1980

Stanley Martin Redd, Sheila M. Redd, His Wife; Sterling Hardson Redd, Jill D. Redd, His Wife; Paul Dutson And Donna Dutson, His Wife v. Western Savings & Loan Company : Brief of Appellants

Utah Supreme Court

IN THE SUPREME COURT OF THE STATE OF UTAH

STANLEY MARTIN REDD, SHEILA M. REDD, his wife; STERLING HARDSON REDD, JILL D. REDD, his wife; PAUL DUTSON and DONNA DUTSON, his wife,

Plaintiffs-Appellants,

vs.

WESTERN SAVINGS & LOAN COMPANY,

Defendant-Respondent.

Case No. ~~16549~~ 17231

BRIEF OF APPELLANTS

Appeal from Summary Judgment in favor of the Respondent by the Third Judicial District Court of Salt Lake County, Utah, the Honorable Kenneth Rigtrup, Judge, presiding.

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STATEMENT OF THE NATURE OF THE CASE

The Respondent, pursuant to "due on sale" provisions contained in a trust deed, but not in the promissory note itself, commenced non-judicial trust deed foreclosure proceedings against Appellants' real properties solely as a result of the contract sale of those properties by the Appellants who were the original borrowers. The purpose of the foreclosure proceedings was to permit the Respondent to obtain an increase in the interest rate payable under the trust deed note, as well as to obtain payment of prepayment or refinance charges. The Appellants, as a result, commenced this action for a declaratory judgment to determine that the Respondent had no right to foreclose its trust deed, for injunctive relief against those administrative foreclosure proceedings, and for damages. The Respondent filed its Motion to Dismiss alleging that the Appellants' complaint failed to state a cause of action against the Respondent.

DISPOSITION IN THE LOWER COURT

The Third District Court of the State of Utah, the Honorable Kenneth Rigtrup, presiding, after hearing arguments on Appellants' Motion for Preliminary Injunction and the Respondent's Motion to Dismiss, and after treating the Respondent's motion as a Motion for Summary Judgment, granted Summary Judgment in favor of the Respondent.

RELIEF SOUGHT ON APPEAL

The Appellants respectfully request that the Summary Judgment of the Third District Court be reversed and that this matter be remanded for trial on the issues.

STATEMENT OF FACTS

A. Preliminary Statement.

The issues in this case involve consideration and application of language in mortgages and trust deeds commonly referred to as a "due on sale" clause, which purports to permit a lender to accelerate the mortgage note to require immediate payment of all remaining indebtedness upon the sale, transfer or further encumbrance by the borrower of any of the borrower's interest in real property securing the loan. At the present time, application and scope of "due on sale" clauses are being widely litigated in state and federal courts; are the subject of numerous commentaries in legal periodicals as well as publications directed at the real estate and mortgage loan markets; and are the subject of concern by state and federal regulatory agencies.

The application and scope of "due on sale" clauses have a pervasive affect in both the real estate markets and the mortgage loan industries and, as an ultimate result, directly affect individual rights and ownership in real property. Thus, applicability of "due on sale" clauses has a broad social and economic impact on the ownership and transferability of real property, not only in Utah but nationwide.

The instant case is the result of a groundswell of current activity in Utah whereby many lenders have aggressively attempted to enforce the "due on sale" clauses commonly contained in most mortgages and trust deeds. While these important issues have been litigated in other jurisdictions, the instant case involves legal and equitable issues of first impression in Utah, which transcend the specific disputes between the parties hereto.

B. Facts of the Instant Case.

On or about November 18, 1976, the Appellants executed a Trust Deed Note in favor of the Respondent in the principal sum of $108,000.00 (R.33), and all payments to Respondent were current at the time the disputes, which are the subject of this action, arose (R.38, 40). This Trust Deed Note is secured by a Deed of Trust on a twenty-four (24) unit apartment building in Salt Lake County, Utah (R.22). The "boilerplate" language in the Trust Deed securing the obligation includes "due on sale" language purporting to permit the Respondent to accelerate the note and to require immediate payment of all remaining indebtedness, upon the sale, transfer

or encumbrance by the borrowers of any of their interest in the subject property. The applicable language is as follows:

> 29. Trustor agrees to notify the Beneficiary in writing should said property or any interest therein be conveyed, transferred or assigned, whether by deed, contract of sale, lease with option to buy or otherwise, and whether or not the instrument of conveyance, transfer or assignment be recorded. Should said property or any interest therein be so conveyed, transferred or assigned, whether or not Trustor gives written notice thereof, all indebtedness secured hereby shall forthwith, without notice, become due and payable at the election of Beneficiary, and in addition there shall be due and payable to the Beneficiary an amount equal to the prepayment fee due Beneficiary upon prepayment of the note according to the terms of the note and should Beneficiary not so elect and the person who acquires said property or any interest therein assumes the indebtedness evidenced by the note secured hereby, Trustor waives presentment, demand, protest and notice of nonpayment of said note, and consents to delays, changes in time of payment, and the amount of installments due under said note, and to the reduction or increase of the interest rate thereof.
>
> 30. Should Trustor further encumber said property, or any part thereof, or any interest therein, or agree so to do, without the written consent of Beneficiary being first obtained, Beneficiary shall have the right, at its option, to declare all sums secured hereby forthwith due and payable. Consent to one such encumbrance shall not be deemed to be a waiver of the right to require such consent to future or successive encumbrances. (Emphasis supplied) (R.25).

Concurrently with execution of the Trust Deed, the Appellants executed a separate document entitled "Acknowledgement of Trust Deed Acceleration Clauses," making reference to the paragraph numbers containing above-quoted "due-on-sale" language (R.31), which the Respondent, apparently as a regular matter of practice, requires borrowers to execute.

While, the trust deed note does not contain any similar language, the note does contain the following language imposing substantial costs in the event Appellants elect to prepay or to accelerate the note:

> The privilege is hereby granted to prepay the amount due on this note, in whole or in part, on any interest paying date by paying to the holder hereof, a premium in an amount equal to six (6) months interest on the then unpaid principal balance due hereunder (R.33).

The remaining principal balance, at the time the dispute arose was in excess of $104,000.00 (R.47); and interest on the note is 9-3/4% per annum (R.33). Under the terms of the note, therefore, the Appellants would have been required to pay a substantial penalty in excess of $5,000.00 to have the right to accelerate total payment.

On or about September 25, 1979, the Appellants entered into a contract for the sale of the subject property to third parties, while the Appellants retain fee title to the property (R.3, 41, 111). Under the terms of the contract, the Appellants continue to be obligors under the trust deed note, continue to make payments to the Respondent through an escrow account established for that purpose (R.38, 40), continue to receive payment for their equity in the property (R.41), and are required to convey title to the property only after full and timely payment by the purchasers of the purchase price (R.41).

Subsequent to execution of this contract, the Appellants have continued to pay to the Respondent all loan payments in a timely manner and the Respondent has not alleged any

default in payments (R.38, 39, 40, 42). The Respondent, nevertheless, has returned all tendered payments since the payment due for February 1980 (R.13, 38, 41). The Apppellants have made a continued tender of payments, with those payments presently being deposited in savings account number 01-177353-1 with the Respondent, and all rights to that account have been assigned to the Respondent (R.38, 40).

Solely on the basis of the Appellants' contract for sale of the subject property, and the Appellants' refusal to consent to the requested increase in the interest rate payable to the Respondent, as well as additional financing charges, the Respondent, on March 9, 1980, recorded a Notice of Default commencing non-judicial trust deed foreclosure proceedings on the subject property pursuant to the "due on sale" clause (R.65), which the Respondent contends creates an automatic right in the Respondent to demand acceleration of the trust deed note, declaring the entire balance due and payable (R.13, 29, 45, 46). The purpose of this attempted acceleration is to compel the re-execution of the trust deed note at a substantially higher rate of interest and the payment of additional refinancing charges.

The Appellants filed this action in response to the foreclosure proceedings praying for a declaratory judgment to interpret and determine the rights of the Respondent for a foreclosure of the subject property, for injunctive relief precluding the foreclosure, and for damages for wrongful foreclosure (R.2).

Not only has the Respondent never made any allegations of any default in payments, the Respondent has not alleged the existence of any facts or circumstances which create the likelihood of any future default in payments, damage or potential damage to the properties securing the loan, nor any other default by the Appellants (R.39, 40, 41). The Respondent bases its demand for acceleration solely upon the contract sale of the subject property (R.13) and the intention to require an increase in interest rate over and above the amount originally contracted for between the Appellants and the Respondent at the time the original trust deed note was negotiated and executed, together with other refinancing charges (R.29).

Based upon these transactions and the documentation involved herein, the Honorable Judge Kenneth Rigtrup, without hearing any other evidence (R.110), entered an Order of Summary Judgment (R.110) in favor of the Respondent holding that, in this case, the "due on sale" clause is not an unreasonable restraint on alienation, is not contrary to public policy of Utah, and is a legal, valid and enforceable contract provision which does not work a penalty or forfeiture (R.113). The effect of this judgment is to permit continuation of the pending non-judicial trust deed foreclosure, requiring acceleration of the entire remaining principal balance and the payment of additional fees. The Appellants urge that the effect of this

judgment, also, is to establish a dangerous precedent, recog nizing the right of a lender automatically to require renegoti ation of interest rates, and to obtain the benefit of refinan cing charges, upon the contract sale or other transfer of a interest in property, even though the promissory note itsel contains no language authorizing the acceleration and eve though substantial legal and equitable issues remain unconsid ered by the Courts of Utah.

ARGUMENT I

ENTRY OF SUMMARY JUDGMENT WAS NOT JUSTIFIED OR APPROPRIATE IN THIS CASE

The issues raised in this case involve important and substantial questions of law and equity impacting on the real estate and lending businesses throughout the State of Utah, and involve transactions identical to numerous other common real property transactions in the State of Utah. The Appellants contend that the issues raised in this case, being of substantial interest, concern and impact, require careful and thoughtful judicial consideration in order to lend clarity and guidance to the present uncertainty and concern.

Despite these major and substantive issues of law and equity involved in this case, and the implications involved for the mortgage loan and real estate markets and the transferability of real property by owners, the lower court in entering Summary Judgment held, as a matter of law, that there is no geniune issue as to any material fact in this matter precluding a determination in favor of the Respondent (R.113). The lower court, as a result, was in error, thus

establishing a wideranging precedent without the careful consideration which these significant and complex issues demand.

Clearly, entry of Summary Judgment is not appropriate unless there is no likelihood that any genuine issues of material facts may exist. Rule 56, Utah Rules of Civil Procedure; In re Williams Estates, 10 U.2d 83, 348 P.2d 683 (1960). Likewise, the substantial issues create significant justiciable issues. Holiday Acres No. 3 v. Midwest Fed. Sav. & Loan Ass'n of Minneapolis, 271 N.W. 2d 445 (Minn. 1978).

The parties raised, in their respective affidavits and memoranda submitted to the District Court, substantive and complex issues involving the nature of the transactions between the parties, the nature of the mortgage and lending businesses, and complex economic assumptions involving the secondary mortgage market and its alleged affect upon the mortgage loan industry. Supporting the Respondent's motion were self-serving affidavits and arguments which the lower court obviously accepted on their face. This has precluded discovery, admission of relevant evidence, and findings of fact and conclusions of law to lend certainty and guidance as to the law applicable in the State of Utah. Notwithstanding the determination by the lower court, there are at least the following material issues of fact and law which the Appellants should have the right to present for determination in this case:

1. The "due on sale" language, which is the core of the issues herein, purports to grant an automatic right to accelerate a loan in the event of a sale or transfer, but significantly grants the lender no specific right to increase interest rates, or to accelerate the loan to require an increase of interest rates, and the accompanying refinancing charges, in the event of such a transfer. At best, this clause, standing alone, is ambiguous and misleading to the borrower. It is further ambiguous when compared with the contradictory language of the trust deed note which exacts a substantial penalty in the event of early payoff (in this case, the prepayment penalty would be in excess of $5,000.00). The lower court's findings of fact, however, do not address this basic issue, i.e., the interpretation and scope of the note and trust deed language itself to determine the rights of the parties thereunder, although other courts have recognized the need first to examine the contract language. Silver v. Rochester Sav. Bank, 424 N.Y.S. 2d 945, 947-48 (1980); Nichols v. Ann Arbor Fed. Sav. & Loan Ass'n, 73 Mich. App. 163, 250 N.W.2d 804 (1977); Clark v. Lachemeier, 237 So.2d 583 (Fla. 1970).

2. Equally important, no evidence was presented nor examined by the lower court relative to the significant fact that the "due on sale" language is included only in the documents providing security for the note, but not in the promissory note itself. No evidence was presented to the lower court as to whether, in this case, the language should, therefore, be construed solely for the purpose of protecting the lender's security, and not as part of the agreement concerning interest rates.

3. No evidence was presented to the lower court concerning the circumstances surrounding the execution of the subject documents in order to determine the respective intentions and understandings of the parties at the time of execution.

4. The Respondent made numerous allegations and arguments regarding the requirement of a "due on sale" clause being necessary to preserve adequate secondary mortgage market funding, conclusions strongly disputed by the Appellants, and arguably without substance unless the Respondent can show evidence of any adverse affect on lending practices in the states where the courts have rejected the Respondent's arguments. No evidence was presented, nor examined, in the trial court, relative to that critical issue, although the findings of fact accept the Respondent's position as true on its face.

5. The Court heard no evidence concerning the nature or operation of the Respondent's practices, requirements and regulatory frameworks in the mortgage lending business nor, indeed, any other financial institution in the State of Utah or elsewhere. Notwithstanding this fact, the lower court apparently accepted, on their face, the Respondent's arguments as to the desirability of allowing mortgage lenders periodically to adjust portfolios to current market interest rates regardless of the specific interest rates previously negotiated.

6. No finding has ever been made by the Court regarding any different application, or emphasis, if any, of "due on sale" clauses in "commercial" vs. "residential" transactions and settings, a distinction raised by the Respondent before the lower court and obviously relied on by the lower court in its findings of fact (R.110).

7. Despite findings of the trial court that the "due on sale" clause, as worded in this case and as treated in this case, is not against public policy (R.113), no evidence was presented nor findings made as to the public policy considerations which should be examined by the Courts in this state and elsewhere.

8. Despite the finding of the trial court that the transactions in this case did not constitute unreasonable restraints on alienation (R.113), no evidence was presented as to whether or not such a "due on sale" clause in the first place constitutes a restraint on alienation and, if so, whether such a restraint is an unreasonable restraint. The treatment and analysis of this issue has been a central point of departure in cases resulting in opposite holdings, e.g. Occidential Sav. & Loan Ass'n v. Venco Partnership, 293 N.W.2d 843 (Neb. 1980), Wellenkamp v. Bank of America, 148 Cal. Rptr. 379, 582 P.2d 970 (1978).

9. Without specific evidence or findings justifying its conclusion, the lower court was in error in determining that the Respondent's actions did not constitute a penalty or forfeiture, but constituted valid transactions.

10. The Court did not determine or examine whether, under the Court's equitable powers, the foreclosure herein, even if allowed, should have been treated as a mortgage foreclosure, allowing a redemption period, rather than as a non-judicial trust deed foreclosure allowing no redemption after the initial ninety (90) day period, although the affect of Respondent's acceleration is to accelerate the total balance as a mortgage foreclosure action does.

11. No determination was made by the trial court as to the affect, from "due on sale" clauses, on mortgagors' anticipations and setting of rents, costs, charges, tax affects and other economic considerations in property transactions nor the extent to which lenders are in the better position to anticipate and protect themselves against future economic fluctuations.

12. No evidence of any nature, other than bare assertions by the Respondent, was offered to the lower court to show that unenforceability of "due on sale" clauses would have a materially adverse affect upon lenders and upon the mortgage market in the State of Utah.

13. No findings or determinations were made by the lower court as to whether a "due on sale" clause in a mortgage or trust deed is the appropriate or equitable vehicle to control interest rates and adjustments in the face of a changing economy.

14. Issues were raised, but unresolved, in the lower court relative to the supposed federal preemption of Utah real property law involving the "due on sale" clauses and the scope and nature of Sections 7-7-5.1 and 7-13-14, Utah Code Annotated (1953), as amended (R.19, 58, 112, 113). While the Findings of Fact state that the Appellants "misanalyze the scope and nature of" those sections (R.113), the lower

court failed to state or clarify the applicability of those statutes.

Given the fact that the issues in this case involve substantial and complex issues of law, equity, economics, lending practices, real estate ownership considerations, interpretation of commonly used mortgage and trust deed language, and public policy considerations, the failure of the lower court to allow the Appellants to present evidence involving these issues was clearly in error, and that court's judgment should be reversed and, at the very least, remanded for consideration of evidence to determine the interpretation and applicability of the language at issue in this case; the intentions of the parties at the time of execution of the loan documents; whether, even if applicable, the "due on sale" language is a restraint on alienation and, if so, whether it is an unreasonable restraint; whether "due on sale" language is automatically enforceable absent a showing of jeopardy to the lender; whether automatic application of the "due on sale" language is contrary to public policy; whether the applicable language constitutes a penalty or forfeiture; and whether legal or equitable circumstances exist in this case requiring separate treatment or application of the law.

ARGUMENT II

THE "DUE ON SALE" LANGUAGE APPLICABLE IN THIS CASE DOES NOT AUTOMATICALLY PERMIT THE INCREASE OF INTEREST RATE IN CONNECTION WITH A TRANSFER OR SALE OF THE SUBJECT PROPERTY

The lower court has made the determination that the language at issue in this case is enforceable under the circumstances of this case. Significantly, no substantive examination of the applicable language itself has been made by the Court.

It is significant to note that the promissory note itself, the primary instrument setting forth the respective rights and obligations of the parties, not only makes no reference to the right of the Respondent to increase interest rates under any circumstances through acceleration of payment, but in fact contains language providing for a "premium" (or, as Appellants urge, a penalty) in the event of prepayment (R.33), which language discourages acceleration by the borrower. If the Respondent's position is accepted, the Respondent, therefore, has the best of all worlds: the lender can, at its option accelerate the loan upon sale or transfer by the borrower of an interest in the property; but if the borrower desires to accelerate the loan, the borrower must pay a substantial penalty.

The "due on sale" language relied upon by the Respondent is language contained solely within a document intended to provide security for payment of the note, not in the note itself. More critically, the language relied on in the trust

deed does not authorize acceleration for purposes of increasing interest rates. The Appellants believe that the language itself is significant in that the parties, if the intention clearly to allow an increase in the interest rates or other alteration of the terms of the note, could easily have put that specific language in the note itself. Indeed, such specific language is not even included in the trust deed language at issue. Certainly, the reliance upon language in the security agreement which does not specifically authorize the actions complained of is inappropriate. At the very least, the Courts should examine the intentions and understandings of the parties at the time the loan papers were executed.

Courts have been divided on this issue, but decisions in other states have recognized problems when the language itself is imprecise. The New York Supreme Court, appellate division, cogently observed:

> At best, such a clause in the mortgage, standing alone, is ambiguous and misleading to the mortgagor. The normal inference to be drawn from it is that the lender is concerned about the security of the mortgage upon the transfer of ownership of the property. To construe it as granting to the lender an unlimited right to decline to accept the grantee for any reason, including the lender's refusal to consent to a change in the mortgage contract by increasing the rate of interest, is a giant step, which, as shown above, many states have, nevertheless, taken. Silver v. Rochester Sav. Bank, 424 N.Y.S. 2d 945, 947 (1980) See Nichols v. Ann Arbor Fed. Sav. & Loan, supra; Clark V. Lachemeier, supra

A student commentator, with simplicity and clarity stated:

> No doubt an argument can be made that a risk from which the lender should be protected is rising interest rates. The point is, however, that history

and custom indicate that consent has never been denied unless the transferee or purchaser was a bad credit risk or a change in the possessory interest would endanger the security interest. Moreover, public policy has heretofore always preferred the free alienability of property over that of the freedom of contract.

In circumspection, therefore, the enforcement of "due on sale" clauses should correspond with the expectations of the parties at the execution of the agreement. If the lender wants to extend control over the property so that the lending rate can be renegotiated, a clear statement of such intent should be evident. Otherwise, lenders should be held to traditional notions of what circumstances justify denial of consent, namely possession or assumption which jeopardizes the lender's security interest. (Footnotes omitted.), Note, "Mortgages - A Catalogue and Critique on the Role of Equity in the Enforcement of Modern Day 'Due-on-Sale' Clauses," 26 Ark.L.Rev. 485 (1973).

It is further significant that, where ambiguities exist in documents, the documents should be construed most strongly against the preparer of the documents (in this case, the Respondent). Smith v. Burton, 4 Utah 2d 61, 63 P.2d 806, 807 (1955).

It is respectfully suggested that the interpretation from the ambiguous language in the security document, which is the subject hereof, allowing automatic increase in interest rates is "a giant step" which should not be allowed for the hidden purpose of raising interest rates, without the Appellants being afforded the opportunity of the Courts at least examining the circumstances involved and the intentions of the parties at the time the loan transactions were consummated.

ARGUMENT III

UNDER UTAH LAW, A "DUE ON SALE" CLAUSE IS NOT AUTOMATICALLY ENFORCEABLE WITHOUT A SHOWING OF GOOD FAITH AND NECESSITY FOR PROTECTION OF THE LENDER

Assuming, ad arguendo, that the Respondent overcomes problems with the ambiguous language itself, the Utah Supreme Court has never been squarely faced with the specific issue as to whether a "due on sale" clause in a security document, which purportedly triggers acceleration of the loan, is automatically enforceable upon any contract sale without the requirement that the lender, in good-faith, determines that the prospect of payment or value of the security is impaired. The issue of the enforceability of "due on sale" clauses as a result of the sale or intended sale of properties is a much-litigated matter in the United States with the Courts being asked to resolve the conflict between contractual langauge, on one hand, and the common-law right to ownership and alienation of property, on the other hand.

In the past several years the authorities have been divided between cases holding "due on sale" clauses automatically enforceable, and cases holding them enforceable only upon the showing by the lender of some impairment or jeopardy to its security by virtue of the transfer.

The Appellants contend that the Utah Supreme Court, in light of previous Utah cases, will and should follow the rationale of the cases holding that a lender must demonstrate that its legitimate interests are threatened because of a contract sale by the borrower to whom the loan in question was

originally made, and also that the lender's attempted actions are equitable, in order to justify acceleration of the loan.

Under Utah law, the lender takes a mortgage (in this case, a Trust Deed) solely as security for payment of the debt:

> ... The main purpose of a mortgage is to ensure the payment of the debt for which it stands as security; and foreclosure is allowed when necessary to carry out that objective. . . The proceeding is one in equity in which principles of equity should be applied consistent with the above stated purpose; and neither the mortgage nor the foreclosure should be used as an instrument of oppression . . . United States v. Loosley, 551 P.2d 506, 508 (Utah 1976).

In State Bank of Lehi v. Woosley, 565 P.2d 413 (Utah 1977), the Utah Supreme Court affirmed a judgment of foreclosure, but only after the findings by the trial court showing that the debtors were $161,000.00 in default, were insolvent, and were unable to pay their debts; the debtors failed to care properly for the collateral; and a substantial amount of collateral was missing. Thus, the Court held that the debtors had not sustained their burden of proving lack of good faith on the lender's part. The Court, in that case, significantly reiterated the governing principal that acceleration and foreclosure are "harsh" remedies 565 P.2d at 418. The inescapable conclusion from a reading of this case, and the authorities cited by the Court in this case, is that under Utah law no acceleration or foreclosure can equitably be justified in the absence of the lender's good faith concerns as to its own jeopardy. The Appellants herein allege that the Respondent's actions are in violation of that equitable and reasonable standard.

A number of the courts, holding that a "due on sale" clause is not automatically enforceable, have based their decision in large part upon the recognition that the "due on sale" clause, in a very real sense, constitutes a restraint on alienation which often is an unreasonable restaint, e.g. Nichols v. Ann Arbor Fed. Sav. & Loan Ass'n, supra; Wellenkamp v. Bank of America, supra; Patton v. First Fed. Sav. & Loan Ass'n of Phoenix, 118 Ariz. 473, 578 P.2d 152 (1978); Sanders v. Hicks, 317 So.2d 61 (Miss. 1975); Tucker v. Lassen Sav. & Loan Ass'n, 116 Cal. Rptr. 633, 526 P.2d 1169 (1974); Tucker v. Pulaski Fed. Sav. & Loan Ass'n, 481 S.W. 2d 725 (Ark. 1972).

As the court in Tucker v. Lassen, supra, examining a "due on sale" clause in the context of a contract sale by the borrower stated:

> We conclude that the automatic enforcement of a "due-on" clause in instances where the trustor-obligor has entered into an installment land contract to sell the secured property would result in a restraint on alienation of very considerable proportions. In fact it is clear that such enforcement would operate to virtually eliminate alienation by installment land contract in all situations where the property to be conveyed was subject to a deed of trust and the obligation under the note remained substantial. From this standpoint the contrast between an outright sale and an executory sale by installment land contract is striking. In the former, as we pointed out in LaSala, the automatic application of the "due-on" clause results in little if any restraint on alienation because the terms of the second sale usually provide for full payment of the prior trust deed. In other words, the trustor-vendor normally receives enough money through the financing of the second sale to pay off his note, and he is normally required to do so. Little if any restraint on alienation results through enforcement of the provision.

> In the case of the installment land contract, however, the matter is otherwise. The trustor-vendor normally receives a relatively small down payment upon execution of the contract, the remainder of the purchase price to be paid through monthly installments. This down payment, like the proceeds of the junior encumbrance involved in LaSala, "does not often provide the borrower with the means to discharge the balance secured by the trust deed." The result is that a conveyance by means of an installment land contract would essentially be precluded in all cases wherein the balance due on the trustor-vendor's note was substantial if the "due-on" clause were to be given automatic effect. Accordingly, although the trustor-vendor might be willing to accept a rate of interest lower than that currently offered by institutional lenders, the prospective purchaser would be compelled to resort to such lenders to finance the acquisition of the property. The result in terms of a restraint on alienation is clear. 116 Cal. Rptr. at 638, 526 P.2d at 1174 (citations omitted).

It is significant to note that, although the California Supreme Court in the above case distinguished between restraints on alienation in contract sales and outright sales, the same court subsequently held that the "due on sale" clause also constitutes a restraint on alienation in outright sales of property. Wellenkamp v. Bank of America, supra.

The Arizona Supreme Court, describing language in a transaction which purported to exact an increase of 1/2% in interest rates and 1% transfer fee, classified the applicable clause as "a very harsh restraint on alienation." Patton, supra at 156. Query the description which the Patton court would have used for the substantially greater interest rate the Respondent desires in this case.

While other courts have refused to hold that a "due on sale" clause constitutes a restraint on alienation (i.e., Occidental Sav. & Loan Assn' v. Venco Partnership, supra), the Appellants urge that an examination of the affects of the "due on sale" clause on real property transactions in daily commerce demonstrate the "restraint" which such a clause imposes, for the reasons set forth in the above quote from Tucker v. Lassen, supra, as well as the practical restraints on the inability of a person to take any actions involving his property without prior consent of a lender. The difficulties of including a lender at all times in negotiations of terms of sale; inability to determine with any certainty whether a lender will or will not attempt to execise the "due on sale" clause; the continuing additional expenses and delays involved in obtaining lender approval; limitations on future ability to obtain financing; and problems of structuring the transactions for tax purposes.

It is clear that under the common law of Utah, any conditions restraining the right to alienation of property, when repugnant to the interest created, are void. See Page v. Page, 394 P.2d 612 (Utah 1964). In the absence of a showing of jeopardy to the Respondent, the threat of acceleration is, in an actual and practical sense, the epitome of a restraint on alienation. Whether the restraint is reasonable is an issue of fact and the province of equity.

The California Supreme Court, through a series of cases, has had considerable opportunity to examine the issues, principles of law and equity, and economic and public policy considerations in "due on sale" clauses. The series of California cases originated in a State having considerable commercial experience and background; the courts of that state have been faced with numerous issues involving the "due on sale" clause; the law of California in this matter has evolved through careful consideration of a series of case and fact issues; the issues before this Court have been presented fully to the California courts; and the cases have been vigorously disputed and litigated.

One of the best-reasoned, and certainly one of the most-cited, cases on point is the Wellenkamp case. The California Supreme Court held that:

> . . . a due-on clause contained in a promissory note or deed of trust cannot be enforced upon the occurrence of an outright sale unless the lender can demonstrate that enforcement is reasonably necessary to protect against impairment to its security or the risk of default. 582 P.2d at 976-977 (citations omitted)

In this case before this Court, the Appellants, unlike the situation in Wellenkamp, have not conveyed fee title but, rather, retain an interest in the property until full payment is made. Hence, the Appellants' case herein is even considerably stronger than Wellenkamp.

Since Wellenkamp articulates especially well the principles of equity governing the conflicting interests of lender and borrower, it is instructive to examine Wellenkamp'

rationale in some depth (this case going even beyond the facts in the instant case):

> Defendant contends that the risk of waste and default is significant in an outright sale because both possession and legal title to the property are transferred, thereby eliminating any incentive or aoility that the seller/trustor would have to avoid realization of these risks by action of the buyer. Although we have previously distinguished on this basis both the junior encumbrance, where neither possession nor legal title was transferred (La Sala) and the installment land contract, where possession but not legal title was tranferred (Tucker), we are now convinced that, although the original borrower/seller no longer retains an interest in the property after transfer of legal title in an outright sale involving no secondary financing by the seller, this fact does not necessarily increase the risk to the lender that waste or default will occur. Thus the buyer in an outright sale, in order to pay off the seller's equity, may make a large down payment on the property, thereby creating an equity interest in the property in him which is sufficient to provide an adequate incentive not to commit waste or permit the property to depreciate. Moreover, the buyer in such an outright sale may be at least as good, if not a better credit risk than the original borrower-seller. We therefore conclude that although circumstances may arise in which the interest of the lender may justify the enforcement of a due-on clause in the event of an outright sale, the mere fact of sale is not in itself sufficient to warrant enforcement of the clause, and the restraint on alienation resulting therefrom, in the absence of a showing by the lender that such circumstances exist. 582 P.2d at 975-76 (citations omitted) (Emphasis added)

Numerous other recent cases in various jurisdictions hold that no automatic right of acceleration exists in the absence of a showing that acceleration is justified to protect the legitimate interests of the lender, e.g. Patton v. First Fed. Sav. & Loan Ass'n of Phoenix, supra; Continental Fed. Sav. & Loan Ass'n v. Fetter, 564 P.2d 1013 (Okla. 1977); Nichols v. Ann Arbor Fed. Sav. & Loan Ass'n, supra; Sanders v. Hicks, supra; Tucker v. Lassen Sav. & Loan Ass'n, supra;

Tucker v. Pulaski Fed. Sav. & Loan Ass'n, supra; Home Fed. Sav. & Loan Ass'n of Palm Beach v. English, 249 So. 2d 707 (Fla. App. 1971); Clark v. Lachemeier, supra.

Perhaps the most direct example of the differences i the cases considering application on the "due on sale" clause is the comparison of the Wellenkamp rationale and reasonin with the decision in Occidental, supra, and strongly relied o by the Respondent in the lower court. The Occidental cas refused to accept much of the Wellenkamp reasoning and hel that a "due on sale" clause does not constitute an unreasonabl restraint on alienation and permitted acceleration of the not in that case. It is significant to note, however, in th Occidental case that:

1. Even that court held "that a 'due on sale clause in an otherwise valid mortgage is enforceable absent pleading and proof by the mortgagor that suc enforcement would be inequitable" 943 N.W.2d at 8 (Emphasis supplied). That court further acknowledge that a "due on sale" clause "should be subject to th same rules as other acceleration clauses, includi the protection of equitable defenses" 293 N.W.2d a 849. The Appellants in the instant case have bee precluded from offering such evidence.

2. Occidental significantly justifies part o its reasoning by noting that the note and mortgage i that case contained no prepayment penalty. 293 N.W.

at 848. In the instant case, the note contains a substantial prepayment penalty (R.33).

3. Occidental recognizes the court's continuing powers in this case to consider and fashion equitable defenses and relief. 293 N.W.2d at 849.

4. It is informative to note that the Occidental case, unlike the instant case, arose in the context of (a) unimproved land which would require subsequent financing for construction of improvements thereon; and (b) the seller-mortgagor did not even appear to dispute foreclosure, and his default was entered. 293 N.W.2d at 848.

In holding that a "due on sale" clause does not constitute a restraint on alienation, Occidental relied, to a considerable degree, upon the definition contained in the Restatement of Property and, therefore, did not go behind that definition to look at the practical affect of the "due on sale" language. The Michigan Supreme Court, in Nichols v. Ann Arbor Fed. Sav. & Loan Ass'n, supra, presented with the same argument, and after giving a practical and considered examination of that type of language, significantly stated:

> If the mortgage clause defendant seeks to enforce can be labeled a restraint on alienation only by expanding the restatement definition, we do not hesitate to stretch the term to include this "due-on-sale" clause. "[I]t would appear that the due-on-sale clause is so closely akin to the promissory restraint as to justify designating it a direct restraint." 250 N.W.2d at 806 (citation omitted).

It should be noted that Occidental contains an appendix to the majority opinion containing a valuable and thorough summary of cases and articles on the subject of "due on sale clauses.

ARGUMENT IV

INCREASE OF INTEREST RATES ALONE IS NOT JUSTIFICATION FOR ACCELERATION THROUGH THE "DUE ON SALE" CLAUSE

The Respondent, as further justification for its attempted actions, made various arguments before the lower court regarding the commercial benefits to the lending institutions. One would think, by reading these arguments, that the Respondent is really not motivated by a desire to exact extra profits at the expense of the borrowers. Rather, the impression is that the primary motive for exacting additional interest rates is to benefit the borrowing public by setting "fair and reasonable interest rates" and by preserving the secondary mortgage market. While these issues are ultimately relevant to the trial court's considerations, the Appellants suggest that the trial court should consider with healthy scepticism these professed humanitarian motives and the fear that the equitable decision will bring the mortgage loan industry to its knees. Indeed, no showing (or, indeed, allegation) has been made that financial chaos has fallen upon the states who have rejected the Respondent's position. At the very least, the Appellants are entitled to present this issue to the trial court, but they were denied this opportunity in

this case. Without belaboring this argument, it is sufficient to note that these arguments were rejected by the California Supreme Court in perceptive analysis in three cases:

> In any event, a restraint on alienation cannot be found reasonable merely because it is commercially beneficial to the restrainor. Otherwise one could justify any restraint on alienation upon the ground that the lender could exact a valuable consideration in return for its waiver, and that sensible lenders find such devices profitable. LaSala v. American Sav. & Loan Ass'n, 97 Cal. Rptr. 849, 881, 489 P.2d, 1113, 1124, n. 17 (1971).

> We reject the suggestion that a lender's interest in maintaining its portfolio at current interest rates justifies the restraint imposed by the exercise of a "due-on" clause upon the execution of an installment land contract. Whatever cogency this argument may retain concerning the relatively mild restraint involved in the case of an outright sale (a matter to which we do not now address ourselves), it lacks all force in the case of the serious and extreme restraint which would result from the automatic enforcement of "due-on" clauses in the context of installment land contracts. Tucker v. Lassen Sav. & Loan Ass'n ,supra at 1775-1176, n. 10. (citations omitted)

> We furthermore reject Defendant's contention that the lender's interest in maintaining its loan portfolio at current interest rates justifies the restraint imposed by exercise of a due-on clause upon transfer of title in an outright sale. Although we recognize that lenders face increasing costs of doing business and must pay increasing amounts to depositors for the use of their funds in making long-term real estate loans as a result of inflation and a competitive money market, we believe that exercise of the due-on clause to protect against this kind of business risk would not further the purpose for which the due-on clause was legitimately designed, namely to protect against impairment to the lender's security that is shown to result from a transfer of title. Economic risks such as those caused by an inflationary economy are among the general risks inherent in every lending transaction. They are neither unforeseeable or unforeseen. Lenders who provide funds for longterm real estate loans should and do, as a matter of business necessity, take into

> account their projections of future economic conditions when they initially determine the rate of payment and the interest on these long-term loans. Unfortunately, these projections occasionally prove to be inaccurate. We believe, however, that it would be unjust to place the burden of the lender's mistaken economic projections on property owners exercising their right to freely alienate their property through the automatic enforcement of a due-on clause by the lender. Wellenkamp, supra at 976 (citations omitted) (emphasis added)

ARGUMENT V
APPLICATION OF LAWS OF UTAH AT ISSUE ARE NOT SUPERSEDED OR PREEMPTED BY FEDERAL REGULATION

In an apparent attempt to avoid a head-on analysis and application of Utah real property law, the Respondent argued in the lower court that the Respondent can nevertheless accelerate the loan by virtue of the existence of a federal regulation allowing "due-on" language to be used in trust deed by federal savings and loan associations (R.19-20). With real imagination, the Respondent (a state chartered savings and loan) relied upon Sections 7-7-5.1 and 7-13-14, Utah Code Annotated (1953), as amended, in an attempt to argue "pass through" of a federal regulation affecting federally chartered savings and loans. The Court's Findings of Fact refer to this dispute but do not address the issue itself to clarify the interpretation, applicability or scope of these statutes. Rather, the lower court simply stated, without elaboration, that the Appellants have "misananalzed" the scope and nature of those statutes (R.113).

The Respondent's reliance, in the lower court, on the issued of federal preemption, fails for at least five (5) reasons:

1. Determination of rights to real property has traditionally been left to the states. See La. Power & Light Co. v. City of Thibodaux, 360 U.S. 25 (1959); Kaiser Steel Corp. v. W. S. Ranch Co., 391 U.S. 583 (1968).

2. The Respondent, as a state-chartered savings and loan is subject to state regulations and interpretation of its powers, including the interpretation of the scope and application of state statutory authority.

3. It is the Utah Courts which interpret the scope of the Respondent's rights in real property and the intention of the legislature in passing the statutes relied upon (query whether the Utah legislature intended to subordinate its regulation of state chartered financial institutions and real property law to all present and future regulations adopted by the federal bureaucracy).

4. The Respondent by contract agreed that the laws of Utah would govern the interpretation and application of the trust deed.

5. Even if, ad arguendum, federal regulations are applicable to allow due-on-sale clauses in trust deeds, federal law does not determine or dictate the states' application of laws affecting real property.

The United States District Court for the Middle District of Florida, in the recent case of Kirkland v. Fidelity Fed. Sav. & Loan Ass'n of Jacksonville (May 16, 1980), articulated the appropriate relationship between the federal regulations and the state control of real property law in response to arguments of federal preemption, a stronger issue even than those arguments arised by the Respondent:

> Defendants argue that federal regulation has totally preempted the law in this case and that the court must look solely to federal law and regulations as it does, for example, in the area of labor law. Defendant's contention would be correct if Plaintiffs were challenging the validity or interpretation of the federal regulations. Further, if the state were attempting to place additional regulations on a federally chartered savings and loan, it would be precluded from doing so by federal preemption. . . .
>
> However, Plaintiffs in this case raise an entirely different question. They do not challenge the validity of the "due on sale" clause nor request an interpretation of the federal regulation. Nor is this a case in which the state is attempting to regulate the practices of a federal association. Plaintiffs instead ask only for an interpretation of the mortgage contract. They raise questions governed by contract and real property law. The law of real estate mortgage has not been totally preempted by federal law even though the mortgage is issued by a federally chartered lending institution. In fact, most mortgage foreclosures are appropriately brought in state courts, and even when brought in federal court generally are governed by state law.
>
> Even though federal law has not preempted the entire field, in light of the almost verbatim adoption of the federal regulation as a provision of the contract, it is possible that state law on this particular point may have been preempted by implication. Though federal preemption may sometimes be implied, the implication should be accepted only where the intention is clearly manifest. This is particularly true in the area of rights to real property which traditionally has been left to the states.

No such congressional, or even regulatory, intent is manifest in this case. The regulation permitting the clause in question was prompted by a desire to protect the federal association's interest in the property and should be construed with that in mind. Given the predominance of state law in the field of real property, this goal can only be reached by construing the clause under the state law. The effect of a "wraparound" mortgage may vary from state to state. Therefore, its effect on the lender's interest in the property may also vary among states. Thus, in one state the right to call a mortgage due upon exercise of a subsequent wrap-around mortgage may be necessary to protect the association's interest in the property, while under the laws of another state the interests of the parties may be so defined as to make such a right unnecessary. Therefore, paragraph 17 will and should be construed differently under the laws of the various states.

Further, the document itself reflects an understanding between the parties that the case be governed by state law. Paragraph 15 reads, "This mortgage shall be governed by the law of the jurisdiction in which the property is located." Even if this were not the case, the court would almost be forced to look to state law. There is no federal law governing the interpretation of mortgages. Defendant's position would require the court to fashion an entire body of federal law to govern real estate mortgages, which the court is unwilling to undertake without explicit congressional direction. The mere delegation of rule-making authority does not constitute such direction. pp. 2-5 (citations omitted) (emphasis added)

ARGUMENT VI

EVEN IF FORECLOSURE WERE PERMITTED, THE FORECLOSURE SHOULD BE CONSTRUED AS A MORTGAGE FORECLOSURE PERMITTING A REDEMPTION PERIOD

By reliance upon ambigous language in the trust deed, the Respondent has attempted to require the entire principal balance under the loan payable, while, at the same time, precluding the normal six (6) month redemption period which normally would be involved under a mortgage for the protection of

the borrower after the additional period of time required to obtain a judgment permitting foreclosure.

Under the Laws of Utah, the trust deed foreclosure provides for the non-judicial foreclosure of property by the lender, with the provision that the redemption period terminates after three (3) months from the initial recording of a notice of default. 57-1-28(2), Utah Code Annotated (1953), as amended. On the other hand, a Court supervised mortgage foreclosure proceeding allows the lender a six (6) month redemption period from and after the period of time required to obtain a judgment of foreclosure. 78-37-8, Utah Code Annotated (1953), as amended; Rule 69(f), Utah Rules of Civil Procedure. The policy behind the two approaches is clear. It is presumed that the non-judicial trust deed foreclosure is normally not as harsh a remedy, requiring a redemption period, because a borrower, in order to stop the proceedings, can simply tender the delinquent payments with the attendant costs, and reestablish the obligation in full force. 57-1-31, Utah Code Annotated (1953), as amended. A mortgage, on the other hand, allows a lender to require the entire principal amount due and payable but, as a protection to the borrower, allows a six (6) month redemption period.

The net effect of the Respondent's interpretation and application of the "due on sale" clause is to require the entire principal amount to be due and payable, as in a mortgage, but without the attendant protection to the borrower of the time for redemption.

Clearly, this Court has the power to interpret the nature and proceedings of real property transactions, and to apply the remedies, in an equitable manner for the protection of all parties. This Court, has on numerous occasions, recognized various equitable powers of the court to construe real property transactions to prevent injustice to persons having interests in the real property. e.g., Rodgers v. Hansen, 580 P.2d 233 (Utah 1978) (construction of Uniform Real Estate transactions as an equitable mortgage); Johnson v. Carman, 572 P.2d 371 (Utah 1977)(determination that forfeiture provision in contract was inequitable and unenforceable); Nagle v. Club Fontainbleu, 17 Utah 2d 125, 405 P.2d 346 (1965) (note allowing forfeiture construed as a mortgage); Bybee v. Stuart, 112 Utah 462, 189 P.2d 118 (1948)(warranty deed construed as a security document).

Under the circumstances of this case, the Appellants urge that, at the very least, if foreclosure proceedings are permitted which require the complete payment of all accrued principal, such an action in effect constitutes a mortgage foreclosure action with the Appellants retaining their six (6) month redemption period after court order allowing foreclosure. Any other approach would clearly be inequitable allowing the lenders, as a result of a contract sale, transfer or encumbrance, to circumvent the protection of the mortgage foreclosure laws, an action which clearly is contrary to public policy.

CONCLUSION

The issues raised by the Appellants involve substantial issues of fact and law which affect a wide range of commercial transactions within the State of Utah and should be examined and determined by the Court to allow understanding and certainty by the various parties involved.

The lower court was in error in entering a Summary Judgment without consideration of these facts and legal issues and should be reversed.

Respectfully submitted,

NEIL R. SABIN
Attorney for Appellants

CERTIFICATE OF SERVICE

I hereby certify that on the 6th day of October, 1980, I served two (2) copies of the attached Brief of Appellants on Richard W. Giauque and James R. Holbrook, of Berman & Giauque, 500 Kearns Building, Salt Lake City, UT 84101, attorneys for Respondent, by hand delivering two (2) copies thereof.