BARRON | SMITH | DAUGERT PLLC

ATTORNEYS AT LAW

# BUSINESS AND EMPLOYMENT NEWSLETTER

SECOND QUARTER, 2009

## PURCHASING DISTRESSED ASSETS

By Kirsten Barron

What better time to talk about purchasing distressed assets – there are lots of them around right now and this is an area that has drawn significant interest. We have represented several clients in purchases of distressed assets.

This article focuses on the work that we have been involved in of late – purchasing the assets of an operating company that is operating "underwater," running out of capital, insolvent or in other financial distress.

While assets can be purchased from an entity or person that has filed bankruptcy; however, this article does not address purchasing assets out of a bankruptcy. Note that there are ways to purchase assets out of a bankruptcy – i.e. under §363 of the Bankruptcy Code, under a Chapter 11 plan of reorganization or from a post-confirmation liquidating trust. Bankruptcy adds an additional complication to the distressed assets equation and we suggest you seek the advice of counsel before you venture into purchasing assets out of a bankruptcy.

**Identifying Distressed Assets**

First off, what is a distressed asset? It can be almost any asset, from non-performing mortgages to the assets of an operating business and everything in between.

Our clients have identified distressed assets in two ways: word of mouth or inquiry. You may hear that a business is struggling or read in the public notices that a tax lien has been filed. This is the perfect time to call a business and inquire. I have had two clients call a business owner and make an inquiry about purchasing their business to find that it is perfect timing for both parties. In short, be aware of the information around you and do not be afraid to ask.

**What You Need**

First of all, you need cash or access to cash. Lending is still tight, so move as far down the financing path as you can before you make an offer. You also need to make sure your team of professionals is in place – at minimum you should have an attorney and an accountant. You may want to consider hiring a consultant who has expertise in your area of business and in acquisitions. You also

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CRAM'S SUPERIOR MAP OF WASHINGTON, 1909

## WHY DO BUSINESS IN WHATCOM COUNTY?

By Debbie Nelson

Whatcom County is located within 90 miles of Seattle, Mount Baker Ski Lodge and Vancouver British Columbia. The renowned San Juan Islands and Canadian waters are easily accessible by boat or ferry from marinas and boat launches all over the County. If that is not enough, Whatcom County has exceptional transportation access, including water, rail, highway and air making our county a great choice for trade and economic growth. It is no wonder this is such a desirable place to live and work.

Are you thinking of starting a new business in Washington, or more specifically, Whatcom County? Do you have an established business that is suffering the effects of these uncertain economic times? There is plenty of information available online to assist you with these questions, which can be very helpful, but exhausting to sort through; therefore, I will touch on a couple of important points that will help get you started. Of course, we are always available to answer any questions you may have.

**Tax Incentives/Loan Programs**[1]

The Department of Revenue has a terrific overview, which sets forth tax credit, waiver, and deferral programs for qualifying manufacturers, research and development, high technology, warehousing, and distribution firms. Visit the following link to find detailed information about qualifying programs: http://www.dor.wa.gov/content/findtaxesandrates/taxincentives/incentiveprograms.aspx.

The Federal American Recovery and Reinvestment Act ("Recovery Act"), signed in February by President Obama, is an unprecedented effort to jump-start our economy, create or save millions of jobs. If your small business is having difficulty meeting expenses during these economic times, the U.S. Small Business Administration has a new loan program designed to meet your needs. SBA's America's Recovery Capital Loan Program can provide up to $35,000 in short-term relief for viable small businesses facing immediate financial hardship to help ride out the current uncertain economic times and

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## WE'VE BEEN FLAMINGOED!

Thank you, Flamingos and Friends, for such a delightful and creative way of raising awareness and money in order to fight against cancer. Cancer has touched most of our lives in some way, and we feel honored to have been flamingoed.

## WASHINGTON SUPREME COURT REVERSES RULING REGARDING CANCELLED LLCS

By Sallye Quinn

In the Winter of 2007, we brought you an article regarding a trio of Washington Court of Appeals cases. The court held that lawsuits can be brought against a dissolved limited liability company (LLC) for three years after dissolution, even if a Certificate of Cancellation has been filed, but that an LLC that has been dissolved and either voluntarily or involuntarily filed a Certification of Cancellation cannot bring affirmative claims during the same three year period. *Chadwick Farm Owners Association vs. FHC, LLC*, 139 Wn.App. 300 (2007) (*"Chadwick I"*); *Emily Lane Homeowners Association vs. Colonial Development, LLC*, 139 Wn.App. 257 (2007) ("*Emily I*") and *Maple Court Seattle Condominium Association vs. Roosevelt, LLC*, 139 Wn.App. 257 (2007) (*"Maple Court"*). In addition, in *Emily I*, the Washington Court of Appeals held that members of LLCs can be personally liable for failure to comply with the provisions of the Limited Liability Company Act (the "Act") with regard to winding up a dissolved LLC. All three cases involved suits by condominium owners' associations against condominium developers.

In May of 2009, the Washington Supreme Court issued a combined opinion in which it simultaneously overturned and affirmed portions of *Chadwick I* and *Emily I*. *See Chadwick Farms Owners Association v. FHC, LLC, et al/Emily Lane Homeowners Association v. Colonial Development, LLC*, 2009 Wash. LEXIS 522 (May 14, 2009) ("*Chadwick/Emily II*")[1]. In *Chadwick/Emily II*, the Washington Supreme Court overturned the Washington Court of Appeals' rulings in *Chadwick I* and *Emily I* that lawsuits can be brought against a dissolved LLC where a Certificate of Cancellation has been filed, whether voluntarily or involuntary. The Washington Supreme Court affirmed the rulings that such cancelled LLCs cannot bring affirmative claims and that members who fail to properly

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## CANCELLATION OF INDEBTEDNESS CAN RESULT IN TAXABLE INCOME

By Dennis Williams

As a general rule, the cancellation of a debt creates taxable income to the debtor in an amount equal to the difference between the amount due on the obligation and the amount paid by the debtor. The realization of discharge-of-indebtedness income assumes an economic gain to the debtor from the discharge.

**I. Transactions That May Be Subject to Discharge of Indebtedness Income**

A variety of transactions may produce discharge-of-indebtedness income, but the most common are short sales or foreclosures of real property owned by the debtor.

A sale of property that is encumbered by liabilities can result in a capital gain or loss, or it may result in discharge-of-indebtedness income. Generally, the amount realized from the sale or disposition of property includes the amount of any liability from which the taxpayer is discharged.

For cash method taxpayers, the discharge of an obligation that would have been deductible if paid, does not result in discharge-of-indebtedness income. The discharge of indebtedness attributable to a previously deducted expense of an accrual method taxpayer will generally give rise to discharge-of-indebtedness income.

**II. Exclusions of Discharge-of-Indebtedness Income**

Taxpayers can exclude discharge-of-indebtedness income if: (1) the discharge occurs in a bankruptcy or insolvency case; (2) the indebtedness is qualified farm indebtedness; (3) the indebtedness is qualified real property business indebtedness; or (4) the discharge is qualified principal residence in-

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**To read past issues of our Newsletter, visit our website at:**

**www.barronsmithlaw.com and click on "Links and Resources."**

# *** CHANGE IN 2009 ***
# LLC REINSTATEMENT PERIOD INCREASED TO 5 YEARS

By Debbie Nelson

Effective July 26, 2009, a limited liability company administratively dissolved under RCW 25.15.285 (further defined below) may apply to the Secretary of State for reinstatement within five (5) years after the effective date of dissolution. HSB 1592 http://apps.leg.wa.gov/documents/billdocs/2009-10/Pdf/Bills/House Passed Legislature/1592-S.PL.pdf

**Administrative Dissolution**

The Secretary of State has the authority to administratively dissolve a limited liability company if: 1) the limited liability company does not pay any license fees or penalties when they become due; 2) the limited liability company does not deliver its completed initial report or annual report to the Secretary of State when it is due; 3) the limited liability company is without a registered agent or registered office in this state for sixty days or more; or 4) The limited liability company does not notify the secretary of state within sixty days that its registered agent or registered office has been changed, that its registered agent has resigned, or that its registered office has been discontinued.

**Reinstatement**

Should the Secretary of State exercise its authority and administratively dissolve a limited liability company and the limited liability company did not intend for this to take place, it may now apply to the Secretary of State for reinstatement within five (5) years after the effective date of dissolution. When the reinstatement is effective, it relates back to and takes effect as of the effective date of the administrative dissolution and the limited liability company resumes carrying on its business as if the administrative dissolution had never occurred.

Dissolving a limited liability company is a major decision and one that could potentially affect the lives of its members. Before proceeding with any dissolution process, it is a good idea to consult your attorney and your accountant. See Sallye Quinn's article regarding the cancellation of LLCs on page 3.

Of course, we are available at any time to answer your questions. Please feel free to call us at 360-733-0212.

# CANCELLATION OF INDEBTEDNESS—CONTINUED

debtedness (see below). In return for the exclusions, taxpayers must reduce specific tax attributes, including the adjusted bases of property, to the extent that the discharged indebtedness is excluded from gross income. Section 108 of the Internal Revenue Code provides certain rules regarding the basis reduction required by or elected under these provisions.

**III. Principal Residence Indebtedness**

In December, 2007, Congress enacted the Mortgage Forgiveness Debt Relief Act to provide an exclusion from the normal income recognition rules for forgiveness of indebtedness on a qualified principal residence. The exclusion permits taxpayers to exclude up to $2 million ($1 million for married taxpayers filing separately) from forgiveness of indebtedness. The exclusion applies to forgiveness transactions occurring after 2006 and before 2013. This exclusion is specifically applicable to foreclosures or short sales relating to principal residences.

**IV. Reporting to the IRS.**

Lenders are required to report forgiveness of indebtedness income on Form 1099-C by January 31 of the year following the transaction. The amount reported is income to the taxpayer unless one of the above exceptions applies.

Please note that there are exceptions and limitations to many of the rules, so you will need to carefully review the specific facts in your case before taking any action.

The next edition of this newsletter will feature an article by Sallye Quinn addressing when and how lenders can obtain deficiency judgments against borrowers and guarantors after a non-judicial or judicial foreclosure.

## CANCELLED LLCS—CONTINUED

wind up an LLC during the period of dissolution can be personally liable. Notably, even with the Washington Supreme Court's recent rulings in *Chadwick/Emily II*, our ultimate advice on when and how members of LLCs should dissolve and allow cancellation remains the same, as is addressed in full further on in this article.

In coming to its decision in *Chadwick/Emily II*, the Washington Supreme Court, like the Court of Appeals, went to great lengths to describe the provisions of the Act dealing with dissolution and cancellation. Dissolution can occur in a number of ways, namely (i) the occurrence of an event specified in the limited liability company agreement; (ii) by consent of the members; (iii) by judicial dissolution; and (iv) by administrative dissolution by the secretary of state. RCW 25.15.270. After dissolution, the LLC must be "wound up," which involves "liquidating assets, paying creditors, and distributing proceeds from liquidation of assets to the members of the company." *Chadwick/Emily II*, 2009 Wash. LEXIS 522 at *10-11 (quoting 1 Nicholas Karambelas, Limited Liability Companies, Law, Practice and Forms, Sec. 9:6, at 9-8); RCW 25.15.270; RCW 25.15.295.

In contrast to dissolution, cancellation occurs either when a LLC voluntarily files a certificate of cancellation with the secretary of state after dissolution, or as a matter of law if an administratively dissolved LLC does not seek reinstatement within two years after the date of dissolution[2]. RCW 25.15.080; RCW 25.15.290. Upon cancellation, the limited liability company ceases to exist. *See* RCW 25.15.070, which states that a "limited liability company formed under this chapter shall be a separate legal entity, the existence of which as a separate legal entity shall continue until cancellation of the limited liability company's certificate of formation."

The court then addressed in succession the following three issues: whether a limited liability company may be sued after cancellation;whether a limited liability company has the capacity to sue after cancellation; and whether members of a limited liability company can be personally liable for failure to properly wind up

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## IMPORTANT REMINDER FOR EMPLOYERS: UPDATE YOUR LEAVE POLICIES!!!

Given the abundance of leave law changes in the past eighteen months, including the changes to the Family Medical Leave Act (FMLA) which went into effect on January 17, 2009 and the additional leave entitlements for pregnancy and domestic abuse victims under Washington state law, it is important that employers take time now to properly train their supervisors and HR personnel, and update their leave policies to stay in compliance.

Here's a snapshot of the types of new leave that you want to be sure that your policies address:

- Military Caregiver Leave – up to 6 months (only employers with 50+ employees)
- Military Deployment Leave – up to 12 months for specific deployment-related family responsibilities (only employers with 50+ employees)
- Pregnancy Disability Leave – as much as medically necessary (all employers in Washington)
- Domestic Violence Victim Leave – as much as reasonably necessary to address specific safety, legal and medical needs for the victim and/or family members (all employers in Washington)

Failure to provide required leave could leave you exposed to legal liability, so be sure to take time out now to get in compliance.

For further details, please see articles in past issues of our newsletter: "New FMLA Rules Effective January 16, 2009," 4th Quarter 2008; "Family/Medical Leave Update for Employers," 3rd Quarter 2007; "Leave for Victims of Domestic Violence," 2nd Quarter 2008.

As always, we are available to assist as you navigate these challenging issues and are always happy to answer any questions that you may have about this or any other employment or business law issue.

## CANCELLED LLCS—CONTINUED

after dissolution.

As to the first question of whether a limited liability company may be sued after cancellation, the court held that it cannot, reasoning that pursuant to RCW 25.15.070(2), an LLC ceases to exist as a separate legal entity once the certificate of formation is cancelled. Suits cannot be brought against a cancelled LLC and any suits existing at the time of cancellation abate. Unlike the Washington Court of Appeals, the Washington Supreme Court held that the survival statute of RCW 25.15.303 did not allow suits against a cancelled LLC, only suits against dissolved LLCs during the three year period after the effective date of dissolution. The Washington Supreme Court held that RCW 25.15.303 "means that an action against a limited liability company, whether arising before or after dissolution, must be brought within three years of dissolution, but an action against a limited liability company will abate upon cancellation." *Chadwick/Emily II*, 2009 Wash.LEXIS 522 at *23.

The condominium owners' associations' argued that, unless RCW 25.15.303 were applied to cancelled LLCs, a LLC could ignore its payment obligations, wait two years until it could no longer be sued, or alternatively file a certificate of cancellation in order to avoid liability. The Court correctly noted that under the Act, a dissolved corporation must properly complete the winding up process, which involves paying or making arrangements to pay known obligations and claims. Failure to properly wind up exposes members of a LLC to individual liability. Accordingly, if an LLC were to use the mechanism of cancellation in order to avoid liability, the consequences for the members could be very harsh.

As a final note on the ability to sue cancelled LLCs, the court emphasized that if its interpretation of the Act was not what the legislature had intended, the legislature should change the Act to obtain the result it wanted. However, the court found that the relevant statutes plainly provide that suits against LLCs whose certificates of formation have been cancelled are not authorized by the Act.

As to the second issue of whether a limited liability company has the capacity to sue after cancellation, the court's analysis was brief and succinct. It held that a canceled LLC lacks the capacity to sue, citing RCW 25.15.295(2) and RCW 25.15.070(2). Accordingly, the court upheld the Washington Court of Appeals' rulings in *Chadwick I* and *Emily I*

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## WAGE GARNISHMENTS AND THE FEDERAL MINIMUM WAGE

On July 24, 2009, the federal minimum wage will increase from $6.55/hr. to $7.25/hr. Though Washington has its own minimum wage, the federal amount affects Writs of Garnishments for Continuing Lien on Earnings issued in this state.

When an employer receives a Writ of Garnishment for a current employee, they are required to withhold a portion of that employee's earnings for a period of 60 days in order to satisfy a judgment against the employee defendant. RCW 6.27.150 provides for the amount of earnings exempted from garnishment, or the minimum amount the employee must be paid during the garnishment period. Except for garnishments based on a judgment or other court order for child support or spousal maintenance, the exempt amount is 75% of the *disposable* earnings of the defendant, or 30 times the federal minimum wage, per week. Beginning July 24th, the new minimum exempt amounts will be as follows:

If paid weekly: $217.50
If paid bi-weekly: $435.00
If paid semi-monthly: $471.25
If paid monthly: $942.50

These amounts will apply for the entire 60 day garnishment period.

## IS YOUR ENTITY REQUIRED TO REGISTER AS A CHARITABLE ORGANIZATION?

By Debbie Nelson

The Washington State legislature recently amended the Charitable Solicitations Act, RCW 19.09, to include registration provisions for Charitable Organizations and Commercial Fundraisers. This act requires organizations and commercial firms that raise money from the public for charitable purposes to register with the state and report the financial details of their fundraising campaigns. The intent of the changes is to increase accountability and transparency of nonprofit organizations.

To determine whether your entity falls into the category of having to register as a charitable organization, please review the *Summary of Washington State's Charitable Solicitations Act* provided by the Washington Secretary of State at http://www.secstate.wa.gov/documentvault/SummaryofRegistrationRequirements-2295.pdf. The summary provides an overview of the types of organizations and activities subject to registration as well as those that may be exempt.

The Charitable Solicitations Program registers individuals, organizations, and commercial fundraisers that solicit charitable donations from the general public. Both the benefiting charities as well as independent, for profit entities soliciting funds must, in most cases, register annually. Registration forms and additional information are available at http://www.secstate.wa.gov/charities/. The filing fee for a new registration is $20.00; annual renewals are $10.00.

You can contact a Charities Customer Service Representative by email at charities@secstate.wa.gov or by phone at 800-332-4483. Of course, if you have any questions regarding your entity, please give us a call at (360) 733-0212.

### DID YOU KNOW???

Effective July 27, 2009, an additional recording fee of **$20.00** will be assessed by the Auditor's Office for most documents, making the new recording fee **$62.00** for the first page, and $1.00 for each additional page. This increase does *not* apply to the following documents: appointment of trustee, substitution of trustee, assignment of deed of trust, birth, marriage, divorce, or death or any documents exempted from a recording fee under state law. A deed of trust will cost $63.00 for the first page.

Call the Whatcom County Auditor's Office with any questions at 360-676-6740.

## WASHINGTON LEGISLATURE AMENDS DEED OF TRUST STATUTE

By Sallye Quinn

After nearly 10 years with no amendments to the deed of trust statute, the Washington State legislature has now amended the statute for the second time in a 15-month period. In March 2008, Governor Christine Gregoire signed into law two bills amending the deed of trust statute. Those changes were effective as of June 12, 2008 and were detailed in an article in our 2008 Spring Quarter newsletter. On April 30, 2009, the Governor signed Engrossed Senate Bill 5810, which once again significantly revises the deed of trust statute. The changes will take effect on July 26, 2009.

The new changes focus almost entirely on providing additional protection to homeowners and tenants during and after foreclosure, especially with regard to subprime loans. In fact, one of the most significant changes applies only to deeds of trust securing non-commercial loans that were made between January 1, 2003 and December 31, 2007, during the key subprime lending period. The same law expires on December 31, 2012. Presumably, if such subprime deeds of trust were to go into foreclosure, the foreclosure would have been commenced by the December 31, 2012 expiration date. The changes force lenders to have greater contact with borrowers prior to foreclosure being initiated and greatly enhance the notice requirements and time to vacate properties of tenant-occupied residential properties.

The specifics of the changes are detailed as follows:

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# PURCHASING DISTRESSED ASSETS—CONTINUED

need time. It takes a tremendous amount of time to wade through this process. If you do not have the time or the financial wherewithal to do this right, it is better to stay on the sidelines than to purchase assets that you know to be under distress or at risk.

**Due Diligence**

We have touted the importance of due diligence when purchasing anything, and it is even more true in the distressed asset purchase. Because there is financial distress, you can be certain that there will be some lien or claim against the assets, such as an unpaid creditor, back taxes, or a contract out of

compliance. Therefore, it is very important to carefully review the financials and the existing contracts, to ask for a disclosure of any claims against the assets, and to confirm that all taxes and wages have been paid. You may have to take over some existing debt or obtain the approval of lenders, landlords or others in contractual relationships with the seller. Due diligence is the time to figure this out. Due diligence is the most important aspect of purchasing distressed assets.

**Asset Purchase Agreement and Representations and Warranties of the Seller**

Any asset sale should be documented by an Asset Purchase Agreement (APA). A good APA will contain representations and warranties about the assets. Representations and warranties (or reps and warrants for short) are basically promises about the assets. Reps and warrants can include promises that there are no liens or claims against the assets, taxes are paid, contracts are not in breach, etc. Reps and warrants dovetail with due diligence in that you should confirm what your investigation has shown and what it cannot show – such as whether there are any unrecorded claims against the assets. It is critical that you clearly indicate what you are buying and what you are not, what you are responsible for and what you are not and what promises about the assets the seller makes. APAs can be complicated agreements in the best of situations, and it is especially important to seek legal counsel to help you navigate through a sale complicated by a financial distress situation.

**Value**

We have found that the quicker the buyer can come up with the cash, the better the deal or, rather, the lower the price. While due diligence may be the most important factor in purchasing distressed assets so you know what you are getting into, the biggest benefit is that your price is usually deeply discounted. The buyer should consider what the liquidation value of the assets is – it may be that liquidation is the seller's only option if a sale does not go through quickly. A buyer should also consider what would happen if the assets went into bankruptcy. A buyer will likely want to offer more than the liquidation value or more than the seller would get in a bankruptcy. The buyer has tremendous leverage over the seller because the seller is often out of options. I have found these purchases are most successful when the acquired assets have a value greater to the buyer than the purchase price – the purchased assets create a synergy or leverage another aspect of the buyer's business. In other words, the existing business and the acquired assets together have a value greater than the individual values of the two.

**Conclusion**

The current economic situation has lots of challenges and lots of opportunities. The purchase of distressed assets is not for the faint-hearted. It can be a lengthy, difficult and risky process. The sale of a business usually comes with celebratory champagne or sparkling cider. In our experience, distressed asset sales often end with a bittersweet taste, but they can also be a great opportunity.

## DOING BUSINESS IN WHATCOM COUNTY—CONTINUED

return to profitability. Each small business is limited to one ARC loan. ARC loans will be offered by some SBA lenders for as long as funding is available or until September 30, 2010, whichever comes first. Click on the following link to see if your company is eligible:

http://www.sba.gov/recovery/arcloanprogram/REC_ARCLOAN_ELIGIBLE.html.

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For a list of grant opportunities for businesses in Washington visit: http://access.wa.gov/business/grants_forprofit.aspx

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For a list of federal grant opportunities for businesses visit: http://www.grants.gov/search/category.do

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To search for loans, grants & financing visit: http://search.business.gov/startLoans.html

**Additional Resources**

Whatcom County

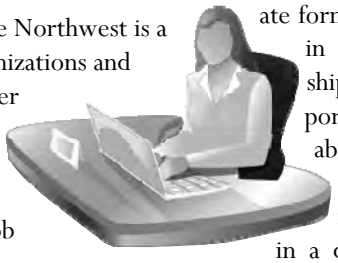
Following are some useful links to groups located in Whatcom County that assist new or existing businesses:

- Bellingham/Whatcom Chamber of Commerce & Industry is a great networking resource, organizing a monthly Networking Breakfast and sponsoring a monthly After Business program in a casual, social environment. Visit: http://www.bellingham.com/

- Western Washington University's College of Business and Economics offers no-cost, one-to-one, confidential, customized business counseling and technical assistance to businesses in Whatcom County. Visit: http://www.cbe.wwu.edu/sbdc

- SCORE (Service Corps of Retired Executives) is a nonprofit association dedicated to entrepreneur education and the formation, growth and success of small business nationwide. For information about workshops, business resources, and FAQs related to Whatcom County's local SCORE office. Visit: http://www.scorechapter591.org

- WorkSource Northwest is a network of organizations and "one-stop" Career Centers that offer a variety of services to businesses and job seekers. Visit: http://www.nwboard.org/index.htm



Washington State

- CTED (Washington State Department of Community, Trade and Economic Development) recently published the 2009 CTED Guide for Small Business in Washington. This guide assembles in one handy reference, information on organizations, services and programs throughout the state. Visit: http://www.choosewashington.com/business_resources/2009_Guide_for_Small_Business.asp

- Department of Labor and Industries (L&I): http://www.lni.wa.gov/

- Department of Licensing (DOL): http://www.dol.wa.gov/business/

- Department of Revenue (DOR): http://dor.wa.gov/content/doingbusiness/

- Employment Security Department (ESD): http://www.esd.wa.gov/

- Office of the Secretary of State (SEC): http://www.secstate.wa.gov/corps/

We frequently assist startup companies with choosing the appropriate form of business entity and in structuring partnerships, joint ventures, corporations and limited liability companies. We are committed to helping each client succeed in a dynamic business environment. We are available to answer any questions you may have regarding this article, or any other business questions you may have.

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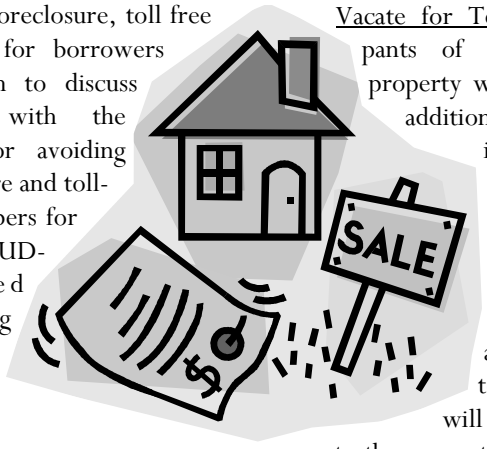
[1]We note that most of these opportunities require a written business plan. Tom Dorr, a small business advisor, states "[t]here is one proven way to increase your businesses likelihood of success, whether your business is a start-up or 15 years old: WRITE A BUSINESS PLAN." Visit: http://www.cbe.wwu.edu/sbdc/public/plan.doc.

## DEED OF TRUST STATUTE—CONTINUED

1. "Meet and Confer" Obligation. The legislature added an entirely new provision to the Deed of Trust statute that requires lenders to contact non-commercial borrowers 30 days prior to sending out a Notice of Default. All contact can be made by letter or phone and must "assess the borrower's financial ability to pay the debt secured by the deed of trust and explore options for the borrower to avoid foreclosure." The borrowers must also be provided with the toll-free telephone numbers for HUD-certified housing counseling agencies, the Department of Financial Institutions and the statewide civil legal aid hotline. During the initial contact, the beneficiary must advise the borrower that he or she has the right to request an additional meeting.

If a subsequent meeting is requested, the meeting must be scheduled within 14 days of the request. The requirement to meet with the borrower can be waived if, despite due diligence on the lender's behalf, the lender is unable to contact the borrower. Lenders are also required to post a link on their home page to certain information such as options available to borrowers who wish to avoid foreclosure, a list of documents borrowers should collect and have when discussing options to avoid foreclosure, toll free numbers for borrowers who wish to discuss options with the lender for avoiding foreclosure and toll-free numbers for finding HUD-certified housing counseling agencies.




The "meet and confer" requirement does not apply if:

a) the borrower has already surrendered the property to the lender;

b) the borrower has filed for bankruptcy and the stay remains in place or relief from the stay has been obtained;

c) the deed of trust secures a commercial loan;

d) the deed of trust secures the obligations of someone other than the borrower or a guarantor;

e) the deed of trust secures an obligation that was financed all or in part by the seller; or

f) the deed of trust was not entered into between January 1, 2003 and December 31, 2007.

Notices of Defaults must contain a declaration from the beneficiary as to the beneficiary's compliance with the "meet and confer" requirement.

The provisions of the "meet and confer" requirement expire on December 31, 2012.

2. Additional Notice to Tenants in Possession; Additional Time to Vacate for Tenants. Occupants of tenant-occupied property will now receive additional notice advising them that the property may be sold at foreclosure 90 days or more after the notice and advising tenants that they will have 60 days to vacate the property after the sale. This new notice must be posted on the property and mailed to "Resident of property subject to foreclosure sale." After the sale is completed, purchasers of tenant-occupied property must provide notice to tenants and occupants advising them (1) of the date of sale; (2) that previous owners and occupants have 20 days to vacate; and (3) that tenants and occupants have 60 days to vacate.

Tenants or subtenants now have 60 days to vacate as opposed to the previous 20 days. However, tenants can be evicted prior to that time if they are committing waste or nuisance. In addition, the change specifically provides that purchasers at a trustee's sale can negotiate a new purchase or rental agreement with the tenants.

Interestingly, the new 60-day requirement conflicts with new federal law, which provides tenants 90 days to vacate. As noted in a recent article in the Seattle Times, the conflict between the two laws remains confusing as to which time period should apply. *See* http://seattletimes.nwsource.co

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## DEED OF TRUST STATUTE—CONTINUED

m/html/localnews/2009421916_renters06m.html Notably, the federal law requires that tenants continue to pay rent during the 90–day period, whereas the Washington Law does not require tenants to pay rent during the 60-day period. For the time being, lenders will want to evaluate on a case-by-case basis which law they choose to apply, but the most careful of lenders will likely attempt a melding of the two, which would allow tenants to stay rent-free for 90 days.

3. Non-Waiver of Claims. The new law provides that certain claims relating to foreclosures of owner-occupied residential property are no longer waived if a borrower or grantor fails to bring a civil action to enjoin a foreclosure sale. Those claims include common law fraud or misrepresentation, violations of Title 19 RCW and failure of the trustee to materially comply with the requirements of a non-judicial foreclosure. Any suit must be brought within two years of the sale and is limited to seeking monetary damages. The claim cannot affect the validity or finality of the foreclosure sale or a subsequent transfer, or encumber or cloud title. The statute even prohibits the filing of a lis pendens in connection with such claim.

4. Proof as to Holder of Obligation. Prior to recording the Notice of Trustee's Sale, the trustee must have proof that the beneficiary is the owner of the promissory note or obligation secured by the deed of trust. A declaration signed by the beneficiary and made under penalty of perjury will satisfy this requirement and the trustee is entitled to rely on the declaration as evidence of proof.

5. Trustee's Duties. In the revisions to the deed of trust statute that were enacted in 2008, the legislature clarified that the trustee has no fiduciary duty or fiduciary obligation to the grantor or other persons with an interest in the property subject to the deed of trust. Now, the legislature has revised the law to presumably clarify that the lack of fiduciary duty does not mean that the trustee can act in bad faith by specifically providing that the "trustee or successor trustee has a duty of good faith to the borrower, beneficiary, and grantor."

For many lenders, the "meet and confer" requirement simply puts into legislation what they in practice already do. However, the legislation makes the process more technical and formal. For a number of lenders, however, especially those that own notes that have been bundled and sold a number of times and that outsource servicing of their loans offshore to places such as India, this requirement will be onerous and will force them to have contact with borrowers that never would have occurred otherwise. Trustees will need to exercise great care in dealing with large institutional lenders to make sure that the sworn statements as to compliance with the "meet and confer" requirement can be trusted and have been signed by someone with the authority to act on behalf of the borrower.

In addition, trustees will need to update their checklist for foreclosure of residential properties as follows: 1) inclusion of the declaration from the beneficiary as to the "meet and confer" requirement in the Notice of Default; 2) receipt of a declaration from the beneficiary as to ownership of the note or obligation; and 3) posting and mailing of additional notice for tenant-occupied properties. Lawyers who are asked to evict owners, occupants or tenants by purchasers at a foreclosure sale will need to either send the newly required post-sale notice or have their clients send such notice prior to commencing eviction proceedings.

### DID YOU KNOW???

Effective July 1, 2009, filing fees in the state courts were increased to help cover a budget shortfall. The filing fee for civil cases is now $230 in Superior Court, and $73 in district court (including small claims). The Court of Appeals filing fee has been increased to $280.

For more information on the filing fees in our local courts, visit Whatcom County's website at:

http://www.co.whatcom.wa.us

## CANCELLED LLCS—CONTINUED

that a LLC whose certificate of formation has been cancelled has no ability to sue.

The Washington Supreme Court's ruling as to the final issue of personal liability of members for failure to properly wind up dissolved LLCs is the one we find to be the most important to our clients' analysis of whether to dissolve or cancel the certificate of formation. The court held that although members and managers of LLCs are generally not personally liable for the LLC's debts, obligations and liabilities, a member can be liable for improperly winding up. *Chadwick/Emily II*, 2009 Wash.LEXIS 522, *35-36. After dissolution, a LLC must pay or make reasonable provisions for paying all claims and obligations known to the LLC, including contingent, conditional, or unmatured claims and obligations. RCW 25.15.300(2). The failure to comply with the requirements of the Act as to winding up can subject members to personal liability. *Id.* at 36-37.

Given the Washington Supreme Court's decision, how should our clients who are members of LLCs respond? Our advice after *Chadwick/Emily II* remains exactly the same as it was after *Chadwick I* and *Emily I*. The Washington Supreme Court's ruling provides assurance to LLCs that they can no longer be sued after cancellation, but there is no protection for the members if they have not properly wound up the company during dissolution. As we stated in Winter of 2007, members and managers of LLCs must seriously consider whether dissolution is a prudent business risk based on whether winding up can effectively deal with all claims and obligations known to the LLC, including contingent, conditional, or unmatured claims and obligations. Clearly, the nature of the LLC's business will play an important role in this decision. A LLC formed for a short-lived small business that incurred little to no actual or contingent liability does not face the same risk as a real estate development LLC facing potential claims from homeowners' associations or even individual homeowners for construction defects.

One thing is clear, however – if the decision to dissolve is made, members and managers must properly wind up the business of the LLC or face personal liability. Winding up includes making reasonable provision for contingent, conditional or unmatured claims. At this point, little guidance exists as to what constitutes "reasonable provisions," but they could likely include procuring insurance or having funds set aside for potential claims. Whatever provisions the LLC makes, we suggest that it be documented in writing – whether a written consent in lieu of a meeting or in minutes from the meeting at which the "reasonable provisions" are made.

If the risk is great, however, the best course of action appears to be not to dissolve. Until dissolution occurs, there is no obligation to wind up and thus no obligation to make provision for creditors, beyond the already existing obligations relating to piercing the corporate veil. At this point, if no winding up occurs, there is no potential for personal liability of members and managers who fail to properly wind up.

If you have questions regarding a potential dissolution or cancellation of your LLC, we are happy to help in analyzing what course of action makes sense for your situation.

[1] It does not appear that parties in *Maple Court* requested any review by the Washington Supreme Court. However, to the extent that *Chadwick/Emily Lane I* reversed certain rulings by the Washington Court of Appeals in *Maple Court*, the *Maple Court* case is no longer good law on those issues.

[2] Effective July 26, 2009, the time period for seeking reinstatement of an administratively dissolved LLC will increase from two years to five years. This change will resolve a conflict between the Act's survival statute, which allows suits to be brought against dissolved LLCs for three years after dissolution, and the time within which the secretary of state cancels the LLC's certificate of formation of an administratively dissolved LLC, which until July 26, 2009 is only two years. The result of the two year/three year conflict is that an administratively dissolved LLC could have its certificate of formation cancelled before the full three-year period during which suits can be brought during dissolution has run. The increase of the two-year period to five years will resolve this by allowing the full three-year period to run before the secretary of state can cancel the certificate of formation of an administratively dissolved LLC.

## A PERSONAL NOTE FROM THE DEPARTMENT:

By Kirsten Barron

I am confident that I will be telling my grandchildren about the economic "crash", "situation," "almost meltdown" – or whatever the media currently fancies – of 2008 and 2009. Between my husband and I, we have six children. I am certain some of these fabulous children will produce progeny. Will I be telling our grandchildren about tough, scary times and 10% unemployment or will I be talking about the riches of the 80's, 90's and early 2000's? Will our economy be back to "normal" or languishing? I often tell my children that in any other time in the world's history, our lives would be those of royalty. We have lived in a period of great prosperity. While it is something they do not always like to hear, it is true. I had a deep respect for my grandfather and the fact that he lived through the Great Depression. I was incredibly struck that he actually stayed a kind and loving man in spite of what he experienced. He chose to look at the bright side of life - I will gladly carry on that tradition.

I admire our clients and the work they do, the businesses they run, the families they raise and the communities they support. We are in the midst of creating a history that we will talk about for generations to come. One of the things I look forward to telling my grandchildren is that there were amazing folks working hard and staying true to their vision, who were resourceful and scrappy.

It continues to be a pleasure to work with you all – even during these times. Maybe it is another depression, maybe not, but I know that this is an extraordinary time and one worth remembering.

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