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UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON

FIRST SOUND BANK, a Washington
corporation,

Plaintiff,

v.

LARASCO, INC., a Washington
corporation; LOUIS A. SECORD, JR., an
individual; and RICHARD A. SECORD,
an individual,

Defendants.

No.

COMPLAINT

Plaintiff First Sound Bank alleges:

I. INTRODUCTION

1. This case arises out of a series of misrepresentations and omissions by defendants in the sale of their equipment leasing business, Puget Sound Leasing Co., Inc. (“PSL CO”). Defendants made these misrepresentations to induce plaintiff First Sound Bank (“FSB”) to purchase a portion of the assets of PSL CO for FSB stock, cash, and other valuable consideration. In purchasing PSL CO’s assets, FSB reasonably believed, based on defendants’ representations, that it was acquiring rights to leases of high quality (*i.e.*, with low delinquency and charge-off rates), and other assets necessary to operate a profitable leasing business.

1 Richard Secord was a member of the FSB Board of Directors from April, 2004 until May,
2 2007. Richard Secord is an owner of Larasco.

3 6. In this Complaint, defendants Louis Secord and Richard Secord are
4 sometimes collectively referred to as “the Secord Defendants.”

5 III. JURISDICTION AND VENUE

6 7. This Court has subject matter jurisdiction over the federal securities claims
7 asserted herein because these claims arise under the laws of the United States. 28 U.S.C. §
8 1331. This Court has supplemental jurisdiction over the remaining claims asserted herein
9 because the claims arise out of the same nucleus of operative facts as plaintiff’s federal
10 securities claims. 28 U.S.C. § 1367.

11 8. Venue is proper in this district because a substantial part of the events or
12 omissions giving rise to plaintiff’s claims occurred in the Western District of Washington.
13 28 U.S.C. § 1391(b).

14 9. This Court has personal jurisdiction over the defendants because each
15 defendant is domiciled in and/or conducts business in King County, Washington.

16 IV. BACKGROUND

17 A. Puget Sound Leasing Co.

18 10. The Secord Defendants founded PSL CO in 1985. PSL CO was in the
19 business of originating and servicing commercial equipment leases. PSL CO entered into
20 leasing agreements with customers—typically businesses in need of equipment—under
21 which PSL CO would acquire the needed equipment and provide it to the customer. In
22 return, PSL CO’s customers agreed to make future monthly payments to PSL CO. PSL
23 CO’s lease agreements typically provided that, at the end of the lease payment, the
24 customer could purchase the leased equipment from PSL CO in return for a payment
25 known as a “residual payment.”
26

1 11. After originating its lease agreements with customers, PSL CO frequently
2 sold its rights to the lease payments (known as “lease payment streams”) to banks or other
3 financial institutions (“Investor Banks”). PSL CO entered into agreements called Program
4 Agreements with the Investor Banks. The Program Agreements set forth the terms under
5 which the Investor Banks could, over time, buy from PSL CO portfolios of lease payment
6 streams.

7 12. Under the Program Agreements, PSL CO retained responsibility for
8 servicing the leases. That is, PSL CO would continue to collect the lease payments from
9 customers, and would forward the money due to the Investor Banks. PSL CO also retained
10 certain rights under the leases, including the right to any residual payments and to collect
11 certain fees from the customers.

12 13. PSL CO also entered into Performance Incentive Agreements with the
13 Investor Banks. The Performance Incentive Agreements provided that PSL CO was
14 entitled to a bonus for each lease payment stream sold to the Investor Bank if, at the end of
15 the lease term, the Investor Bank had received all scheduled payments due under the lease
16 payment stream. For this reason, and other reasons, PSL CO’s profitability was directly
17 related to the quality of the leases it issued, even though in most cases it sold the payment
18 streams to Investor Banks.

19 14. By mid-2007, PSL CO was servicing over 9,000 individual leases. PSL CO
20 had sold the payment streams for most of these lease agreements to Investor Banks pursuant
21 to Program Agreements.

22 **B. The Asset Purchase Agreement**

23 15. Beginning in September, 2004, PSL CO became an FSB customer,
24 maintaining deposits at FSB and obtaining financing from the bank. Other close
25 relationships existed between FSB and PSL CO. Richard Secord was one of FSB’s largest
26 shareholders and had been an FSB director since the bank’s founding. A current FSB board

1 member, James H. Jackson, had in the past provided accounting services to PSL CO, but
2 ceased doing so upon the formation of FSB.

3 16. As a result of the close connections between FSB and PSL CO, the
4 companies began in March, 2007 to discuss the possibility of FSB acquiring most of PSL
5 CO's assets in return for FSB stock, cash, and other consideration. FSB was represented in
6 these discussions by FSB Chairman and CEO Don Hirtzel and FSB President Steve
7 Shaughnessy. PSL CO was represented by defendants Richard Secord and Louis Secord.
8 During many of these discussions (until May 2007), Richard Secord was a member of the
9 FSB Board of Directors.

10 17. FSB was interested in purchasing PSL CO's assets because the Secord
11 Defendants had represented to FSB over time that: (1) PSL CO had a history of excellent
12 financial performance, and that its business model was a highly profitable one; (2) the
13 leases originated by PSL CO were of high quality (i.e., that the delinquency rates associated
14 with the leases were very low), and (3) PSL CO's business practices were sound. Louis
15 Secord told FSB that PSL CO employed the "best controls" and had the "best underwriting"
16 practices in the leasing business, that PSL CO was "run like a bank," and "reported [its
17 financial information] like a bank." The Secord Defendants made these statements and
18 statements similar to them on numerous occasions.

19 18. In connection with their discussions regarding PSL CO's potential sale of
20 assets to FSB, PSL CO provided written financial information to FSB and its agents. The
21 financial information included PSL CO's financial statements for June 30, 2007 and
22 September 30, 2007. FSB also had copies of PSL CO's audited year-end financial
23 statements for each of the years 2000 through 2006. FSB relied on this financial
24 information—including PSL CO's significant profitability as reflected in these financial
25 statements—in evaluating the desirability and terms of a potential purchase of assets from
26 PSL CO.

1 19. On September 24, 2007, FSB, PSL CO and the Secord Defendants entered
2 into an Asset Purchase Agreement. Under the Asset Purchase Agreement, FSB purchased
3 some, but not all, of the assets of PSL CO. Among the purchased assets were PSL CO's
4 rights under most of the leases originated by PSL CO. The purchased assets also included
5 PSL CO's inventory of repossessed equipment and the name "Puget Sound Leasing." The
6 assets not sold to FSB were retained in PSL CO, which was renamed "Larasco," and which
7 is owned by the Secord Defendants.

8 20. In payment for the assets purchased pursuant to the Asset Purchase
9 Agreement, FSB conveyed to PSL CO: (1) 437,500 shares of First Sound Bank stock
10 (valued at \$6,278,125), (2) \$4,500,000 in cash, (3) an agreement to make certain future
11 payments (contingent upon the earnings of the purchased assets), (4) a Consulting
12 Agreement with Richard Secord and an Employment Agreement with Louis Secord, and
13 (5) other valuable consideration.

14 21. As part of the Asset Purchase Agreement, defendants warranted that the
15 information they had provided FSB in connection with the Asset Purchase Agreement was
16 accurate and complete. Specifically:

17 a. In Section 5.13 of the Asset Purchase Agreement, defendants
18 warranted that the financial statements attached to the Agreement were true, and in
19 all material respects fairly represented the financial condition of PSL CO;

20 b. In Section 5.14 of the Asset Purchase Agreement, defendants
21 warranted that PSL CO had no undisclosed liabilities;

22 c. In Section 5.21 of the Asset Purchase Agreement, defendants
23 warranted that PSL CO was in compliance with all contracts to which it was bound;

24 d. In Section 5.28 of the Asset Purchase Agreement, defendants
25 warranted that no representation made by defendants in connection with their sale of
26 assets to FSB contained any untrue statement of material fact, and further warranted

1 that defendants had not omitted any material fact necessary to make the statements
2 made not misleading; and

3 e. In the Closing Certificate, executed on February 29, 2008, defendants
4 again warranted that each representation and warranty set forth in Article V of the
5 Asset Purchase Agreement (including each warranty described in the preceding four
6 subparagraphs) was true and correct.

7 22. Unbeknownst to FSB, each of defendants' warranties was false.

8 **C. Defendants Misrepresented Their Business.**

9 23. Following Closing, FSB began originating and servicing equipment leases
10 under the name "Puget Sound Leasing, a Division of First Sound Bank." Over time, FSB
11 discovered that the information it had received from defendants about PSL CO was, in
12 substantial part, misstated, incorrect and incomplete. Defendants' misrepresentations and
13 omissions materially overstated the financial condition of PSL CO's business, the quality
14 of its leases, its profitability, and the value of the assets that FSB purchased.

15 24. **Misrepresentations Regarding the Quality of the Leases.** The principal
16 misrepresentations made by defendants related to the quality of the leases it had originated
17 and sold to FSB, and the degree to which those leases were delinquent. Defendants
18 represented to FSB that very few leases were delinquent, that PSL CO's delinquency ratio
19 (the percentage of leases greater than 30 days past due) and its charge-off rates were
20 historically insignificant.

21 25. In fact, the delinquency rates of the loans originated by defendants were
22 higher than represented to FSB. Defendants' financial records were maintained in a manner
23 that significantly understated and failed to properly disclose the number of leases in default.
24 For example, in cases where PSL CO had repossessed property on delinquent loans, PSL
25 CO had applied the proceeds of the repossession to future payments due on the loan. In
26 these cases, the financial records PSL CO provided to FSB reflected that the loans were

1 fully performing even though, in reality, the leases had defaulted and were no longer
2 secured by the leased property (which had been repossessed).

3 26. In addition to disguising the level of delinquency in the loans PSL CO had
4 sold to FSB, defendants made additional misrepresentations and omissions that overstated
5 PSL CO's profitability and the value of its assets. These misrepresentations and omissions
6 included:

7 a. **Concealed Liabilities.** Defendants failed to disclose to FSB certain
8 liabilities of PSL CO to brokers, including the business practices that resulted in
9 these liabilities. Defendants' omission of information about these secret costs of
10 PSL CO's business caused FSB to overvalue the profitability of PSL CO and to
11 overestimate the viability of its business model. For example, when PSL CO
12 originated many of its leases, it entered into agreements ("Broker Side
13 Agreements") with the brokers who had referred the customer to PSL CO. The
14 Broker Side Agreements provided that, in addition to paying the broker a
15 commission when the lease was originated, PSL CO would pay the broker a
16 commission when the customer paid the residual payment at the conclusion of the
17 lease. Defendants did not disclose the existence of the Broker Side Agreements to
18 FSB and the liabilities resulting from the Broker Side Agreements were not
19 reflected on PSL CO's financial statements. Defendant Louis Secord maintained
20 the Broker Side Agreements in separate files in his office and did not make the files
21 available to FSB.

22 b. **Inflation of Income.** PSL CO manipulated its financial statements
23 to create the impression that the business's income was substantially higher than its
24 actual income. For example, PSL CO's lease agreements provided that, in cases
25 where a customer failed to make a lease payment on time, PSL CO could "boost"
26 the value of the optional residual payment that the lessee could make to purchase the

1 leased property at the end of the lease term. Under generally accepted accounting
2 principles, PSL CO could only treat the boosted residual payment as income if and
3 when the lessee actually made the residual payment. PSL CO, however, treated the
4 “boosted” residual as income at the time PSL CO “boosted” the residual payment.
5 Because, in many cases, customers never actually made the “boosted” residual
6 payment, this accounting process reflected income that PSL CO never earned.

7 c. **Overstatement of Assets.** Defendants misrepresented the value of
8 the assets to be transferred to PSL CO in connection with the Asset Purchase
9 Agreement. For example, defendants represented on PSL CO’s financial statements
10 that PSL CO’s warehouse contained over \$450,000 worth of repossessed equipment
11 that was the property of PSL CO. In fact, almost all of the equipment belonged not
12 to PSL CO, but to the Investor Banks who owned the payment streams associated
13 with the repossessed property.

14 27. The foregoing misrepresentations and omissions, among others, were
15 calculated to induce, and did induce, FSB to purchase PSL CO’s assets in return for FSB
16 stock, cash, and other consideration. Had FSB known the truth, including material
17 information that defendants failed to disclose to FSB, FSB would not have purchased
18 PSL CO’s assets.

19 **D. Defendants’ Post-Closing Misconduct**

20 28. After the Closing of the Asset Purchase Agreement, Louis Secord, who was
21 then a director of FSB and president of its new Puget Sound Leasing Division, took steps to
22 conceal and perpetuate the misrepresentations and omissions identified above, and to
23 improperly benefit defendants Larasco, himself and Richard Secord at the expense of FSB.

24 29. For example, in March, 2008 (just after the transaction had closed), Louis
25 Secord caused FSB’s Puget Sound Leasing Division to make payments to Investor Banks
26 and take write offs in the amount of \$949,487.43. These payments and write offs were the

1 responsibility of PSL CO—not FSB—because they were associated with payments made
2 (or in the case of write offs, payments not made) to PSL CO before the transaction closed.
3 Defendants failed to fully reimburse FSB for the \$949,487.43—paying FSB only
4 \$460,332.31—and did not disclose and/or attempted to conceal from FSB the fact that FSB
5 had not fully been reimbursed.

6 30. When confronted with this misconduct, Louis Secord admitted defendants’
7 responsibility for failing to reimburse FSB for the full \$949,487.43. Defendants and FSB
8 then entered into a contract entitled Agreement to Clarify Operating Procedures (the
9 “Clarification Agreement”), which was intended to address this issue along with other
10 problems that had arisen after the asset sale. As part of the Clarification Agreement,
11 defendants promised to reimburse FSB for the portion of the \$949,487.43 for which they
12 had not yet made reimbursement.

13 31. However, soon after entering into the Clarification Agreement, defendants
14 disclaimed any obligation to comply with its terms, contending that the Agreement was not
15 enforceable for want of consideration. In fact, the Clarification Agreement was supported
16 by ample consideration, including, among others, FSB’s (1) issuance of a \$2,000,000 line
17 of credit to Larasco, and (2) agreement to increase the value assigned to goodwill under the
18 Asset Purchase Agreement, which was a benefit that defendants had requested.

19 32. On November 19, 2008, FSB relieved defendants Louis Secord and Richard
20 Secord of all responsibilities for operating FSB’s Puget Sound Leasing Division. On
21 January 12, 2009, Louis Secord resigned from the FSB Board of Directors.

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1 **FIRST CLAIM FOR RELIEF**
2 **(Violation of Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5)**
3 **(Against All Defendants)**

4 33. FSB repeats and realleges each and every allegation contained above as if
5 fully set forth herein.

6 34. Defendants made the misrepresentations and omissions identified herein to
7 FSB in connection with FSB's sale to defendants of FSB stock.

8 35. The misrepresentations were false when made. The omissions consisted of
9 information necessary to make statements made, in light of the circumstances under which
10 they were made, not misleading.

11 36. Defendants knowingly and intentionally made the misrepresentations and
12 omissions with the intent to deceive FSB for the purpose of causing FSB to sell defendants
13 the FSB stock. In the alternative, defendants made the misrepresentations and omissions
14 with a deliberate disregard for the truth of the misrepresentations and the misimpressions
15 created by the omissions.

16 37. The misrepresentations and omissions were material to the sale of FSB's
17 stock to defendants. FSB reasonably relied on the misrepresentations and omissions. Had
18 FSB known of the falsity of the misrepresentations, or of the information omitted by
19 defendants, FSB would not have sold its stock to defendants, or it would have sold the stock
20 on terms substantially different than those described in the Asset Purchase Agreement.

21 38. Defendants violated SEC Rule 10b-5 in that they:

22 a. Employed devices, schemes and artifices to defraud;

23 b. Made untrue statements of material facts and omitted to state
24 material facts necessary in order to make statements made, in light of the
25 circumstances under which they were made, not misleading; and/or

26 c. Engaged in acts, practices, and a course of business that operated as a
fraud or deceit on FSB in connection with the sale of its stock.

1 39. FSB was damaged as a consequence of defendants' misrepresentations and
2 omissions. FSB is therefore entitled to rescission of the Asset Purchase Agreement or to an
3 award of damages in an amount to be determined at trial.

4 **SECOND CLAIM FOR RELIEF**
5 **(Violation of the Washington State Securities Act)**
6 **(Against All Defendants)**

7 40. FSB repeats and realleges each and every allegation contained above as if
8 fully set forth herein.

9 41. Defendants made the misrepresentations and omissions identified herein to
10 FSB in connection with FSB's sale to defendants of FSB stock.

11 42. The misrepresentations were false when made. The omissions consisted of
12 information necessary to make statements made by defendants not misleading under the
13 circumstances in which they were made.

14 43. The misrepresentations and omissions were material to the sale of FSB's
15 stock to defendants. FSB reasonably relied on the misrepresentations and omissions. Had
16 FSB known of the falsity of the misrepresentations, or of the information omitted by
17 defendants, FSB would not have sold its stock to defendants, or it would have sold the stock
18 on terms substantially different than those described in the Asset Purchase Agreement.

19 44. Defendants violated the Washington State Securities Act (RCW 21.20.010)
20 in that they:

21 a. Employed devices, schemes and artifices to defraud;

22 b. Made untrue statements of material facts and omitted to state
23 material facts necessary in order to make statements made, in light of the
24 circumstances under which they were made, not misleading; and/or

25 c. Engaged in acts, practices, and a course of business that operated as a
26 fraud or deceit on FSB in connection with the sale of its stock.

1 45. FSB was damaged as a consequence of defendants' misrepresentations and
2 omissions. FSB is therefore entitled to rescission of the Asset Purchase Agreement or to an
3 award of damages in an amount to be determined at trial.

4 **THIRD CLAIM FOR RELIEF**
5 **(Fraudulent Inducement of Contract)**
6 **(Against All Defendants)**

7 46. FSB repeats and realleges each and every allegation contained above as if
8 fully set forth herein.

9 47. Defendants made the misrepresentations and omissions identified herein to
10 FSB in connection with the negotiation of the Asset Purchase Agreement. The
11 misrepresentations were false when made, and the omissions were misleading in light of
12 the circumstances under which other statements were made.

13 48. Defendants knew that the misrepresentations were false when made, and
14 further knew that the omissions were misleading in light of the circumstances under which
15 other statements were made.

16 49. The misrepresentations and omissions were material to the Asset Purchase
17 Agreement.

18 50. FSB entered into the Asset Purchase Agreement in reasonable reliance on
19 the misrepresentations. FSB would not have entered into the Asset Purchase Agreement
20 had it known the information defendants failed to disclose as a consequence of the
21 omissions.

22 51. FSB has been harmed by the misrepresentations and omissions and is
23 entitled to rescission or to damages in an amount to be determined at trial.

24 **FOURTH CLAIM FOR RELIEF**
25 **(Breach of Contract—Asset Purchase Agreement)**
26 **(Against All Defendants)**

52. FSB repeats and realleges each and every allegation contained above as if
fully set forth herein.

1 63. Defendant Richard Secord owed FSB a fiduciary duty to place FSB's
2 interests before his own. This fiduciary duty arose as a result of Richard Secord's position
3 as a director of FSB from April, 2004 until May, 2007 and because other facts and
4 circumstances indicated that FSB reposed in Richard Secord the trust that Richard Secord
5 would place FSB's interests before his own.

6 64. Defendant Richard Secord breached his fiduciary duty to FSB by failing to
7 reveal to FSB the true nature of PSL CO's business, including the falsity of the
8 misrepresentations and the omitted information identified herein.

9 65. Defendant Richard Secord's breaches of fiduciary duties damaged FSB in an
10 amount to be determined at trial.

11 **SEVENTH CLAIM FOR RELIEF**
12 **(Breach of Fiduciary Duty)**
13 **(Against Defendant Louis Secord)**

14 66. FSB repeats and realleges each and every allegation contained above as if
15 fully set forth herein.

16 67. Defendant Louis Secord owes FSB a fiduciary duty to place the interests of
17 FSB before his own interests. This fiduciary duty arises out of Louis Secord's positions as
18 a former member of the FSB Board and as the President of FSB's Puget Sound Leasing
19 Division, and because other facts and circumstances indicated that FSB reposed in Louis
20 Secord the trust that Louis Secord would place the interests of FSB before his own interests.

21 68. Defendant Louis Secord breached his fiduciary duty to FSB by failing to
22 reveal to FSB the true nature of PSL CO's business, including the falsity of the
23 misrepresentations and the omitted information identified herein, and by acting to conceal
24 this information after Closing.

25 69. Defendant Louis Secord further breached his fiduciary duty to FSB by taking
26 steps to benefit defendants at the expense of FSB, including his attempt to provide only

1 partial reimbursement for the \$949,487.43 in payments and charges made by FSB that were
2 the responsibility of defendants.

3 70. Defendant Louis Secord's breaches of fiduciary duties damaged FSB in an
4 amount to be determined at trial.

5 **EIGHTH CLAIM FOR RELIEF**
6 **(Unjust Enrichment)**

7 71. FSB repeats and realleges each and every allegation contained above as if
8 fully set forth herein.

9 72. The value of the FSB stock, cash and other consideration provided to
10 defendants substantially exceeded the value of the assets defendants provided to FSB.
11 Defendants continue to hold the FSB stock, cash, and other consideration. Under the
12 circumstances, defendants' continued retention of these benefits is unjust, and equity
13 compels that they be returned to FSB.

14 **PRAYER FOR RELIEF**

15 WHEREFORE, First Sound Bank respectfully requests the following relief:

- 16 A. Rescission of the Asset Purchase Agreement, including the return to FSB of all
17 stock, cash and other consideration conveyed as part of the transaction, plus
18 statutory interest and incidental damages;
- 19 B. For damages in an amount to be proven at trial;
- 20 C. For FSB's attorney fees, litigation expenses and other costs of suit; and
- 21 D. For such further relief as the Court deems just and proper.

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1 Dated: January 14, 2009.

YARMUTH WILSDON CALFO PLLC

2
3 By 

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