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NO. 69365-4-I

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

COLUMBIA ASSET RECOVERY GROUP, LLC,
a Washington limited liability corporation,

Appellant,

v.

JOSEPH R. KELLY, as the Successor Personal Representative of
THE ESTATE OF WILLIAM D. PHILLIPS, SR., deceased.

Respondent.

REPLY BRIEF OF APPELLANT

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I. ARGUMENT IN REPLY

A. Standard of Review.

The standard of review is *de novo* despite the Phillips Estate's ("Estate") attempt to frame CARG's appeal as being from implied findings of fact which this Court should review for "abuse of discretion." *Resp. Br. at 19-20.*

The Estate moved to dismiss for what it called "lack of personal jurisdiction," but the basis for its motion was an argument that the King County venue provision[s] in the Columbia State Bank Business Loan Agreement and Promissory Note had been extinguished by the Bank's assignment of the Loan to CARG, an LLC associated with Tim Kennedy, a Guarantor of the loan. CP 10. It was undisputed that CARG had paid the bank the full amount then owing under the Guarantee and that in exchange the Bank had assigned its rights against Phillips (and thus the Phillips Estate) to CARG for collection against the Estate. (CP-9-10) As a consequence, no finding(s) of fact were necessary concerning any underlying transactional facts.

The only thing one can fairly infer from the trial court's decision to dismiss is that it did conclude that the choice of jurisdiction provisions in the Business Loan Agreement and Promissory Note were extinguished. If the trial court's ruling is treated as amounting to the grant of summary

judgment to the Estate, the standard of review is *de novo*. *E.g., Afoa v. Port of Seattle*, ___ Wn.2d ___, 2013 Wash. Lexis 76 *4 (Jan. 31, 2013). But, even if the dismissal ruling is not treated as a summary judgment ruling, the question of whether an assignment of a debt precludes an assignor from enforcing the obligation in the agreed upon jurisdiction is purely a question of law, and rulings on questions of law are reviewed *de novo*. *Happy Bunch, LLC v. Grandview N., LLC*, 142 Wn. App. 81, 88, 173 P.3d 959 (2007), *rev. denied*, 164 Wn.2d 1009 (2008) (Where the relevant facts are undisputed and the parties dispute only the legal effect of those facts, the standard of review is *de novo*); *and see Edwards v. Edwards*, 83 Wn. App. 715, 720, 924 P.2d 44 (1996) (whether debt is dischargeable is question of law subject to *de novo* review on appeal).

Moreover, even if this appeal called for review of findings of fact – and it does not – the standard would not be “abuse of discretion,” *Resp. Br. at 20*, but rather whether substantial evidence supported the challenged findings. *E.g., McClearly v. State*, 173 Wn.2d 477, 515, 269 P.3d 227 (2012); *Merriman v. Cokeley*, 168 Wn.2d 627, 230 P.3d 162 (2010).¹

¹ The decision on which the Estate relies, *Fernando v. Nieswandt*, 87 Wn. App. 103, 108, 940 P.2d 1380, *rev. denied*, 143 Wn.2d 1014 (1997), is inapposite for two reasons: it was a parenting plan case, and this case is not; and it explains that, although the appellate court “reviews a trial court’s findings for a parenting plan for abuse of discretion,” it “will not disturb the trial court’s findings so long as they are supported by “ample evidence” (quoting *In re Marriage of Schneider*, 82 Wn. App. 471, 476, 918 P.2d 543 (1996)). Thus, the standard of review, even in parenting-plan cases, ultimately

B. The Debtor is Not a Party to the Guaranty, and the Guarantor is Not a party to the Principal Obligation.

The Estate argues that an assignment by a bank of a loan agreement and promissory note discharges the debt if the assignor is a limited liability company associated with a guarantor and the assignment operates to satisfy the guaranty. *Resp. Br. at 20, 28, 29, 30, 31*. Not only is the debt discharged, according to the Estate, but all related rights including the jurisdictional consent provisions in the loan agreements are extinguished by the assignment. CP 18-19.

A false premise underlying each of the Estate's arguments is that a guarantor and principal obligor are joint debtors owing a single obligation. Washington law, however, holds that a guarantor's promise to perform in the event of nonperformance by another is a separate and independent promise distinct from the principal obligation. *Robey v. Walton Lumber Co.*, 17 Wn.2d 242, 255, 135 P.2d 95 (1943). In *Robey* the court explained:

The debtor is not a party to the guaranty, and the guarantor is not a party to the principal obligation. The undertaking of the former is independent of the promise of the latter; and the responsibilities which are imposed by the contract of guaranty differ from those which are created by the contract to which the guaranty is collateral. The fact that both

comes down to whether evidence supports the trial court's findings; the standard is not pure "abuse of discretion."

contracts are written on the same paper or instrument does not affect the independence or separateness of the one from the other.

Id. at 255. Because the principal debtor's obligation is separate from the obligation undertaken by the guarantor, a satisfaction of the guarantee does not discharge the underlying principal obligation. *National Bank of Wash. v. Equity Investors*, 86 Wn.2d 545, 556, 546 P.2d 440 (1976).

The Estate fails to cite a single authority supporting the central contention of its argument that the satisfaction of a guarantee extinguishes the primary obligation. Instead, the Estate's argument for extinguishing the debt is premised on outdated law, e.g. *Duke v. Benson*, 134 Wash 493, 499 (1925), applicable, at best, to the discharge of joint debtors.

C. A Guarantor's Satisfaction of His Guaranty Obligation Does Not Discharge the Underlying Debt but Instead Results in Equitable Subrogation of the Guarantor to the Creditor's Rights Against the Principal Obligor.

In Washington, when a guarantor pays the debt of the principal obligor, the debt is not extinguished as the Estate repeatedly argues without citation to pertinent authority. Instead, the guarantor is subrogated to the creditor's rights and steps into the creditor's shoes. *National Bank of Wash. v. Equity Investors*, 86 Wn.2d 545, 556, 546 P.2d 440 (1976) (guarantor has right in equitable subrogation to step into shoes of the creditor); *Warren v. Nat'l. Sur. Co.*, 149 Wash. 378, 385, 271 P. 69 (1928) (upon payment of a judgment against one guaranteeing a loan, guarantor

entitled to assignment of all legal or equitable rights and interests of the principal debtor, held as security for payment of the debt). The Washington Supreme Court has bluntly stated:

[E]quity will treat the surety as though he were an assignee of the creditor, standing in his shoes to enforce the debt against the debtor

National Bank of Wash., supra at 557. The Estate ignores the distinction between a guarantor and the principal obligor, arguing incorrectly that they are both debtors with joint liability for the same debt. *Resp. Br.* at 30.

1. The Estate Relies on the Outdated Ancient Rule of Discharge in Cases of Joint Debtors, Ignoring the Modern Rule Adopted by the Washington Supreme Court that Follows the Parties' Intentions.

Even if the Court were to ignore the distinction between a guarantor and a principal obligor, the Estate's authorities fail to reflect the current law on the discharge of joint debtors. In 1995, the Washington Supreme Court abrogated the rule of discharge to the extent a creditor reserves rights against non-settling joint debtors. *Seafirst Center Ltd. Partnership v. Erickson*, 127 Wn.2d 355, 370, 898 P.2d (1995). Washington no longer applies the rule of inadvertent discharge advocated by the Estate (sometimes referred to as the "Ancient Rule") but instead applies the Modern Rule based on the intention of the parties:

We are in accord with the trend of modern authority, which tends to modify the strict

common law rule by which joint contract obligors were often released from the burden of their contract by an inadvertent or ill advised release of one of their number. In connection with such questions as this, the modern rule that *the intent of the parties, as expressed by their acts, and particularly by their writings, should receive a greater measure of consideration in determining contract rights*, is clearly expressed in standard texts and judicial decisions.

Seafirst Center, 127 Wn.2d at 364 (citing *Johnson v. Stewart*, 1 Wn.2d 439, 96 P.2d 473 (1939)). Here, the Loan Assignment itself demonstrates that the parties intended to reserve rights against the Estate rather than discharge them. In assigning the debt to CARG, the Bank obligated itself to cooperate with CARG's collection efforts and to verify the amount due to "facilitate . . . collection of the loan from . . . the Estate of Phillips." (CP-272).

There is no evidence that the Bank, CARG, or Kennedy intended to discharge the Estate from its obligations under the Loan and it is implausible that they did so intend. The Estate's argument that the debt was inadvertently extinguished because the intention was to satisfy Kennedy's guarantee makes no sense if the parties were jointly bound to collection efforts against the Estate as well as assigning and preserving the Bank's preferred mortgage against a vessel and security interests in other assets. (CP-271-272).

2. An Assignee Steps in the Shoes of Its Assignor.

In *Puget Sound Bank v. Dep't. of Rev.*, 123 Wn.2d 284, 288 ___ P.2d ___ (1994), the Washington Supreme Court observed that “[a] fundamental understanding of commercial law is that all contracts are assignable unless such assignment is expressly prohibited by statute or is in contravention of public policy.” (citing *Schultz v. Werelius*, 60 Wn. App. 450, 453, 803 P.2d 1334, *review denied*, 116 Wn.2d 1027 (1991); *International Comm'l. Collectors, Inc. v. Mazel Co.*, 48 Wn. App. 712, 716-17, 740 P.2d 363 (1987)). The Court further observed:

An assignee of a contract “steps into the shoes of the assignor, and has all of the rights of the assignor.” *Estate of Jordan v. Hartford Accident & Indem. Co.*, 120 Wn.2d 490, 495, 844 P.2d 403 (1993).

Id. at 292.

The Estate does not dispute that Phillips borrowed and owed over \$1,000,000.00 to the Bank. *Resp. Br. at 10*. The Estate similarly does not dispute that it defaulted on the Loan and that CARG purchased it from the Bank at full face value for \$1,026,071.94. *Resp. Br. at 11 and 13*. Nor does the Estate dispute that the Bank timely filed its probate claim against the Estate. *Res. Br. at 24*. There is no public policy or statutory contravention for the assignment of such a debt. To the contrary,

Washington public policy and commercial law favors assignment. *Puget Sound Bank*, 123 Wn.2d at 288.

While it is of little moment, as all contract rights are assignable and there is an express provision in the Loan Agreement allowing assignment, the Estate suggests in a footnote that the Loan is not a negotiable instrument under the UCC. CP 33; *Resp. Br.* at 27. The Promissory Note nevertheless does contain an unconditional promise to pay the sums owed. CP 36; RCW 62A.3-104(a).

In any event, the Estate has failed to offer any public policy rationale for why a bank should be precluded from selling a commercial loan and promissory note to an LLC managed by a guarantor of that same obligation. Similarly, the Estate offers nothing that would justify the imposition of an equitable remedy such as disregard of a legal entity. Moreover, the Estate argues that the LLC and the Guarantor are one and the same even though that result would not make any difference since, either way, the alter egos would hold the same rights as either assignee or by subrogation to the rights of the Bank.

3. The Bank's Assignment of Its Loan to CARG is Not Invalid Merely Because a Guarantor is a Member of CARG.

The Estate asserts that CARG and Kennedy are alter egos and that CARG as a legal entity may be disregarded because Kennedy satisfied his

guaranty by the assignment to CARG and then used CARG to enforce the Loan Agreement and Note against the Estate by use of the Bank's properly filed probate claim. *Resp. Br.* at 24-28. The Estate suggests that that this is a "scheme" to allow the Guarantor to enforce the Bank's rights against the Estate where the Guarantor had not independently filed a probate claim for the debt. This is, the Estate argues, exactly the kind of "misrepresentations" and injustice that the alter ego doctrine is intended to avoid. *Resp. Br.* at 24-25.

In general, two separate and essential factors must be established in order to pierce the corporate veil. *Dickens v. Alliance Analytical Labs.*, 127 Wn. App. 433, 440 (2005) (citing *Truckweld Equip. Co. v. Olson*, 26 Wn. App. 638, 643, 618 P.2d 1017 (1980)). "First, the corporate form must be intentionally used to violate or evade a duty." *Id.* at 441 (citing *Meisel v. M&N Modern Hydraulic Press Co.*, 97 Wn.2d 403, 410, 645 P.2d 689 (1982)). "Second, the fact finder must establish that disregarding the corporate veil is necessary and required to prevent an unjustified loss to the injured party." *Id.*

Here, the Estate asserts an equitable right of disregard in order to work, and not prevent, an unjustified loss. Having defaulted on its loan obligations and thereby creating the situation resulting in the Bank's demand on Kennedy as Guarantor, the Estate seeks to retain a \$1,250,000

windfall resulting from its own breach of its loan obligations. Absurdly, the Estate asserts it is entitled to this result because Kennedy did honor his guarantee obligations to the Bank.

Corporate disregard applies “when the corporation has been intentionally used to violate or evade a duty owed to another.” *Morgan v. Burks*, 93 Wn.2d 580, 585, 611 P.2d 751 (1980). Here the Estate seeks to foreclose the Bank’s assignee, CARG, the opportunity to collect the debt in the contractually agreed upon jurisdiction where payment was to be made because, the Estate argues, CARG was used to satisfy, not avoid, a duty owed to the Bank. In comparison, the Estate argues this Court should impose the equitable remedy of disregard to unjustly enrich the Phillips Estate and allow it to avoid contractual duties it owes. The trial court erred and incorrectly applied the law in granting the Estate’s motion.

D. Request for Award of Attorney Fees for Appeal.

Pursuant to RAP 18.1(b) and the Agreement and Note, CP 33, 38, CARG requests an award of attorney fees for appeal.

II. CONCLUSION

For the reasons explained above, the trial court erred by granting the Phillips Estate’s CR 12(b)(2) motion and dismissing CARG’s complaint. This Court should vacate the Dismissal Order and the

Reconsideration Order and remand to the trial court for further proceedings.

RESPECTFULLY SUBMITTED this 8th day of February, 2013.

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CERTIFICATE OF SERVICE

I hereby certify under penalty of perjury that under the laws of the State of Washington that on the 8th day of February, 2013, I caused a true and correct copy of the foregoing document, "Brief of Appellant," to be delivered in the manner indicated below to the following counsel of record:

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DATED this 8th day of February, 2013, at Seattle, Washington.



Mary Philomeno, Legal Assistant