DISTRICT COURT, ADAMS COUNTY, COLORADO Adams County Justice Center 1100 Judicial Center Dr. BRIGHTON CO 80601	
Plaintiff: HERITAGE GREENS AT LEGACY RIDGE HOMEOWNERS ASSOCIATION, INC., a Colorado nonprofit corporation, on its own behalf and on behalf of its Unit Member Owners as their Attorney-in-Fact **Defendants:** HERITAGE GREENS AT LEGACY RIDGE, L.L.P., CESSNA ASSOCIATES, LTD., a Colorado corporation, BARRY L. SINKEY and RICHARD G. POSTON, individually.	▲ **COURT USE ONLY** ▲
Attorney: Scott F. Sullan, No. 9985 Curt T. Sullan, No. 18010 Ronald M. Sandgrund, No. 12505 SULLAN[2], SANDGRUND, SMITH & PERCZAK, P.C. 1875 Lawrence Street, Suite 850 Denver CO 80202 Telephone: 303-779-0077 Fax No: 303-779-4924 Email: csullan@vsss.com	Case Number: **2006 CV 713** Div.: **A**

PLAINTIFF'S OBJECTION TO DEFENDANTS' NOTICE OF POSTING OF COST BOND (AND ATTACHED SUPERSEDEAS BOND)

Plaintiff, Heritage Greens at Legacy Ridge Homeowners Association, Inc. ("the Association"), through its attorneys, Sullan[2], Sandgrund, Smith & Perczak, P.C., responds and objects to *Defendants' Notice of Posting of Cost Bond (and Attached Supersedeas Bond)* ("Defendants' *Notice*") as follows:

Conferral Certification

In accordance with C.R.Civ.P. 121 § 1-15.8 the undersigned wrote to Defendants' counsel identifying various concerns with the form and substance of Defendants' cost bond. Defendants responded, offering to meet many of the Association's objections to the bond's form, but rejecting its objections to the surety.

Procedural Posture, Burden of Proof and Standard of Review

C.R.Civ.Proc. 121 § 1-23 prescribes the procedure for posting and objecting to a bond required by C.R.Civ.P. 62(b) intended to both secure and stay execution on the Association's October 12, 2008 judgment. Although that judgment exceeds $16 million, the parties agreed that the amount of an otherwise proper bond equaling $14,595,000 would suffice to stay execution pending the Court's ruling on Defendants' motion to amend the judgment in light of their objections to the determination of prejudgment interest on the underlying $11,676,000 verdict. (An additional or separate cost bond will become necessary once the Court rules on the Association's pending motion for costs.)

Under Rule 121 § 1-23.3(a), Defendants are entitled to a *temporary* stay of execution if they post a bond equaling "125% of the total amount of the judgment entered by the court (including any prejudgment interest, costs and attorneys fees awarded by the court)." Defendants' current bond is tentatively effective since it was issued by a "corporate suret[y] presently authorized to do business in the State of Colorado." However, the Association is entitled to object to the bond pursuant to Rule 121 § 1-23.6. Ultimately, the "party tendering the supersedeas bond bears the burden of proving that its surety, whether corporate or individual, is a sufficient surety." 4 C.J.S. APPEAL AND ERROR § 541 (June, 2008). The "court's role is not to

rubber-stamp whatever bond the judgment debtor presents." *Rand-Whitney Containerboard L.P. v. Town of Montville*, 245 F.R.D. 65, 68 (D.Conn. 2007).

The Association has found no case law construing Rule 1-23, and spare Colorado case law construing bond requirements in general. The leading case is *Muck v. Arapahoe County District Court*, 814 P.2d 869 (Colo. 1991), which discusses Colorado's "long history" of requiring a proper bond as a condition to stay execution, and that the purpose of the bond is "protecting the appellee's interest in the judgment" and "guaranteeing appellee collection of the judgment should he win on appeal." *Id.* at 872-73 (emphasis added). *See, generally*, Martin D. Beier, "Bonds in Colorado Courts, a Primer for Practitioners," 34 *The Colo. Lawyer*, 3, at 62-66 (March, 2005) (hereafter, "*Beier*").

The amount, terms and conditions of the bond are left to the trial court's "broad discretion." *Muck*, 814 P.2d at 782, note 8. Each party against whom judgment has been rendered must post a bond to stay execution – no party may rely on another's posting of a bond for such a stay. *Beier*, at 62.

Argument

Defendants' corporate surety bond should be rejected because Defendants have failed to meet their heavy burden of proving that the existing Western Surety bond is adequate security – that it "guarantees" payment of the Association's judgment in full. Defendants can offer no justification for not securing a bond from an A.M. Bests' highest rated "A++" surety, falling in the "Group XV" financial size, rather than a surety rated two levels below this standard and falling five levels below this financial size. The Association, as judgment-creditor, should not be

asked to extend a "loan" of $14.5 million to the judgment-debtor Defendants based on the promise of a surety with less than an A++ rating.

The Court should order that Defendants post a cash bond in the amount of 125% of the judgment, especially in harsh light of today's economic landscape. For maximum security, the Court should direct the Clerk to use the cash bond to purchase 30-day U.S. government securities that automatically roll-over. If Defendants and/or their liability insurer, American Family Insurance Group, do not tender the cash, then the Association should be allowed immediate execution on its judgment.

A. A Cash Bond Is Required Because Defendants Cannot Meet Their Burden of Proving that a Bond Issued by Anything Less than an A++, Group XV Surety Might Reasonably "Guarantee" Payment of the Judgment.

In an October 24, 2008 press release, CNA Surety (stock exchange: SUR), Western Surety's parent company, issued the following warning:

> The Company's business is subject to certain risks and uncertainties associated with the current economic environment and corporate credit conditions. In the past, the Company's performance has been materially impacted by a significant increase in corporate defaults on a worldwide basis. Because the nature of the business is to insure against non-performance, future results of operations could be negatively impacted by adverse trends in corporate defaults.

See hand-written page 2 of CNA Third Quarter 2008 Press Release, copy attached as *Exhibit* 1 (emphasis added). This warning regarding "adverse trends in corporate defaults" can only be intelligently examined against the current economic environment, which supports the conclusion that a "tsunami" of corporate defaults lies ahead.[1]

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[1] Former Federal Reserve Chairman Alan Greenspan testified before Congress last week that, "We are in the midst of a once-in-a century credit tsunami." *See* Greenspan statement, reported in the Wall Street Journal at http://blogs.wsj.com/economics/2008/10/23/greenspan-testimony-on-sources-of-financial-crisis/ (last checked October 28, 2008).

The past three months have been the most tumultuous three months in the United States economic history since the Great Depression. During that time, the nation's five largest investment banks have faced insolvency, one of which took bankruptcy (Lehman Bros., in the country's largest bankruptcy filing ever), two of which were bought out by commercial banks (Bear Stearns and Merrill Lynch, both with government support), and two of which changed their status to commercial banks to avoid insolvency (Morgan Stanley and Goldman Sachs). All four surviving companies (or their successor companies) were the beneficiaries of over $1 trillion in U.S. loan guarantees and capital infusions made necessary to stave off imminent bankruptcy. The country's largest private mortgage guarantors, Fannie Mae and Freddie Mac, were taken over by our federal government and their massive debts guaranteed by the taxpayer. And, the country's largest insurer, AIG, was provided loans totaling over $125 billion to remain solvent – and its management promptly spent some of the loaned money on spa treatments, exotic getaways and multi-million dollar executive bonuses. In addition, the Federal Reserve has taken unprecedented steps to make cheap credit available to hundreds of financial institutions to render them solvent, paid for by running up our national debt to over $10 trillion.

Meanwhile, some of the largest commercial banking failures in history have occurred, including the biggest ever, Indymac, and the sale or merger of two of our nation's largest banks, Washington Mutual and Wachovia, due to their imminent insolvency and collapse. No economist denies that our country's economy is in a recession, and the only unanswered question is whether events will evolve into a massive, long-term recession or a full-fledged depression.

Against this background of economic uncertainty and turmoil, where major financial concerns like Lehman Brothers flaunted Moody's and Standard and Poor's "A" ("good security")

credit ratings on Friday, September 11, 2008, only to take bankruptcy three days later on Monday, September 14, it has become clear that credit-rating agencies are uninformed or unreliable. Much of the subprime and other mortgage debt that triggered the current crisis was top-rated "AAA" debt for years until this debt was on the doorstep of default; FBI investigations into the rating agencies and rated companies are ongoing. *See "FBI Investigates Four Firms at Heart of the Mess,"* Sept. 24, 2008, Wall Street Journal.[2] The financial crisis has led to the bailout of Iceland's, Hungary's and Ukraine's economies by the International Monetary Fund, with the Baltic States, Pakistan, South Korea and Brazil next in line.[3] China, whose dollar purchases have propped up the U.S. economy, is anticipating decoupling from the dollar.[4]

It is not altogether clear that insurer AIG will avoid bankruptcy even with the help of the government's $125 billion unless it sells off nearly all its non-insurance assets. Yet, AIG still enjoys its now-stale "A" rating by A.M. Best's, the nation's leading insurance rating company, just as Western Surety enjoys a stale "A" rating. On October 25, 2008, the Wall Street Journal reported that "New York Life Insurance Co., one of the highest rated insurers in the U.S.," is seeking aid from the "government's $700 billion rescue program."[5]

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2 Full story available online from the Wall Street Journal at (http://online.wsj.com/article/SB122221103979869021.html?mod=googlenews_wsj) (last checked October 22, 2008).

3 "The International Monetary Fund may soon lack the money to bail out an ever growing list of countries crumbling across Eastern Europe, Latin America, Africa, and parts of Asia, raising concerns that it will have to tap taxpayers in Western countries for a capital infusion or resort to the nuclear option of printing its own money." From Britain's *Telegraph*, story available online at http://www.telegraph.co.uk/finance/comment/ambroseevans_pritchard/3269669/IMF-may-need-to-print-money-as-crisis-spreads.html (last checked October 28, 2008).

4 *See Reuter*'s story, quoting *The People's Daily*, the communist party's newspaper: http://www.reuters.com/article/email/idUSTRE49N1XX20081024 (last checked October 27, 2008).

5 Story available online from the Wall Street Journal at

Given this background, it is unreasonable for Defendants to ask this Court to accept as credit-worthy their proposed surety, Western Surety Company, based solely on an A.M. Bests' outdated "A" rating issued December, 2007. *See Exhibit* B to Defendants' *Notice*. Specifically, the following facts militate in favor of rejecting this bond and requiring Defendants (and their liability insurer) to post a cash bond:

First, an "A" rating is not close to the top ratings offered by A.M. Best. "A++" and "A+" are the top ratings, and are defined as "superior" ratings, categories wholly separate from and above a rating of "A." *See* 2008 Edition of Best's Rating System and Procedures (hereafter, "*Best's Guide*").[6] Since the bond here is supposed to "guarantee" payment if Defendants' appeal is unsuccessful, *Muck*, 814 P.2d 872-73, at a minimum the Association is entitled to a surety with the highest rating, A++. 24% of insurers receive A++ "superior" ratings from A.M. Best, but none of them were selected by Defendants here.[7] Why did Defendants select a surety lacking a "superior" rating? The answer is clear, to save themselves money on the bond premium, since higher-rated sureties charge more for bond premiums because they offer a lower risk of non-payment. The Association should not be required to accept anything less than the highest-rated A++ surety just so Defendants or their liability insurer can money on their bond premium.

Second, A.M. Best's also rates companies based on their "financial size," a calculus derived from the insurer's adjusted policyholder's surplus. Western Surety is rated "IX" by Bests. *See Exhibit* 2. There are six financial sizes *greater than* this, "X" through "XV". Again,

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http://online.wsj.com/article/SB122487244838367321.html (last checked October 25, 2008).

[6] *Best's Guide* available at http://www.ambest.com/ratings/pcbirpreface.pdf (last checked October 22, 2008), at hand-written page 4. Copy attached as *Exhibit* 2.

[7] *See Best's Guide*, note 6, at hand-written page 16 (Chart: *Rating Distribution by Individual Companies*).

the Association should not be required to accept a surety whose adjusted policyholder's surplus falls below 20%[8] of A.M. Bests rated sureties. The Association's damages judgment is presumed to be proper and valid under the law. *See O'Donnell v. State Farm Mut. Auto. Ins. Co.*, 186 P.3d 46, 48, note 2 (Colo. Jun 09, 2008) (because "a judgment is presumed valid," absent a bond, a "judgment creditor can pursue collection of the judgment while the case is being appealed"). This judgment must be protected by an A++, XV surety.

Third, an A.M. Bests rating based on out-dated *December 18, 2007* financial data (and, more likely, based on Western Surety-produced quarter-end financial data no more current than *September 30, 2007*), is meaningless because pricing of Western Surety assets has been severely impaired due to the across-the-board devaluation of stocks, bonds and other securities since then. Where these assets consist of stocks, the stock market's Standard & Poor's (S&P's) average has fallen 42% (from 1,455 to 849) from December 17, 2007 through October 27 2008 (*see Exhibit* 3, S&P value graph). Where these assets consist of bonds, the bond market has essentially become frozen since that date and it is nearly impossible to value such bonds. Where these assets consist of real estate, both residential and commercial property values have fallen precipitously since that date. Strikingly, CNA Surety (SUR) stock prices have fallen from $19.88 as of December 17, 2007 to $10.46 as of October 27, 2008, or 47% during this same time. *See* CNA Surety stock value chart, copy attached as *Exhibit* 4.

Under the current circumstances, and given the Defendants' failure and/or inability to establish the highest A.M. Bests' "A++" credit-worthiness and "Group XV" financial size of their proposed bond surety, the Court should vacate its stay of execution within 10 days of its

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8 *See Best's Guide*, note 6, at hand-written page 16 (Chart: *Financial Size Category by*

granting this *Objection* unless Defendants and their liability insurer post a cash bond equal to 125% of the judgment within that time.

B. The Form of the Bond is Fatally Deficient

The Association and Defendants have communicated extensively regarding a number of deficiencies in the bond's form. Defendants have represented that they intend to secure a replacement bond from Western Surety curing these deficiencies. If the Court does not reject Western Surety as surety here for the reasons set forth above, then the Court should condition any further stay of execution on the issuance of a new bond that corrects these deficiencies, which are catalogued below. Before analyzing these deficiencies, however, a short review of the nature of surety bonds is appropriate.

A surety bond is a promise by the surety to pay the debt of another, called the principal, to a third-party, the obligee. *See, generally, Helmsman Management Services, Inc. v. Colorado Dept. of Labor and Employment*, 31 P.3d 895, 897 (Colo. App. 2000), *cert. den., citing with authority*, RESTATEMENT (THIRD) OF SURETYSHIP AND GUARANTY § 69 (1995). Because a surety bond is a contract, it is important that its terms are complete and unambiguous, and that the bond leaves no room for the surety to argue that it is not immediately and directly liable in the event the condition precedent to payment is met, that is, that the principal's appeal fails and execution on the judgment ripens. *Cf. Gardner Bros. & Glenn Const. Co. v. American Sur. Co. of New York*, 37 P.2d 384 (Colo. 1934) (surety bond "should be enforced, like other contracts, according to the plain meaning and intention of the words employed.") See also *Rand-Whitney Containerboard L.P. v. Town of Montville*, 245 F.R.D. 65, 67 (D.Conn. 2007) (language in

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Individual Companies).

supersedeas bond must be "clear and unambiguous"; bond rejected because its language lacked specificity required for court approval).

Here, the face of Western Surety's bond, *Exhibit* B to Defendants' *Notice*, is incomplete and contains potential ambiguity. If the Court does not reject Western Surety as surety, then the Court should condition any further stay of execution on the issuance of a new bond that corrects the following deficiencies:

Missing Judgment Date and Amount of Bond. The bond is missing the judgment date, October 1, 2008: the line for the judgment date is blank. A new A++, XV bond must issue correctly identifying the judgment date, and the Court should order that Defendants obtain such replacement bond in the amount of 125% of any amended judgment.

Incomplete Identification of Principals. The bond references that a judgment has been obtained against a Principal, American Family, and the bond protects the Principal against the judgment. This is incorrect. Instead, the judgment has been obtained against the four named Defendants, and the bond needs to protect them, as Principals, against the judgment. A new bond must issue correctly identifying the full names of the four Defendants along with that of their liability insurer, American Family Insurance Group, and identifying all five as "Principals."

Failure to Reference All Applicable Rules. The bond refers to Colorado Appellate Rule 8(b). While the bond may suffice as a supersedeas bond even though no appeal has yet been filed, it is currently intended to serve as a bond against execution on the judgment under Colorado Rule of Civil Procedure 62 (pending a ruling on your motion to amend the judgment). This fact is not recited in the bond. A new bond must issue stating that it is intended to secure

payment of the judgment pursuant to *both* Colorado Rule of Civil Procedure 62 and Colorado Appellate Rule 8(b).

Potential Ambiguity as to Conditions Upon Which Bond Payable. Arguably, the bond suggests that payment under the bond may be *secondary* to a failure by the Principals to satisfy the judgment. Instead, a new bond should issue expressly stating that it is *not contingent* on the failure of one or more of the Principals to satisfy the judgment. To this end, the new bond should do the following

a. Delete the words "*not to exceed*" regarding the bond's principal amount because they create a potential ambiguity as to how much is being bonded. Leaving these words in is like the surety saying "I promise to pay you an amount not to exceed $100, and my paying you $25 would satisfy the condition." If this change is made, the surety is protected because it can only be called on to pay the amount of the unsatisfied judgment, whatever that amount is, but in no event is it promising to pay more than the principal amount of the bond.

b. Add the following words before the bond's last sentence: "*Notwithstanding anything else in this bond to the contrary, Surety agrees to satisfy the judgment remaining after appeal in accordance with this bond, even if the amount of the judgment is reduced as a result of that appeal, and without regard to whether any demand has first been made upon any Principal to satisfy the judgment or whether any other steps have been taken to execute upon the judgment.*" This language will help preclude the surety from urging that it is not required to pay the judgment if the judgment amount is reduced following appeal, but the judgment itself is not reversed. And, this change will help preclude the surety from arguing that the Association must first establish that the Principals have failed to or cannot satisfy the judgment before the Association seeks to execute on the bond.

Conclusion

The Court should reject Defendants' bond and proposed surety because they do not provide adequate security. The Court should vacate its stay of execution within 10 days of the Court granting this *Objection* unless Defendants and their liability insurer post a cash bond equal to 125% of the judgment. Alternatively, the cash bond requirement should be vacated only if Defendants tender a proper bond issued by a surety with the very highest A.M. Bests' rating,

"A++," and qualifying for A.M. Bests' largest financial category, "Group XV," but only if such rating has issued no later than within thirty days of the Court's order. The bond face amount must equal at least 125% of the judgment, and the bond text must cure all the drafting deficiencies described in Part B above. Further, the Court should order that if a bond is posted, that the Association be granted leave to later object to the bond and its surety based on any new, adverse financial conditions that may arise.

Respectfully submitted,

SULLAN[2], SANDGRUND SMITH & PERCZAK, P.C.

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In accordance with C.R.C.P. 121 § 1-26(9), a printed copy of this document with original signature(s) is maintained by Sullan[2], Sandgrund Smith & Perczak, P.C., and will be made available for inspection by other parties or the Court upon request.

CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of October, 2008, a true and correct copy of the foregoing *Plaintiff's Objection to Defendants' Notice of Posting of Cost Bond (and Attached Supersedeas Bond)* was efiled with the Court and served via Lexis Nexis as follows:

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