1983

Continental Bank & Trust v. A Corporation, F. A. Badger, Adrienne Badger, John N. Busk, Patricia C. Busk, H. Mervin Wallace, Virginia S. Wallace, Robert M. Wallace And Carolyn M. Wallace : Brief of Respondent

IN THE SUPREME COURT

OF THE STATE OF UTAH

CONTINENTAL BANK & TRUST, a corporation, Plaintiff-Respondent, v. UTAH SECURITY MORTGAGE, INC., a corporation, F. A. BADGER, ADRIENNE BADGER, JOHN N. BUSK, PATRICIA C. BUSK, H. MERVIN WALLACE, VIRGINIA S. WALLACE, ROBERT M. WALLACE AND CAROLYN M. WALLACE, Defendants-Appellants.	)	Supreme Court No. 19086

BRIEF OF RESPONDENT

ALBERT J. COLTON
RANDALL A. MACKEY
FABIAN & CLENDENIN,
A Professional Corporation
800 Continental Bank Building
Salt Lake City, Utah 84101

Attorneys for Plaintiff-Respondent

JAMES R. BROWN
JARDINE, LINEBAUGH, BROWN & DUNN
370 East South Temple, Suite 401
Salt Lake City, Utah 84111

Attorneys for Defendants-Appellants

RONALD C. BARKER
2870 South State Street
Salt Lake City, Utah 84111

Attorney for Defendant-Appellant
Adrienne Badger

IN THE SUPREME COURT

OF THE STATE OF UTAH

CONTINENTAL BANK & TRUST, a corporation, Plaintiff-Respondent, v. UTAH SECURITY MORTGAGE, INC., a corporation, F. A. BADGER, ADRIENNE BADGER, JOHN N. BUSK, PATRICIA C. BUSK, H. MERVIN WALLACE, VIRGINIA S. WALLACE, ROBERT M. WALLACE AND CAROLYN M. WALLACE, Defendants-Appellants.	)	Supreme Court No. 19086

BRIEF OF RESPONDENT

ALBERT J. COLTON
RANDALL A. MACKEY
FABIAN & CLENDENIN,
A Professional Corporation
800 Continental Bank Building
Salt Lake City, Utah 84101

Attorneys for Plaintiff-Respondent

JAMES R. BROWN
JARDINE, LINEBAUGH, BROWN & DUNN
370 East South Temple, Suite 401
Salt Lake City, Utah 84111

Attorneys for Defendants-Appellants

RONALD C. BARKER
2870 South State Street
Salt Lake City, Utah 84111

Attorney for Defendant-Appellant
Adrienne Badger

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES

TREATISES

IN THE SUPREME COURT

OF THE STATE OF UTAH

CONTINENTAL BANK & TRUST, a corporation, Plaintiff-Respondent, v. UTAH SECURITY MORTGAGE, INC., a corporation, F. A. BADGER, ADRIENNE BADGER, JOHN N. BUSK, PATRICIA C. BUSK, H. MERVIN WALLACE, VIRGINIA S. WALLACE, ROBERT M. WALLACE AND CAROLYN M. WALLACE, Defendants-Appellants.	)	BRIEF OF RESPONDENT Supreme Court No. 19086

Plaintiff and respondent Continental Bank and Trust Company (hereinafter the "Respondent") by and through its attorneys Fabian & Clendenin, submit the following brief in response to the brief on appeal of defendants and appellants.

STATEMENT OF THE CASE

Respondent seeks to enforce the liability of individual defendants and appellants John N. Busk, Patricia C. Busk, H. Mervin Wallace, Virginia S. Wallace, Robert M. Wallace and Carolyn M. Wallace (hereinafter the "Appellants") as guarantors for three promissory notes.

DISPOSITION OF CASE IN LOWER COURT

On December 13, 1982, Judge Fishler of the Third District Court for Salt Lake County, State of Utah, granted Respondent's

motion for summary judgment in an action arising out of a defa[ult] three promissory notes. A judgment was later entered on Februar[y] 22, 1983, finding Appellants liable in the amount of $101,605.7[8] plus interest and attorneys' fees.

STATEMENT OF FACTS

Appellants' statement of facts contains several important omissions and misstatements which must be addressed in order to assure a proper understanding of the issues involved. Thus, a br[ief] recitation of the facts is in order.

Respondent commenced this action in the court below to recover the unpaid balances on three promissory notes that totaled $87,745.42 that were executed by F. Alonzo Badger on behalf of Utah Security Mortgage, Inc., of which he was the President. The unpaid notes covered three separate loans made to Utah Security Mortgage, Inc. (R. 76-79). In making these loans to Utah Security Mortgage, Inc., Respondent relied upon a Corporate Resolution Authorizing Borrowings that was executed on June 28, 1977, authorizing Mr. Badger to borrow money on behalf of Utah Security Mortgage, Inc. (R. 205-06).[1/]

1/ The Corporate Resolution Authorizing Borrowings was a standard form that Respondent required all corporations to execute before they are lent money; it was signed by Dee F. Murphy, the Vice President of Utah Security Mortgage, Inc. and provided that at a Board of Directors meeting held on June 28, 1977 a resolution was adopted authorizing the following:

> [T]hat [Utah Security Mortgage, Inc.] borrow money from time to time from [Continental Bank] in such amounts as may be deemed necessary for the use of [Utah Security Mortgage, Inc.] by the officers herein authorized and empowered to execute and deliver the obligation or obligations of [Utah Security Mortgage, Inc.

(Footnote continued on next page)

The unpaid notes were executed by Utah Security Mortgage, as part of an arrangement with Respondent for warehousing assignments of trust deeds as security for a line of credit -- a practice that is common in the banking industry. (R. 338-39, 448-49, 464). Under this arrangement Respondent made loans to Utah Security Mortgage, Inc. in order to finance mortgage loans that Utah Security Mortgage, Inc. had made to certain borrowers for the purchase of real property. The mortgage loans made by Utah Security Mortgage, Inc. were secured by trust deeds from the borrowers. (R. 338-398, 464). The trust deeds were then assigned to Respondent by Utah Security Mortgage, Inc. as collateral until Utah Security Mortgage, Inc. sold the trust deeds in the secondary market to either the Utah Housing Finance Agency, the Federal National Mortgage Association, or other entities in the business of purchasing trust deeds. When a trust deed was sold in the secondary market, Utah Security Mortgage, Inc. would use the money to repay its loans from Respondent. (R. 345-46, 349, 358).

Respondent did not perfect its security interest in the assignments of the trust deeds, because to do so would have restricted the subsequent sale of the trust deeds in the secondary

---

(Footnote continued from previous page)

> and that F. Alonzo Badger, President [is] hereby authorized and empowered to execute and deliver in the name of [Utah Security Mortgage, Inc.], and under or without its corporate sela, its promissory note or notes therefor to [Respondent] for all such sums so borrowed.

205-06). A similar Corporate Resolution Authorizing Borrowings was executed on behalf of Utah Security Mortgage, Inc. on February 1978, by its president, F. Alonzo Badger. (R. 207-08).

market.[2] (R. 142, 166-70). In order to obtain additional security for the notes, and as a condition for extending the line of credit to Utah Security Mortgage, Inc., Respondent required Appellants to execute guaranties on June 29, 1977, February 2, 1978 and May 5, 1978. (R. 174-76).

The guaranty of May 5, 1978 is the one relied upon by Respondent in bringing this action. It covered all debts extended to Utah Security Mortgage, Inc. by Respondent up to $350,000, and contained the following provision:

> [Respondent] shall not be required to proceed first against [Utah Security Mortgage, Inc.] or any other person, firm or corporation or against any collateral security held by it before resorting to the Guarantor[s] for payment; and the liability of the Guarantor[s] shall not be affected, released or exonerated by release or surrender of any security held for the payment of any of the debts hereinabove mentioned. (Emphasis supplied.)

(R. 176).

In accordance with the warehousing arrangement between Utah Security Mortgage, Inc. and Respondent, the three unpaid promissory notes were secured by the assignments of four trust deeds. These trust deeds were sold in the secondary market to the Utah Housing Finance Agency in August of 1979. The proceeds of the sale, which under the warehousing arrangement were to go from the buyer to Respondent, instead went from the buyer to Utah Security Mortgage Inc. The proceeds were never paid over to Respondent by Utah

---

[2] For example, the Utah Housing Finance Agency, to which Utah Security Mortgage, Inc. sold many of its trust deeds, issued regulations that prohibit the agency's purchase of any trust deeds which are subject to an existing assignment. (R. 142, 167-173).

Security Mortgage, Inc. despite the repeated requests for payment by Respondent made to Mr. Badger.

It was later learned that these proceeds were embezzled by Mr. Badger who used them to invest in Bonneville Thrift and Loan Company ("Bonneville Thrift"). (R. 479-81). In addition to his position with Utah Security Mortgage, Inc., Mr. Badger was the President of Bonneville Thrift. Appellants H. Mervin Wallace and Robert M. Wallace were at that time directors of both Bonneville Thrift and Utah Security Mortgage, Inc. Bonneville Thrift had been notified by the Commissioner of Financial Institutions (the "Commissioner") that its capital was impaired, and that it would not be permitted to continue its operations unless it received $100,000 in additional capital.

When Respondent learned of the embezzlement, its Vice President and loan officer, Lohr S. Livingston, arranged a meeting with Mr. Badger and H. Mervin Wallace to discuss the three unpaid notes. The meeting took place on or about November 30, 1979 in Respondent's main office. (R. 479). At the meeting, Mr. Badger admitted he had wrongfully taken the money that was supposed to be paid to Respondent. Mr. Wallace offered to pledge 52,170 shares of stock in Bonneville Thrift as security on the notes. The offer was then accepted by Respondent. (R. 479-80).

On May 23, 1980, the Commissioner took possession of Bonneville Thrift. Six days later, on May 29, 1980, James R. Brown, counsel for Appellants, sent a letter to Glen E. Clark, then counsel for Respondent, requesting that Respondent sell the shares of Bonneville Thrift stock that it held, with the proceeds from the

sale to be applied towards the unpaid balances on the promissory notes. (R. 80). Since receiving Mr. Brown's letter, Respondent has at all times been willing to sell the stock, but it has never been contacted by anyone interested in purchasing any of the stock. Because the Commissioner had taken possession of Bonneville Thrift, any purchase of its stock or assets would have to be negotiated with, and approved by, the Commissioner.[3/]

Respondent is still holding 52,170 shares of Bonneville Thrift stock that are worthless. The three promissory notes executed by F. A. Badger for Utah Security Mortgage, Inc. remain unpaid. Relying upon the continuing guaranty signed by all of the individual defendants on May 5, 1978, Respondent brought an action in the Third District Court, State of Utah, against Appellants to recover the unpaid balances on the notes. On December 13, 1982, Judge Fishler granted Respondent's motion for summary judgment.

[3/] After the Commissioner took over Bonneville Thrift on May 23, 1980, Citizens Bankshares was then required to deal directly with the Commissioner in purchasing any assets of Bonneville Thrift. On July 8, 1980, Michael R. Carlston, counsel for Citizens Bankshares, submitted a written proposal on its behalf to the Commissioner proposing the purchase of certain assets of Bonneville Thrift. (R. 84-86). An agreement between Citizens Bankshares and the Commissioner was signed on August 18, 1980 in which Citizens Bankshares acquired some of the assets of Bonneville Thrift. (R. 87-90). At no time, however, did Citizens Bankshares ever make an offer to purchase any of the stock in Bonneville Thrift, including the stock pledged to Respondent. (R. 99-100).

ARGUMENT

APPELLANTS WAIVED THEIR RIGHTS TO THE COLLATERAL UNDER THE EXPRESS TERMS OF THE GUARANTY AGREEMENT.

Appellants cite several cases -- including Shaffer v. Davidson, 445 P.2d 13, 5 UCC Rep. 772 (Wyo. 1968) -- for the proposition that Appellants have been discharged from their contractual obligations under the guaranty agreement by virtue of Respondent's alleged failure to prevent impairment of both types of collateral -- the assignments of trust deeds and the Bonneville Thrift stock. In so arguing, Appellants overlook the fact deemed decisive by the court below in granting Respondent's motion for summary judgment -- that by the express terms of the guaranty agreement, Appellants consented to any such impairment of the collateral.

Section 3-606(1)(b) of the Uniform Commercial Code, Utah Code Annotated § 70A-3-606, provides:

> The holder discharges any party to the instrument to the extend that without such party's consent the holder . . . unjustifiably impairs any collateral for the instrument given by or on behalf of the party or any person against whom he has a right of recourse. (Emphasis supplied).

The statute, by expressly conditioning discharge by impairment of collateral on the lack of consent of the party seeking discharge, plainly contemplates that a party may waive his impairment defense. This principle is underscored by Comment 2 to § 3-606, which contemplates that such a waiver may be granted by contract:

> Consent may be given in advance, and is commonly incorporated in the instrument; or it may be given afterward. It requires no consideration and operates as a waiver of the consenting party's right to claim his own discharge. (Emphasis supplied).

2 White and Summers, Uniform Commercial Code, 2nd ed. at p. 527.

The guaranty agreement between Respondent and Appellants contains the type of consent envisioned by the draftsmen of the Uniform Commercial Code. The agreement provides:

> . . . the said Bank shall not be required to proceed first against the Debtor or any other person, firm or corporation or against any collateral security held by it before resorting to the Guarantor for payment; and the liability of the Guarantor shall not be affected, released or exonerated by release or surrender of any security held for the payment of any of the debts hereinbefore mentioned, nor by the release of any other guarantor or surety.

(R. 176). By agreeing to be liable as guarantors notwithstanding any "release or surrender" of the collateral, Appellants waived any rights to claim discharge by virtue of impairment of the collateral, whether by Respondent's alleged failure to perfect a security interest in the trust deeds, or by Respondent's allegedly negligent failure to sell the shares of Bonneville Thrift.

A. <u>The Guaranty Agreement Expressly Provided that Respondent had No Duty to Perfect a Security Interest in the Trust Deeds</u>.

Appellants, by waiving their rights to discharge resulting from a "release or surrender" of the collateral, relieved Respondent of any duty it would otherwise have had to protect the trust deeds by perfecting a security interest in them. Several cases have held that identical or similar language in loan agreements prevented borrowers or sureties from claiming discharge due to failure on the part of the lender to perfect a security interest.

The leading case on this point is <u>Etelson v. Suburban Trust Co.</u>, 283 A.2d 408, 9 UCC Rep. 1371 (Md. 1971). In <u>Etelson</u>, the secured party's failure to file a security interest in the collateral caused the secured party to lose all rights in the

collateral when its owner was declared bankrupt. 283 A.2d at 409. The sureties, citing some of the same cases cited by Appellants herein, claimed that the secured creditor's failure to perfect was an unjustified impairment of the collateral under § 3-606(1)(b) of the Uniform Commercial Code, which discharged their liability as sureties on the underlying promissory note. The court rejected this argument, because the borrowers, by consenting under provisions of the note to the "release or exchange of any collateral without notice" waived any claim they might have had to discharge through unjustified impairment. The court held that failure to perfect a security interest was a type of "release" of the collateral:

> It is clear from the express wording of the endorsement that the [secured creditor] could have released the collateral at any time to the Etelsons and without the release affecting the Etelsons' obligation to pay. It would be illogical to rule that the [secured creditor] had a duty to file the financing statement and its failure to do so released the endorsers, when under the endorsement, it could have released the collateral with impunity.

Id. at 410.

That a contractual waiver covering a "release" of collateral includes a failure to perfect a security interest in that collateral was also made clear in the recent case of Executive Bank of Fort Lauderdale v. Tighe, 429 N.E. 2d 1054, 32 UCC Rep. 894 (N.Y. 1981). In Tighe, the lower court distinguished a "release" from a failure to file on grounds that the former is "a deliberate act at a future time whereas the latter is a negligent act which occurs at the threshold of the transaction." The New York Court of Appeals followed Etelson in rejecting this distinction:

> From a guarantor's point of view, it makes no difference when or with what intent, short of bad faith, the collateral is reduced

> or released. From his point of view, the effect (increase of potential liability through the decrease of his source of reimbursement) is exactly the same.

420 N.E.2d at 1058.

In Reeves v. Hunnicutt, 168 S.E.2d 663, 6 UCC Rep. 92 (Ga. App. 1969), a debtor claimed that his obligations under a promissory note were discharged because the secured creditor failed to perfect a security interest in the collateral. The court rejected this argument, because the note contained a provision that the "surrender or release" of any collateral by the secured creditors would not affect the debtor's liability. 168 S.E.2d at 664. Hunnicutt is particularly apposite to this case, because its provision consenting to the "surrender or release" of collateral is virtually identical to the provision here, which speaks of "release or surrender" of collateral.

The holdings of Etelson and Hunnicutt have been accepted by every court which has dealt with this issue. Indeed, at least two appellate courts have relied on Etelson to affirm motions for summary judgment against guarantors who consented to a "release" or "surrender" of collateral yet claimed unjustified impairment by virtue of the secured party's failure to perfect. In Greene v. Bank of Upson, 201 S.E.2d 463, 13 UCC Rep. 1102 (Ga. 1973), the guaranty agreement permitted the secured party to "without notice, surrender . . . all or any part of the collateral." 201 S.E. 22 at 464. The Georgia Supreme Court affirmed the lower court's granting of summary judgment, as "under the agreements here, the appellant consented to the impairment of the collateral and can not now complain". Id. Similarly, in Haney v. Deposit Guaranty National Bank, 362 So.2d

, 25 UCC 206, (Miss. 1978), the Mississippi Supreme Court, relying on Etelson and Greene, affirmed summary judgment against a guarantor whose payment agreement provided that "the Bank may at its discretion surrender any collateral without affecting the liability of any obligor"; the court held that failure to perfect the security interest was one method of surrendering the collateral, which the guarantor had agreed would not extinguish her obligation. 362 So.2d at 1252.

Etelson was also followed in American Bank of Commerce v. Covolo, 540 P.2d 1294, 17 UCC Rep. 1052 (N.M. 1975), the case relied on by the court below. Under the Covolo guaranty agreement, the lender bank had the right to "waive and release" the security at any time without affecting the guarantor's obligation to pay. Id. at 1298. The court held that by agreeing to such express language, the guarantor could not claim that his liability was extinguished by the bank's failure to perfect a security interest:

> Where a guarantor or surety expressly and unequivocally consents to a waiver or release of his rights in the collateral, he will not be heard to complain of the failure of the guarantee to perfect its security therein in the first instance.

Id. at 1299.

Covolo is especially relevant to this case because the guarantor there argued, as do Appellants here, that the secured creditor owes the guarantor a duty to perfect his security interest in collateral, and failure to do so discharges the guarantor, even if he consented to the failure to perfect. To this effect, both the guarantor in Covolo and Appellants here cited St. Paul Fire and Marine Insurance Co. v. New Jersey Bank and Trust, 250 A.2d 57 (N.J.

Sup. 1969), rev'd on other grounds, 137 N.J. Super. 294, 349 A.2d (1971). Covolo rejected this argument as applying solely to suretyships at common law, 540 P.2d at 1296, fn. 2, thus establishing that the enactment of UCC § 3-606 modifies the common law of suretyships by allowing guarantors to waive their rights the collateral.

Appellants argue that Covolo is distinguishable from the present case by claiming that a contractual provision for the waiver of guarantor's rights in the security was present in Covolo, yet absent here. This contention is wholly without merit. The Covolo guaranty agreement provided that the lender may "waive and release the security without affecting the guarantor's liability, while the present contract speaks of "release or surrender" of the security. Even assuming that a "surrender" of collateral is not equivalent to a "waiver" of it, so that Covolo would not precisely cover this situation, Hunnicutt, Greene and Haney can be cited for the proposition that a guarantor who gives the secured party a right to "surrender" the collateral has consented to any failure to perfect and cannot claim that such a failure extinguishes his liability.

Appellants also attempt to distinguish Covolo as applying only to situations in which the documents "specified on their face that they were to be unsecured. This argument is misleading. A section of the Covolo opinion did deal with a promissory note that on its face specified that it was to be unsecured but the section which Respondent and the lower court here rely discussed a separate promissory note which did not state on its face that it was to be unsecured. Covolo, 540 P.2d at 1298-99.

Appellants would also distinguish Covolo from the present case in that here extrinsic evidence -- mainly in the form of the guaranty agreement and the course of dealing between Utah Security Storage, Inc. and Respondent -- is available to prove that the parties intended Respondent be liable for failure to perfect its security interest in that the collateral, notwithstanding the explicit provision to the contrary in the guaranty agreement. Even if extrinsic evidence would so indicate, Utah law makes the evidence unavailable here, because the guaranty agreement -- the source of the obligations between Appellants and Respondent -- is clear and unambiguous on this point.

This Court has repeatedly stressed that extrinsic evidence is available only if the instrument embodying the contract and obligations between the parties is ambiguous, see, e.g. Williams v. First Colony Life Insurance Co., 593 P.2d 534, 536 (Utah 1979), and parol evidence, such as evidence relating to the course of dealing, can be used only as a last resort in the event that both the instrument and contemporaneous writings are ambiguous, Continental Bank and Trust v. Bybee, 306 P.2d 773, 775 (Utah 1957). Here, under Steison and its progeny -- all of which decided the issue by looking solely to the respective writings, and not to extrinsic evidence -- the instrument clearly provides that Appellants are not relieved of liability by Respondent's failure to perfect a security interest, so Utah law, as expressed in Williams and Bybee, requires that extrinsic evidence not be considered here.

It is also argued in Appellant's Brief that Covolo is distinguishable from the present case because Respondents acted in

with a lack of "good faith" and "honesty in fact" in arranging loan to Utah Security Mortgage, Inc. Appellants assert that Respondent induced Utah Security Mortgage, Inc. to agree to a unsecured loan agreement, knowing that Utah Security Mortgage, believed it had obtain a loan unless it was secured. Brief of Appellants at p. 18. Even assuming that there is a factual basis for this contention, it cannot lie for procedural reasons. This allegation of bad faith is merely a rewording of Appellants' allegation of fraud that was made before the District Court. This allegation was disregarded by the court below because it was made for the first time on oral argument before the District Court. Continental Bank and Trust Co. v. Utah Security Mortgage, Inc. et al., Civil No. C81-3162 (Third District Court, December 13, 1982). The lower court's decision on this issue should be affirmed. Fraud is an affirmative defense under Rule 8(c) of the Utah Rules of Civil Procedure, so like other affirmative defenses, it must be pleaded by the party opposing summary judgment in its affidavits on the motion for summary judgment or in its answer to the complaint. Rossiter v. Vogel, 134 F.2d 908, 912 (2nd Cir. 1943), 6 Moore's Federal Practice, p. 56-736. Since upon review of a lower court decision granting summary judgment, this Court applies the same standards as the trial court in determining the existence of material issues of fact, Durham v. Margetts, 571 P.2d 1332, 1334 (Utah 1977), this Court should disregard Appellants' allegations of "bad faith" and refuse to distinguish Covolo on this point.

The Guaranty Agreement Expressly Provided that Respondent Had No Duty to Sell the Stock Before it Depreciated.

Appellants also allege that Respondent's failure to sell stock of Bonneville Thrift when the stock was worth enough to pay the amount of the loan constituted an impairment of the collateral which relieves them of their obligations under UCC 3-606, Utah Code Annotated § 70A-3-606. Again, even assuming there is a factual basis for these allegations, Appellants have no cause to complain, because they consented to any such failure by agreeing that their liability would not be affected by "release" of the collateral.

As discussed above, courts have construed such a provision as a consent by the guarantor to any action or omission on the part of the secured creditor which reduces the value of the collateral or makes it worthless. In Tighe, supra, the court held that a provision consenting to a "release" of the collateral operates a consent to any act or omission that increases the guarantor's potential liability through the decrease of his source of reimbursement", 429 N.E.2d at 1058.

This principle was illustrated in De Kalb County Bank v. Haldi, 246 S.E.2d 116, 24 UCC Rep. 716 (Ga. App. 1978). In Haldi, the creditor failed to procure credit life insurance on the life of the borrower, as required by the loan and guaranty agreements. The court held that even though the creditor's omission did amount to an impairment of the collateral, the guarantor could not claim relief, because he "expressly consented to such impairment when he signed the guaranty agreement," 246 S.E.2d at 117.

Tighe and Haldi clearly establish that a guarantor who consents to a release of collateral consents to any omission by a secured party which results in a loss of the collateral's value. Since Appellants consented to any such omission, they cannot now complain of Respondent's alleged failure to sell the Bonneville Thrift shares when they had some value.

C. Appellants Could Have Prevented Any Alleged Depreciation in the Value of the Shares.

Appellants' claim that they were injured by Respondent's failure to sell the shares of Bonneville Thrift pledged as collateral at a time when they allegedly had value is further undermined by the fact that Appellants could have obtained the shares at such time and sold them. Under the doctrine of subrogation, Appellants, as guarantors of Utah Security Mortgage's obligation to Respondent, would have become entitled to the shares upon payment in full of the amounts due on the promissory notes. See Restatement of Restitution, § 76 (1954); 73 Am.Jur.2d Subrogation § 53 (1974). Upon obtaining possession of the shares, Appellants could have then sold the shares by themselves, thereby eliminating any alleged harm to them which resulted from Respondent not selling the shares.

II. RESPONDENT OBSERVED STANDARDS OF REASONABLE CARE AS ESTABLISHED IN THE GUARANTY AGREEMENT.

Appellants, by permitting Respondent to "release or surrender" the collateral, not only consented to Respondent's conduct, but also agreed to modify the standard of reasonable care in preserving the collateral that Respondent was required to observe under UCC § 9-207, U.C.A. § 70A-9-207.

Section 9-207(1) provides:

> A secured party must use reasonable care in the custody and preservation of collateral in his possession. In the case of an instrument or chattel paper reasonable care includes taking necessary steps to preserve rights against prior parties unless otherwise agreed.

Comment 1 to § 9-207 states that under § 1-102(3) the parties to a security agreement may determine what constitutes "reasonable care" for the purposes of their agreement, so long as the standards set are not "manifestly unreasonable".

Courts have given the parties to a guaranty agreement broad powers to determine the applicable standard of care under § 9-207. In Union Planters National Bank v. Markowitz, 468 F. Supp. 529 (W.D. Tenn. 1979) the guaranty agreement provided:

> . . . In order to hold the undersigned liable hereunder, there shall be no obligation on the part of [the secured creditor] at anytime to first resort to, make demand on, file claim against, or exhaust its remedies against the Debtor, anyone or more of the undersigned, . . . or to resort to and exhaust its remedies against any collateral [or] security . . . .

468 F.Supp. at 533 (emphasis supplied). The court held that this provision set a standard of reasonable care, that freed the secured creditor from any duty to perfect a security interest in the collateral, and that the provision was valid under § 9-207(1):

> The first sentence of [§ 9-207(1)] essentially requires a secured party to use reasonable care not to destroy or injure collateral in his possession . . . The second sentence of [§ 9-207(1)] adds the element that the duty of reasonable care requires that the secured party take steps to preserve his rights in that collateral unless otherwise agreed. We interpret this to mean that the duty of reasonable care does not require a secured party to preserve its rights in collateral when the parties agree otherwise. Here, the guaranty agreement clearly states that [the secured party] need not take steps to protect his rights in the collateral. Thus, [his] obligation of reasonable care under [§ 9-207] was satisfied.

468 F. Supp. at 534 (emphasis in original).

Many of the cases the hold that a failure to perfect a security interest in collateral constituted a "release" consented by contract also contain an alternative holding that the contract provision established a standard of performance, disclaiming any obligation to perfect on the part of the secured creditor, that was valid under § 9-207(1). See, e.g., Etelson, supra, 283 A.2d at 410. In Covolo, supra, the court held that the agreement, by giving the secured creditor the right to "waive and release" the collateral, established a standard of reasonable care that was not "manifestly unreasonable," so the agreement was valid under § 9-207(1) as a determination of the standard of care of the collateral to which the secured party would be held. Therefore, the Covolo court concluded, the guarantor could not claim discharge under § 9-207 because the secured party failed to perfect a security interest. 540 P.2d at 1298.

Applying these precedents to the instant case, it must be concluded that Respondent had no duty to perfect a security interest in the trust deeds, since the guaranty agreement validly disclaimed such a duty by allowing Respondent to "release or surrender" the collateral. Furthermore, because Etelson and Covolo indicate that valid consent for the purposes of § 3-606(1)(b) also constitutes a modification of the "reasonable care" standard of § 9-207(1), the "release or surrender" provision also operates to modify the standard of care applicable to the Bonneville Thrift stock. Since the "release or surrender" provision constituted consent to the alleged failure to make a proper sale of the stock -- for reasons discussed above -- it also establishes the standard of care

applicable to the stock, under which Respondents had no duty to sell the stock before it became worthless.

III. RESPONDENT HAD NO DUTY TO PURSUE ANY OTHER SECURITY BEFORE BRINGING THIS ACTION AGAINST APPELLANTS.

A. Recent Opinions of This Court Have Expressly Rejected the Existence of Such a Duty.

This Court has repeatedly held in recent cases that a secured creditor whose security consists solely of personal property has no duty to proceed against the collateral before bringing an action against sureties or absolute guarantors. In Kennedy v. Bank of Ephraim, 594 P.2d 881 (Utah 1979), a secured creditor brought an action against the surety and other parties liable on a promissory note. The parties claimed that they should not be held personally liable, because the secured creditor is required to satisfy its debt from the collateral before proceeding against the surety and the other parties. The court rejected this argument for situations in which the collateral is personal property by looking to § 9-501 of the Uniform Commercial Code, Utah Code Annotated § 70A-9-501, which provides:

> When a debtor is in default under a security agreement, a secured party . . . may reduce his claim to judgment, foreclose or otherwise enforce the security interest by any available judicial procedure.

Relying upon Michigan National Bank v. Marston, 185 N.W.2d 47, 8 UCC Rep. 1375 (Mich. App. 1970), this Court read the Uniform Commercial Code as allowing the secured party a broad choice of remedies. Quoting Marston, this Court added:

> The existence of a security interest in no way affects the existence of the debt. It merely provides the secured party

with an immediate source of recovery in addition to the st... remedies of an unsecured creditor.

594 P.2d at 884.

This Court then concluded in Kennedy:

> We hold that the [secured creditor] has an option to pursue ... of the parties liable on this note, which is secured solely ... personal property, and may also, at its option, ignore that security and satisfy its judgment from other property in the hands of the judgment debtor.

Id. Since the collateral here is in the form of personal prope... Respondent had no duty to proceed against the collateral before bringing this action against Appellants as sureties.

The strong policy in favor of giving secured parties a broad choice of remedies in case of default was reiterated by t... Court in Strevell-Paterson Co. v. Francis, 646 P.2d 741 (Utah 1982). In that case, the guarantor signed an absolute guaranty ... a loan to the corporation of which he was a director; in additio... the guaranty, the corporation granted the creditor a security interest in the corporation's inventory and accounts receivable. When the corporate borrower defaulted, the secured creditor obta... a default judgment against it. Instead of collecting on that judgment, the secured creditor brought a separate action against guarantor, who argued that the secured creditor must first exha... its remedies against the debtor and the collateral before comme... an action against the guarantor. This Court rejected the guarantor's argument because he was liable under an absolute guaranty:

> The guarantee at issue in this appeal is an absolute guarant... of payment . . . It contains no express or implied conditio... liability and no contractual requirement that the creditor ... satisfaction elsewhere before commencing action on the

guarantee. The fact that the creditor obtained a judgment against the debtor but failed to allege execution on that judgment or exhaustion of his remedies against the debtor or the security does not alter the nature of the guarantor's independent obligation as a guarantor.

Id. at 743-44. In so holding, this Court upheld the lower court's grant of summary judgment against the guarantors. Since Appellants concede that the guaranty in this case is an absolute guaranty (Appellants' Brief, at p. 11), under Strevell-Paterson they cannot defend this action by claiming that Respondents have failed to proceed against the collateral.

Appellants' position in this case is even weaker than the positions of the guarantors in Kennedy and Strevell-Paterson. In this case, the guaranty agreement contains express language providing that the liability of the guarantor would not be affected by the release or surrender of any security, while the guaranty agreements in Kennedy and Strevell-Paterson contained no such language. Thus, there is an even stronger basis here than here was in Kennedy and Strevell-Paterson for holding that Respondent had no duty to proceed against the collateral before commencing this action against Appellants.

B. Doctrine of Election of Remedies Inapplicable.

Appellants seek to distinguish Strevell-Paterson and Kennedy from the present case in that here Respondent had a choice of two remedies -- proceeding against the collateral or proceeding against Appellants as guarantors -- and exercised the former choice by allegedly giving notice of an election to sell the Bonneville Project shares. Appellants assert that since Respondent made this election, it is barred from exercising the other alternative --

proceeding against Appellants -- by the doctrine of election of remedies. Assuming arguendo that there is a factual basis for this argument, it is inapplicable here for both procedural and substantive reasons.

This Court should disregard Appellants' argument on this issue because it was not presented to the court below. This Court will not consider on appeal a legal theory not presented to the lower court, Branch v. Western Petroleum, Inc., 657 P.2d 267, 276 (Utah 1982). Appellants did not raise the issue of election of remedies before the District Court, either in their memorandum in support of their motion for summary judgment, or in their memoran in opposition to respondent' motion for summary judgment, so the issue is not properly before this Court and should be disregarded.

Even if the issue of election of remedies were properly raised, it would still be inapplicable to this case, as the transactions here are governed by the Uniform Commercial Code. Section 9-501(1) of the Code, Utah Code Annotated § 70A-9-501(1), provides:

> When a debtor is in default under a security agreement, a secured party has the rights and remedies provided in this Pa and . . . those provided in the security agreement. He may reduce his claim to judgment, foreclose or otherwise enforce security interest by any available judicial procedure . . . T rights and remedies referred to in this subsection are cumulative.

All courts that have construed this provision have held that by expressly making cumulative the remedies of the secured party upo default, it eliminates the common law doctrine of election of remedies. See 69 Am.Jur.2d § 557, P. 446, and cases cited there Utah adopted this position in Kennedy v. Bank of Ephraim, supra.

Kennedy, this Court relied heavily on Michigan National Bank v. Marston, 185 N.W.2d 47, 8 UCC Rep. 1375 (Mich. App. 1970), which, as Kennedy noted, found that the intent of the Code is to "broaden the options open to a creditor after default rather than to limit them under the old theory of election of remedies". 594 P.2d at 884.

The inapplicability of the doctrine of election of remedies to cases governed by the Uniform Commercial Code was stressed in Ceres Fertilizer, Inc. v. Beekman, 308 N.W.2d 347, 31 UCC Rep. 1489 (Neb. 1981). In Beekman, a secured creditor brought an action against a debtor who had defaulted on a promissory note and obtained a judgment against the debtor. The judgment was later vacated, and the lower court held that the secured party could not maintain a separate action under the security agreement because he had elected to proceed against the debtor, and under the doctrine of election of remedies, his rights accrued solely from the judgment. The Nebraska Supreme Court reversed, holding that under § 9-501(1), a secured creditor by pursuing one remedy, is not precluded from asserting his rights under another remedy. 308 N.W. 2d at 349.

In accord with Beekman is Ruidoso State Bank v. Garcia, 587 P.2d 435 (N.M. 1978), a case involving facts very similar to those in Beekman. In construing § 9-501(1), the Ruidoso court stated:

> There is nothing ambiguous about this statutory provision. It plainly states that all the remedies of proceeding on the note and the security agreement are cumulative. Each of them remains in force although efforts have been made to collect the debt by the alternate means.

587 P.2d at 437.

Beekman and Ruidoso establish that even if Appellants could prove as a matter of fact that Respondent attempted to sell the

Bonneville Thrift stock, it is not barred from utilizing the alternative remedy of proceeding against Appellants as guarantors. Thus, Appellants' allegation that Respondent attempted to dispose the stock presents no issue of fact that is material to the outcome of this case.

CONCLUSION

The decision of the District Court granting summary judgment in favor of Respondent should be affirmed.

Respectfully submitted this ____ day of July, 1983.

FABIAN & CLENDENIN,
A Professional Corporation

By _____
Albert J. Colton

By _____
Randall A. Mackey

CERTIFICATE OF SERVICE

This is to certify that on this 15th day of July, 1983, I caused to be mailed two true and correct copies of the foregoing Brief of Respondent, postage prepaid, to James R. Brown, Esq., Jardine, Linebaugh, Brown & Dunn, 370 East South Temple, Salt Lake City, Utah 84111; to Ron S. Barker, 2870 South State Street, Salt Lake City, Utah 84115; and to Adrienne Badger, pro se, 694 East 1900 South, Bountiful, Utah 84010.