

Honorable Thomas S. Zilly

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON AT SEATTLE

FIRST SOUND BANK, a Washington
corporation,

Plaintiff,

v.

LARASCO, INC., a Washington corporation;
LOUIS A. SECOND, JR., an individual;
RICHARD A. SECOND, and individual;
LASCOR, LLC, a Washington limited liability
company; RASCOR LLC, a Washington
limited liability company; ROBERTS
PROPERTIES, INC., a Washington
corporation; SR DEVELOPMENT, LLC, a
Washington limited liability company; DEL
NORTE, LLC, a Washington limited liability
company; BAY HOUSE AT CHELAN, LLC, a
Washington limited liability company; and
SEVRO II, a Washington limited liability
company,

Defendants.

WELLS FARGO EQUIPMENT FINANCE,
INC., a Minnesota corporation; PLAZA BANK,
a Washington corporation; REGAL
FINANCIAL BANK, a Washington
corporation; COWLITZ BANK, a Washington
corporation; WASHINGTON FEDERAL, INC.,

NO. C09-0056 TSZ

FIRST SOUND BANK'S
POST-TRIAL BRIEF RE:
NONDISCHARGEABILITY AND
CONTRACTUAL INDEMNITY
CLAIMS

FIRST SOUND BANK'S POST-TRIAL BRIEF RE:
NONDISCHARGEABILITY AND CONTRACTUAL
INDEMNITY CLAIMS - 1
No. C09-0056 TSZ

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1 a Washington corporation; BANNER BANK, a
2 Washington corporation; and WESTAMERICA
3 BANCORPORATION, a California
4 corporation,

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6 Plaintiff-Intervenors,

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8 v.

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10 FIRST SOUND BANK, a Washington
11 corporation; and LARASCO, INC., a
12 Washington corporation,

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14 Defendants-in-Intervention.
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16 Pursuant to the Court's direction, First Sound Bank ("FSB" or the "Bank") submits this
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18 post-trial brief addressing the claims to be decided by the Court: (1) the Bank's claim that
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20 Defendants' liability for breach of the APA, as found by the jury, is nondischargeable in
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22 bankruptcy pursuant to 11 U.S.C. § 523(a)(2)(A) and (B); and (2) Defendants' claim for
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24 contractual indemnity.

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26 **A. FSB'S NONDISCHARGEABILITY CLAIMS ARE MOOT.**

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28 FSB's claims for nondischargeability in bankruptcy would have applied only to any
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30 liability of Louis Secord or Richard Secord that remained after FSB executed on the writ of
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32 attachment. Given the amount of the jury's award of damages on FSB's claim, the judgment that
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34 will be entered in favor of FSB will not exceed the value of the real property that is the subject of
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36 the writ of attachment. Therefore, barring any retrial after appeal, the nondischargeability claims
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38 are moot. FSB reserves the right to renew those claims in the event of such retrial.
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1 **B. DEFENDANTS ARE NOT ENTITLED TO INDEMNITY FOR ANY COSTS**
2 **ASSOCIATED WITH WELLS FARGO'S CLAIMS.**

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4 **1. The Claims Wells Fargo Tried Against Defendants Were Based Solely on**
5 **Defendants' Conduct Prior to Closing of the APA.**

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7 The evidence presented at trial, as well as Wells Fargo's filings immediately before and
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9 during trial, confirm that Wells Fargo's claims against Defendants do not fall within the scope of
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11 FSB's indemnity obligation under the APA. FSB therefore relies upon its prior briefing on this
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13 issue, Dkt. 515, pp. 31-33. We reproduce for the Court's convenience, and supplement, that
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15 briefing here.

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17 The governing term is APA Section 8.3, which provides in relevant part as follows:

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19 **8.3 INDEMNIFICATION OF SELLER.** In addition to specific
20 indemnity and hold harmless provisions contained elsewhere in this
21 Agreement, Buyer shall indemnify, defend and hold Seller [Larasco] and
22 Shareholders [the Secords] harmless from and against all Indemnified
23 Liabilities [defined in Section 8.2 but irrelevant here] . . . resulting from or
24 arising out of (a) the inaccuracy of any representation or warranty made by
25 Buyer in this Agreement, (b) the nonperformance of any covenant of
26 Buyer set forth in this Agreement, and (c) any and all liabilities and
27 obligations arising from events occurring in connection with the Assets,
28 the Real Property or the Business after the Closing, to the extent not
29 assumed by Buyer pursuant to this Agreement.

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31 TE 89-0032. Wells Fargo's claims against Defendants fall outside the three categories of
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33 "Indemnified Liabilities" identified in Section 8.3. First, Wells Fargo's claims plainly are not
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35 based on any representation, warranty, or covenant made by FSB under the APA, so categories
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37 8.3(a) and 8.3(b) do not apply.

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39 The category of events or claims set forth in Section 8.3(c) is broader than the previous
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41 two categories, as it is not tied to undertakings made in the APA. However, Section 8.3(c) is
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43 limited to "liabilities . . . arising from events occurring in connection with the Assets . . . or the
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1 Business *after the Closing*” (Emphasis added). Wells Fargo’s claims fall outside this
2 definition as well.
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5 Wells Fargo, an investor bank, logically could allege harm in this case from only three
6 categories of conduct: (1) misrepresentations that induced Wells Fargo to purchase lease pools;
7 (2) a failure by a Wells Fargo counterparty to perform on a contract obligation to repurchase
8 defaulted leases or pay on a UNL term; and (3) the termination of the “no-loss” policy in
9 September 2008. The arguments advanced by Wells Fargo and the evidence adduced at trial
10 make clear that Wells Fargo made no claim against Defendants for termination of the no-loss
11 policy, so the third category of conduct is irrelevant and does not bring Wells Fargo’s claim
12 within the APA indemnity.
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21 Nor do the former two categories of conduct trigger any indemnity obligation on the part
22 of FSB. Most fundamentally, it is undisputed that Wells Fargo purchased no lease pools *from*
23 *FSB* (*i.e.*, after Closing, as opposed to from PSL pre-Closing). Therefore, any claim by Wells
24 Fargo that Defendants’ misrepresentations induced that investor bank to purchase lease pools, or
25 otherwise led to damages, is outside the APA Section 8.3 indemnity. Consistent with this point,
26 Wells Fargo’s Trial Memorandum [Dkt. 502] and Proposed Findings of Facts and Conclusions of
27 Law [Dkt. 503] make clear that its claims against Defendants were based entirely on alleged
28 misrepresentations made and breaches of contract by Defendants prior to March 1, 2008, the
29 Closing of the APA. *E.g.*, Dkt. 502 ¶¶ 31-34; pp. 8-9; Dkt. 503 ¶¶ 34, pp.7-8.
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39 Wells Fargo’s claims at trial for breach of contract likewise pertain only to pre-Closing
40 conduct and do not trigger the APA indemnity terms. The relevant contracts are the UNL terms
41 under the Lease Purchase Agreement (“LPA”) and the Secords’ personal guarantees of the lease-
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1 repurchase obligations under the LPA. As the Court is aware, Wells Fargo settled with FSB in
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3 2009. [Dkt. 518-1]. That settlement resolved all of Wells Fargo's claims for conduct committed
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5 on FSB's watch, *i.e.*, post-Closing. As the Court correctly observed during the hearing on
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7 September 12, 2011, Wells Fargo's claimed damages fell into two "buckets," one for pre-Closing
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9 activity of the Secords and one for post-Closing actions, such as the termination of the no-loss
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11 policy. The claims that Wells Fargo presented at trial involved only the former "bucket" of
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13 damages.

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15 Consistent with the settlement agreement, Wells Fargo has specifically forgone any claim
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17 at trial for damages for breaches of the LPA occurring after the Closing of the APA. *E.g.*, Wells
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19 Fargo's Third Supplemental Trial Brief [Dkt. 545] pp. 5 n.10; 9:20-24. The claims under the
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21 personal guarantees signed by the Secords, backing the repurchase obligations under the LPA,
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23 therefore are subject to the same limitation. *E.g.*, Wells Fargo's Second Supplemental Trial
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25 Brief [Dkt. 517] p. 8 ("The Secord Defendants have never revoked either [personal] Guaranty,
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27 and FSB did not undertake to personally guarantee the performance of the leasing division after
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29 certain assets of PSL were sold to FSB."). In sum, Wells Fargo's claims are not within the
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31 indemnity in APA Section 8.3.

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33 **2. The Defendants' Material Breach of the APA Discharges the Bank From**
34 **Any Indemnity Obligation Under That Contract.**

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36 Even if Wells Fargo's claims fell within APA Section 8.3, which they do not, FSB would
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38 not be obligated to indemnify Defendants against defense costs associated with those claims.
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40 That is the case because Defendants' breaches of the APA were "material" within the meaning of
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42 Washington law. As the Court instructed the jury, "[a] 'material breach' is one that substantially
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44 defeats the purpose of the contract, or relates to an essential element of the contract, and deprives
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1 the injured party of a benefit that he or she reasonably expected.” WPI 302.03 (Supp. 2011). A
2 non-material or “partial” breach, in contrast, is one that is “slight or insubstantial,” *Colorado*
3 *Structures, Inc. v. Ins. Co. of the West*, 161 Wn.2d 577, 589, 167 P.3d 1125 (2006), or “trivial or
4 inconsequential.” *Campbell v. Hauser Lumber Co.*, 147 Wn. 140, 265 P. 468 (1928).
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9 The breaches found by the Court and, now, the jury, plainly were not “slight,
10 insubstantial, trivial, or inconsequential.” The Court held that Defendants breached the APA by:
11 (a) conveying over \$2 million of leases that were in default at Closing; and (b) providing the
12 Bank with financial statements showing boosted residuals as a \$2.5 million asset being
13 conveyed. The jury likewise found that Defendants breached the APA. These breaches carried
14 damages of nearly half of the purchase price paid by FSB, and plainly went to the heart of this
15 asset-purchase transaction: the value of the assets being conveyed.
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23 The fact that the jury ultimately awarded lower damages than FSB claimed does not
24 change that result. First, the Washington case law concerning the materiality inquiry uniformly
25 speaks in terms of the nature and significance of breach itself, not the amount of damages that
26 may flow from the breach. Second, the jury’s award to FSB of \$1.22 million is hardly “slight,
27 insubstantial, trivial, or inconsequential.”
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33 Defendants’ material breach of the APA discharged FSB from its obligations under the
34 APA, including the indemnity obligations in Section 8.3. *E.g.*, *Colorado Structures*, 161 Wn.2d
35 at 588-89 (“[I]f the breach is ‘material,’ the promisee . . . may treat the breach as a failure of a
36 condition that excuses further performance, and thus terminate the contract” (footnote
37 omitted)); *Bailie Commc’ns, Ltd. v. Trend Bus. Sys., Inc.*, 53 Wn. App. 77, 81, 160, 765 P.2d 339
38 (1988) (“A material failure by one party gives the other party the right to withhold further
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1 performance as a means of securing his expectation of an exchange of performances. . . . A
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3 material breach suspends the injured party's duties until the breaching party cures the default.
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5 The breaching party has a reasonable time to cure, after which the injured party may either sue
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7 for total breach or rescind and obtain restitution." (citations omitted)). Defendants never cured
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9 that breach. Accordingly, FSB "sue[d] for total breach," and its own obligations under the APA
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11 were discharged.

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13 DATED this 7th day of October, 2011.

14
15 **GORDON TILDEN THOMAS & CORDELL LLP**
16 Attorneys for Plaintiff

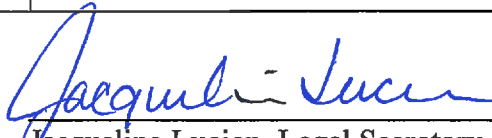
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CERTIFICATE OF SERVICE

I hereby certify that on October 7, 2011, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system, which will send notification of such filing to the following.

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