needed working capital. RP Vol. X 125:1-7; RP Vol. XIV 46:21-47:7; 48-52. Although EC asserts that Motors Holdings was ready to make a \$2.5 million investment in EC, in fact Mr. Reggans testified that Motors Holdings advanced \$500,000 in October 2008 instead of the \$800,000 EC needed to meet GMAC's conditions because "General Motors[sic] did not have the money to advance," and therefore in early December declined Mr. Reggans request for an additional \$300,000. RP Vol. X 124-127. Despite this testimony, EC asserts that Motors Holdings was ready to invest \$2.5 million only weeks later.

immediately make demand. Instead, GMAC made two stop-gap increases of its floor plan vehicles to EC (December 9 and 11), effectively increasing its loan to EC. *Id.*

Despite EC's continuing financial deterioration since October 2007, and after July 31, GMAC did not change the conditions in its July 31 letter. But by mid-December 2008 EC had not met GMAC's July 31 restructure conditions and was repeatedly "out of trust."

Thus, only after an extended time period, only after advancing additional funds in November 2007 and again in December 2008, and only after repeated "out of trust" situations, did GMAC finally exercise its contractual remedies in December 2008. GMAC Brief at 12-14. GMAC gave notice under its security agreement to "account debtors" GM and EC's retail banks to pay GMAC. RCW 62A.9-607(a). GMAC terminated its lending arrangement with EC and made demand for payment. *Id.*

Unfortunately, instead of complying with its contractual obligations to pay GMAC, EC and Mr. Reggans started selling vehicles without paying GMAC any of the proceeds.¹⁵ By the time GMAC could obtain a TRO to halt this conversion of its security interest in the collateral, EC had converted the proceeds of 33 vehicles totaling

¹⁵ This is conversion. GMAC Brief at 42-43.

approximately \$778,000. RP Vol. VI 27:14-30:22; RP Vol. VIII 9:2-16; R Ex. 52.¹⁶

In sum, the facts showed that GMAC was responding like any prudent lender to a borrower in bad financial condition. The July 31 letter honestly told EC of GMAC's financial concerns, its proposed restructure terms, and its actions if EC could not meet its terms. Only when EC was unable to meet the July 31 conditions and EC was repeatedly "out of trust" did GMAC exercise its right to make demand.¹⁷ In the face of EC's own financial records and GMAC's restraint in exercising its remedies, there are no facts that support EC's and the trial court's contention that GMAC had a hidden agenda to manufacture a default or to shut down the dealership or that GMAC took any improper actions that caused EC to fail.¹⁸ No reasonable person could review these facts or the applicable law and claim that GMAC did not deal in good faith or honestly with EC.

¹⁶ These facts, which are central to GMAC's decision to file suit and obtain injunctive relief, and which explain why the trial court confirmed the TRO as a preliminary injunction, appear to be entirely omitted from EC's Brief.

¹⁷ The trial court had it backward. Even though GMAC's financial analysis showed EC's continued deterioration, GMAC did not change the proposed restructure terms contained in the July 31 letter to increase GMAC's requirements, which shows GMAC was trying to work with EC, not trying to put EC out of business with "false targets."

¹⁸ GMAC is not acting in bad faith in exercising contractual remedies simply because this made EC's situation worse. EC was already failing. As the court in *Allied Sheet Metal Fabricators, Inc. v. Peoples National Bank of Washington* noted:

"Demand notes with the security agreements here executed indeed put the bank in a position where if it takes action, as a practical matter, the company is in trouble because it has lost its

C. The Trial Court Failed to Apply Controlling Precedent Governing the Duty of Good Faith.¹⁹

EC's Brief proposes various alternative theories of good faith at odds with *Badgett* and established case authority. The trial court's primary error was its failure to enforce clear contract terms and to follow the clear dictates of *Badgett*.²⁰

1. *Badgett*: The Duty of Good Faith Applies Only to Specific Contract Terms.

Perhaps the most striking aspect of EC's Brief, like the trial court's Oral Opinion, is that it fails to identify any specific contract term GMAC allegedly violated by "bad faith" conduct.²¹ Contrary to EC's argument that good faith is a determination based on the "totality of the circumstances" (EC Brief at 31), *Badgett* is crystal clear: the duty of good

financing, but that is the agreement that the parties made by appropriate written instruments."

10 Wn. App. 530, 534, 518 P.2d 734 (quoting trial judge), *review denied*, 83 Wn.2d 1013, *cert. denied*, 419 U.S. 967 (1974). EC's argument that *Allied* dealt with a demand promissory note is a distinction without a difference. EC simply fails to recognize that the UCC Official Comment upon which the courts have relied applies to both "demand instruments or obligations." In other words, any contractual "demand obligation" by its very nature is not subject to the duty of good faith.

¹⁹ EC's Brief at 29, *et seq.* discusses the duty of good faith in broad generalities. But GMAC does not seek to "repudiate" the duty of good faith but rather to have the duty applied properly under *Badgett*, *Allied*, and the relevant UCC or case law. When considered under the proper application of the law, GMAC's actions in fact were taken in good faith.

²⁰ *Badgett v. Sec. State Bank*, 116 Wn.2d 563, 570, 807 P.2d 356 (1991).

²¹ EC's Brief often cites to the Oral Opinion as if it were self-validating, rather than citing to the record or the applicable law.

faith applies to existing contract terms and cannot be used to add duties to those contained in a contract.²² EC's Brief makes repetitious conclusory claims of bad faith built upon the numerous ostensible duties erroneously created by the trial judge, but fails to identify any express contract terms breached by GMAC.²³ EC's argument fails because all of the numerous new duties the trial court purported to impose upon GMAC are legally baseless.²⁴ GMAC Brief at 26-30. The trial court's ruling makes an alleged breach of the duty of good faith into a separate cause of action, contrary to well-established law. *See* GMAC Brief n.38; Official Comment to RCW 62A.1-203 ("This section does not support an independent cause of action for failure to perform or enforce in good faith.").

²² There is no "free-floating duty of good faith" and fair dealing that is unattached to an existing contract. *Badgett*, 116 Wn.2d at 570. The duty of good faith cannot be used to "inject substantive terms into the parties' contract." *Id.* at 569. It cannot be used "to create obligations on the parties in addition to those contained in the contract." *Id.* at 570.

²³ EC's argument circles from conclusory allegation to conclusory allegation without ever grounding the arguments in specific facts and specific contract terms. *See, e.g.*, EC Brief at 48-51.

²⁴ As Court Commissioner Ellis correctly observed, "There is nothing in any of the financing contracts that obligates GMAC to make other loans, to consider alternate business structures, or to explain its reasons for asking for changes to Everett's capitalization." Commissioner's Ruling Granting Motion for Discretionary Review at 11.

2. *Badgett*: The Duty of Good Faith Does Not Apply to Restructuring Negotiations.

Many of the acts of bad faith EC alleges arise out of GMAC's July 31 letter and GMAC's delay in exercising its remedies to give EC time to address the proposed restructure terms.²⁵ However, the fact that GMAC proposed, in the face of EC's worsening financial condition, to continue to finance EC only if certain conditions were satisfied is no violation of the duty of good faith.²⁶ Giving EC time to consider and meet those terms as GMAC did here – instead of making demand immediately – does not violate the duty of good faith, nor does it expand the scope of the duty of good faith. *E.g., Rosemark Gardens Funeral Chapel-Cemetery, Inc. v. Trustmark Nat'l Bank*, 330 F. Supp. 2d 801, 811 (S.D. Miss. 2004) (“A number of courts have implicitly recognized, in fact, that a duty of good faith and fair dealing does not arise even where a lender begins

²⁵ GMAC's July 31 letter proposed to restructure the terms of EC's existing financing arrangement with GMAC. “In order to continue the financing arrangement between the Dealership and GMAC and to help mitigate GMAC's credit risk, GMAC requires, at a minimum, the following” R Ex. 1 (emphasis added).

²⁶ *Badgett* itself is a leading case for the proposition that a lender has no duty of good faith to cooperate in efforts to restructure a loan.

By urging this court to find that the Bank had a good faith duty to affirmatively cooperate in their efforts to restructure the loan agreement, in effect the [debtors] ask us to expand the existing duty of good faith to create obligations on the parties in addition to those contained in the contract – a free-floating duty of good faith unattached to the underlying legal document. This we will not do. The duty to cooperate exists only in relation to performance of a specific contract term.

Badgett, 116 Wn.2d at 570.

negotiations towards restructuring an existing loan.”).²⁷ Conducting restructuring negotiations does not disable or prevent lenders, under the duty of good faith, from enforcing their contracts.²⁸ Indeed, placing such

27

See, e.g., Carter’s Court Assocs. v. Metropolitan Fed. Sav. and Loan Ass’n, 844 F. Supp. 1205, 1210 (M.D. Tenn. 1994) (holding that lender was not under a duty to restructure the loan under the express terms of the loan documents or under any implied terms; that “in the absence of an express contract term, there is no duty on the part of a lender to negotiate a workout or provide increased credit;” that “there is no breach of good faith for a party to act consistently with the terms of a written agreement;” and that therefore, even after it began negotiating, lender had no duty of good faith and fair dealing); *cf. Teachers Ins. & Annuity Ass’n of America v. LaSalle Nat. Bank*, 295 Ill. App. 3d 61, 691 N.E.2d 881, 229 Ill. Dec. 408 (Ill. App. 1998)

Rosemark Gardens, 330 F. Supp. 2d at 811; *see also Price v. Wells Fargo Bank*, 213 Cal. App. 3d 465, 261 Cal. Rptr. 735, 742 (1989) (covenant of good faith and fair dealing is not breached when lender takes “hard line” in loan repayment negotiations since “[c]ontracts are enforceable at law according to their terms”); *Carney v. Shawmut Bank, N.A.*, No. 07-P-858, 2008 Mass. App. Unpub. LEXIS 458, at *9 (Mass. App. Ct. Sept. 19, 2008) (“While Shawmut was free to negotiate with Carney, it was under no obligation to do so, and was equally free to exercise the rights which it had acquired under the loan agreements.”).

²⁸ *Rosemark Gardens*, 330 F. Supp. 2d at 810-11 (“Countless other cases have recognized this same fundamental principle. *See, e.g., Bank of Am. N.T. & S.A. v. McMahon*, 8 F.3d 25, 1993 WL 366663, *3 (9th Cir. 1993) (holding that ‘the covenant of good faith and fair dealing is not breached when a lender takes a “hard line” in loan repayment negotiations’ since ‘contracts are enforceable at law according to their terms’); *Glenfed Financial Corp., Commercial Finance Div. v. Penick Corp.*, 276 N.J. Super. 163, 176, 647 A.2d 852, 858 (N.J. Super. A.D. 1994)”).

However, this duty of fair dealing does not “alter the terms of a written agreement.” *Rudbart v. North Jersey Dist. Water Supply Comm’n*, 127 N.J. 344, 366, 605 A.2d 681, *cert. denied*, 506 U.S. 871, 113 S. Ct. 203, 121 L. Ed. 2d 145 (1992). Consequently, it may not be invoked by a commercial debtor to preclude a creditor from exercising its bargained-for rights under a loan agreement. *See Hall v. Resolution Trust Corp.*, 958 F.2d 75, 79 (5th Cir.1992) (“[A]n ‘agreement made by the parties and embodied in the contract itself cannot be varied by an implicit covenant of good faith and fair dealing.’”) (quoting

a good faith limitation upon work-out or restructuring negotiations would be bad commercial law policy.²⁹ GMAC could have simply demanded full payment in July 2008, or at any time earlier or later, instead of giving EC almost half a year to meet GMAC's conditions to continue financing. Under the duty of good faith, GMAC was free to require different terms to continue its financing of EC, but GMAC was not compelled to do so, and GMAC was not thereby foreclosed from exercising its contractual rights.

Exxon Corp. v. Atlantic Richfield Co., 678 S.W.2d 944, 947, 28 Tex. Sup. Ct. J. 68 (Tex.1984); *Terry A. Lambert Plumbing, Inc. v. Western Sec. Bank*, 934 F.2d 976, 983 (8th Cir.1991) (“Acting according to express terms of a contract is not a breach of good faith and fair dealing.”); *Kham & Nate’s Shoes No. 2, Inc. v. First Bank of Whiting*, 908 F.2d 1351, 1357 (7th Cir.1990) (“Any attempt to add an overlay of ‘just cause’ . . . to the exercise of contractual privileges [based on the UCC’s requirement of ‘honesty in fact’] would reduce commercial certainty and breed costly litigation.”); *Price v. Wells Fargo Bank*, 213 Cal. App. 3d 465, 261 Cal. Rptr. 735, 742 (1989) (The duty of good faith and fair dealing “does not impose any affirmative duty of moderation in the enforcement of legal rights.”); *accord Fasolino Foods Co. v. Banca Nazionale Del Lavoro*, 961 F.2d 1052, 1056-58 (2nd Cir.1992); *Government St. Lumber Co. v. AmSouth Bank, N.A.*, 553 So.2d 68, 72-73 (Ala.1989); *Creeger Brick & Bldg. Supply, Inc. v. Mid-State Bank & Trust Co.*, 385 Pa. Super. 30, 560 A.2d 151, 154 (1989); *Badgett v. Security State Bank*, 116 Wash. 2d 563, 807 P.2d 356, 360 (1991).

Glenfed Fin. Corp. v. Penick Corp., 276 N.J. Super. 163, 647 A.2d 852, 857-58 (App. Div. 1994) (alterations in original).

²⁹ *Fasolino Foods Co. v. Banca Nazionale del Lavoro*, 961 F.2d 1052, 1057 (2d Cir. 1992) (“Indeed, a contrary view would discourage lenders from allowing borrowers leeway and encourage those lenders to play hardball in the face of every default, no matter how minor.”); *Kham & Nate’s Shoes No. 2, Inc. v. First Bank of Whiting*, 908 F.2d 1351, 1357 (7th Cir. 1990) (“Any attempt to add an overlay of ‘just cause’ . . . to the exercise of contractual privileges [based on the UCC’s requirement of ‘honesty in fact’] would reduce commercial certainty and breed costly litigation.”).

3. *Badgett*: GMAC Had No Duty to Provide EC with Details of Its Financial Analysis; No False Targets Were Given to or Expected of EC.

Badgett rejected any broad free-floating duty for a lender to provide information, and expressly rejected *Liebergessell v. Evans*, 93 Wn.2d 881, 613 P.2d 1170 (1980), in the context of lending contracts. *Badgett*, 116 Wn.2d at 570 n.2.³⁰ EC Brief at 31-32. There was no contract term requiring GMAC to provide such information;³¹ therefore, there is no contract breach, and no breach of the duty of good faith. The trial court's creation of a duty for GMAC to provide detailed information about its credit analysis to EC was error.

This error by the trial court led to further error through sheer speculation. The trial court speculated that GMAC had set "false targets"

³⁰ GMAC Brief at 32-33. There was no evidence that GMAC had ever provided its credit analysis information to EC in the course of their 12-year contractual relationship or that EC had any expectation of receiving such information.

³¹ Nevertheless, GMAC's July 31 letter made it clear that GMAC was analyzing, and responding to, EC's financial problems as disclosed by EC's financial reports:

Based on an analysis of the Dealership's operating trends, repayment capacity, and available security, GMAC is unable to increase the limit of the Dealership's Revolving Line of Credit or extend a working capital loan to the Dealership.

Further, the deteriorating operating trends and credit base of the Dealership and its poor wholesale performance increase GMAC's credit risk associated with the Dealership's account.

R Ex. 1 (emphases added). Mr. Reggans is an experienced auto dealer with 19 years of experience in the industry, including 12 years operating the EC dealership with GMAC as his floor plan lender. R Ex. 100; RP Vol. X 63:2-64:6. It is not credible to suggest that he did not know that GMAC analyzed his financial information in monitoring the EC loan.

because its financial analysis showed that EC's condition continued to deteriorate over 2008 even though GMAC did not change its proposed restructure terms.³²

This logic is specious and unsupported by any facts. It is undisputed that GMAC did not ask EC to meet any conditions except those contained in the July 31 letter, even though its financial analysis showed EC's continuing financial deterioration. Despite the trial judge's aggressive cross-examination,³³ GMAC's Michele Smith repeatedly testified that GMAC would have honored the July 31 letter had EC met its stated terms. RP Vol. IX 134:19-136:16.

The trial court's "false targets" theory is nothing more than speculation about what GMAC might have done if EC had met its stated restructure terms and if GMAC had then, hypothetically, asked for different restructure terms. It is undisputed that EC never met GMAC's conditions. The trial court's theory of "false targets" misleading EC is

³² The trial court's faulty logic was that because GMAC's financial analysis showed that EC was in worse shape in July and later than was shown in EC's April 2008 financial report, GMAC's July 31 stated conditions were "false targets" and EC actually needed to meet different conditions that addressed its true, much worse financial condition. But GMAC never sought any different restructure terms from EC.

³³ The trial court's "false targets" theory was introduced late in the proceedings by the trial court, not EC, in an extended cross-examination of a GMAC witness by the trial judge himself. RP Vol. IX 131-146.

unsupported by any facts in the record. Bad faith cannot be established through a trial court's speculation about hypothetical possibilities.

4. EC Relies upon Inapposite Case Authority.

EC's argument to apply good faith to the exercise of a contractual right to make demand rests largely on a small number of cases from other jurisdictions that are inapplicable to demand obligations and have been rejected by the majority of courts. *K.M.C. Co. v. Irving Trust Co.*, 757 F.2d 752 (6th Cir. 1985); *Brown v. AVEMCO Inv. Corp.*, 603 F.2d 1367 (9th Cir. 1979); *Reid v. Key Bank of S. Me., Inc.*, 821 F.2d 9 (1st Cir. 1987).

Brown is inapposite: *Brown* was concerned with the use of an acceleration clause as an excuse to advance the due date of a promissory note and does not mention demand obligations. *Solar Motors, Inc. v. First Nat'l Bank of Chadron*, 4 Neb. App. 1, 537 N.W.2d 527, 534 (1995), *aff'd*, 545 N.W.2d 714 (1996).³⁴ *Brown* is inapplicable to the "demand obligation" issues. *K.M.C.* relied upon *Brown*. *K.M.C.* has been widely, and correctly, rejected as authority in demand obligation cases, because the court failed to recognize the fundamental difference between making a

³⁴ EC suggests that GMAC relies only on *Solar Motors*. See GMAC's Brief for the extensive case authority supporting GMAC's position. *Solar Motors* is simply representative of the view of the majority of courts and contains a good concise statement of the reasons why *K.M.C.*, *Brown*, and *Reid* have remained a distinctly minority view.

“demand” and “acceleration.” *Id.* at 536.³⁵ Finally, *Reid* in turn relies upon *K.M.C.* as authority. But the facts in *Reid* are not remotely similar to those presented here.³⁶

D. GMAC’s Wholesale Security Agreement Contained a “Demand Obligation.”

EC attempts to avoid *Badgett* and related cases through a variety of arguments. EC Brief at 37, *et seq.* None of these arguments is meritorious.

First, EC argues that the Wholesale Security Agreement (WSA) is not a demand note or a negotiable instrument.³⁷ These arguments completely miss the point. The WSA contains EC’s obligation “upon demand to pay to GMAC the amount it advances or is obligated to advance.” R Exs. 3, 6.³⁸ *Badgett* holds that “[a]s a matter of law, there cannot be a breach of the duty of good faith when a party simply stands on

³⁵ The *K.M.C.* court stated that “[t]he demand provision is a kind of acceleration clause, upon which the Uniform Commercial Code and the courts have imposed limitations of reasonableness and fairness.” 757 F.2d at 760. A “demand” provision is not an “acceleration” provision.

³⁶ In *Reid*, a loan agreement provided for a loan commitment, and the lender demanded payment under the demand note before the commitment was fulfilled. GMAC had provided funds to EC for 12 years.

³⁷ Contrary to EC’s assertions, GMAC does not argue that the WSA is a demand “note” or a “negotiable instrument.” It is the “very nature” of a “demand obligation” that is the relevant consideration under the cited Official Comment.

³⁸ EC attempts to use an amendment to the WSA, the “delayed payment amendment” (R Ex. 7) to argue that the parties amended the “payable on demand” provision. EC Brief at 38. That amendment applied only to a limited type of sales (commonly known as “fleet sales”) by EC that required pre-approval from GMAC. R Ex. 7, ¶¶ 3-4 (“more than one vehicle per individual transaction, to a customer”).

its rights to require performance of a contract according to its terms.” *Badgett*, 116 Wn.2d at 570.³⁹ Accordingly, GMAC was entitled to be paid “on demand,” regardless of whether the WSA is, or is not, a demand “note” or “negotiable instrument.”

In addition, as numerous courts have recognized, the Uniform Commercial Code’s (UCC) Article 1 excludes “demand instruments or obligations” from the duty of good faith because the “very nature” of “demand instruments or obligations” permits call “at any time with or without reason.”⁴⁰ Official Comment to RCW 62A.1-208.⁴¹ This provision applies to “demand obligations” and is not limited to negotiable instruments or demand notes. EC submits no case authority dealing with

³⁹ See *Glenfed*, 647 A.2d at 857 and numerous cases cited therein (“[The] duty of fair dealing does not ‘alter the terms of a written agreement.’” (citation omitted)).

⁴⁰ GMAC Brief at 21-23. GMAC does not rely on *Allied* for its right to make demand at any time with or without reason. Rather, it relies on the WSA contract language itself. *Allied* explains that the consequence of such a “demand” provision may be that a business is in trouble because it has “lost its financing,” but “that is the agreement that the parties made by appropriate written instruments” and does not violate the duty of good faith. 10 Wn. App. at 534 (quoting trial judge).

⁴¹ “Obviously, this section has no application to demand instruments or obligations whose very nature permits call at any time with or without reason.” Official Comment 1 to UCC § 1-309. Revised Article 1 of the UCC was approved by the National Conference of Commissioners on Uniform State Laws and The American Law Institute in 2001, but it has not been adopted in Washington. Former Section 1-208 is now designated as Section 1-309 in revised Article 1, and this specific sentence in the comment has been relocated to the comments to Section 1-309 to revised Article 1. Washington has retained this sentence in its comment to RCW 62A.1-208.

“demand obligations” where the non-applicability of a duty of good faith turns on “negotiability.”⁴²

Both *Badgett* and the UCC Article 1 Official Comments reach the same result: making demand under a demand obligation does not violate the duty of good faith. Thus, the relevant rights and obligations of the parties at issue here are governed by the specific contract terms of the parties’ contract, *Badgett*, and UCC Article 1, not Article 3.⁴³

Likewise, EC proposes to distinguish pure “demand” notes from “demandable” notes, a theoretical distinction advanced in law review articles from the 1980s and 1990s.⁴⁴ Notably, the distinction was not adopted by the UCC and EC does not cite a single case in which this theory was adopted by a court with respect to the duty of good faith.

⁴² The drafters explicitly recognize that “negotiability” requirements are not intended to dictate results. Official Comment 2 to UCC § 3-104 states that even where a promise does not meet the “negotiability” requirements, “nothing in Section 3-104 or in Section 3-102 is intended to mean that in a particular case involving such a writing a court could not arrive at a result similar to the result that would follow if the writing were a negotiable instrument.” Here, the outcome does not turn in any way upon “negotiability.” Instead, it turns on the nature of demand, which is recognized in Article 1 as existing in “demand obligations” or “demand instruments,” and which excludes the application of the duty of good faith by its “very nature.”

⁴³ EC’s claim that Article 9 governs in case of a conflict between Article 3 and Article 9 is not applicable because Article 1 governs this issue concerning “demand obligations.” In any case, RCW 62A.9A-201(a), to the extent it is applicable, provides that “a security agreement is effective according to its terms between the parties.”

⁴⁴ EC cites a single law journal article, *Banking Law Journal* Vol. 113, No. 8, 815. The proposed distinction would have applied the duty of good faith to a demandable note but not to a demand note.

E. GMAC's Remedies Against Its Collateral Were Conditioned upon a Default; GMAC's Right to Make Demand Was Not; *Coffee* Supports GMAC's Argument.

EC asserts that the WSA contains default contingencies that apply to the “payable upon demand” provision. EC Brief at 39. In fact, the WSA contains no default contingencies that apply to the “demand” obligation.⁴⁵ Instead, GMAC’s *remedies against its collateral* required that the borrower default in one of several ways. R Exs. 2, 3, 6.⁴⁶ But GMAC did not seek replevin against EC until after it had made demand, after EC defaulted, and after EC and Mr. Reggans had converted \$778,000 of collateral proceeds.⁴⁷

Because the “default contingencies” in the WSA apply only to GMAC’s collateral remedies, they do not affect the nature of the “payable on demand” obligation. Thus, EC’s argument – that a default had to occur before GMAC could make demand (and that GMAC “manufactured”

⁴⁵ It is plain from a reading of the WSA that the “default contingencies” apply only to GMAC’s resort to its remedies against the collateral. R Ex. 3.

⁴⁶ In fact, EC correctly states in its brief that “GMAC may repossess vehicles upon enumerated events of default.” EC Brief at 39-40. In addition, it may exercise its other Article 9 rights against collateral other than the vehicle collateral. As the *Glenfed* court noted, Article 9 provisions “govern . . . the handling and disposition of collateral.” 647 A.2d at 859. EC’s suggestion that Article 9 applies to making demand is meritless. EC Brief at 33.

⁴⁷ GMAC filed this lawsuit seeking injunctive relief and replevin on December 31, 2008.

EC's default so it could make demand) – is unsupported by the facts or the contract.

Coffee v. GMAC, 5 F. Supp. 2d 1365 (S.D. Ga. 1998), contrary to EC's argument, recognized that a demand provision is fully enforceable even though it appeared in a contract that contained other provisions (termination of line of credit) that required a default before becoming enforceable.⁴⁸ GMAC Brief at 24-26.

Washington rules of contract interpretation (as EC acknowledges, EC Brief at 47), require a court to interpret a contract in a way, if possible, that gives effect to all of the contract's provisions, and a court should avoid a construction that renders any portion of the contract meaningless. *Seattle-First Nat'l Bank v. Westlake Park Assocs.*, 42 Wn. App. 269, 274, 711 P.2d 361 (1985). Here, both GMAC's right to be paid upon demand and the requirement of a default before exercising remedies against collateral can be given effect.

⁴⁸ Thus, while GMAC was entitled to demand payment of the advances it had made pursuant to the line of credit at any time, it could not terminate the line of credit in the absence of one of the specific events of default enumerated in paragraph 3 of the Loan Agreement.

Coffee, 5 F. Supp. 2d at 1377 (emphasis added and omitted). By comparison, GMAC's WSA with EC does not contain "default contingencies" governing either the "payable on demand" provision or provisions governing termination or suspension of the lending contract. Thus, the default contingencies in the WSA at issue here apply only to GMAC's exercise of its remedies against its collateral.

F. EC's Brief Contains Misleading and Exaggerated Factual Assertions.

EC's argument, like the Oral Opinion, is riddled with misleading and exaggerated statements, including claims that GMAC's actions somehow caused EC's financial downfall that contradict the facts.⁴⁹

1. GMAC Audits

EC exaggerates the supposed impact of GMAC's audits on EC. GMAC had the contractual right to inspect the vehicles and EC's books.⁵⁰ Until December 5, when GMAC discovered EC was seriously "out of trust," GMAC's audits were few and intermittent. R Ex. 97.⁵¹ Mr. Reggans claimed that GMAC's presence on EC's dealership premises⁵² conducting audits in November and the week of December 8 interfered with EC's sales efforts.⁵³ Several witnesses attempted to testify

⁴⁹ The trial court ruled at the commencement of the replevin hearing that damages were not being determined in the hearing (and permitted such evidence only as "background"). RP Vol. I 9:1-7. Thus, proof of damages was not presented and damages issues have not been tried.

⁵⁰ The WSA expressly provided GMAC with a right of access and inspection of the vehicles and related records. R Ex. 3, ¶ 5. GMAC started conducting daily audits after December 5, when GMAC learned that EC was "out of trust" on eight vehicles totaling over \$132,000 since late November. R Ex. 97; RP Vol. I 37:13-38:17, 39:24-40:11.

⁵¹ GMAC conducted a total of 23 audits in the first 11 months of 2008, or approximately two per month on average. R Ex. 97. Nine of these 23 audits were conducted in October and three in November.

⁵² At most, at any one time, there were two GMAC individuals present. RP Vol. II 136.

⁵³ Doug Hobbs, EC's general manager, contradicted this. RP Vol. II 61. As Mr. Reggans had admitted that auto sales went "off a cliff" in 2008, Mr. Hobbs likewise

using as a “script” written statements that originated from a meeting with Mr. Reggans. RP Vol. II 64:20-65:9, 145-147.⁵⁴ EC has a large dealership premises, and it is unlikely that one or two individuals could have much of an effect on any sales. But in any event, putting aside the credibility of such testimony, it is clear that GMAC audits did not “interfere” with EC’s sales efforts prior to late November 2008, at the tail end of EC’s extended financial deterioration (EC’s monthly operating losses totaled \$717,000 through November 2008).

2. GMAC’s Curtailment Demands/Audit Charges

EC also exaggerates the impact of curtailment payments on EC’s operations. A “curtailment” request by a floor plan lender is a common industry practice. RP Vol. II 13:16-14:23 (Cady); R Ex. 115. It is a demand for a partial payment to reduce the outstanding loan balance that is based upon the depreciation of a dealer’s inventory.⁵⁵ RP Vol. VII 10:13-22.

admitted that the market for GM vehicle sales were “substantially down” in December 2008 and had been down throughout 2008. RP Vol. II 84-87.

⁵⁴ Over GMAC’s objection, the trial court permitted several witnesses to testify from written statements they had prepared at Mr. Reggans’ request. RP Vol. II 92-93, 127-129.

⁵⁵ GMAC’s right to demand payment included the right to demand a partial payment. The WSA provided that EC agreed “upon demand to pay to GMAC the amount it advances or is obligated to advance.” R Exs. 3, 6. Because GMAC could make demand for the full amount, GMAC could make demand for partial payments.

The trial court found that GMAC's demand for a "curtailment" payment of approximately \$172,000 in November 2008 was arbitrary because it was not based upon depreciation of a vehicle. GMAC Brief App. at 12-13.⁵⁶ Again, putting aside the trial court's mistaken theory of depreciation, this curtailment demand had no actual effect upon EC's financial condition or operations because EC never paid the \$172,000. EC actually made curtailment payments of approximately \$43,000 in 2008. RP Vol. X 19:5-12.⁵⁷

EC's Brief substantially exaggerates the actual facts. GMAC's requests for curtailment and audit payments, in reality, had virtually no impact on EC's financial problems. Instead, as EC's own financial records establish, EC's extended string of substantial monthly losses were caused by auto sales "going off a cliff" in 2008, not by any act of GMAC.

⁵⁶ This was another example of the trial court reaching a factual conclusion without any supporting testimony. Depreciation of a dealer's *inventory* is based not upon mileage and wear and tear (the vehicles are not being driven) but on the fact that older cars are not eligible for rebates and other sales incentives that make older cars less valuable to dealers because they are not as profitable to sell. RP Vol. IX 104:9-106:18. The trial court's personal opinion of how depreciation of an auto dealer's inventory is calculated is not evidence.

⁵⁷ Likewise, while in the July 31 letter GMAC requested \$500 per audit to cover the cost of the audits it conducted, this only amounted to about \$11,500 through November, 2008, most or all of which was not paid to GMAC.

3. GMAC Used EC's Own Records to Determine Sales Dates and "Out of Trust" Sales

EC argues that GMAC erroneously and arbitrarily determined the "sales date" for EC's sales of vehicles to show that GMAC had "manufactured" a "default" (sales "out of trust") so that GMAC could make demand. While EC spent days and days of testimony at the replevin hearing on this subject, because GMAC had a right to be paid on demand, GMAC did not need to "manufacture" a default in order to make demand. GMAC Brief 18-24. But EC's argument was also contradicted by its own records and the testimony of EC's employees.

GMAC used *EC's own records* to establish the sale dates for vehicles. RP Vol. II 158-159 (Modrzejewski testimony).⁵⁸ Terry Cady, EC's experienced auto dealer office manager,⁵⁹ testified that EC's own records established the sales dates. RP Vol. I 161, 164; R Exs. 11, 12.⁶⁰ Other EC employees confirmed this fact.⁶¹ This was not surprising: EC

⁵⁸ This fact was noted in the July 31 letter: "Audits are based upon information provided by the Dealership." R Ex. 1.

⁵⁹ In October 2008, Ms. Cady replaced Ms. Iverson, who quit over her concern for EC's nonpayment of taxes. RP Vol. I 166-167.

⁶⁰ Ms. Cady had worked at a number of dealerships, including dealerships financed by GMAC. RP Vol. I 166-167.

⁶¹ Linda Welch, EC's title clerk, confirmed this. RP Vol. XI 90:18-91:15, 93:16-95:4. Doug Hobbs, EC's general manager, did also. RP Vol. II 63-64.

had been a dealer with GMAC for 12 years.⁶² Moreover, there was no evidence that EC had previously disputed sales dates (indeed, how could Mr. Reggans legitimately quarrel with EC's own records?) until the replevin hearing, when Mr. Reggans first asserted that the sales dates should be different from what EC had been putting in its own financial records in the ordinary course of its business for years. RP Vol. XIII 76:1-13 (Reggans' testimony). In short, this dispute over sales dates is contradicted by EC's own business records and employees, and was newly "manufactured" by Mr. Reggans in an 11th-hour attempt to create a claim of bad faith.

4. Unsupported Assertions by the Trial Court

Throughout the Oral Opinion the trial court made statements, apparently based upon the judge's personal opinions, without evidentiary support in the record or contradicting the evidence. (1) The trial court's Oral Opinion contains numerous conclusions about what was commercially reasonable or arbitrary. E.g. GMAC Brief App. at 5,12, 14,15,20. But EC produced no witnesses to establish what practices were or were not commercially reasonable in this industry. The trial court's

⁶² If the three-day release privilege was being used to "assault EC's working capital," as the trial judge colorfully put it, GMAC had been using it for 12 years against EC without success. In reality, GMAC had not changed its practice.

personal opinion of what constituted commercial reasonableness in the auto dealership industry is not evidence.⁶³ (2) The trial court concluded that EC was a “high over head business [that] generally showed losses at the beginning of the year. GMAC Brief. App at 7.⁶⁴ (3) The trial court stated that GMAC did not openly and honestly disclose that it did not want to do business with EC in the future, even though the trial court characterized the July 31 letter as a “drop dead” letter (which the trial judge defined as a letter communicating to the reader that the relationship is over and it is just a matter of time before the end (GMAC Brief App at 7)), and even though GMAC did what it said it would do when EC did not meet the July 31 letter’s requests. EC Brief at 22.⁶⁵ (4) The trial court concluded that GMAC was “unreasonable” in refusing to make a real estate loan to EC (EC Brief at 4),⁶⁶ even though GMAC was under no

⁶³ This was not the trial court’s assessment of evidence presented, but rather the complete substitution of the trial court’s personal opinions where no pertinent evidence, expert or otherwise, was offered by EC. There is no way to know the source of the trial court’s personal opinion, or to know if it is based upon his experience in completely different circumstances, and no way to rebut a judge’s personal opinion. Moreover, the trial court’s conclusions often directly contradicted the contract terms. GMAC Brief at 30-32.

⁶⁴ No witness testified that this accounting theory applied to EC’s operations.

⁶⁵ To make the trial court’s view even more confusing, the letter was clearly a “drop dead” letter and was also simultaneously an attempt to mask GMAC’s intent to put EC out of business. EC Brief at 6.

⁶⁶ No witness testified to any standard for considering or making such loans.

obligation to make a real estate loan to EC,⁶⁷ or to notify EC of its decision in any time frame or manner.⁶⁸ (5) The trial court concluded that a personal guaranty means that a “business has no value.” GMAC Brief App. at 10.⁶⁹ (6) The trial court stated that GMAC’s termination of the RLCA and increase of the interest rate were arbitrary actions that were not commercially reasonable, even though both actions were specific contract rights. EC Brief at 2.⁷⁰ (7) The trial court concluded EC was led to believe its past good relationship with GMAC still existed (EC Brief at 22), even though EC produced no evidence that showed that EC’s past good relationship would lead GMAC to ignore EC’s financial deterioration or excuse repeated “out of trust” sales. In sum, the trial court often relied upon conclusory assumptions from his own personal views that were without any supporting testimony or which contradicted the contract terms.

⁶⁷ Mr. Reggans wanted GMAC to provide 100% financing (RP Vol. XIII 100:18-101:3), which GMAC declined to do. RP Vol. I 20:20-23:9. GMAC had no obligation to make a real estate loan to EC. RP Vol. XIV 45:4-46:6.

⁶⁸ The trial court’s logic is difficult to follow. The court claimed that a dealer would want 50 days to adjust to the new conditions, yet the July 31 letter gave EC an additional 90 days to respond beyond Mr. Vick’s first discussion with Mr. Reggans in early June. If anything, the June meeting gave EC an additional 50 days. GMAC then extended its deadline another month to the end of November, and did not make demand until mid-December. In reality, EC had substantial time to meet GMAC’s proposed restructured lending terms, but the continued deterioration of its financial condition did not permit EC to do so.

⁶⁹ No witness testified to this. In fact, personal guaranties are often taken by lenders in a variety of circumstances.

⁷⁰ See GMAC Brief n.52.

G. GMAC Properly Exercised Its Remedies Against GM's Open Account and EC's Retail Banks.

EC claims that GMAC interfered with EC's bank financing in December 2008 and improperly asserted rights against EC's Open Account with GM. EC Brief at 18. GMAC had a right to exercise its contractual remedies against its collateral, which included giving notice to an account debtor to pay GMAC rather than EC. RCW 62A.9A-607(a); 62A.9A-406.

EC's Security Agreement and the RLCA granted GMAC security interests in, among other things, EC's accounts and general intangibles. R Exs. 3, 8. EC's "Open Account" with GM represented money owed to EC by GM.⁷¹ EC's retail banks owed money to EC when a retail customer financed a purchase of a vehicle from EC through one of the banks. Accordingly, these accounts or general intangibles were subject to GMAC's security interest. GMAC therefore had the right to exercise its rights against this collateral by giving notice to these parties to pay GMAC rather than EC.⁷² RCW 62A.9A-607(a); 62A.9A-406. R. Exs. 56, 76. Likewise, later in December, GMAC gave notice to a number of EC's

⁷¹ The term "accounts," as defined in the UCC, includes "a right to payment of a monetary obligation, whether or not earned by performance." RCW 62A.9A-102(2). The term "general intangibles" includes payment intangibles. RCW 62A.9A-102(42).

⁷² This is similar to *Allied*, where the bank had rights against the debtor's accounts with the bank. *Allied*, 10 Wn. App. at 537.

retail banks when GMAC learned that EC was selling vehicles but not paying any proceeds to GMAC. R Ex. 16. Under RCW 62A.9A-406, GM and the retail banks were required to pay GMAC. EC's claim that GMAC "interfered" with its bank financing, when EC was converting the proceeds of vehicle sales, is baseless.

H. Ex Parte Injunctive Relief Was Necessary to Halt EC's and Reggans' Conversion.

EC claims that the TRO shut down EC's business for approximately two weeks in early January 2009. Remarkably, the most relevant facts underlying the TRO and preliminary injunction are entirely omitted from EC's Brief. In the last two weeks or so of December 2008 preceding GMAC's TRO, it is undisputed that EC and Mr. Reggans had converted the proceeds of 33 vehicles totaling approximately \$778,000.⁷³ A TRO was necessary to stop the conversion.

EC's argument is extraordinary and unsustainable. EC contends that its mere *allegations* of bad faith gave EC license to convert sales proceeds⁷⁴ and freed EC from any obligation to comply with its obligations to GMAC – while GMAC simultaneously lost all rights.

⁷³ By omitting these central facts, EC is free to suggest that GMAC obtained the TRO and shut down the business in an oppressive manner, but actual facts show that EC and Mr. Reggans were, in fact, converting sales proceeds payable to GMAC. That is bad faith conduct by EC.

⁷⁴ A security interest in proceeds is a property interest. GMAC Brief at 42-43.

(“GMAC does not have any legal or equitable rights because it breached the Wholesale Security Agreement.” EC Brief at 54.) Not surprisingly, such an argument is not supported by any authority. To the contrary, the very expression of such an extreme position helps explain why injunctive relief was necessary.⁷⁵

The propriety of the TRO was confirmed when the trial court converted the TRO to a preliminary injunction on January 14, 2009.⁷⁶ GMAC Brief at 42-43. EC provided no evidence at the replevin hearing to show that the need to stop EC’s and Mr. Reggans’ conversion of sales proceeds had changed.⁷⁷

If EC were ultimately to prevail on a bad faith claim, it would be entitled to prove its damages, not to convert a property interest, GMAC’s security interest in sales proceeds. Thus, regardless of what the trial court “later” knew about “bad faith,” the trial court had all the relevant facts at

⁷⁵ Unfortunately, not only was there not an adequate remedy at law for GMAC, even a court order was not enough to stop EC and Mr. Reggans from more acts of conversion. GMAC Brief at 14. In March and April 2009, while the replevin hearing was proceeding and despite the outstanding injunction requiring EC to pay GMAC when it sold vehicles, EC sold another 18 vehicles without paying any proceeds to GMAC. CP 52-86.

⁷⁶ The trial court’s preliminary injunction found that “GMAC is in danger of losing their [sic] property and their [sic] remedies under the security agreement signed by both parties” CP 333-337.

⁷⁷ The purpose of a preliminary injunction is to preserve the status quo of the subject matter of a suit until a trial can be had on the merits. *Ameriquist Mortgage Co. v. Attorney Gen.*, 148 Wn. App. 145, 157, 199 P.3d 468 (2009). As noted, in March and April 2009, while the replevin hearing was proceeding, EC and Mr. Reggans ignored the injunction and continued to sell vehicles without paying proceeds to GMAC. CP 52-86.

the time the preliminary injunction was issued. EC was not, under any outcome of this case, entitled to convert the proceeds of vehicle collateral. The injunction was necessary to prevent wrongful conversion of property, was not ‘wrongfully’ issued, and should not have been dissolved.

I. Equitable Principles Are Not Applicable and Were Not Argued.

EC quotes, in sweeping general statements, principles of estoppel, fraud, duress, and coercion as bars to GMAC’s claims for replevin and injunctive relief. EC Brief at 51.⁷⁸ The trial court did not rely upon these theories, they were not argued below, and EC cannot introduce them on appeal. And because GMAC has not yet proceeded with replevin against the vehicle collateral, these cases are not relevant to the issues before the Court. Finally, as RCW 62A.1-103 states, equitable principles may apply “[u]nless displaced by the particular provisions of this Title.” The

⁷⁸ The cited cases have few, if any, legal or factual similarities to this case. How they might apply here is left to pure speculation. *See Brown*, 603 F.2d 1367 (acceleration case); *Bowen v. Danna*, 276 Ark. 528, 637 S.W.2d 560 (1982) (acceleration case); *Urdang v. Muse*, 114 N.J. Super. 372, 276 A.2d 397 (Essex County Ct. 1971) (enforceability of acceleration clause); *Nat’l Bank of N. Y. v. Shaad*, 60 A.D.2d 774, 400 N.Y.S.2d 965, 966 (1977) (“[T]he bank is estopped from asserting any interest in the travel lift by reason of its conduct and oral assurance by its vice-president Keane to defendant that it had no interest therein.”); *Shallcross v. Cmty. State Bank & Trust Co.*, 180 N.J. Super. 273, 434 A.2d 671 (Law Div. 1981) (dispute between creditors); *Gen. Ins. Co. of Am. v. Lowry*, 570 F.2d 120 (6th Cir. 1978) (imposition of equitable lien under unusual circumstances of case); *Lane v. John Deere Co.*, 767 S.W.2d 138 (Tenn. 1989).

provisions of Article 9 “displace” these equitable principles,⁷⁹ and such equitable principles may only be used rarely under Article 9.

J. The Trial Court’s Award of Fees to EC Was Error.

EC was not entitled to an award of attorneys’ fees for defending the replevin motion because this work was not done “solely” to dissolve the injunction. GMAC Brief at 46-48. The trial court invented another new theory to avoid this rule by ruling that the replevin motion and the injunction were “irrevocably intertwined.” The trial court cited no authority for this new rule and admitted at the hearing that he might be making new law and that this was a “new animal.” Appendix hereto, Transcript of July 28 hearing at 46:8-12.

In fact, the situation facing the trial court was not a “new animal.” The trial court simply refused to apply the existing rule of law, which, by its very expression, is designed for circumstances when injunctive relief is sought at the same time other claims are before the court. The rule

79

Article 9, however, compels a different conclusion. Phoenix complied with statutory provisions intended to immunize secured creditors from such claims in all but the rarest of cases. As this is not that sort of case, the equitable impulse for restitution must yield to the Legislature’s command.

Knox v. Phoenix Leasing Inc., 29 Cal. App. 4th 1357, 35 Cal. Rptr. 2d 141, 149 (1994).

expressly and plainly limits the fees recoverable in those situations to fees “solely” expended to dissolve the injunction.

EC never moved to dissolve the injunction. Instead, EC expended all of its fees to present its defenses to the motion for replevin. Accordingly, none of its fees were incurred solely to dissolve the injunction. The trial court’s award of fees was error.

K. The Motion to Amend the Complaint Should Have Been Granted.

EC mistakes the pre-trial replevin hearing conducted in this case for a trial. No trial was scheduled, and the trial court clearly anticipated a subsequent trial.⁸⁰ Leave to amend is to be liberally granted. CR 15. With no trial date even set, there is no basis to assert that EC cannot prepare to respond to the amended claims. Even if EC ultimately proved any bad faith conduct (and EC did not and cannot do so), EC has yet to prove a penny of damages, an issue expressly left for trial by the trial court. EC still actually owes GMAC millions of dollars. Any such amounts awarded to EC would have to set off against EC’s debt to GMAC.⁸¹ The trial court abused its discretion in denying the motion.

⁸⁰ In response to GMAC’s motion to exclude evidence of damages in the hearing, the trial court expressly noted that the replevin hearing was not a damages hearing. RP Vol. I 9:1-2.

⁸¹ The amended complaint also added a claim against Mr. Reggans for conversion, which amounts to nearly \$1 million, which has not been addressed except to the extent

L. An Award of Attorneys' Fees Under the Contract Is Premature.

EC has requested its reasonable attorneys' fees on appeal based upon the reciprocal contract attorneys' fees statute. RCW 4.84.330; R Ex. 3. But the request is premature. No fees can be awarded based upon the contract attorneys' fee clause until the case is concluded and a prevailing party is determined.⁸² Contract fee awards must await a final judgment.

II. CONCLUSION

Under *Badgett*, *Allied*, and the other extensive case authority GMAC submitted, no legal or factual grounds for any findings of "bad faith" can be found in the record. Instead, the record shows the GMAC responded prudently and with restraint to EC's deteriorating financial condition. GMAC was entitled to exercise its contractual remedies, and the trial court should have enforced clear contract provisions. GMAC was entitled to replevy its collateral. The injunction was necessary to prevent EC's and Mr. Reggans' continuing conversion of the proceeds of GMAC's vehicle collateral and was not "wrongfully issued." No fees

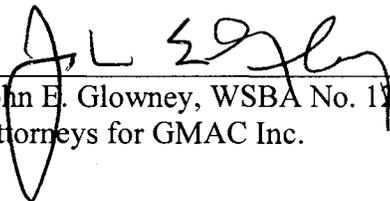
the injunctive relief prevented more acts of conversion. GMAC has filed a separate lawsuit against Mr. Reggans for conversion in King County, where Mr. Reggans resides. The King County Superior Court stayed that action. After remand of this case, GMAC will pursue its conversion claim in a single, appropriate forum and will dismiss one of the actions for conversion.

⁸² "As used in this section 'prevailing party' means the party in whose favor final judgment is rendered." RCW 4.84.330.

should have been awarded to EC because the injunction should not have been dissolved and because EC failed to show that its fees were incurred “solely” to obtain dissolution of the injunction. The motion to amend should have been granted because EC failed to show it could not prepare to meet claims when no trial is yet scheduled. The trial court’s two orders should be entirely reversed and its “findings” of bad faith discarded as lacking legal substance and unsupported by substantial evidence.

Dated this 1st day of March 2010.

STOEL RIVES LLP



John E. Glowney, WSBA No. 12652
Attorneys for GMAC Inc.

CERTIFICATE OF SERVICE

I hereby declare under penalty of perjury under the laws of the State of Washington that I caused a true and correct copy of the foregoing **APPELLANT'S REPLY APPELLATE BRIEF**, to be served on the following:

Counsel for Defendant

Richard A. Bersin
Law Office of Richard A. Bersin
10500 NE 8th St., Suite 1900
Bellevue, WA 98004

Via Email/U. S. Mail

info@bersinlaw.com



Teresa Bitseff, Legal Secretary

Dated: March 1, 2010 @ Seattle, WA

APPENDIX

7 April and March, it's about all the cars that have
8 been converted and which is ongoing, at least up to
9 the June 5th ruling by the Court of Appeals. So
10 putting in two pages of the brief is simply again
11 misleading.

12 The third point is I didn't raise the issue over
13 the Court's jurisdiction. I raised it before, because
14 it was a different issue. I didn't raise it here,
15 because I don't argue that the Court doesn't have
16 jurisdiction. I think the Court has jurisdiction to
17 hear this motion.

18 But on the rules that govern when and whether the
19 Court should grant fees or not fees under those rules,
20 not under the jurisdiction rule, this Court doesn't
21 have settled law before it, and they are not entitled
22 under the arguments I made before. So I didn't raise
23 it, because I am not making that argument. It's not a
24 question of Court's jurisdiction, it's a question of
25 directly applying the rules that apply to this issue.

□

46

1 Thank you, your Honor.

2 THE COURT: All right. Here is what I'm going to
3 do, and as I've indicated earlier in this proceeding I
4 don't like to be making new law, but maybe that's what
5 we are doing in this case.

6 Mr. Glowney has made an argument that I can't award
7 attorney's fees unless it's solely an injunctive

8 action. But I think that this is sort of a new
9 animal. I think that the replevin and the injunction
10 were irrevocably intertwined. And the response I got
11 from counsel didn't convince me any differently. And
12 maybe that's new law on this case.

13 I can't see how, when the plaintiff makes the
14 choice to combine a replevin action and an injunction,
15 especially in this particular case where the scope of
16 the original TRO was way excessive, that was even
17 observed by Judge Allendoerfer after two weeks and he
18 backed that off significantly.

19 I can't see how that would require Everett
20 Chevrolet to somehow make a selection of which cause
21 of action to defend, the replevin or the injunction or
22 somehow split them and try and seriate them. That
23 doesn't make any sense either. You are going to have
24 to do the best you can with what you are faced with.

25 That's addressing the argument that you made about

47

1 this isn't applicable, unless you are solely resisting
2 an injunction.

3 I think they are irrevocably intertwined. I think
4 that's the responsibility of GMAC. And I do not think
5 that defeats the motion for attorney's fees.

6 Given that posture, I do believe that this Court,
7 after a month about, had a full hearing on this, on
8 those issues. And I would remind everyone here that

20

THE COURT: All right.

21

22

23

24

25

MR. WHEELER: As of today, we should have been able to go against this bond. And the fact that Mr. Glowney has questioned this bond, can we have an order from the Court directing Mr. Glowney to inquire of this bonding company whether they are going to stand

□

59

1

2

3

4

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

behind this bond and pay it? And if their answer is no, then we should immediately be able to proceed with the contempt action against GMAC for forcing us to go through all of this litigation when they had no right to force it, they had no right to force us to go through all of these machinations.

THE COURT: So, Mr. Glowney, what's your position on that?

MR. GLOWNEY: That seems to be a relatively confused position to my mind, because the bond wasn't necessary for the replevin action.

THE COURT: All right.

MR. GLOWNEY: It related --

THE COURT: So go ahead and draft the order. When you come up with something, present it.

Court is in recess.

(Proceedings concluded.)