

Honorable Thomas S. Zilly

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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; RICHARD A. SECORD, an 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.

NO. C09-0056-TSZ

SUPPLEMENTAL MEMORANDUM
REGARDING FIRST SOUND BANK'S
NONDISCHARGEABILITY CLAIM
AND DEFENDANTS'
INDEMNIFICATION CLAIM

1 WELLS FARGO EQUIPMENT
2 FINANCE, INC., a Minnesota
3 corporation; PLAZA BANK, a
4 Washington corporation; REGAL
5 FINANCIAL BANK, a Washington
6 corporation; COWLITZ BANK, a
7 Washington corporation;
8 WASHINGTON FEDERAL, INC., a
9 Washington corporation; BANNER
10 BANK, a Washington corporation; and
11 WESTAMERICA BANCORPORATION,
12 a California corporation,

13
14 Plaintiff-Intervenors,

15 v.

16 FIRST SOUND BANK, a Washington
17 corporation; and LARASCO, INC., a
18 Washington corporation,

19 Defendants-In-Intervention.
20

21
22 Defendants submit this memorandum regarding the claims
23 remaining to be tried to the Court following the Verdict entered October 3, 2011.

24
25 **NON-DISCHARGEABILITY**

26 First Sound Bank has asserted that its claims against Louis Secord
and Richard Secord are nondischargeable under 11 U.S.C. §523(a)(2)(A) and

1 §523(a)(2)(B). First Sound Bank has asked the Court to rule on this claim. *See* First
2 Amended Pretrial Order, Section II(A)(6) and (7). Dkt. No. 489.¹

3 The jury found in favor of First Sound Bank on its breach of contract
4 claim against Larasco and the Secords. The jury awarded First Sound Bank
5 approximately \$1.2 million against Larasco and the Secords on this claim.

6 The jury's award to First Sound Bank was significantly less than the
7 amount the jury awarded to the Secords on their counter-claims against First
8 Sound Bank. The jury awarded approximately \$2 million to Louis Secord for the
9 breach of his employment agreement, and more than \$1.4 million to Richard
10 Secord for the breach of his consulting agreement.

11 The Asset Purchase Agreement provides a right of offset under
12 paragraph 8.6 for any monetary obligations or damages due Seller or Shareholders
13 pursuant to the Asset Purchase Agreement or the Ancillary Documents. First
14 Sound Bank invoked this right of offset when it notified the Secords that it would
15 withhold payment under their employment and consulting agreements:

16 [P]lease be advised that First Sound Bank has elected to
17 exercise the right of offset provided by Section 8.6 of the
18 Asset Purchase Agreement, and accordingly will be
19 withholding any payments due Richards Secord under the
20 terms of his Consulting Agreement with First Sound Bank.
21 Similarly, First Sound Bank will be withholding salary
22
23

24
25 _____
26 ¹ Wells Fargo Equipment Finance Inc. also asserted a nondischargeability claim. *See* First Amended
Pretrial Order, Section II(C)(4) and (5). Dkt. No. 489. Wells Fargo's claim is mooted by Wells
Fargo's failure to prevail on its claims at trial.

1 payments due Lou Secord under the terms of his
2 Employment Agreement.

3 TE 210-001.

4 The Secords join First Sound Bank in invoking the contractual right
5 of offset. Because the claims between First Sound Bank and defendants arose from
6 the same transaction, defendants have a right of recoupment as well as a right of
7 offset. Defendants hereby exercise their rights under both doctrines. Defendants
8 will seek entry of judgment in favor of Louis Secord and Richard Secord for net
9 amounts that reflect the offset of First Sound Bank's award. Given that First Sound
10 Bank has no net recovery, the nondischargeability claim should be dismissed
11 based on the bank's failure to establish that it is a creditor.
12
13

14 In addition, First Sound Bank failed to establish the other elements of
15 its nondischargeability claim. The jury rejected First Sound Bank's argument that
16 the Secords were terminated "for cause" based on willful misconduct. The jury
17 also rejected Wells Fargo's fraud claim. These findings by the jury are
18 fundamentally inconsistent with the elements required to prove a
19 nondischargeability claim.
20

21 Defendants respectfully request that the Court dismiss First Sound
22 Bank's claim for nondischargeability with prejudice.
23
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1 **INDEMNIFICATION**

2 Larasco and the Secords have asserted a claim against First Sound
3 Bank for indemnification for losses, including attorneys' fees, incurred in
4 connection with claims asserted by Wells Fargo. The Court has been asked to rule
5 on this claim. See First Amended Pretrial Order, Section II(B)(1)(e). Dkt. No. 489.

7 Pursuant to Section 8.3 of the Asset Purchase Agreement ("APA"),
8 First Sound Bank is obligated to indemnify and hold Larasco and the Secords
9 harmless from:

11 [A]ny and all Indemnified Liabilities (including but not
12 limited to reasonable attorneys' fees incurred in connection
13 with a third party claim . . .) resulting from or arising out of
14 . . . the nonperformance of any covenant of Buyer set forth in
15 this Agreement, and . . . any and all liabilities and
16 obligations arising from events occurring in connection with
17 the Assets . . . or the Business after the Closing, to the extent
18 not assumed by Buyer pursuant to this Agreement.

19 TE 0089-032. Indemnified Liabilities are defined in Section 8.2 of the APA as "any
20 and all claims and causes of action, damages, costs, expenses, liabilities and
21 judgments". TE 0089-031.

22 In connection with the APA, First Sound Bank assumed Puget Sound
23 Leasing's responsibility for performing the contractual relationship between Puget
24 Sound Leasing and Wells Fargo. Section 2.5 of the APA provides:

25 ASSIGNMENTS. Seller shall transfer and assign all
26 Seller Agreements to Buyer, and Buyer shall assume all
Seller Agreements from Seller, as of the Closing Date.

1 TE 0089-015. Section 1.1 of the APA provides that "Seller Agreements" has the
2 meaning specified in Section 2.1(f). TE 0089-010. Section 2.1(f) of the APA
3 provides that the Purchased Assets include: "all Contracts listed or described in
4 Schedule 2.1(f) . . ." TE 0089-012. Schedule 2.1(f) lists the servicing for Wells Fargo
5 Equipment Finance as a Seller Agreement. TE 0089-128.

7 Section 2.3 of the APA provides:

8 ASSUMED LIABILITIES. . . . Buyer shall execute and
9 deliver to Seller the Assignment and Assumption
10 Agreement pursuant to which Buyer shall assume and agree
11 to discharge, when due (in accordance with their respective
12 terms and subject to the respective conditions thereof), the
following Liabilities . . .

13 (a) all obligations and liabilities of Seller under the
14 Seller Agreements that arise on or after the Closing Date or
15 arise prior to the Closing Date to the extent requiring
performance after the Closing Date . . .

16 TE 0089-014.

17 Section 4.4(a) of the APA provides that "At or prior to the Closing,
18 Seller shall deliver to Buyer . . . [the] Assignment and Assumption Agreement duly
19 executed by Seller." TE 0089-017. At closing, the parties executed the Assignment
20 and Assumption Agreement which provides:

22 PUGET SOUND LEASING CO., INC., a Washington
23 corporation, and its shareholders, LOUIS A. SECORD, JR.
24 and RICHARD A. SECORD (collectively "Seller"), in
25 consideration of the payment to it of the sum of Ten Dollars
26 and no/100 (\$10.00) and other good and sufficient
consideration by FIRST SOUND BANK, a Washington state-
chartered commercial bank ("Buyer"), the receipt of which is

1 hereby acknowledged, by these presents, does hereby
2 bargain, sell, grant, convey, transfer, assign and deliver unto
3 buyer, the Contracts, Governmental Permits (to the extent
4 assignable), Equipment Leases, Pending Equipment Leases,
5 leases and subleases of Real Property used by Seller in the
6 Business (collectively "Real Property Leases") and other
7 Seller Agreements (collectively "Seller Agreements"), except
8 any Excluded Assets, purchased or acquired pursuant to
9 that certain Asset Purchase Agreement dated as of
10 September 24, 2007 (the "Asset Purchase Agreement"),
11 between Seller and Buyer, and described in the attached
12 schedules. Seller represents and warrants that, except as
13 disclosed or limited in the attached Asset Purchase
14 Agreement, Seller has good right and full authority to
15 transfer such Contracts, Governmental Permits (to the extent
16 assignable), Equipment Leases, Pending Equipment Leases,
17 Real Property Leases and Seller Agreements.

12 * * *

13 In consideration of this agreement and subject to any
14 required third party consent, Assignee hereby covenants and
15 agrees to pay all charges, and to perform and be bound by
16 all the terms, covenants, conditions, and stipulations of the
17 Seller Agreements to be performed by the Assignor, to
18 assume the position of Assignor under the Seller
19 Agreements, and to indemnify and hold Assignor harmless
20 against all actions, claims and demands whatsoever in
21 respect of said charges, terms, covenants, conditions and
22 stipulations or anything relating thereto, from and after the
23 Effective Date.

20 TE 0089-0049. The effective date for purposes of the closing was March 1, 2008.

21 See Certificate of Closing. TE 0089-00209.

23 Don Hirtzel, Chairman and CEO of First Sound Bank, admitted at
24 trial that First Sound Bank assumed responsibility for performing the contractual
25 relationship between Puget Sound Leasing and Wells Fargo:
26

1 Q Do you agree that First Sound Bank, under the terms
2 of this Asset Purchase Agreement, assumed
3 responsibility for the existing contractual
4 relationships between Puget Sound Leasing and
5 Wells Fargo?

6 A No.

7 Q Is there something in this agreement you rely on
8 when you say that?

9 A Well, again, that was a portfolio that was purchased
10 before our – before the Asset Purchase Agreement
11 was executed – or before the closing was executed.

12 Q Isn't every lease we're talking about in this case,
13 almost, a lease that was purchased before the Asset
14 Purchase Agreement was executed?

15 A Yes.

16 Q But that's what you were buying. You were buying
17 the owned portfolios, owned by Puget Sound
18 Leasing, and you were acquiring the right to service
19 the sold portfolios, weren't you?

20 A We were acquiring the right to service the sold
21 portfolios, yes.

22 Q And you were assuming those obligations relating to
23 servicing those, weren't you?

24 A The obligations, but not the – the agreement that they
25 had with Wells Fargo relating to the loss – the NOL.
26 The NOLs.

Q Do you believe there is somewhere in this Asset
Purchase Agreement that carves that out?

A That was in an agreement that came later.

1 Q Okay. But at the date of closing, you understood that
2 under the terms of this Asset Purchase Agreement,
3 you were assuming responsibility for performing the
4 contractual relationship between Puget Sound
Leasing and Wells Fargo?

5 A Yes.

6 Partial Verbatim Report of Proceedings Before the Honorable Thomas S. Zilly,
7 United States District Judge, dated September 19, 2011, p. 15, line 2 through p. 16,
8 line 7.

9
10 Wells Fargo asserted a breach of contract claim against Larasco
11 under the Lease Purchase Agreement, and a claim for fraud against Larasco and
12 the Secords. The breach of contract claim and the fraud claim were essentially
13 identical in terms of the evidence presented. The damage claims were largely
14 overlapping.² There is no need to debate whether First Sound Bank would have
15 been obligated to indemnify the Secords and Larasco from fraud claims had they
16 not been accompanied by breach of contract claims. No additional legal fees or
17 expenses were incurred in defending the fraud claims.
18

19
20 The evidence indicated that First Sound Bank failed to perform the
21 Lease Purchase Agreement, and then filed a pre-emptive suit against Wells Fargo
22 (and other investor banks), and Larasco. In response, Wells Fargo sued First
23 Sound Bank, the Secords and Larasco. First Sound Bank then settled with Wells
24 Fargo and left the Secords and Larasco to fend for themselves.
25

26 ² See Wells Fargo damage exhibits. TE 608 and 609.

1 At trial, Wells Fargo failed to prove any of its claims against Larasco
2 and the Secords. Accordingly, Larasco and the Secords are prevailing parties
3 with respect to Wells Fargo's claims.
4

5 The Lease Purchase Agreement provides a one-way attorney fee
6 provision in favor of Wells Fargo. Lease Purchase Agreement, ¶16(f). TE 500-009.
7 Under Washington law, a one-way attorneys' fee provision must be applied
8 reciprocally. RCW 4.84.330. However, the Lease Purchase Agreement provides
9 that it is to be governed by Minnesota law. Lease Purchase Agreement, ¶16(e).
10 TE 500-009. Unlike Washington, Minnesota does not appear to require reciprocal
11 treatment of a one-way contractual attorneys' fee provision. It is not clear
12 whether Wells Fargo is required to pay defendants' attorneys' fees under the
13 Lease Purchase Agreement.
14
15

16 Consequently, First Sound Bank should be required to indemnify
17 the Secords and Larasco for all legal fees and expenses incurred in connection
18 with their successful defense of the Wells Fargo claims.
19

20 DATED this 7th day of October, 2011.

21 HALL ZANZIG CLAFLIN
22 McEACHERN PLLC

23 By /s/ Spencer Hall
24 Spencer Hall, WSB No. 6162
25 Janet D. McEachern, WSB No. 14450
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BUSH STROUT & KORNFELD LLP

By /s/ Gayle E. Bush

Gayle E. Bush, WSB No. 07318

Christine Tobin-Presser, WSB No. 27628

Attorneys for Defendants Larasco, Inc.,
Louis A. Secord, Jr., Richard A. Secord,
Lascor, LLC, and Rascor, LLC