

No.68978-9-I

COURT OF APPEALS
DIVISION I
OF THE STATE OF WASHINGTON

WASHINGTON FEDERAL SAVINGS AND LOAN ASSOCIATION,
a federal association,

Plaintiff/Appellant,

v.

THE McNAUGHTON GROUP, a Washington limited liability
company, and SILVER LAKE WATER AND SEWER DISTRICT,

Defendants/Respondents.

**BRIEF OF RESPONDENT
SILVER LAKE WATER AND SEWER DISTRICT**

INSLEE, BEST, DOEZIE & RYDER, P.S.
Eric C. Frimodt, WSBA #21938
Attorneys for Silver Lake Water and Sewer District
777 - 108th Avenue N.E., Suite 1900
P.O. Box 90016
Bellevue, Washington 98009-9016
Telephone: (425) 455-1234

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WAC 173-240-1046

I. INTRODUCTION

Unfortunately, Respondent Silver Lake Water and Sewer District (“District”) has found itself in the middle of a dispute between Washington Federal Savings and Loan Association (“Washington Federal”) and The McNaughton Group (“TMG”) over the parties’ competing claims of an entitlement to receive “latecomers payments” that are being collected by the District pursuant a Latecomers Agreement entered into in accordance with Chapter 57.22 RCW. For the most part, the District has attempted to remain in a neutral position with respect to the rights and entitlements of Washington Federal and TMG under the Latecomers Agreement that is the subject of the lawsuit and this appeal. As reflected in the District’s Answer to the Complaint and Cross-Claims filed on February 17, 2011 (CP 1348-95), and as reflected in the Stipulation and Agreed Order Relating to Payments Received by the District Pursuant to a Latecomers Agreement entered by the Court on March 24, 2011 (CP 1362-69), the District has acknowledged that Washington Federal and TMG have competing and conflicting claims that need to be resolved by the court. Once the legal issues are resolved, the District intends to abide by the final binding order of the court.

The arguments made by Washington Federal that the Sewer Facilities covered by the Latecomers Agreement constitute “improvements” or “fixtures” raise important public policy issues that required the District’s participation in the underlying litigation and in this appeal. The District is concerned about the potential impact that the Court’s ruling could have on the District, as well as other water-sewer districts in the state, if the Court agrees with Washington Federal’s position that the Sewer Facilities were collateral for the loan and are covered by the deed of trust signed by TMG. The District is submitting this brief with the intent of making sure the Court understands and considers the potential implications of Washington Federal’s arguments.

II. STATEMENT OF THE CASE

For the most part, the District does not take issue with Washington Federal’s statement of the case as it relates to the District’s involvement in the developer extension process through which the Sewer Facilities were constructed. Therefore, the District is only providing a limited statement of the case for the purpose of drawing the Court’s attention to some of the facts that the District believes are important for the Court’s consideration of the issues on appeal.

A. The Developer Extension Agreements Contemplated a Transfer of the Sewer Facilities and a Portion of the Sommerwood Property to the District.

TMG entered into two separate Developer Extension Agreements with the District. One Extension Agreement was dated April 24, 2003 (CP 328-39) (Ex. C to Nesteroff Decl.) and the other Extension Agreement was dated July 14, 2006 (CP 340-55) (Ex. D to Nesteroff Decl.). The 2003 Extension Agreement contained the following provisions:

Paragraph 5(e):

Upon completion of the construction, and after acceptance of the facilities by the District, the Developer shall convey the facilities to the District by means of a bill of sale. . . .

Paragraph 10:

. . . District will accept title to the extension at such time as all work which may, in any way, affect the lines constituting the Extension has been completed, and any damage to said Extension which may exist has been repaired, and District has made final inspection and given its approval to the Extension as having been completed in accordance with the Agreement, the Plans, General Conditions, and Specifications and other requirements of District. The proposed lift station is to be located on a tract within the plat proposed on owner's property, which tract will be dedicated to the District. In the event construction of the lift station is completed and accepted by the District prior to recording of the final plat for owner's property, Developer and owner will execute

necessary easements for operation and maintenance of the lift station until such time as the final plat is recorded dedicating the lift station tract to the District.

CP 331, 334 (emphasis added). The 2006 Extension Agreement contains the same language, with the exception that the last two sentences in Paragraph 10 regarding the dedication of the lift station tract were omitted. CP 347, 349.

It is clear and undisputed that under both the 2003 and 2006 Extension Agreements that the Sewer Facilities being constructed were going to be conveyed and transferred to the District once they were completed. Further, it is clear that under the 2003 Extension Agreement that the tract of land where the wet well and lift station were going to be constructed was going to be severed from the remainder of the Sommerwood property and dedicated to the District.

Pursuant to a Bill of Sale dated February 26, 2009, TMG conveyed and transferred ownership of the following sewer facilities to the District, as originally contemplated by the Extension Agreements: (1) 2,475 lineal feet of 8" HDPE force main; (2) 92 lineal feet of 8" ductile iron pipe; (3) 965 lineal feet of 10" PVC pipe; (4) 68 lineal feet of ductile iron pipe; (5) 24 lineal feet of 12" PVC pipe; (6) five 48"

manholes; (7) one wet well; (8) one lift station; (9) security fencing and gate; (10) generator and fuel tank; and (11) landscaping (the “Sewer Facilities”). CP 362-65 (Ex. F to Nesteroff Decl.). Importantly, approximately 3,300 lineal feet of the force main and pipes are located off of the Sommerwood property and are located within public right of way. CP 549 (Washington Federal’s Second Motion for Summary Judgment, page 8, lines 1-6).

The transfer of ownership of the Sewer Facilities to the District occurred before Horizon Bank’s (Washington Federal’s predecessor in interest) foreclosure of the Sommerwood property which occurred on September 21, 2009. CP 1309-14 (Ex. L to McKenzie Decl.). Further, the tract of land upon which the wet well and lift station were constructed was severed from the remainder of the Sommerwood property as part of the platting process and was conveyed to the District by a statutory warranty deed dated March 23, 2012. CP 677-78 (Ex. 10 to Brain Decl.). As such, the District is the owner of the Sewer Facilities and the small tract of land where the wet well and lift station were constructed. The District’s ownership of the Sewer Facilities and

the associated tract containing the wet well and lift station was expressly contemplated by the 2003 and 2006 Extension Agreements.

B. The District is the Only Entity that can Lawfully Own and Operate the Sewer Facilities at issue in this Case.

The District is authorized by Chapter 57.08.005 to provide sewer and water service within its jurisdictional boundaries. There are three primary methods used by water-sewer districts to finance and/or construct water and sewer facilities: (1) developer extension projects, (2) District extension projects, and (3) projects that are financed and constructed through the formation of a Local Improvement Districts or Utility Local Improvement Districts (LID/ULID). In this case, the Sewer Facilities were constructed as a developer extension project pursuant to the terms of Developer Extension Agreements entered into in accordance with Chapter 57.22 RCW. CP 328-39, 340-55 (Ex. C and D to Nesteroff Decl.). The conveyance and transfer of the Sewer Facilities and the tract of land containing the wet well and lift station to the District was required because domestic sewage facilities, like the Sewer Facilities at issue in this case, are required to be owned and operated by a public entity. WAC 173-240-104.

III. ARGUMENT

A. Public Policy Considerations.

The issue before this Court appears to be a case of first impression. Therefore, the District feels compelled to express its concern about Washington Federal's arguments that attempt to characterize the Sewer Facilities as being collateral which is subject to the deed of trust signed by TMG.

Boiled down to its essence, Washington Federal asserts that the Sewer Facilities are either "improvements" or "fixtures" because they were constructed and attached to the Sommerwood property and are not easily capable of being removed from the property. However, Washington Federal's arguments ignore the statutory process specifically authorized by Chapter 57.22 RCW whereby such Sewer Facilities once constructed will be transferred to the District so that the District becomes responsible for the operation and maintenance of the Sewer Facilities as part of the District's public sewer system for the benefit of the public. In addition, Washington Federal's arguments overlook the fact that a significant portion of the Sewer Facilities are located off site in public right of way and have no connection or attachment to the Sommerwood

property. Finally, Washington Federal's arguments also ignore the fact that the tract of land upon which the wet well and lift station were built was severed from the Sommerwood property and conveyed to the District by statutory warranty deed.

The arguments asserted by Washington Federal suggest that the Sewer Facilities should be treated the same as private sewer and water facilities or irrigation facilities discussed in several cases cited in Washington Federal's brief. Taken to their logical conclusion, if sewer facilities and improvements like those at issue in this case are considered collateral (i.e., whether "improvements" or "fixtures") subject to deeds of trust, creditors like Washington Federal could seek to foreclose on, and take ownership of, public sewer facilities and improvements constructed through the developer extension process which would undermine the construction of public sewer and water facilities using the developer extension process authorized under Chapter 57.22 RCW.

B. The Sewer Facilities are Not Collateral Subject to the Deed of Trust.

Washington Federal cites to a number of cases in support of its arguments that the Sewer Facilities should be treated as collateral for the loan in the nature of "improvements" or "fixtures" since those terms are

included in the deed of trust. However, none of the cases relied upon by Washington Federal specifically addressed public sewer or water facilities like those at issue in this case that were built as part of the developer extension process authorized by Chapter 57.22 RCW. As such, most of the cases relied upon by Washington Federal are simply not relevant to the issues in this case. Moreover, two of the cases relied upon by Washington Federal actually support the District's position that the Sewer Facilities are neither "improvements" nor "fixtures" subject to the deed of trust.

1. The Sewer Facilities are Not Improvements.

Washington Federal cites to *Pinneo v. Stevens Pass, Inc.*, 14 Wn. App. 848, 545 P.2d 1207 (1976) as support for its position that the Sewer Facilities are "improvements" under the deed of trust. *Pinneo* was a case involving a personal injury action resulting when a skier who was night skiing fell and slid into a steel support tower for a chair lift. The specific issue involved in *Pinneo* was whether a ski lift constituted an "improvement" upon real property under RCW 4.16.300 *et seq.* (a series of statutes relating to limitation of actions). Although the facts and legal issues of the *Pinneo* case are not particularly relevant to the issues

before this Court, the *Pinneo* Court's ruling does offer some general guidance relating to the definition of an "improvement" to real property.

The *Pinneo* Court specifically found as follows:

The word "improvement" has been construed previously by a number of cases without reference to these statutes. The term was defined in *Siegloch v. Iroquois Mining Co.*, 106 Wash. 632, 181 P. 51 (1919), as any betterment of a permanent nature which added to the value of the property as real property, and all buildings, structures, and machinery of a permanent nature that tended to increase the value of the property were to be included.

Pinneo, 14 Wn. App. at 851 (emphasis added). Importantly, the definition of an improvement necessarily requires the particular betterment at issue to be "of a permanent nature" upon the real property.

Unlike the ski lift structure at issue in *Pinneo*, the Sewer Facilities were never intended to be of a permanent nature as it relates to the Sommerwood property. In fact, both the 2003 and 2006 Extension Agreements clearly contemplated that once the Sewer Facilities were constructed that they would be transferred and conveyed to the District and would become part of the District's public sewer system. Once conveyed, the District became responsible for future operation, maintenance and repair of the Sewer Facilities.

Moreover, a significant portion of the Sewer Facilities are located off of the Sommerwood property and in public right of way and have no attachment to the Sommerwood property. Finally, the tract of land containing the wet well and lift station was severed from the rest of the Sommerwood property and was conveyed to the District by statutory warranty deed. As such, the facts simply don't support Washington Federal's argument that the Sewer Facilities were intended to be a permanent part of the Sommerwood property. Therefore, the Court should reject Washington Federal's argument that the public Sewer Facilities are "improvements" subject to the deed of trust.

Washington Federal also places emphasis on the fact that when the District approved of the Latecomers Agreement it referred to the Sewer Facilities as "improvements and betterments." Brief of Washington Federal, page 17. Washington Federal's argument in this regard demonstrates a general lack of familiarity with the public utility industry where sewer and water infrastructure is regularly referred to as "sewer improvements" or "water improvements." For example, RCW 57.16.010 provides, in part, as follows: "Before ordering any improvements or submitting to vote any proposition for incurring any

indebtedness, the district commissioners shall adopt a general comprehensive plan for the types of facilities the district proposes to provide.” The fact that the District Board of Commissioners referred to the Sewer Facilities as “improvements and betterments” or the State legislature uses the term “improvements” has no legal relevance or significance to the legal determination of whether the Sewer Facilities constitute collateral under the note and deed of trust signed by TMG.

2. The Sewer Facilities are Not Fixtures.

Washington Federal also argues that the Sewer Facilities are “fixtures” covered by the deed of trust. In support of its position, Washington Federal cites to *Dep’t of Revenue v. Boeing Co.*, 85 Wn.2d 663, 538 P.2d 505 (1975). The specific issue in the *Boeing* case was whether its “jigs” (a tool or equipment used to hold large sections of the aircraft steady and in alignment) qualify for manufacturing tax credits under RCW 82.04.435. While the *Boeing* case does not specifically address the issues presented in our case, the Court’s ruling is still useful in understanding the common law definition of a “fixture” to real property. The Court noted that:

Our starting point is the oft-repeated common law principles, most recently reiterated in *Lipsett Steel*

Products v. King County, 67 Wash.2d 650, 409 P.2d 475 (1965), that:

“The true criterion of a fixture is the united application of these requisites: (1) Actual annexation to the realty, or something appurtenant thereto; (2) application to the use or purpose to which that part of the realty with which it is connected is appropriated; and (3) the intention of the party making the annexation to make a permanent accession to the freehold.”

Boeing, 85 Wn.2d at 667 (emphasis added).

With respect to the actual annexation requirement, as mentioned above, a significant portion of the Sewer Facilities are off site and were not annexed to the Sommerwood property. Further, with respect to the intent of the party making the annexation, it is undisputed that the Sewer Facilities were going to be conveyed and transferred to the District once they were constructed. It is also undisputed that the tract containing the wet well and lift station was going to be severed from the remainder of the Sommerwood property and conveyed to the District. It is clear that TMG did not have the intent to make the Sewer Facilities a permanent part of the Sommerwood property. Therefore, the Court should reject Washington Federal’s argument that the Sewer Facilities are “fixtures” subject to the deed of trust.

IV. CONCLUSION

If sewer facilities and improvements like those at issue in this case are considered collateral (i.e., whether “improvements” or “fixtures”) subject to broad form deeds of trust, creditors like Washington Federal could seek to foreclose on, and take ownership of, public sewer facilities and improvements constructed through the developer extension process. This would undermine the construction of public sewer facilities using the developer extension process which is specifically authorized under Chapter 57.22 RCW. Under the facts of this case, there is no factual or legal basis for characterizing the Sewer Facilities as “improvements” or “fixtures” that are subject to the deed of trust signed by TMG. As a result, the Court should reject Washington Federal’s arguments which seek to extend the concept of collateral under the deed of trust to the Sewer Facilities that were clearly intended to be publicly owned from the beginning of the project.

RESPECTFULLY SUBMITTED this 21st day of November, 2012.

INSLEE, BEST, DOEZIE & RYDER, P.S.

By 
Eric C. Frimodt, W.S.B.A. #21938
Attorneys for Defendant Silver Lake
Water and Sewer District

DECLARATION OF SERVICE

I HEREBY DECLARE that under penalty of perjury under the laws of the State of Washington that on this 21st day of November, 2012, I caused to be served a true and correct copy of the **Brief of Respondent Silver Lake Water and Sewer District** to the individuals named below in the specific manner indicated:

Attorneys for Plaintiff

Gregory R. Fox
Michael A. Nesteroff
Ryan P. McBride
Lane Powell PC
1420 Fifth Avenue, Suite 4100
Seattle, WA 98101-2338
Phone: (206) 223-7000

- Legal Messenger
- U.S. Mail
- Certified Mail
- Overnight Mail
- Fax #
- Email: foxg@lanepowell.com
nesteroffm@lanepowell.com

Attorney for The McNaughton
Group LLC

Christopher I. Brain
Mary B. Reiten
Tousley Brain Stephens PLLC
1700 Seventh Avenue, Suite 2200
Seattle, WA 98101
Phone: (206) 682-5600

- Legal Messenger
- U.S. Mail
- Certified Mail
- Overnight Mail
- Fax #
- Email: cbrain@tousley.com
mreiten@tousley.com

DATED this 21st day of November, 2012, at Bellevue, Washington.


Michelle L. Phommahaxay