1980

First Security Bank of Utah v. Colonial Ford, Inc. et al : Brief of Appellants

Utah Supreme Court

H. Ralph Klemm; Attorney for Appellants;
Steven H. Gunn; Attorney for Respondent;

IN THE SUPREME CO

IRST SECURITY BANK OF UTAH, N
corporation,

Respondent,

-vs-

LONIAL FORD, INC.,

Defendant,

and

GRANDE L. BELNAP and
RIS BELNAP,

Appellants.

ON APPEAL FR
OF

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IN THE SUPREME COURT OF THE STATE OF UTAH

FIRST SECURITY BANK OF UTAH, N.A.,
a corporation,

Respondent,

-vs-

COLONIAL FORD, INC.,

Defendant,

and

LEGRANDE L. BELNAP and
DORIS BELNAP,

Appellants.

Case No. 15745

BRIEF OF APPELLANTS

ON APPEAL FROM THE THIRD JUDICIAL DISTRICT COURT
OF SALT LAKE COUNTY, STATE OF UTAH

HONORABLE G. HAL TAYLOR
District Judge

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IN THE SUPREME COURT OF THE STATE OF UTAH

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Defendant,	)	Case No. 15745
and	)	
LEGRANDE L. BELNAP and DORIS BELNAP,	)	
Appellants.	)	

BRIEF OF APPELLANTS

ISSUES ON APPEAL

The District Court erred when it denied defendants' Motion to amend their Answer to include allegations of contractual mistake and misunderstanding as a defense to plaintiff's Complaint.

The District Court abused its discretion when it denied defendants' Motion to amend their Answer to include allegations of contractual mistake and misunderstanding of the parties as a defense to plaintiff's Complaint.

NATURE OF THE CASE

This case involves the contractual responsibility of two individual defendants for a corporate debt which they allegedly assumed by written guarantee at the time the corporate obligation was incurred.

DISPOSITION IN LOWER COURT

The case came to trial on the issue of whether the written guarantee signed by the defendants was induced by the fraud of bank representatives. At the conclusion of the evidence, the defendants made a Motion for leave to amend their Answer to conform to the evidence by adding an affirmative defense of mistake and misunderstanding of the parties as a defense to plaintiff's Complaint. The court denied the Motion and entered judgment against the defendants in the sum of $33,236.80, plus interest, attorney's fees and court costs.

RELIEF SOUGHT ON APPEAL

Defendants seek on this appeal to have the judgment vacated and set aside and to have the Supreme Court order that a new trial be held to determine if the written guarantee executed by the defendants should be rescinded because of the mistake and misunderstanding of the parties.

STATEMENT OF FACTS

Plaintiff filed this action in the District Court of Salt Lake County against the defendant, Colonial Ford, Inc., to recover sums due under a promissory note executed by the corporation on September 14, 1976. In a second cause of action, the plaintiff sought to recover a similar amount from defendants, LeGrande L. Belnap and Doris Belnap, on the basis of a written guarantee which they executed with the corporate note.

Judgment by Default was entered against the corporation on December 14, 1976, but the individual defendants filed an Answer alleging that the written guarantee was obtained through the fraud of corporate agents. (R.12-13) The question of the personal liability of the Belnaps was tried by the court, sitting without a jury, on February 2, 1978. At the conclusion of the evidence, the defendants moved to amend their Answer to conform to the evidence by including an affirmative defense to the effect that the written guarantee was based on the mistake and misunderstanding of the parties. (R.249) That Motion was denied. (R.249) The court then found the issues in favor of the plaintiff bank and entered judgment against the defendants for the amount owed by the corporation under the promissory note. (R.120)

Although the testimony of defendants' witnesses at the trial was first designed to prove fraud on the part of the bank's agent in obtaining the signatures of the defendants on the guarantee, it also appeared from the evidence that the execution of the guarantee was based on the reasonable but mistaken belief of the defendants that they were signing something else.

Ronald Folkerson was the branch manager at the Sugarhouse office of First Security Bank in September, 1976. (R.209) He became concerned about a sizeable overdraft in the checking account of Colonial Ford, Inc. (R.209) He called defendant Doris Belnap on the telephone to discuss the overdraft. (R.209) He asked her to sign

a note and to guarantee the overdraft. (R.172) She refused because it was a corporate obligation and because her husband and attorney were both out of town at that time. (R.172-3) He then asked her to have the attorney get in touch with him when he returned. (R.173)

Mrs. Belnap later told her attorney about the conversation with Folkerson and asked him to handle it for her. (R.173) The attorney met with Mr. Folkerson at the bank office a few days later. (R.158-9) Folkerson suggested that Colonial Ford sign a promissory note to cover the overdraft, and the attorney agreed to have the officers of Colonial Ford sign such a note. (R.160) Mr. Folkerson also requested that Mr. and Mrs. Belnap execute the note as co-signe The attorney refused to do that. (R.120, 216) As an alternative, Folkerson suggested that the Belnaps sign a guarantee for the note. The attorney again refused because the form used by the bank is unconditional and guarantees anything and everything. (R.160-1) The attorney also objected to having the Belnaps sign an outright guarantee for payment of the overdraft because it was not their obligation. (R.169) However, Belnaps' attorney suggested that if Folkerson would have the bank's attorney contact him, he would recommend to the Belnaps that they sign a "guarantee of collection." (R.161) The content of such a guarantee was to be worked out between the attorneys. (R.161) Neither of the Belnaps were present at the meeting held at the bank. (R.165)

On September 14, 1976, Mr. Folkerson called the Colonial Ford Company and spoke with Mrs. Belnap. (R.174) He insisted that he come to the dealership that day and get the overdraft covered by a note. He stated that he had to have a corporation note because the auditors were at the bank and the overdraft was causing him some problems. (R.175)

Mrs. Belnap told him that she would consult with her attorney and then call him back. When she called the attorney's office, he was unavailable. (R.176) She returned the call to Mr. Folkerson and told him that she couldn't meet with him that day because the attorney was unavailable. Mr. Folkerson told her that he knew the attorney couldn't be there, but he said he had to have the note. He told her that he had prepared the papers in accordance with her attorney's instructions, and he insisted on completing the transaction that day. (R.176)

Folkerson said nothing about the personal guarantees in that telephone conversation. He merely stated that he had the papers and he would bring them down to the dealership. (R.176-7) After some discussion, Mrs. Belnap consented that Mr. Folkerson could come to the agency with the papers later that same afternoon. (R.177) When he arrived at the agency, Mrs. Belnap called her attorney on the telephone and told him that Mr. Folkerson was there with the papers in his hand. (R.177) The attorney was unable to meet with them, and he had no idea what was in the documents. (R.163) However, the attorney told Mrs. Belnap that if Folkerson would represent to them that he had prepared the papers in accordance with his discussion with her attorney, then he would recommend that they sign those papers.

(R.177) She advised her husband of the attorney's statement, and her husband turned to Mr. Folkerson and asked him if these were the papers that Mr. Rothey had instructed him to prepare. Folkerson answered in the affirmative and said that they had been prepared as instructed by their attorney. (R.177-8)

In a previous phone call, Mr. Folkerson had told Mrs. Belnap that he knew that her attorney wouldn't let her or her husband guarantee the note because it was a corporate obligation and was not her personal obligation. Because of this, Mrs. Belnap was not concerned about signing a personal guarantee. (R.177)

Based on the representation made by Mr. Folkerson regarding the preparation of the papers, Mr. and Mrs. Belnap signed the papers. (R.178) At that time, the Belnaps thought they were signing a document that had been negotiated by their corporate and personal attorney and had been prepared in accordance with his instructions. (R.180) They didn't read the document because Mr. Folkerson told them that it had been prepared in accordance with their attorney's instructions. (R.179) Mrs. Belnap would not have signed the document without the Folkerson representation. (R.181, 191) She never intended to sign a personal guarantee of a corporate obligation. (R.184)

Mr. Belnap also relied upon the Folkerson representation. Except for Mr. Folkerson's assurance that the papers had been agreed upon by his attorney, Mr. Belnap never would have signed those papers on that date or at any other time. (R.197) He never read the document and he relied solely upn the representation made by Folkerson. (R.197) He was not aware that his attorney had not examined the papers (R.200)

ARGUMENT

POINT NO. I

THE DISTRICT COURT ERRED WHEN IT DENIED DEFENDANTS' MOTION TO AMEND THEIR ANSWER TO INCLUDE ALLEGATIONS OF CONTRACTUAL MISTAKE AND MISUNDERSTANDING AS A DEFENSE TO PLAINTIFF'S COMPLAINT

Rule 15(b), Utah Rules of Civil Procedure, deals with amendments to conform to the evidence and reads as follows:

> "When issues not raised by the pleadings are tried by express or implied consent of the parties they shall be treated in all respects as if they had been raised in the pleadings. Such amendment of the pleadings as may be necessary to cause them to conform to the evidence and to raise these issues may be made upon motion of any party at any time, even after judgment; but failure to so amend does not affect the result of the trial of these issues. If evidence is objected to at the trial on the ground that it is not within the issues made by the pleadings, the court may allow the pleadings to be amended when the presentation of the merits of the action will be subserved thereby and the objecting party fails to satisfy the court that the admission of such evidence would prejudice him in maintaining his action or defense upon the merits. The court shall grant a continuance, if necessary, to enable the objecting party to meet such evidence."

In construing and applying this rule, the Supreme Court has held that it has two separate parts. The first part is applicable when issues not raised in the pleadings are tried by express or implied consent of the parties, and the second part is applicable where a motion to amend is made in response to an objection by the opposing party to the introduction of evidence. In the first case the court has no discretion and it must allow the amendment. Only in the second case may the court determine whether prejudice, undue

delay or laches ought to prevent the amendment. See General Insurance Company of America v. Carnicero Dynasty Corp., 545 P2d 5[illegible]

In the cited case, the trial court had denied defendant's motion to amend his answer to include lack of consideration as an affirmative defense. The motion was made to conform defendant's pleadings to the evidence after witnesses had testified that the indemnity agreement relied upon by the plaintiff had been obtained from defendant as an afterthought long after the original bonding agreement had been signed by the primary obligor. Because the evidence on which the motion was based was introduced without objection from the plaintiff, the court ruled that the issue was tried by implied consent. Relying on its construction of Rule 15(b) referred to above, the Supreme Court held that the trial court's refusal to allow the proposed amendment was error and sent the case back for a new trial. The court reasoned that Rule 15(b) mandated the trial court to grant the motion under the circumstances of that case.

In the action now before the court, similar circumstances were before the trial court when a similar motion was denied. Without objection from the plaintiff, the defendants testified that when they executed their personal guarantee of a corporate obligation, they mistakenly believed that they were signing something else. The facts brought out at the trial strongly support their assertions in this regard.

When the Branch Manager at plaintiff's Sugarhouse Office contacted Mrs. Belnap about a sizeable overdraft in the checking account of Colonial Ford, Inc., she refused to sign a note to guarantee the corporate obligation. Then she turned the matter over to her attorney for a final determination. When the attorney met with bank representatives, he agreed that the corporation would sign a note to cover the overdraft, but he expressly refused to have Mr. and Mrs. Belnap execute the note as co-signers. When bank personnel suggested as an alternative that the Belnaps sign a guarantee, the attorney again refused because the form used by the bank is unconditional in nature. The attorney also objected to the guarantee for payment because the obligation was that of the corporation.

The testimony also revealed that defendants' attorney would recommend that they sign some kind of a guarantee if a satisfactory document could be worked out between the attorneys. Neither of the Belnaps were present at the meeting held at the bank, and they left the details to their own attorney.

Without any consultation between the attorneys, plaintiff's representative called the Colonial Ford Company and insisted that the overdraft be covered by a note. Defendants' attorney could not meet with them on that date, but he advised Mrs. Belnap that if the bank representative would represent to them that the papers to be signed had been prepared in accordance with their attorney's instructions, then they should go ahead and sign them. The bank representative

made that representation, and the documents were executed without being read by the defendants. The attorney also had no knowledge of their contents. At that time, the Belnaps thought they were signing a document that had been negotiated by their corporate and personal attorney and had been prepared in accordance with his instructions. They never intended to sign a personal guarantee of a corporate obligation. They thought they were signing a document, which, in fact, was non-existent.

The evidence clearly showed that the defendants were mistaken when they signed the document upon which their liability was based. At the conclusion of the evidence, their counsel moved to amend their Answer to conform to that evidence. That motion was abruptly denied by the court. That ruling was in error because under Rule 15(b) the issue of mistake of the parties had already been tried by implied consent. Under the interpretation of the Rule made by the court in General Insurance Company of America v. Carnicero Dynasty Corp., Supra., the granting of the motion was mandatory. Denial of the motion was erroneous, and the case should be remanded to the court for a new trial.

In support of the trial court's ruling on defendants' motion to amend, plaintiff will undoubtedly argue that Rule 8(c), Utah Rules of Civil Procedure, requires that affirmative defenses be pleaded and that failure to do so is fatal to any such defense. The Supreme Court faced this same argument in Cheney v. Rucker, 14 U2d 205, 381 P2d 84 (1963), where the court stated that the rules must be considered in

the light of their purpose of liberalizing both pleading and procedure when resolving any discrepancy in their content. The language of the court in the Cheney case, all of which appears to be applicable to the matter now before the court, reads as follows:

> "Plaintiff also raises the procedural point that since defendants did not plead the subsequent agreement as an affirmative defense, they should not have been permitted to rely thereon. It is true, as plaintiff insists, that Rule 8(c), U. R. C. P., requires that affirmative defenses be pleaded. It is a good rule whose purpose is to have the issues to be tried clearly framed. But it is not the only rule in the book of Rules of Civil Procedure. They must all be looked to in the light of their even more fundamental purpose of liberalizing both pleading and procedure to the end that the parties are afforded the privilege of presenting whatever legitimate contentions they have pertaining to their dispute. What they are entitled to is notice of the issues raised and an opportunity to meet them. When this is accomplished, that is all that is required. Our rules provide for liberality to allow examination into and settlement of all issues bearing upon the controversy, but safeguard the rights of the other party to have a reasonable time to meet a new issue if he so requests. Rule 15(b), U.R.C.P., so states. It further allows for an amendment to conform to the proof after trial or even after judgment, and indicates that if the ends of justice so require, 'failure so to amend does not affect the result of the trial of these issues.' This idea is confirmed by Rule 54(c)(1), U.R.C.P.: '[E]very final judgment shall grant the relief to which the party in whose favor it is rendered is entitled, even if the party has not demanded such relief in his pleadings.'
>
> Although the plaintiff did object to evidence on the issue of subsequent agreement, when it was overruled, he made no request for a continuance nor did he make any representation to the court that he was taken by surprise or otherwise at a disadvantage in meeting that issue. The trial court not only did not abuse his

discretion in allowing the issue to be raised and receiving the contract in evidence, but he would have failed the plain mandate of justice had he refused to do so." (Emphasis applied)

POINT NO. II

THE DISTRICT COURT ABUSED ITS DISCRETION WHEN IT DENIED DEFENDANTS' MOTION TO AMEND THEIR ANSWER TO INCLUDE ALLEGATIONS OF CONTRACTUAL MISTAKE AND MISUNDERSTANDING OF THE PARTIES AS A DEFENSE TO PLAINTIFF'S COMPLAINT

If the court should determine in its deliberations that t question of whether defendants should be allowed to amend their Ans to conform to the proof was a matter within the discretion of the court, then defendants further assert that such discretion was abus in this instance.

As noted above, the second part of Rule 15(b), Utah Rules of Civil Procedure, is applicable where a motion to amend is made i response to an objection by the opposing party to the introduction evidence. Although such an objection was not forthcoming in this ca the cases cited under this rule show that any discretion of the co allowed in determining motions to conform to the evidence should be exercised liberally and in the interest of justice. See Cheney v. Rucker, Supra.; General Insurance Company of America v. Carnicero Dynasty Corp., Supra.; and Morris v. Russell, 120 U 545, 236 P2d 43

Rule 54(c)(1) requires that every final judgment shall gra the relief to which the party in whose favor it is rendered is entit

even if the party has not demanded such relief in its pleadings. The Supreme Court declared in Palombi v. D & C Builders, 22 U2d 297, 452 P2d 325, that this rule indicates that there shall be liberality of procedure to reach the result which justice requires.

The Supreme Court has shown this liberality in construing the rule as it concerns amendments to the pleadings during the trial. In Buehner Block Company v. Glezos, 6 U2d 226, 310 P2d 517, the court allowed an unpleaded partnership issue to be determined at trial where it was not objected to by the defendant and both sides went into the facts of the partnership during the testimony at the trial.

The court ruled in Cheney v. Rucker, Supra., that the trial court properly allowed the pleadings to be amended and an affirmative defense to be included as an issue where the opposing party made no request for a continuance and made no representation to the court that he was taken by surprise or otherwise at a disadvantage in meeting the issue. The court also noted that although Rule 8(c) requires that affirmative defenses be pleaded, that rule must be ruled in the light of the fundamental purpose of the Rules of Civil Procedure of liberalizing the requirements of pleading and procedure so that parties can properly present their legitimate contentions in one proceeding.

The Supreme Court noted in General Insurance Company of America v. Carnicero Dynasty Corp., Supra., that the purpose of the amendment to conform to the proof is to bring the pleadings in line with the actual issues upon which the case was tried.

Keeping in mind the liberality of the court in these mat we turn to the issues of this case. The defendants are alleging th the guarantee that they signed should be rescinded because of thei unilateral mistake. They had not seen the papers prior to the tim of signature. They didn't read them at that time because they rel upon Mr. Folkerson's representation to them that the papers had be prepared in accordance with the instructions of their own attorney. They believed that they were signing something that was non-existe at that time. Both the defendants and their attorney had advised t bank that they would not sign a promissory note or give an unlimite guarantee to the bank. They had no intention to do so when the doc ment was signed.

The Supreme Court of Utah has had prior occasion to deal with the contractual defense of unilateral mistake. In Ashworth v. Charlesworth, 119 U 650, 231 P2d 724, the court stated the general rule in such matters by quoting from an annotation in 59 ALR 809 as follows:

> "Equitable relief from a mutual mistake is frequently given by a reformation of the contract. But a contract will not be reformed for a unilateral mistake. Equitable relief may, however, be given from a unilateral mistake by a rescission of the contract. Essential conditions to such relief are (1) The mistake must be of so grave a consequence that to enforce the contract as actually made would be unconscionable. (2) The matter as to which the mistake was made must relate to a material feature of the contract. (3) Generally the mistake must have occurred notwithstanding the exercise of ordinary diligence by the party making the mistake. (4) It must be possible to give relief by way of rescission

> without serious prejudice to the other party except the loss of his bargain. In other words, it must be possible to put him in statu quo."

The above language was adopted as the law of Utah in the cited case and has been subsequently quoted and followed in the case of Davis v. Mulholland, 25 U2d 56, 475 P2d 835.

When applying the facts of this case to the standards set forth above, we find that the defense of unilateral mistake would clearly be applicable to the Belnap circumstances. The first condition listed above is that the mistake must be so grave a consequence that to enforce the contract as actually made would be unconscionable. The amount involved in this action exceeds $40,000.00. If the Belnaps were required to pay this amount from their personal funds and assets, it would be a great burden to them. On the other hand, the plaintiff can still look to the corporation for satisfaction of its prior judgment for the overdraft amount. As was stated on several occasions during the trial of the case, the overdraft obligation was that of the corporation and not that of its individual stockholders. The purpose of organizing the corporation in the first place was to insulate the stockholders from personal liability. It was also pointed out during the trial that the overdraft came from corporate activities and not from any personal loans or transactions made by its officers or these defendants. The note was given to cover a corporate obligation. It would certainly be unconscionable to require the Belnaps to pay this amount unless they knowingly accepted that obligation.

The second condition stated above requires that the mista must relate to a material feature of the contract. The materiality the guarantee is self-evident here and need not be discussed at an great length.

The third requirement is that the mistake must have occurr despite the exercise of ordinary care on the part of the Belnaps. is the only requirement that might give the court trouble in this c It is conceded that the Belnaps did not read the guarantee before t signed it. However, they were relying upon the representation of t bank representative to the effect that the document had been prepar in accordance with the instructions of their attorney. They were n even aware of what those instructions were, and reading the contract wouldn't have given them great enlightenment in this regard. They were following the advice of their own counsel and relying upon the representations of the bank manager when they signed the document. It certainly isn't negligence to rely upon the advice of your own counsel and to accept the word of an important officer of the bank. Mrs. Belnap had expressly refused to sign a blanket guarantee or even co-sign on the promissory note. She had no reason to believe that the bank officer would present papers that achieved the very thing she had refused to do in the first place.

The fourth requirement of unilateral mistake is that the court can give relief by way of rescission without serious prejudice to the other party except the loss of his bargain. In this instance

it should be remembered that the bank has a judgment by default against the corporation. This judgment is fully effective and collectable by normal means. The corporation owns a large piece of property that is to some degree subject to the corporate obligations. The plaintiff's interests would not be seriously prejudiced by a judgment for the defendants on the question of personal liability.

In refusing to grant the Motion to amend to conform to the evidence, the court abused its discretion and denied the defendants their normal rights under the procedures of the court. A reversal of the trial court's decision is mandatory in this instance.

CONCLUSION

For reasons set forth above, the court should reverse the trial court's decision and remand the matter for further proceedings and for a new trial.

RESPECTFULLY SUBMITTED,

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NOTICE OF MAILING

Mailed two copies of this Brief to Respondent's attorney, Steven H. Gunn, 400 Deseret Building, Salt Lake City, Utah, 84111, by United States Mail, postage prepaid, this 7th day of September 1978.