2010 WL 5241377 (Mo.Cir.) (Trial Motion, Memorandum and Affidavit)
Circuit Court of Missouri.
Jackson County

HAWTHORN BANK, Plaintiff/Counterclaim, Defendant,

v.

BLUE BRANCH DEVELOPMENT, LLC, et al., Defendants/Counterclaimants.

No. 0916-CV29013.
November 5, 2010.

Division: 2

Defendants' Reply to Plaintiff's Motion in Limine and Supplement to Defendants' Trial Brief

Respectfully submitted, Mitchell & Associates L.C., David L. Zeiler 806, 3100 SW 7 Highway, Suite A - Palo Center, Blue Springs, MO 64014, 816-224-1100, 816-224-1101 [Fax], dzeiler@bluespringslaw.com, Attorney for the Defendants/ Counterclaimants.

Defendants Blue Branch Development, LLC, Sean Tebbe, and Gina Tebbe (collectively the "Defendants") by and through their counsel, state and allege as follows:

LEGAL ARGUMENT AND AUTHORITY

I. THE APPLICATION OF THE CREDIT AGREEMENT STATUTE OF FRAUDS

In Plaintiff's Motion In Limine and Trial Brief, Plaintiff improperly relies on Sections 432.045 and 432.047 RSMo (the "Credit Agreement Statute of Frauds"). Furthermore, even if Defendants are not allowed to bring in evidence about the existence of a new refinancing agreement, Defendants have independent grounds to support their claims.

a. The Missouri Court of Appeal's exception to the Credit Agreement Statute of Frauds applies in this case.

There is an exception to the Credit Agreement Statute of Frauds when a party can show evidence of fraud by the lender. This rule applies to all claims arising from the contract and not just actions for fraud. *See Mika v. Central Bank of Kansas City*, 112 S.W.3d 82, 90 (Mo. App. W.D. 2003) ("[W]e hold that the fraud exception is applicable to the credit agreement statute of frauds ... Accordingly the trial court erred in granting summary judgment to [the borrowers' breach of contract, specific performance and setting aside foreclosure claims].").

As *Mika* made clear, where a party can show evidence of fraud, the exception to the Credit Agreement Statute of Frauds applies to any claims arising from the contract in question, not just claims for fraud. In the instant case, Defendants can show evidence of fraud through Plaintiff's handling of the Loans. Plaintiff's loan officer, Chris Adams, made numerous assertions to Defendants that Plaintiff would refinance the Loans; these assertions included specific terms and interest rates. Mr. Adams further informed Defendants that Hawthorn Bank had approved the new refinancing agreement and he was just waiting on the new loan documents. Whenever Defendants would inquire on the status of the new refinancing documents, Mr. Adams stated he was still waiting on the new documents. By leading Defendants to believe the refinancing agreement was forthcoming, Plaintiff was able to convince Defendants to continue to submit draw requests so that interest was paid on the Loans, to the Defendants' detriment, for nine months. Additionally, Mr. Adams representations led Defendants to cease efforts for refinancing or to sell

the properties. Thus, since the Loans were being paid under their terms, Plaintiff's actions kept the status of the Loans from showing any loss to the Bank so that Plaintiff did not have to claim a loss to its bottom line. Plaintiff was then able to foreclose on the properties once the interest payments were exhausted, without giving Defendants adequate time to obtain alternative **financing** or to sell the properties.

b. Even if the Court finds that the Credit Agreement Statute of Frauds bars evidence of a separate refinancing agreement, Defendants have independent grounds to support their breach of the covenant of good faith and fair dealings claim.

As it is not necessary for Defendants' breach of the covenant of good faith and fair dealings claim, Defendants never plead that a separate refinancing agreement existed. See *Answer, Affirmative Defenses, and Counterclaims of Defendants/Counterclaimants to Plaintiff's Petition.* A showing that "a valid enforceable contract" existed is necessary for a breach of covenant of good faith and faith dealings claim. *See Gilomen v. Southwest Mo. Truck Center*, 737 S.W.2d 499, 500-01 (Mo. App. 1987). However, even without evidence of an oral refinancing agreement, a valid enforceable contract still exists.

The valid enforceable contracts in this case are the original agreements governing the Loans. Defendants are not asserting that Plaintiff had an obligation to refinance; however, Plaintiff had a duty to exercise its rights and remedies under the Loans documents in good faith. Instead Plaintiff chose to mislead Defendants by proposing refinancing agreements, telling Defendants that refinancing was forthcoming, telling Defendants that new loan documents were being prepared, drawing the remaining interest from the reserve, and creating an artificial deficiency when foreclosing on the properties. While Plaintiff had a right to collect on the Loans and foreclose on the properties, Plaintiff also had a duty under the original Loan documents to exercise their rights in good faith and with fair dealings. By stringing Defendants along for nine months with promises to refinance, Plaintiffs were able to continue to deduct interest payments off the Loans at Defendants' liability and keep the Loans from being declared a loss on Plaintiff's **financial** statements. Additionally, during this long waiting period, the economic downturn worsened to the point that Defendants could not refinance the Loans or sell the properties because of the Bank's improper delay.

Plaintiff also alleges that Defendants cannot prove that Plaintiff **exploited** changing conditions to make gains in excess of those reasonably anticipated. However, discovery has shown several examples of the Plaintiff **exploiting** the Defendants' situation for Plaintiff's **financial** gain:
• Plaintiff continuously led Defendants to believe Plaintiff would refinance the loans so that Defendants would continue to make interest draws, would not seek alternative **financing**, and would not sell the properties.

• Plaintiff had their loan officer "propose" a refinancing agreement; however, contrary to the loan officer's statements to Defendants, the loan officer stated in the refinancing proposal that he did not wish to do further business with the Defendants.

• Plaintiff waited nine months to send the first Demand Letter.

• Plaintiff sent the first Demand Letter three weeks after Plaintiff could no longer pull interest payments from the interest reserves. Plaintiff's loan officer said the timing of the Demand Letter and the exhaustion of the interest reserve was mere "coincidence."

• Plaintiff used an inside appraiser to appraise the properties at a lower value before selling it, then hired an outside appraiser who appraised the properties at a higher value after Plaintiff purchased the properties.

This evidence demonstrates that, regardless of Plaintiff's rights under the contract, Plaintiff exercised those rights in a way that violated their duty to perform on the contract in good faith and with fair dealings.

c. Contrary to Plaintiff's assertions, the evidence supports Defendants' prima facie tort claim.

Plaintiff also alleges that the Credit Agreement Statute of Frauds bars Defendants' prima facie tort claim. Plaintiff misapplies the statute. While the Credit Agreement Statute of Frauds bars actions under "certain oral agreements," the statute does not "extend to actions involving such oral agreements which sound in tort." *Mika v. Central Bank of Kansas City*, 112 S.W.3d at 93. Therefore, it would be improper to apply to Credit Agreement Statute of Frauds to Defendants' tort claims.

Furthermore, even if the Court finds that the Credit Agreement Statute of Frauds bars evidence of a separate refinancing agreement, Defendants have independent grounds to support their prima facie tort claim. As it was not necessary for Defendants' prima facie tort claim, Defendants never plead that a separate refinancing agreement existed. See *Answer, Affirmative Defenses, and Counterclaims of Defendants/Counterclaimants to Plaintiff's Petition.* The evidence instead shows that Plaintiff foreclosed on the properties with intent to cause Defendants injury absent sufficient justification.

Plaintiff further alleges that Defendants cannot show evidence of actual malice; however, discovery has revealed ample evidence of actual malice:
• Plaintiff's representative, Chris Adams, stated that he believed there was "bad blood" between himself and Defendants.

• Mr. Adams's refinancing application, which he submitted on the Defendants' behalf, stated that he had no intention of doing any business with the Defendants.

?? Mr. Adams stated that this was because the bank was no longer in the business of construction and development loans; however, the Plaintiff's president and CEO, James Smith, stated that at that time the bank was still seeking construction loans.

• Mr. Adams's statement that it was mere "coincidence" that the Demand Letter came within three weeks of the interest reserve running out.

• Mr. Adams, the sole bank employee responsible for managing the Loans, continuously mislead the Defendants, making them believe it was Plaintiff's intention to refinance the Loans.

Plaintiff also asserts that reported cases regarding prima facie tort claims are rare; however, whether prima facie tort claims are rare is irrelevant. Defendants have plead the necessary elements of the claim and the evidence demonstrates that the Plaintiff committed a lawful act to injure the Defendants without sufficient justification.

II. PLAINTIFF'S INTERNAL POLICIES

Plaintiff also claims that any evidence regarding Plaintiff's internal policies would be irrelevant. "To be admissible, evidence must be logically and legally relevant." *UMB Bank, N.A. v. City of Kansas City*, 238 S.W.3d 228, 232 (Mo. App. 2007) (citations omitted). "Evidence is logically relevant if it tends to prove or disprove a fact in issue or corroborates other evidence." *Id.* "Legal relevance involves a process through which the probative value of the evidence ... is weighed against the dangers of unfair prejudice, confusion of the issues, misleading the jury, undue delay, waste of time or needless presentation of cumulative evidence ...." *Id.* "Logically, relevant evidence should not be excluded unless it pertains to collateral matters, which would result in confusion of the issues or would cause prejudice wholly disproportionate to the value and usefulness of the offered evidence." *Id.*

Evidence of Plaintiff's internal policies, and evidence that those policies were not followed, tends to prove that Plaintiff evaded the spirit of the transaction to deny Defendants the expected benefit of the refinance. *See Wulfing v. Kansas City Southern Ind*, 842 S.W.2d (Mo. App. W.D. 1992) (In a breach of the covenant of good faith and fair deals claim, the claimant must show

that a party "exercise[ed] a judgment ... to evade the spirit of the transaction ... to deny the other party the expected benefit of the contract."). This evidence is highly probative as it directly relates to Defendants' claims and has little prejudicial value, as evidence of Plaintiff's internal policies would result in more clarity for the jury rather than confusion when the jury decides whether Plaintiff properly handled the Loans. Furthermore, evidence of Plaintiff's internal policies show that Chris Adams was negligent in his handling of the Loans by, among other actions, failing to follow the policies Plaintiff had in effect at that the time the Loans matured.

In cases involving a company's employment policies, and whether or not those companies are following their policies, to decide whether companies are discriminating against employees. *See Romano v. U-Haul Intern.,* 233 F. 3d 655 (10th Cir. 2000); Cadena v. Pacesetter Corp., 224 F. 3d 1203 (10th Cir. 2000); *Ogden v. Wax Works, Inc.,* 214 F. 3d 999 (8th Cir. 2000); *Passantino v. Johnson & Johnson Consumer Products,* 212 F. 3d 493 (9th Cir. 2000); *Lowery v. Circuit City Stores, Inc.,* 206 F. 3d 431 (4th Cir. 2000); *Deffenbaugh- Williams v. Wal-Mart Stores, Inc.,* 188 F. 3d 278 (5th Cir. 2000). Though not on all fours, these cases are persuasive because Defendants will similarly use Plaintiff's company policies to show that Plaintiff failed to follow its policies regarding the management of post-maturity loans. This failure to follow policy is evidence that tends to prove the elements of Defendants' claims.

III. PLAINTIFF'S NEGLIGENCE

Plaintiff alleges that no duty exists because there has been no specific legislation creating a statutory duty that banks must have towards customers. However, "the duty to exercise care may be a duty imposed by common law under the circumstances of a given case." *Hoover's Dairy, Inc. v. Mid-America Dairymen,* 700 S.W.2d 426, 431 (Mo. 1985) (citations omitted). Furthermore, Missouri courts have held that, at times, a fiduciary duty can exist between a bank and a customer, which is a higher duty than negligence. *See Hall v. NationsBank,* 26 S.W.3d 295, 297 (Mo.App. E.D., 2000) (stating that a duty may exist if the bank uses the customer's information to its advantage) *see also Pigg v. Robertson,* 549 S.W.2d 597 (Mo.App. W.D. 1977) (holding the bank has a duty to its customer when a person acting as a bank employee took information regarding a piece of property the customer was interested in purchasing and used that information to purchase the property before the customer had the opportunity). It is axiomatic that if courts recognize situations where a fiduciary duty can exist between banks and their customers, situations can also arise where banks owe a simple negligence duty to their customers.

The evidence in this case demonstrates that Plaintiff was negligent in managing the Loans. Mr. Adams's assertion that he did not communicate with Defendants for seven months, if true, was well beyond the ordinary custom of Plaintiff's loan officers. Contrary to these assertions, the evidence suggests that Mr. Adams made numerous assurances that the Loans would be refinanced, at times even giving Defendants specific terms and conditions of the refinancing agreement. By continuously leading Defendants to believe the Loans were going to be refinanced, Plaintiff not only assumed a duty to Defendants, but also breached that duty to exercise ordinary care in the management of the Loans. These negligence actions directly caused Defendants' injuries, as Defendants were unable to seek alternative **financing** once the Demand Letter was sent out.

IV. TARP FUNDS

Plaintiffs have asserted that they did not receive TARP funding from the federal government. However, Hawthorn Bancshares, the corporation that owns Plaintiff, has received TARP funds. While Defendants have dismissed their breach of contract - third party beneficiary claim, Hawthorn Bancshares's TARP funds are relevant evidence of Plaintiff's motive to keep the Loans from showing any negative impact on Plaintiff's **financial** statements. By having the Loans shown as performing, rather than having to take a loss on Plaintiff's **financial** statements, Hawthorn Bancshares was in a better position to qualify for TARP funding.

Respectfully submitted,

MITCHELL & ASSOCIATES L.C.

By: <<signature>>

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