

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2009-000411

02/24/2011

HONORABLE J. KENNETH MANGUM

CLERK OF THE COURT
D. Glab
Deputy

FIRST CREDIT UNION

MILTON A WAGNER

v.

R CLINTON ALLRED, et al.

R SCOTT CURREY

RULING

This matter was tried to the Court on February 18, 2011. Having considered the pleadings on file, the testimony of the witnesses and the exhibits admitted into evidence, the Court makes the following Findings of Fact and Conclusions of Law. If any Finding of Fact is more appropriately a Conclusion of Law or vice versa, it shall be so considered.

Findings of Fact

1. This hearing is to determine the fair market value ("FMV") of the defendants' formerly owned residential lot at 7044 East Terrace Estates Circle, Carefree, Arizona 85377.
2. Generally speaking, testimony is summarized under each person's name and is generally in the first person. Undisputed matters are set forth by separate heading.

Stipulated Facts

3. First Credit Union ("FCU") is an Arizona non-profit corporation doing business in Maricopa County, Arizona.

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4. The Allreds at all times material hereto were residents of Maricopa County, Arizona.
5. The Allreds are married and their acts as described herein were undertaken on behalf of and for the benefit of their marital community.
6. On August 22, 2006, FCU agreed to loan the Allreds \$1,374,750, the loan being evidence by a promissory note ("Note").
7. Also on August 22, 2006, the Allreds executed a Deed of Trust in favor of FCU for the purpose of securing payment of the debt to FCU.
8. On August 22, 2006, and in connection with the Note and Deed of Trust, FCU and the Allreds also entered into a Residential Construction Loan Agreement.
9. The Note, Deed of Trust and Residential Construction Loan Agreement were secured by that real property commonly known as 7044 East Terrace Estates Circle, Carefree, Arizona 85377 ("property").
10. The maturity date of the loan was February 25, 2008. The Allreds failed to pay off the loan at maturity, thereby defaulting under the Note.
11. Pursuant to the default, and upon proper notice and pursuant to Arizona law, FCU caused a Trustee's Sale of the property to be scheduled.
12. On November 7, 2008, the property was sold at a Trustee's Sale. FCU made a credit bid in the amount of \$1,100,000. There were no other bidders.
13. As of November 7, 2008, the principle due on the Allreds' loan was \$1,257,768.
14. As of November 7, 2008, the Allreds were additionally indebted to FCU for the following items:

Interest on Principal as of Trustee's Sale (2-25-08 to 11-7-08 at 18% /annum	\$140,801.00
Non-legal costs incurred prior to Trustee's Sale	
Appraisal	775.00
Title Fees	7,495.00

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Locks	171.00
Total	\$149,242.00

15. Pursuant to the note, Deed of Trust, and Construction Loan Agreement, the Allreds were additionally indebted to FCU for insurance, homeowner's dues, and taxes, if any, incurred by FCU on the subject property as of November 7, 2008.
16. On February 3, 2009, within ninety days after the date of the Trustee's Sale and in accordance with A.R.S. §33-814, FCU initiated this lawsuit against the Allreds.

Joseph Guyton

17. Joseph Guyton is the Senior Vice President of FCU.
18. I was chief lending officer from June 2008 through December 31, 2011. I was in charge of lending, collections, Real Estate Owned properties, etc.
19. FCU is a cooperative owned by it's members. The deposits equal shares of ownership. We're a non-profit company.
20. The defendants borrowed \$1,374,750 in August 2006, and February 25, 2008, was the maturity date. The loan is in default. The money initially went to pay off the prior lender and then to construct the home. It had been under construction for years.
21. We tried to modify the loan, but we gave notice of foreclosure on July 26, 2008. The September 2008 sale date was continued and carried out on November 7, 2008. We bid \$1.1 million and there were no other bidders.
22. We did an appraisal of \$1 million but bid a higher amount to avoid this law suit.
23. Our figures are as follows:

Amount owed	\$1,257,768.00
Interest , Appraisal, Title and Locks	149,242.00
Insurance and taxes (paid by FCU prior to the foreclosure sale)	8,447.32

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Total	\$1,415,457.32
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24. At the time of the foreclosure sale, the house had *none* of the following: carpet, HVAC, most kitchen cabinets, appliances, fixtures and plumbing, landscaping, pool, driveways, paths to house, finished hardware, electrical and trim.
25. Our estimate to complete the house was \$292,062. We didn't install a pool, although the original plans were for one. We put the house up for sale right away and listed it as subject to completion, meaning that we would pay for all of the final construction costs per the plans we had. Our initial listing price was \$1,450,000. We interviewed two-three brokers and picked one and paid a commission when it was sold.
26. The house next door sold at a trustee sale for a different borrower.
27. We hired Schultz Development Corp to complete the house for \$203,215 without the pool. It took from January to June 2009. The first offer we received was \$1 million after it was completed in September 2009. We incurred fees to the town of Carefree, HOA fees, and taxes.
28. We sold the house in May 2010 for \$1,050,000.

John Rooney

29. John Rooney is the plaintiff's expert appraiser.
30. I have a BS from ASU in Real Estate and have been a licensed appraiser as well as realtor since 1984. I am certified to appraise houses over \$1 million, and I've done hundreds of appraisals.
31. I researched the ownership history, MLS listings, I visited the property and neighborhood and talked to people familiar with the property. For example, the neighbor across the street saw water in the house and rotting wood and Styrofoam soon after he moved into his house in 2003. (2001 is when construction was begun on this subject house.) Thus, there are structural issues in the subject house and there is a risk for the buyer of that home.
32. An income analysis works for rentals or income property, cost of construction works for new properties, and sales comparison is best for existing homes. Exhibit 2 is my

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appraisal.

33. There were 15 homes for sale in Carefree ranging from \$582,000 to \$2.95 million, all of them fully completed and similar in size and value. Four comparables sold in one year, indicating a four year supply of homes in the area. Thus, there is an oversupply.
34. We considered four comparables in Carefree and Cave Creek with unadjusted prices of \$819,000 to \$1,050,000. \$168,000 was the estimate to finish the home. This subject house had none of the features that some better homes have, such as detached guest quarters, home movie theater, wine rooms, etc. We adjusted the comps mostly for the unfinished condition of the subject house. A contractor or investor would be the likely purchaser of this house. It's highly unlikely that a purchaser would buy it for personal use in this unfinished condition. There is the completion cost and the risk factor involved, as well as the marketing and sales cost and the carrying costs (such as utilities, insurance, taxes, etc.). I considered \$100,000 as profit for the commercial buyer.
35. Exhibit 10 shows listings, all of which sold for \$200,000 to \$500,000, well below our FMV. If I'd used these, our final appraisal price would have been lower.
36. We selected custom and premium homes from 4000 to 7000 sq. ft., one acre plus lots and unfinished.
37. My opinion of FMV on the date of sale is \$825,000 as is.
38. Defendant's expert report, Exhibit 15, used highest closings with houses much better than the subject home. For example, comp #1 was for \$2.5 million, comp 32 had many additional features. Also, using active listings mean nothing because they are excessive by the nature of selling them. Comp #6 was reduced from \$2.7 million to \$1.98 million and it still didn't sell. In short, Mr. Josephs used the highest end of the market and therefore the comps weren't similar to the subject home. Even so, we adjusted our comps by as much as \$390,000 but Josephs only adjusted his by a maximum of \$275,000.
39. Furthermore, Josephs used Cave Creek and Carefree homes, saying that Cave Creek homes were inferior and therefore worth a \$75,000 downward adjustment. The subject property is one lot from Cave Creek and I think the \$75,000 adjustment is too much. I opine that Carefree and Cave Creek are similar communities.
40. The FMV per MLS is higher for Carefree than for Cave Creek, but this is based on a few reports and may not be accurate.

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41. Fannie Mae and Freddie Mac don't allow adjustments of more than 10% but those rules don't apply since this is not a Fannie Mae or Freddie Mac appraisal. It's OK to exceed a 10% adjustment for luxury homes. Guidelines say the maximum adjustment per line is 10% and 25% for the total adjustment.
42. Two of my four comps are on major arterials, but the subject home is not.
43. We adjusted for the age of comps. I had an 11 year old comp and Josephs had a 12 year old comp. I also adjusted for the size of the lot. One trouble is that there were few good comparables: there were no unfinished houses to compare with. This is an extremely unusual case and therefore requires extreme adjustments.

Jay Josephs

44. Jay Josephs is the defendants' expert appraiser.
45. I have been appraising in Arizona for 20 years and have been certified for 18. I'm also a licensed real estate broker and a certified real estate instructor. I've testified in court many times.
46. I know the Cave Creek area and deal with many luxury homes in that area including homes under construction (i.e., not yet completed).
47. I opine that the subject home is worth \$1.4 million as of the date of the foreclosure sale.
48. My first appraisal of this property was October 6, 2008 and was for Home Quest Mortgage, done "subject to completion." My FMV was \$1.925 million. I had not been contacted by defendants at that time. I didn't know about the loan amount or the claimed deficiency. I may not have had access to the interior of the home on my second visit/appraisal, but I was told there was no change.
49. The November 2008 appraisal has seven comps. I used both Carefree and Cave Creek homes, all in the similar location and generally custom homes. But people pay more for Carefree than Cave Creek homes because they are larger, they have a higher predominant value and a better view. In the zip code, the west side has 41 listings for a average price and 37 closed sales as follows:

	West Side	East Side
41 Listings	\$969,000	\$1.719 Million

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37 Closed Sales	\$735,000	\$1.1 Million
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50. Thus, the Allreds' property benefitted by being on the east side. Even though it's barely over the Carefree line (the second house in), it's still in the NE quadrant of that area which is the higher-value area. Rooney only has one comp in this area.
51. Two of my comps are in Cave Creek as the data in the luxury market is not common so you have to go outside. My comps 5 and 6 are listings only. Most banks require listings in evaluations, but listings get less weight. Comps 1 and 2 are the most relevant. Comp 7 is a pending sale and that's OK to use since this was a retroactive appraisal and it closed a month later. 93% of list price is typical for an arms length sale. The listing of \$1.295 million and the sale for \$1.095 million seem to show a liquidation sale.
52. I did not search by sales price.
53. I considered Rooney's comps, but he had only one sale in the subject area.
54. I used \$200,000 as the estimated cost to complete the home because that's what the attorney for defendants told me, so we added \$75,000 as an adjustment (as compensation for buying an unfinished home). There are time adjustments when the market trends up or down. Since the market was falling, you adjust older homes more.
55. The likely buyer for this house would be an investor or a builder or homeowner. Mr. Rooney used a profit factor and commissions of \$100,000. If you use a real estate commission that only applies to a flip, that's not a definition of FMV.
56. My comp 2 had a temperature controlled wine room and a home theater room, neither of which the subject house had, and which would be worth \$200,000.
57. Buying "as is" means there is no warranty.

Deposition of Howard Thruston

58. Howard Thruston appeared by deposition.
59. I attended Mesa Community College and have a real estate license. I constructed the house in question and the one of the neighboring lot.
60. I or my wife was the former owner of both 7022 and 7044 East Terrace Estates Circle,

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Carefree, having bought it in about 2000. I don't recall the price or how they were purchased, with a loan or with cash. The intent was to resell it or to build a home on it for someone. I planned on selling them as investments and not living there.

61. The 7022 lot was sold to Terry and Yvonne Cook after I sold the house they then had. I made a profit on the sale.
62. I sold 7044 to Clint and Julie Allred, probably making a profit.
63. Both buyers modified the architectural plans a bit. I would expect houses to be completed within two years. I expect that the CC&Rs require a home to be built within a year of initiation. A prior builder had moved dirt on the lot(s) which may have been when the HOA thought construction should be counted.
64. The FCU loans were set up with an interest reserve account to pay for construction and the loan interest. When the money ran out, I started making the payments myself from my own money, based on a moral obligation I felt because the homes were taking so long to complete. That wasn't the fault of the Cooks or the Allreds—it was the fault of my situation with National Bank of Arizona. If the buyers made any payments, then I reimbursed them, but I covered or paid all the loan payments after the reserve accounts ran out.
65. The draws for the construction loans were paid directly to me based on the choice the borrower made. The lender looks out for itself. FCU was fine with how we handled things.
66. I build better custom homes than most builders with more attention to detail, designs, style looks, finishes, etc. Two homes could be similar in terms of structure and layout and quality of the underlaying construction, but one can be worth significantly more because of higher-end finishes.
67. The following needed to be completed on the subject home:

	Items Missing
Outside	paver driveway, light grading, desert landscaping, light fixtures, AC unit, swimming pool

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Inside	plumbing trim, plumbing fixtures, electric fixtures, appliances, bathroom accessories, maybe door hardware inside, some cabinets in the master bathroom with a few doors or drawers, closet shelves
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Conclusions of Law

68. This is an action for a deficiency judgment brought pursuant to A.R.S. §33-814. The deficiency amount is calculated by subtracting from the total amount owed as of the date of the Trustee's Sale the greater of

- a. The FMV of the trust property on the date of the Trustee's Sale, or
- b. The price paid at the Trustee's Sale.

A.R.S. §33-814A. Here, the price paid at the Trustee's Sale is stipulated as \$1,100,000. Thus, the only matters for the Court's determination are the total amount owed by defendants to Plaintiff, the FMV of the property as of November 7, 2008, and the amount of the deficiency.

69. The relevant statute insofar as fair market value is as follows:

A.R.S. §33-814. Action to recover balance after sale or foreclosure on property under trust deed

A. . . . For the purposes of this subsection, "fair market value" means the most probable price, as of the date of the execution sale, in cash, or in terms equivalent to cash, or in other precisely revealed terms, after deduction of prior liens and encumbrances with interest to the date of sale, for which the real property or interest therein would sell after reasonable exposure in the market under conditions requisite to fair sale, with the buyer and seller each acting prudently, knowledgeably and for self-interest, and assuming that neither is under duress. . . .

70. Any deficiency judgment "shall include interest on the amount of the deficiency from the date of the sale at the rate provided in the deed of trust or in any of the contracts evidencing the debt, together with any costs and disbursements of the action." *Id.* Here, the rate provided by the note and Deed of Trust is 18% per annum.

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71. Determining FMV is difficult in a declining market. Also, determining FMV for an unfinished home is similarly difficult.
72. Each appraiser in this case has points in his favor as well as criticisms. For example, Mr. Josephs has selected some comps that are beyond the pale, such as listings and excessively luxurious homes. At the same time, the court agrees that Carefree is generally a more desirable area than the Cave Creek area. Cave Creek is an area that a person would pay more for. And while the home in question is just yards away from the town boundary, access to the home is only available from the east side which is Carefree; this emphasizes the slightly more exclusive area of Carefree. On the other hand, Mr. Rooney uses two homes that are on arterial streets whereas the subject home is tucked away in a secluded area. The proper FMV is below Mr. Josephs' appraisal and well above the appraisal of Mr. Rooney.
73. The court concludes that the FMV of the subject home is \$1,150,000.
74. The court further concludes that the additional amounts owed by the Allreds, including the deficiency, is as follows:

Amount owed on loan	\$1,257,768.00	
Interest	149,242.00	
Insurance and taxes (paid by FCU prior to the foreclosure sale)	8,447.32	
Sub Total Amount Owed by Defendants		\$1,415,457.32
Less FMV on date of Sale		\$ 1,150,000
Net Amount Owed by Defendants		\$ 265,457.32