

SUPREME COURT OF KENTUCKY
2014-SC-000594-D
2011-CA-001771 & 2012-CA-001925

FURLONG DEVELOPMENT CO., LLC and
GORDON STACY

APPELLANTS

V.

**ON APPEAL FROM SCOTT CIRCUIT COURT
HON. ROBERT G. JOHNSON
CIVIL ACTION NO. 11-CI-00111**

GEORGETOWN-SCOTT COUNTY PLANNING
AND ZONING COMMISSION,
EGT PROPERTIES, INC., AND
UNITED BANK & TRUST CO.

APPELLEES

**APPELLANTS' REPLY BRIEF
TO THE BRIEFS OF THE APPELLEES,
GEORGETOWN-SCOTT COUNTY PLANNING
AND ZONING COMMISSION,
EGT PROPERTIES, INC, AND
UNITED BANK AND TRUST CO.**

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the Appellants' Brief was served by first class mail, postage prepaid, on this the 21st day of December, 2015, to the following: Charlie Perkins 209 East Main Street Georgetown, KY 40324; Steven B. Loy and Monica H. Braun Stoll Keenon & Ogden 300 West Vine Street Suite 2100 Lexington, KY 40507; KY 40222; Clerk, Kentucky Court of Appeals 360 Democratic Drive, Frankfort, KY 40601; Hon. Robert G. Johnson, Scott Circuit Court, 119 N. Hamilton Street, Georgetown, KY 40324.

Respectfully submitted,

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REPLY STATEMENT OF THE CASE

All three of the Appellees, United Bank and Trust Company (Bank), EGT Properties, Inc. (EGT), and the Georgetown-Scott County Planning and Zoning Commission (Commission), have made inaccurate statements of fact that need to be addressed. The Commission mischaracterizes the nature of the work that was covered by the bonds in question. Furthermore, the Bank has consistently mischaracterized that the underlying loan to the Appellants was to pay for the finishing work on the subdivision.

The Commission states in its Brief that “the Commission’s regulations required Furlong to either construct and install the public improvements, such as streets, or obtain a bond for 125% of the estimated costs of those improvements before the Commission would approve the final plat.” (Commission’s Brief at p.1) A little common sense and a bit of math is all that is needed to see that this characterization is incorrect. It is also this same mischaracterization that was accepted by the trial court when it said that the argument concerning when the bond is triggered “presumes that a developer builds houses before he builds the infrastructure.” (ROA at 368).

The total amounts of the three bonds in questions equal approximately \$150,000.00. There is no way that this amount is 125% of the cost of the streets, sidewalks and storm drainage. If this were so, the basic street, drainage and sidewalk infrastructure of a 90-unit subdivision would cost \$120,000.00. As stated in the Commission’s regulations that were actually in the lower court record, an additional 25% was added to the bond because of the possible inflation that may occur to cover a future event. (ROA at 315 at VI(B)). It is also worthy to note that Article VI of the regulations also state that the rough grading of the streets and drainage of the streets “shall not be

bonded.” (ROA at 315 at VI(A)(1)). The landscaping referred to in one of the bonds is also addressed in the regulations, which states the landscaping “not installed by the time of issuance of a Certificate of Occupancy” (ROA at 315 at VI(A)(2)). The triggering event of the bonds is not the approval of the final plat, but when Certificates of Occupancy are issued after 80% of the homes have been constructed. It is uncontested that no such Certificates were ever issued in the case at bar.

The Commission also attempts to characterize the 80% rule as only being limited to a design standard regarding the final layer of asphalt. However, the very provision in the regulation concerning the final inch of asphalt references Article VI, which is the Article in the regulations for bonding. (ROA at 232). Secondly, it is also important to note that when it comes to the final inch of finish asphalt, it is clear that the Commission wanted that performed after home construction has taken place before the streets would be dedicated to the City for **maintenance**. (ROA at 333). Neither Georgetown nor Scott County was maintaining the streets of the subdivision and had no reason to maintain the streets at the point when Summary Judgment was granted in the trial court.

In relation to the Bank’s statement that it had loaned the money to Furlong for the very improvements covered by the bond, this is not accurate. Of course, we are only limited to loan records that were selected by the Bank for the court to review below because of the lack of discovery in this case. However, the budget referenced by the Bank as support that it loaned the money for the bonded improvements is not what was actually loaned. The budget is only the basis for the Bank to estimate what money would be needed for the project. It is the actual draws that were approved by the Bank after receiving itemized receipts or invoices for work that represent the money that was loaned.

The budget in the court's record is named "G-town budget 7". (ROA at 152). On appeal, we have no idea what budget 1 through 6 may have said. However, "G-Town budget 7" does reference such things such as public streets, sidewalks and landscaping. Upon closer inspection and when we look at the actual draws that were approved by the Bank, sidewalks are noticeably missing from the draw. (ROA at 165). Also missing is the budgeted cost of the final layer of asphalt and storm drainage clean-up. (ROA 165).

The Bank also cites to the federal case involving Platte River Insurance (PRI) and ask this Court to take Judicial Notice of the Agreed Judgment. (Brief of Bank at p.5). Because of this, the Appellants request that the Court take Judicial Notice of the Joint Motion filed by the PRI and the Appellants in support of the agreed judgment. The Agreed Judgment was entered into to stop the bleeding of the Appellants by having to indemnify PRI for attorney fees and costs of litigation. As stated in the Motion:

The Parties agree that the Agreed Judgment should not be construed as an admission by either Party, nor a waiver or modification by either Party, of any claims or defenses either may have had now or hereafter against any person or entity, public or private, whatsoever. The sole purpose of this Agreed Judgment is to put to an end the expenditure of further time and resources into this litigation

(Joint Motion for Entry of Agreed Judgment in the United States District Court for the Eastern District of Kentucky Case #5:08-cv-00517 Docket #35.).

The final point of the Appellants deals with the trial court's granting of the Appellants' Motion to Amend their Complaint to bring before the court the company known as EKT Properties. (ROA at 351). The trial court did hold a hearing on this matter on July 7, 2011. Appellant's trial counsel requested that EKT be brought in as an indispensable party because it was the current owner of the subject property. (VR No 1:7/7/11 at 11:56). The Order of the trial court granting leave was not entered into the

record until August 2, 2011, which was a little over three weeks before the Court granted Summary Judgment.

REPLY ARGUMENT

INTRODUCTION

The case before the Supreme Court is not about the insurance company, Platte River, no matter how much the Court of Appeals and the Appellees wish it to be. It is about Furlong Development Company and, in all reality, one man named Gordon Stacy. If the Supreme Court were to rule that a city can call a bond when that city has no need to perform the work covered by the bond and when there is another developer ready to finish the project, then a performance bond becomes no more than a penal bond in this situation and will lead to financial ruin for Mr. Stacy. He will be left holding the bag for payment of bonds covering a future event on someone else's subdivision and for reimbursement of the Bank's and PRI's attorney fees as well.

The Commission laments in its Brief that interpreting the performance bonds to be triggered after 80% of the home construction is performed would be disastrous to counties. However, if the Commission would simply follow the statute that requires any developer to post a bond, then the new developer (the one that is making the profit from the sale of lots, which is directly related to the home construction reference by the 80% rule) would be required to provide surety. See KRS 100.281(4). The situation at bar is different than a developer simply walking away from an unfinished project. Instead, Mr. Stacy was forced to transfer the property to a company called EGT Properties instead of giving it back to the Bank. The Commission also knew before it attempted to call the

bonds that the Bank had every intention of finishing the project itself and selling the units.

I. THE BONDS SHOULD BE READ IN LIGHT OF THE
SUBDIVISION REGULATIONS AND NOT HAVE
BEEN CALLED BY THE COMMISSION

The three bonds in question cannot be understood by simply looking at the bonds alone. Each bond clearly references the Commission's regulations and says that the bond is "required pursuant to subdivision regulations of Georgetown-Scott County Planning Commission" (ROA at 14, 16 and 18). The Appellants argue, as was their understanding all throughout litigation, that the regulations and plan approved by the Commission did not require the work on the subdivision's finishing touches to be performed until after the majority of the homes had been built and issued Certificates of Occupancy. The regulations also contemplated that the streets would not be given to the city for maintenance until after this condition had taken place. (ROA at 332-333). This condition set forth in the regulations must be read into the bonding documents. The city or county would not want to accept or to maintain streets damaged by heavy machinery and traffic, such as gravel and concrete trucks, from numerous construction projects.

When looking at the language of the bonds, what does it mean when it says that if the principal does not perform each and every portion of the approved plan, then the bond "shall remain in full force and effect." (ROA at 14,16 and 18). Bear in mind that Furlong did transfer by deed the property to another owner who stepped into the shoes of the developer. Does this mean that the Commission can call a bond whenever a developer, by chance, transfers the property to another developer and get the bond money? Or does it mean that the bond stays in place until the need arises for the

finishing touches and remains unfinished after a developer sell the lots for profit? What happens if a new developer steps in and substantially changes the original configuration of the plat? There are many questions left unanswered by simply looking at the language of the bonds. Simply put, the four corners of these documents do not answer those questions. The bonding documents must be read in light of the regulations and the approved plan.

The Commission cites to City of Merced v. American Motorist Ins, 126 Cal. App. 4th 1316 (2005) in support of the windfall of being able to cash in the bond before the work covered was to be performed. However, there are several reasons to differentiate this case from the one at bar. The first is that the original developer actually not only built, but completed, homes in the subdivision before becoming insolvent. Id. at 1320. No homes were built and not a single lot was sold in the case at bar. Furthermore in Merced, the original developer transferred title back to the bank that had loaned the money after the homes were built. Furlong transferred the property to a company and not the lender. The city also gave the former developer an opportunity to perform the covered work before calling the bonds. Id. at 1320-21. No such demand was made upon Furlong. There was no reason for the Commission to demand performance because the need had not arisen for finishing work on the subdivision. The Commission simply went directly to PRI and demanded the money just a mere two weeks after the Bank made a similar request of the Commission. (ROA 28).

The Merced court addressed the issue of whether the city had been damaged. Specifically, it addressed to the trial court's finding that the city had been damaged by the former developer's refusal to perform after demand. Secondly, it stated that the city had

to spend resources to negotiate with the new developer. Neither of these facts are present in the case at bar. One point that the Merced case does shed light on is that there is, in fact, work that is deferred until a future point in time, such as the finishing work in Mr. Stacy's case. The Merced court also distinguished the facts of its case from that of County of Yuba v. Central Valley Bank, 20 Cal. App. 109 (1971)(this case is cited in appellant's brief at pages 14 and 15) because there was no showing that there was a condition precedent to be fulfilled before the bonds were triggered. Id. at 1326.

In Mr. Stacy's case, the Commission knew that the Bank was going to finish the project before it contacted PRI and demanded the bond money. Fourteen days before the Commission made its demand, it received a letter from the Bank that stated:

The bank acquired this property by deed in lieu of foreclosure and has determined that the public improvements secured by these bonds have not been completed. Therefore, we are writing to request that the Planning Commission in order that the funds can be used to complete the improvement. Our proposal is that the proceeds of the bonds be placed in an escrow account and, as the work is completed and inspected by the City of Georgetown, the funds be released to the bank as reimbursement for construction and completion of the improvements.

(ROA at 37).

This letter tacitly recognizes that the improvements covered by the bonds were not yet to be performed, thus the Bank's need to place the money in an escrow. The letter further told the Commission, that the Bank would be finishing the project. In this situation, the finishing of the project would be the selling of the lots for profit and then doing the finishing work. The **only** improvements that were not done by Mr. Stacy/Furlong in this case were the finishing work referenced in the bonds, and those

improvements were not yet required. The Bank clearly stepped into the shoes of a developer and should have been required to post its own bond.

After the Commission danced to the Bank's tune by demanding the bond money, PRI responded that it had spoken with Planning and Zoning and was advised by Commission's own engineer that the "sidewalks and other improvements covered by the bond" were not to be performed until 80% of the units had been constructed. This allegation of fact is in the record in the trial court, but was not addressed in either the Summary Judgment or the Opinion of the Court of Appeals. The very Summary Judgment shows the trial court did not understand the argument because it disregarded the distinction of the bonded work from that of the basic infrastructure when it said that the argument presumes that the homes would be built before the infrastructure. (ROA at p. 368)

II. UNJUST ENRICHMENT AGAINST THE BANK IS A VIABLE CLAIM

The Bank is arguing that the Deed controls whether Mr. Stacy can make the common law claim of unjust enrichment against it. This argument was accepted by the Court of Appeals in order to conclude that the Bank's communication to the Commission requesting that it call the bonds were only conclusory. It is common knowledge that Kentucky is a notice pleading state. "Inasmuch as notice pleadings prevail in Kentucky practice, we see no necessity for anything more. The emphasis is on substance over form and discovery over pleading." V.S. v. Com. Cabinet for Human Resources, 706 S.W.2d 420, 425 (Ky. App. 1986). Given that that the case at bar was improperly terminated without any discovery, the emphasis in Mr. Stacy's case was the opposite, pleading over discovery.

Secondly, the more that one takes a look at the so-called “deed in lieu of foreclosure” in the case at bar, the more and more it appears like an arms length transaction to a third party, namely EGT Properties. Furthermore, and most noteworthy, the Bank is not a party to the Deed. The Court of Appeals concluded that EGT Properties was only a property management company, but there is no support for this conclusion in the record beyond that it was owned and controlled by the Bank. Further, what exactly was a property management company in this situation? The Appellants contend that it was a successor developer.

The deed cited to KRS 142.050(7)(c) and (j) as the reason that no transfer tax was paid. KRS 142.050(7)(c) states that the tax is not required when a deed is entered into “solely in order to provide or release security for a debt or obligation.” KRS 142.050(7)(c). The deed clearly states “the Security Documents and liens thereof remain in full force and effect, unimpaired by this conveyance and the Security documents and the liens thereof...” Therefore, KRS 142.050(7)(c) does not apply because the mortgage on property was preserved. In KRS 142.050(7)(j), the deed presumably is invoking subsection 2, which states “pursuant to a voluntary surrender under a mortgage in lieu of a foreclosure proceeding.” KRS 142.050(7)(j). Again, this was not a situation where a bank simply took the property back. Instead, this Bank directed that it be transferred to a third-party, EGT Properties. EGT Properties had no right to foreclose upon the subject property at any time. It was the Bank that held this right and continued to do so even after the property was in EGT Properties’ name.

Finally as basis for both the Summary Judgment and the Opinion of the Court of Appeals, the courts focused on the language of the deed that said the Bank was not going

to be liable to third parties. “Furlong’s deed, given in lieu of foreclosure, provided that the bank would not be responsible for Furlong’s obligation to third parties...” Opinion at p. 12. This deed identifies Furlong as the Grantor and EGT Properties as the Grantee. This Deed language that has been so heavily relied upon by the opposing parties does not even include the Bank! It says fully, “there is no assumption of the Grantee [EGT Properties] of the obligations and liabilities of Grantor [Furlong] under the Security Documents or under any instruments or agreement with third parties and all such obligations remain the responsibility of the Grantor.” (ROA at 27 and p. 4 of Deed). Unless the corporate fiction of EGT Properties is completely set aside and held for naught, this deed language has nothing to do with the Bank.

Now that the Deed as a basis for foreclosing the unjust enrichment claim against the Bank is disposed, the Release that was entered into by the Bank and Mr. Stacy should be addressed. The release language that was focused on by Judge Thompson in his dissent does include both the Bank and its subsidiaries and companies. Thus, EGT Properties is also on the hook for the release. Mr. Stacy argues that the reason the dissent focused on the release in this situation is because, based on what we do know about the case, Mr. Stacy put everything he had into this subdivision and worked hard to get the subdivision ready for units to be sold for profit. As stated in the Commission’s Brief, subdivisions are risky business, but at the time of this case, the bottom fell out from under the housing market in an unprecedented manner. Mr. Stacy could not give away the lots at the time no matter how hard he tried to market the property. When he signed the deed and the release, he truly believed that he was out from under the weight of the Enclave. He never expected the Bank to turn around and asked for the bond money when it

provided him with a release that said it would not go after the bonds. (Opinion at p. 15) The construction of this release is essential because the practicality of the situation is that the bond money would eventually be paid to the Bank and, because of the indemnity agreement with PRI, would eventually fall into Mr. Stacy's lap.

The Bank has responded to the Dissent's focus on the release by arguing that the Release was only related to the "...Loan Documents and the Loan..." One thing that Mr. Stacy agrees with the Bank's characterization of what money he borrowed was that the premium for the bonds was loaned to Furlong. The premium was an expensive cost of business and the approximate \$6000.00 was borrowed in good faith. The language that was emphasized by Judge Thompson is very broad when it states "that the releasing party may have or claim to have, arising out of, by reason of, by reason of, in connection with, or in anyway related to the Loan Documents and the Loans." (Opinion at p. 15) Even at the trial court level, the Bank has always maintained that it loaned the money for the premiums and was aware of the bonds in question. Based on this, Mr. Stacy argues that the Bank knew about these bonds and pressured him into the relinquishing of his rights to the subdivision to an entity other than the lender, under the pretense that the Bank would not go after any bonds in relation to the loans. The actions of the Bank was no more than a "bait and switch" scheme that took advantage of the state of the economy and of Mr. Stacy. The Bank and its company truly got a subdivision, a developed piece of property, ready to be sold for profit. All it needed to do was sit on the subdivision until the housing market recovered and then sell the lots for the construction of 90 homes. Instead, in disregard of the release, it contacted the Commission to call the bonds so that it could have that money as well. This was so, even though it would have been useless and

foolish for the finishing work to be done and then that work torn up substantially over an unknown period of time while the houses were being built.

III. DISCOVERY SHOULD HAVE BEEN ALLOWED

By now, it should be apparent that Mr. Stacy's case is more than a four-corners case. There are several questions of fact concerning the Commission's understanding of the 80% rule, how it represented this rule to Furlong and how the rule factored into the improved plans for the subdivision. There are questions concerning the Bank's motivations when it enticed Furlong to relinquish its rights to the property. One of the most frustrating aspects of this appeal has been the lack of a record in the trial court below. It was interesting that the majority Opinion of Court of Appeals took up ten pages of its fourteen page Opinion with a recitation of facts from a case where no discovery was ever allowed.

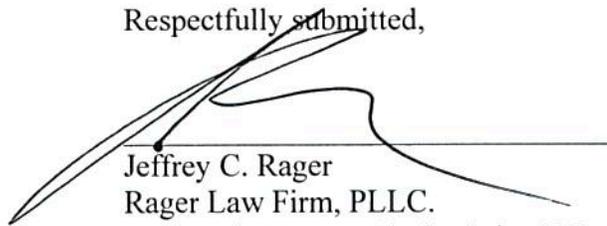
Although the argument set forth by the Appellant in his initial brief concerning the lack of discovery is more than sufficient, there is an additional argument to be made that the gavel was dropped too soon on this case. The Bank argues that the Appellants had a little less than two months to follow through on amending its Complaint to add EKT Properties to the case. As stated above, the record shows that trial counsel for the appellants requested to bring in EKT as an indispensable party to the lawsuit. The actual, written Order was not entered by the Court until August 2, 2011. Even if trial counsel would have immediately issued summons upon the amended Complaint, the trial court issued summary judgment before the time to file a responsive pleading by EKT Properties would have expired. There are already enough issues in this case without having to determine whether EKT Properties was indispensable or not. Regardless, the

fact still remains that the plaintiff's requested that EKT Properties be allowed into the case as being indispensable and the trial court granted the Motion. The trial court then proceeded to dispose of the case without a party that it determined to be indispensable. If the granting of a motion for summary judgment over the objection of a party requesting sufficient time to perform discovery and without all the necessary parties being brought before the trial court is not premature, then its hard to imagine what it means when Kentucky Courts state that litigants should have an ample opportunity to investigate their claims through the discovery process.

CONCLUSION

Based upon the above argument and the argument set forth in the initial Appellant Brief, Furlong and Gordon Stacy request that this Court declare that the bonds should not have been called under the particular facts of this case and that the case be remanded to the trial court so that the appellants may pursue their unjust enrichment claims.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Jeffrey C. Rager', is written over a horizontal line. The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

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