

1989

Washington National Insurance Company, an Illinois corporation v. SHERWOOD ASSOCIATES, a Utah limited partnership; THE RIDGE ATHLETIC CLUB, INC., a Utah corporation, DARRELL D. TANNER, individually, and as Trustee of the Tanner Family Trust; JASON TANNER, an individual; TRACY A. TANNER MCDONALD, an individual; LINLEY A. TANNER, an individual; BRADLEY H. TANNER, an individual; et al. : Reply Brief of Appellants

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Jackson Howard, Leslie W. Slaugh; Howard, Lewis & Petersen; attorneys for appellants.

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UTAH COURT OF APPEALS
BRIEF

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DOCKET NO. 89-0502 OF THE STATE OF UTAH

IN THE COURT OF APPEALS

WASHINGTON NATIONAL	:	
INSURANCE COMPANY, an	:	
Illinois corporation,	:	
Plaintiff-Appellee,	:	Case No. 890502-CA
vs.	:	
	:	Category 14b
SHERWOOD ASSOCIATES,	:	
a Utah limited partnership;	:	
THE RIDGE ATHLETIC CLUB,	:	
INC., a Utah corporation,	:	
DARRELL D. TANNER,	:	
individually, and as Trustee	:	
of the Tanner Family Trust;	:	
JASON TANNER, an individual;	:	
TRACY A. TANNER McDONALD,	:	
an individually; LINLEY A.	:	
TANNER, a individual;	:	
BRADLEY H. TANNER, an	:	
individual; et al.,	:	
Defendants-Appellants.	:	

REPLY BRIEF OF APPELLANTS

APPEAL FROM THE SUMMARY JUDGMENT OF
THE FOURTH JUDICIAL DISTRICT COURT OF UTAH COUNTY
THE HON. RAY M. HARDING

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ATTORNEYS FOR APPELLEES

FILED

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STATE OF UTAH
AUG 17 1990

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Statutes and Rules Cited:

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SUMMARY OF ARGUMENT

The 1985 amendment to Utah Code Ann. § 57-1-31 was not merely remedial or procedural. It increased by ten-fold the amount defendants were required to pay to prevent foreclosure on the subject real property. The change was substantive, and the trial court's application of the 1985 amendment to the subject trust deed unconstitutionally impaired the contract.

The trust deed, which was executed prior to the 1985 amendments, gave the creditor the option to "foreclose this Trust Deed in the manner provided by law for the foreclosure of

mortgages on real property." This provision incorporated the law of foreclosure as it existed when the trust deed was signed.

Even if the 1985 amendment does govern this case, plaintiff did not irrevocably elect to proceed by judicial foreclosure until it filed its complaint herein, which was after defendants had tendered payment of the delinquency. Because plaintiff had not made an irrevocable election, defendants were still entitled to cure the delinquency as provided in the trust deed statutes. Defendants' tender of the delinquency was adequate as a matter of law, because Darrell D. Tanner testified, without contradiction, that he had the ability to cause The Ridge Athletic Club, Inc., to pay the delinquency on the date of the tender.

Finally, plaintiff is not entitled to a security interest in new equipment and other personal property placed on the subject real property by The Ridge Athletic Club, Inc., an entity which did not sign any security agreement or other documents with plaintiff. The plaintiff's security interest extends only to personal property owned or acquired by Sherwood Associates.

ARGUMENT

POINT I

THE 1985 AMENDMENT TO UTAH CODE ANN. § 57-1-31 AFFECTED SUBSTANTIAL RIGHTS.

Plaintiff correctly argues that statutory amendments which affect only remedies or procedures, but which do not affect substantive rights, may be applied to contracts executed prior

to the effective date of the amendment. The amendment at issue in this case is not, however, merely remedial or procedural. The cases cited by plaintiff are distinguishable and can be generally explained as exercises of police power. Retroactive application of the 1985 amendment cannot be justified under the constitutional analysis set forth in recent United States Supreme Court decisions and decision of other states.

Plaintiff relies heavily on the United States Supreme Court case of Home Building and Loan Ass'n v. Blaisdell, 290 U.S. 398 (1934), which upheld a Minnesota mortgage moratorium law passed in response to the Great Depression of the 1930's, and on other cases of a similar vintage. The cases are distinguishable and not applicable to the present situation in Utah. "[I]t is now recognized that the court's holding in Blaisdell was based on the emergency which then existed." Portland Savings Bank v. Landry, 372 A.2d 573, 576 (Me. 1977). The court in Blaisdell upheld the Minnesota act only because it met five criteria related to the emergency:

Upholding the constitutionality of the Minnesota act, the court identified five criteria by which a legislative enactment could survive a challenge based on impairment of contract: (1) an emergency created a need for the measure; (2) the legislation was addressed to a legitimate public purpose and not for the mere advantage of particular individuals; (3) the relief afforded was appropriate to the emergency; (4) the conditions imposed by the act were reasonable; and (5) the statute was temporary and limited to the exigency which called it forth.

Federal Land Bank of Omaha v. Arnold, 426 N.W.2d 153, 159 (Iowa 1988) (citing Blaisdell, 290 U.S. at 444-47).

Recent pronouncements of the United States Supreme Court have refined the balancing test established in Blaisdell to a three-step analysis:

In the years since Blaisdell and Worthen,¹ the United States Supreme Court has refined the test for contract clause challenges to a 3-step analysis: (1) if the state law operates as a substantial impairment of a contractual relationship, (2) the state must have a significant and legitimate public purpose behind the regulation, which (3) adjusts the contracting parties' rights and responsibilities based on reasonable conditions appropriate to the public purpose.

Federal Land Bank of Omaha v. Arnold, 426 N.W.2d 153, 159 (Iowa 1988) (citing Energy Reserves Group, Inc. v. Kansas Power & Light Company, 459 U.S. 400, 411-12 (1983)).

Application of these criteria to the statute at issue in the instant case establishes that it may not constitutionally be applied to contracts executed before the effective date of the 1985 amendment. First, the amendment does operate as a substantial impairment of Darrell Tanner's rights. In the absence of the amendment, defendants would have been required to pay approximately \$119,200.00 to cure the default and prevent foreclosure. (R. 352.) If the 1985 amendment is applied, however, the amount necessary to forestall foreclosure would

¹W. D. Worthen Co. v. Kavanaugh, 295 U. S. 56 (1935), a case which found unconstitutional an Arkansas statute which dramatically changed the terms by which the payment of special assessments on municipal bonds were enforced.

have been approximately \$1,118,984.90. (R. 353-54.) This nearly ten-fold increase in the amount necessary to prevent foreclosure is clearly a substantial and substantive change.

Second, there is no evidence that the State of Utah had any "significant and legitimate public purpose" for giving retroactive effect to such a substantive modification, and indeed there is no evidence that the legislature intended the statute to have retroactive effect.

Third, even if there were some significant public purpose, there is no indication that the 1985 amendment "adjusts the contracting parties' rights and responsibilities based on reasonable conditions appropriate to the public purpose."

Application of these principles have been illustrated in other cases more factually similar to the case at bar. In Portland Savings Bank v. Landry, 372 A.2d 573 (Me. 1977), for example, the court considered a statute which reduced to 90 days the period for redemption after a foreclosure sale, whereas the redemption period had previously been one year. Although application of the arguments espoused by plaintiff herein would indicate that the statute only affected the remedy, the Maine Supreme Court nonetheless held the statute unconstitutional as applied to contracts executed prior to its effective date. Federal Land Bank of Omaha v. Arnold, 426 N.W.2d 153 (Iowa 1988) also dealt with a statutory modification of the redemption period and of other aspects of the foreclosure process. The statute was enacted in response to "the suffering and disloca-

tion which has wracked Iowa farm families in recent years." 426 N.W.2d at 154. Although the Iowa legislature did have a legitimate and significant public purpose, the Iowa Supreme Court held that the statute used was not constitutionally justifiable if applied to existing contracts. See also Burke v. E. L. C. Investors, Inc., 110 Wis.2d 406, 329 N.W.2d 259 (Ct. App. 1982) (also holding unconstitutional a modification of the statutory redemption period).

The cases cited by plaintiff as illustrating permissible modifications of contracts are distinguishable. Plaintiff relies on Columbian Building and Loan Co. v. Meddles, 34 Ohio L. Abs. 484, 35 N.E.2d 902 (1941), and on Whalen v. Citizens Building and Loan Co., 67 Ohio App. 139, 36 N.E.2d 54 (1940). The statute at issue in those two cases was initially enacted in 1937, and subsequently amended in 1939, and provided for a two-year limitation on the enforcement of deficiency judgments. The contracts at issue had been executed and foreclosed upon prior to the enactment of the statutes. The decisions of the Ohio courts in Columbian and Whalen upheld the statute. The decisions can initially be explained as an exercise of police power, because the statute in question was evidently enacted in response to the Great Depression. In addition, the enactment of a statute of limitation on the enforcement of a deficiency judgment is procedural, and does not affect substantive rights to the same extent as the amendment at issue in the instant case.

Plaintiff also relies on Guardian Depositors Corp. v. Powers, 296 Mich. 553, 296 N.W. 675 (1941). The statute at issue, also a depression era statute, limited deficiency judgments to the excess of the debt over the fair market value. The limitation applied only to foreclosures by advertisement where the creditor was the purchaser. The court upheld the statute because of the changed conditions which had occurred since the enactment of the prior statute, which made the amendment necessary to implement the legislative intent of the prior statute:

In the past a public sale has been thought to be the best method of enabling the mortgagor to realize the fair value of his premises. However, when the realty market is demoralized, that method of protecting the rights of a mortgagor becomes a mere formality. It is then within the province of the legislature, in order to prevent injustice, to set up new machinery for the enforcement of the obligation which will safeguard the rights of the debtor and secure to the creditor that which is his due. No one has a vested substantive right to more than is his due.

296 N.W. at 678.

The statute at issue in Guardian is further distinguishable because the legislature had expressly declared its intent that the statute be given retroactive effect. 296 N.W. at 677.

Finally, plaintiff relies on Holloway v. Barrett, 87 Nev. 385, 487 P.2d 501 (1971), which, like Guardian, addressed the constitutionality of a law which limited a deficiency judgment to the difference between the fair market value and the debt, rather than the difference between the foreclosure sale price

and the debt. As in Guardian, the Nevada Supreme Court upheld the statute based on the principle that "mortgagees are constitutionally entitled to no more than payment in full. They cannot be heard to complain on constitutional grounds if the legislature takes steps to see to it that they get no more than that." 487 P.2d at 505 (quoting Gelfert v. National City Bank, 313 U.S. 221 (1941) (citations omitted)).

The 1985 amendment to Utah Code Ann. § 57-1-31 cannot constitutionally be applied to contracts executed before the statute. The amendment cannot be justified on any public policy basis, and it does far more than merely affect procedural rights. The amendment has a significant substantive impact on the amount which the debtor must pay to prevent foreclosure. The trial court erred in denying Tanner's motion for summary judgment and granting the motion of plaintiff.

POINT II

THE TRUST DEED INCORPORATED THE FORECLOSURE PROVISIONS IN EFFECT WHEN IT WAS SIGNED.

Plaintiff argues that the 1985 amendment simply permitted plaintiff to enforce the pervasive boiler plate provisions of the contracts which purported to permit plaintiff to accelerate the unpaid balance due upon default by the debtor. The analysis is incomplete. In addition to providing that the beneficiary under the Trust Deed has the right to accelerate the balance due, the Trust Deed also provided, in paragraph 27, that the beneficiary had the option to "foreclose this Trust Deed in the

manner provided by law for the foreclosure of mortgages on real property" The cases cited in plaintiff's initial brief establish that the law existing at the time of contract is deemed incorporated into the contract. The law existing at the time of the contract did not prohibit the beneficiary from accelerating the unpaid balance, but merely provided, in effect, for a procedure whereby the borrower could cancel the acceleration by paying the amount in default prior to the entry of a decree of foreclosure. If the borrower failed to cure the default, the previously declared acceleration would remain in full effect.

Because the pre-1985 version of Utah Code Ann. § 57-1-31 was incorporated into the contract, the rights of the parties must be governed by the terms of that version of the statute.

POINT III

PLAINTIFF'S NOVEMBER 30, 1987, LETTER DID NOT OPERATE AS AN ELECTION TO JUDICIALLY FORECLOSE THE TRUST DEED.

Plaintiff argues that the letter sent by its counsel to certain of the defendants on November 30, 1987, constituted an election to judicially foreclose the Trust Deed, and thereby prevented the defendants from exercising any of the rights which would be available in a foreclosure by power of sale, but which would not be available in a judicial foreclosure. Tanner acknowledges that the demand letter contains language which is consistent with a judicial foreclosure. (Tanner's initial brief

established that the language is also consistent with a power of sale foreclosure. Brief of Appellants, Point III.)

The issue is not, however, whether the demand letter would have permitted plaintiff to proceed by judicial foreclosure, but rather whether it constituted such a clear election of remedies as to have precluded plaintiff from proceeding with a power of sale foreclosure. The trust deed at issue and the applicable statutes provide that a beneficiary under a deed of trust has the option to foreclose by power of sale or to foreclose by judicial action. Each method has its attendant advantages and disadvantages. The issue in the present case is whether plaintiff could claim the advantages of a judicial foreclosure (or in other words, whether it could deprive Tanner of the advantages of a power of sale foreclosure), without also accepting the disadvantages. There must be a mutuality of obligation. See Resource Management Co. v. Weston Ranch & Livestock Company Inc., 706 P.2d 1028, 1036 (Utah 1985) (mutuality of obligations required for an enforceable contract). If any election of remedies effected by the demand letter was not binding on plaintiff, it cannot have been binding and detrimental to defendants.

The November 30, 1987, demand letter did not constitute a binding election of remedies. An election of remedies occurs only when there is (1) a choice between inconsistent remedies, and (2) a party chooses one remedy in such a manner as to (3) evidence an intent to forego all other remedies. Royal

Resources, Inc. v. Gibraltar Financial Corp., 603 P.2d 793, 796 (Utah 1979); Cook v. Covey-Ballard Motor Co., 69 Utah 161, 253 P. 196, 199 (1927). An election of remedies is generally held to have occurred when a party institutes suit claiming a particular remedy. Cook, supra. Plaintiff clearly elected to proceed by judicial foreclosure when it filed its complaint on December 10, 1987. A notice or demand letter prior to suit, however, generally does not constitute an election of remedies. 25 Am. Jur. 2d Election of Remedies § 15 (1966); Morris Plan Leasing Company v. Karns, 197 Kan. 150, 415 P.2d 291, 294 (1966).

Tanner has established in his initial brief that the language of the demand letter is equally consistent with foreclosure by power of sale. Even assuming, arguendo, that the language is consistent only with judicial foreclosure, however, the foregoing authorities establish that the demand letter did not constitute a clear and binding election to proceed by that remedy only.

Because any statements in the demand letter did not bind plaintiff to proceed only by judicial foreclosure, it similarly did not preclude defendants from exercising rights available under a power of sale foreclosure. Those rights, including the right to cure any default, continued until December 10, 1987, the time when plaintiff made a conclusive election to proceed by judicial foreclosure by instituting this action. Even under the 1985 amendment to Utah Code Ann. § 57-1-31, therefore, defen-

dants had a right to cure the default by paying the delinquent amounts at any time prior to the time plaintiff commenced its action to judicially foreclose the Trust Deed.

POINT IV

RIDGE ATHLETIC CLUB'S TENDER WAS ADEQUATE AS A MATTER OF LAW.

Plaintiff challenges the validity of the tender of Ridge Athletic Club made on December 7, 1987, on the ground that neither the Club nor Darrell Tanner had cash in hand or in an identifiable bank account on that date sufficient to pay the amounts tendered. The elements of a valid tender, however, are otherwise. The Club was not required to have cash in hand or in any bank, but rather was only required to "have the ability to produce it, and [to] act in good faith." Hymas v. Bamberger, 10 Utah 3, 36 P. 202, 203 (1894). The only evidence submitted to the court in this case established that the Club did have the ability to produce the tendered amount and did act in good faith.

Darrell Tanner unequivocally testified by affidavit that "on December 7, 1987, I had the ability to cause Ridge Athletic Club, Inc., to pay the sum of \$119,200.00 as indicated in the tender." (R. 382.) In response to plaintiff's attempts to challenge this statement, Darrell Tanner acknowledged that he did not have that amount of cash in hand. He also clearly testified, however, that he could have obtained it from his brother (Depo. of Darrell D. Tanner, p. 49, lines 10-11), from

credit lines available to him, (Id., lines 18-19), and by an advance on a loan that was in process with Citicorp. (Id. at p. 48, lines 21-25.)

There was no contrary evidence. Although the proceeds of the Citicorp loan were not actually disbursed to Darrell Tanner until December 31, 1987, that does not establish that the disbursement could not have occurred on December 7, 1987, had plaintiff accepted the tender, nor does it establish that Darrell Tanner could not have obtained an advance based on the pending loan application as he testified. There was further no evidence to contradict the testimony that Mr. Tanner's brother was willing and able to advance the funds. Although plaintiff's counsel may have doubted Mr. Tanner's ability to perform, as set forth in their objection to the tender, the doubts of counsel were not in evidence and would not have been admissible had counsel testified.

The only admissible evidence in the record on the subject of the tender establishes that Darrell Tanner had the ability to cause The Ridge Athletic Club, Inc. to perform as promised on December 7, 1987. If plaintiff had contrary evidence, it was required to produce it prior to the ruling on the Motion for Summary Judgment. Based on the record, this Court must hold, as a matter of law, that the tender was valid.

In the alternative, if this Court concludes that the tender is not valid as a matter of law, the case must be remanded for an evidentiary hearing. The testimony of Darrell Tanner at the

very least creates an issue of fact as to whether he had the ability to produce the money and tendered it in good faith.

POINT V

PLAINTIFF DID NOT HAVE A SECURITY INTEREST IN NEW EQUIPMENT OF OTHER PERSONAL PROPERTY ADDED BY TANNER OR THE RIDGE ATHLETIC CLUB, INC.

Plaintiff asserts that its security interest in after-acquired property operates to give it a security interest in personal property (including equipment) placed on the subject real property by Darrell D. Tanner ("Tanner") or The Ridge Athletic Club, Inc. ("Club"). This contention must fail because neither Tanner nor the Club signed a security agreement with plaintiff (the Club in addition did not sign a guaranty or any other document with plaintiff), and the personal property in question was not a replacement of the prior collateral.

Plaintiff relies on three cases: Inter Mountain Association of Credit Men v. Villager, Inc., 527 P.2d 664 (Utah 1974); Smiley v. Wheeler, 602 P.2d 209 (Okla. 1979); and American Heritage Bank & Trust Co. v. O. & E., Inc., 40 Colo. App. 306, 576 P.2d 566 (1978). Each is distinguishable because each case dealt with after-acquired property which was a replacement of the prior property, and the successor debtor was "related" to the original debtor. In Smiley, the creditor had a security interest in equipment, which the successor debtor later replaced with new equipment. 602 P.2d at 211. American Heritage concerned inventory, where the successor debtor mingled the prior inventory with new inventory. 576 P.2d at 567. Villager

also concerned inventory which essentially replaced prior inventory, and this was a major factor in the Court's decision. 527 P.2d at 669. The same logic would not apply to new equipment which was added not as a replacement of prior equipment, but in order to expand the size and quality of the Club.

Properly read, Villager supports the defendants' position in this case. The original debtor in that case merged with three other corporations. The successor corporation claimed its assets were not subject to the security agreement executed by the original debtor. The Court held the property transferred from the original debtor and its replacements subject to the after-acquired property clause of the security agreement. The creditor also claimed, however, that the after-acquired property clause operated to give it a security interest on all of the property acquired by the successor corporation, including that formerly owned by the other three former corporations. The Court rejected that claim, and held that the after-acquired property clause only affected the inventory of the original debtor and its replacements.

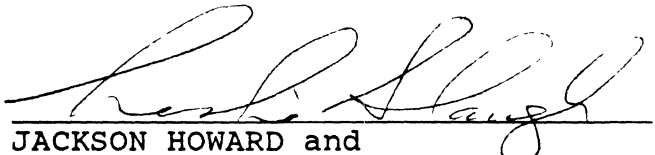
The personal property at issue in this case is predominately equipment added by the Club in connection with an expansion of the Club. In addition, the Club replaced existing equipment which was worn out when the Club purchased the property. This "new" equipment and other personal property is not subject to plaintiff's security interest. The Club has not signed any security agreement or financing statement with plaintiff.

Although the assets it purchased from Sherwood Associates are subject to plaintiff's security interest, the new personal property it later purchased is not subject to plaintiff's security interest. See Q. T., Inc. v. Thomas Russell & Co., Inc. (In re Q. T.), 99 Bankr. 310 (Bankr. E. D. Va. 1989).

CONCLUSION

The 1985 amendments to Utah Code Ann. § 57-1-31 cannot constitutionally be applied to this case. Defendants had a right to cure the default at the time that The Ridge Athletic Club, Inc., tendered payment of the deficiency. The tender was adequate as a matter of law. The case should be remanded with instructions to grant Tanner's Motion for Summary Judgment. In the alternative, the case should be remanded for an evidentiary hearing on the sufficiency of the tender.

DATED this 22nd day of January, 1990.

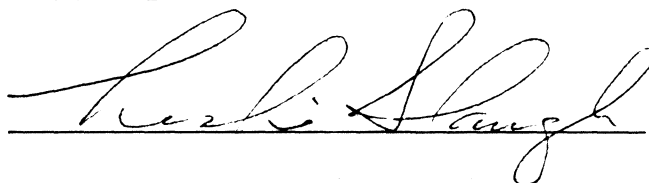
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MAILING CERTIFICATE

I hereby certify that four true and correct copies of the foregoing were mailed to the following, postage prepaid, this 22nd day of January, 1990.

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