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Utah Finance Company of Salt Lake v. Thomas G. Patrick and Mona Rae Patrick : Brief of Appellant

Utah Supreme Court

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IN THE SUPREME COURT OF THE STATE OF UTAH

UTAH FINANCE COMPANY OF SALT LAKE,

Plaintiff and Appellant,

vs.

THOMAS G. PATRICK and MONA RAE PATRICK,

Defendants and Respondents.

No. 10179

BRIEF OF APPELLANT

Appeal from the Judgment of the Third District Court for Salt Lake County Honorable A. H. Ellett, Judge

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STATEMENT OF THE KIND OF CASE

This is an action by plaintiff, an industrial loan corporation, on a promissory note given by defendants to recover a deficiency balance owing after foreclosure of a chattel mortgage by advertisement and sale. Defendant, Thomas G. Patrick, claimed the obligation was discharged in his bankruptcy, and plaintiff contended it was not so discharged because the defendant

furnished plaintiff a false and fraudulent financial statement in writing as an inducement for the extension of credit and the making of the loan.

DISPOSITION IN THE DISTRICT COURT

At the pre-trial the Court granted defendants' Motion to Dismiss as to the defendant, Thomas G. Patrick, and gave judgment as prayed as to defendant, Mona Rae Patrick.

RELIEF SOUGHT ON APPEAL

Plaintiff seeks reversal of the judgment granting the Motion to Dismiss as to defendant, Thomas G. Patrick.

STATEMENT OF FACTS

The plaintiff is an industrial loan company of the State of Utah. Defendants had borrowed money from the plaintiff and given security therefor in the form of a chattel mortgage. The note on which this action is based was given in connection with a renewal of a previous note and the renewal of a previous mortgage, said mortgage covering an old motor vehicle and items of household furniture and furnishings. The plaintiff had foreclosed the chattel mortgage by advertisement and sale in accordance with the statutes of the State of Utah, after default by the defendants, and there

remained owing after application of the proceeds from such foreclosure a deficiency balance of $1,003.00. At the time of the renewal of the said obligation and the signing of the note on which this action is brought and of the chattel mortgage which had secured the same, the defendants, as an inducement to the renewal of the loan and the furnishing of additional funds, executed and delivered to the plaintiff a statement in writing as to their financial condition, which said statement was introduced at the pre-trial as Exhibit PT 2. At the pre-trial, it was admitted ,through statements of counsel, that the defendant, Mona Rae Patrick, had no defense and that plaintiff was entitled to judgment against her as prayed. (R 7). It was likewise admitted that judgment would be entered against Thomas G. Patrick as prayed were it not for the fact that he had taken bankruptcy and had been discharged from his dischargeable debts, said defendant contending that the debt sued upon was so discharged and plaintiff contending that it was not discharged by reason of the furnishing of the false financial statement (Ex. PT 2) as an inducement to the loan and extension of credit. (R 7).

It was further admitted that all charges made by plaintiff and all things done in connection with the loan were in accordance with the statutes and that the amount of the renewal note included therein a charge of $19.04, which was a proper charge under the provisions of the statutes of the State of Utah, 7-8-3 (1) (c), Utah Code Annotated, 1953 as amended. (R 8).

Exhibit PT 1 introduced and received at the pre-trial shows that the financial statement (Ex. PT 2) omitted substantial obligations owing by the defendants at the time of the execution of said Exhibit PT 2 and the execution of the note sued upon.

Motion to dismiss was the made on behalf of defendant, Thomas G. Patrick, "due to the fact that the company has charged for making an investigation and they should have found this by the charge . . . and did not rely on the statement of the creditor." (R 8).

The Court then granted the said defendants' Motion to Dismiss "upon the ground and for the reason that when the plaintiff company charged $19.04, as it had a right to do under the statutes, then it could not rely upon the statements made by the defendant, but was obligated to spend that $19.04 in making its own investigation; that if it did not intend to rely upon the investigation it made in determining whether or not to make the loan, it should not have charged the fee." (R 9).

ARGUMENT

POINT I

THE COLLECTION BY THE PLAINTIFF OF A CHARGE PERMITTED BY THE STATUTE FOR "EXAMINING AND INVESTIGATING THE CHARACTER AND CIRCUMSTANCES OF THE BORROWER" DID NOT

AS A MATTER OF LAW RELIEVE THE BORROWER FROM THE CONSEQUENCES OF ISSUING AND FURNISHING FALSE AND FRAUDULENT INFORMATION ON A FINANCIAL STATEMENT.

There is no contention but that the plaintiff operated in every manner consistent with and as authorized by the statutes of the State of Utah and that the charges made by it were in conformity therewith. The statute specifically involved is included under the general powers of industrial loan corporations and reads in part as follows:

> "7-8-3. General powers — Every industrial loan corporation shall have power:
>
> . . . (c) To charge a fee of $2.00 or less on loans of $100.00 or less and not to exceed 2% or $20.00, whichever is smaller, on loans in excess of $100.00 for expense incurred by it in examining and investigating the character and circumstances of the borrower."

The section of the Bankruptcy Act which would prevent the discharge of the obligation sued upon is contained in *Title II, Section* 35, *U.S.C.A.*, as amended, which reads:

> "(a) A discharge in bankruptcy shall release a bankrupt from all of his provable debts . . . except such as . . . (2) are liabilities for obtaining money or property by false pretenses or false representations, or for obtaining money or property on credit or obtaining an extension or renewal of credit in reliance upon a materially

> false statement in writing respecting his financial condition made or published or caused to be made or published in any manner whatsoever with intent to deceive . . . "

It should be noted that the ruling of the Court was not based upon the fact, or upon any contention, that there was not or could not be presented evidence that the defendant was guilty of "obtaining an extension or renewal of credit in reliance upon a materially false statement in writing respecting his financial condition" etc., so as to prevent his discharge under the provisions of the Bankruptcy Act above quoted. On the contrary, the Court took the view that, notwithstanding any false or fraudulent representations or the submission of any false statement in writing, no matter how flagrant the misrepresentations therein might be, or regardless of whether or not the plaintiff did in fact rely upon such statements, that plaintiff could not claim such reliance by virtue of its having taken the $19.04 which the statute permitted it to take. Such surely cannot be the law, as it would be an open invitation to fraud.

We do not argue with the general proposition of law that when one makes an independent investigation upon which he relies, that he is ordinarily chargeable with knowledge of the facts which his investigation should disclose. The matter does not, however, end there. The rule applicable to this matter is stated in 23 *Am. Jur.* "Fraud and Deceit" Section 144, Page 945, as follows:

"The mere fact that one makes an independent investigation or examination, or consults with others, does not necessarily show that he relies on his own judgment or on the information so gained, rather than on the representations of the other party, nor does it give rise to a presumption of law to that effect. If, under the circumstances, he is unable to learn the truth from such examination or investigation or, without fault on his part, does not learn it and in fact relies on the representations, he is entitled to relief, all other ingredients of liability being present."

The rule is similarly stated in 37 *Corpus Juris Secundum,* "Fraud," Section 37 (b), Page 286, as follows:

" . . . it is generally held that one in fact relying wholly on representations is not barred from relief merely because he made independent inquiry. Redress will not be denied nor lack of reliance conclusively presumed where the investigation failed to reveal the truth, nor will an unsuccessful investigation necessarily deprive the defrauded party of his right to rely on the speaker's representations. This is especially true where the investigation was rendered unsuccessful by the deliberate artifice of the speaker, . . . *or because the facts were peculiarly within the knowledge of the speaker and difficult for the hearer to ascertain.*" (Emphasis supplied).

The Court assumed that by the expeniture of $19.04, which was the maximum the plaintiff could charge under the statute for investigation fee, that plaintiff must be presumed to have learned everything

there was to know and everything which it required as to the financial stability of the borrower and that it therefore relied exclusively upon such information and not upon any representations or information furnished by the borrower. Such, of course, is a fallacy on its face. Let us examine the practical situation in the light of the rules of law above herein referred to.

As indicated, the Legislature limited the amount that could be charged for the examination fee to 2% of the amount of the loan, which in this case was $19.04. In determining whether or not a loan should be made, and investigating the character and circumstances of the borrower, there are a myraid of things whuch must be considered. Where the loan is to be secured by a chattel mortgage, as it was in this case, it requires someone from the lending institution to go out to the home and check and list the items to be included on the mortgage. This entails an examination of the items and inquiries with regard to ownership thereof. It likewise includes checking through the Credit Bureau as well as the public records which will reflect any information with regard to the borrower. These methods and means of checking into the credit and circumstances of the borrower, if followed through to their fullest, would, as will readily be seen, require an expenditure of time, and therefore money, far in excess of the amount which the statute allows. But, this is not the problem involved here. The real problem is that no matter how much time or money might be expended by the lender in an inves-

tigation, all of the pertinent information as relates to the financial status of the borrower cannot be obtained through any sources available to the lender. A considerable part of such information is necessarily within the sole and peculiar knowledge of the borrower. The lender must look to him and depend upon his representations as to such matters. Let us elaborate on this phase of the matter.

In connection with a proposed loan to an ordinary borrower, the lender checks all sources of public information and checks information sources such as credit bureaus, the finance companies' local exchanges, banks and other references given by the borrower, so that it has run down every source normally available to it, and such might reflect that the borrower is in reasonably sound financial circumstances. Assuming, however, that this borrower then owes $1,000.00 to his father, $3,000.00 to a friend, and other monies to various individuals, which obligations are unsecured, how, except through inquiry of the borrower himself, can a lender know of such obligations which affect the financial stability of the borrower. How can the lender learn of obligations which might be owing in connection with purchases made by the borrower, short of circulating every wholesaler and retailer in the entire area, and even beyond? Even such, of course, would not disclose such obligations owing to individuals as relates to obligations for property purchased on Conditional Sales Contracts. Except as relates to motor vehicles, there is

no public record of such obligations or any liens represented thereby. How, except through inquiry of the borrower can a lender learn of such obligations?

If, as the Court held, the lender cannot rely upon the representaions in a written financial statement by the borrower, as to his obligations, we assume the lender likewise could not rely upon representations as to ownership of chattels which might be included on the mortgage. As to such, how can the lender know whether or not such chattels are clear, or what if any obligations exist against the same, unless he can rely upon the representations of the borrower.

It should thus become glaringly apparent that by making the charge permitted by statute for investigating, the lender should not be presumed to have ascertained or be chargeable with knowledge as to the character and circumstances of the borrower, except at most as to those matters which reasonably and ordinarily could and would be ascertained through inquiry through regular and normal channels. Certainly, as the authorities above cited indicate, the lender should not be chargeable with knowledge as to facts peculiarly within the knowledge of the borrower.

If any other conclusion is reached than that the borrower is, when he makes a financial statement, bound at his peril to truthfully set forth his circumstances, there is an open invitation to every borrower to defraud the lender. The law does not, we believe, encourage, nor sanction and protect such deceit. Surely, logic and

common sense would indicate that the Legislature believed the lender of money under the Industrial Loan Act ought be reimbursed for expenses actually incurred by it up to the amount of 2% of the loan in endeavoring to learn about the borrower through the sources ordinarily open to it through normal inquiries. It surely did not contemplate that if such expenditures were made in good faith that the lender then was precluded from relying upon representations made by the borrower as to his financial circumstances, and particularly as would relate to matters which could not, through any other reasonable means be ascertained.

There is a rather extensive discussion of this matter of reliance where an independent investigation has been made in the case of *Baylies vs. Vanden Boom,* (Wyo.) 278 Pac. 551, 70 A.L.R. 924, preceding an annotation in that latter volume. The Court therein cites numerous cases with regard to the matter. The Court, quoting from another case, to-wit, *Hetland vs. Bilstad,* (Iowa) 118 N.W. 422, stated:

> "The fact that one does not procure the information which ordinary prudence would dictate will not defeat recovery, where ,notwithstanding this, he relies on the sellers' misrepresentations."

Again quoting with approval from the case of *Smith vs. Werkheiser* (Michigan) 115 N.W. 964, the Court stated:

> "It is urged that inasmuch as the books were placed at their disposal complainants were bound to ascertain the truth and to place no reliance

upon the false statements that had been made to them. This is not the law. A defrauded party does not owe to the party who defrauds him an obligation to use diligence to discover the fraud."

Later in the decision, that Court quotes with approval from *Omar Oil & Gas Co. vs. Mackenzie Oil Co.*, 138 Atlantic 392, which involved a suit brought on notes and wherein the defense was that execution was induced by fraud, contention being made that an independent investigation was conducted and hence the representations were not relied upon. The quoted language of the Court reads:

> "Relative to false representations, as a ground of defense, there is one fundamental rule, agreed upon by all the authorities, viz., that a buyer shall not be precluded from relying on such representations unless it clearly appears that he relied on his own investigation, and not on the representation. Mr. Pomeroy, at section 895, note 4, states it thus:
>
> " 'The question is, did the party rely on the representation or on his own knowledge? To obviate the effect of the representation, it must be clearly and conclusively shown that he relied on his own knowledge. This, the general doctrine and the qualifications both demand.'
>
> " . . . The better and more reasonable doctrine, the one consistent with the fundamental rule, and supported by the majority of well-considered cases, including those in Texas, is this: The buyer will not be prevented from availing himself of false representations of the seller, unless he makes an investigation on his own account

and it is of such character as to fully acquaint him with the essential facts. If the buyer made an investigation that was free and unhampered, *and conditions were such that he must have obtained the information he desired, or the facts he seeks to know were as obvious to him as to the seller, and their means of knowledge were equal,* he is presumed to have relied on his own investigation, and not on the representation. In such case he could not have been misled by the seller." (Emphasis supplied).

It will be observed that in this and in all other cases which we have been able to find, the only time when it is held as a matter of law that reliance was not placed upon false and fraudulent representations are in circumstances where the party so claiming to rely made a full and unhampered investigation and where the circumstances were such that he must have learned, or be in a position to learn, the facts from such investigation. We have found no case nor authority which held that in spite of any independent investigation a person could not avail himself of false and fraudulent representations made to him if he either (1) in fact relied upon them, or, (2) such representations related to matters peculiarly within the knowledge of the one making such representations, or would be difficult of ascertainment from other sources.

There is nothing to show that plaintiff lender, had it tried through every conceivable means of investigation available, could have learned the facts as to the obligations owing and the financial circumstances of

the defendant borrower in this case. There is nothing to show that it had access to any means of checking the items involved and that it failed to do so. Surely, there can be no presumption of law that by accepting a fee allowed by statute it had agreed to waive any legal rights under the Bankruptcy Act, or otherwise, to which it would be entitled resulting from false and fraudulent representations made to it by a borrower and as a result of which the plaintiff lender suffered damages. We cannot believe that a borrower, by payment of a maximum of $20.00, automatically purchases a statutory immunity from the effects of his willful fraudulent acts.

The construction placed upon the statute by the Court would, as indicated, place a premium on fraud and completely relieve persons borrowing money under the Industrial Loan Act from the necessity of honest dealing and fair disclosure. Borrowing the words of the Court in *Christensen vs. Jauron* (Iowa) 174 N.W. 499, "The law is not thus tender of persons practicing deceit."

CONCLUSION

It is respectfully submitted that the trial court erred in granting the motion of the defendant, Thomas G. Patrick, for summary judgment and that the Court's said Order should be reversed and the case remanded to the District Court for trial on the issues thereof as to said defendant.

Respectfully submitted,

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