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Lavell Kemp and Thelma Alice Kemp v. Zions First National Bank : Appellant's Brief

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**IN THE SUPREME COURT
of the
STATE OF UTAH**

LaVELL KEMP and THELMA
ALICE KEMP, his wife,

*Third Party Plaintiffs
and Appellants,*

vs.

ZIONS FIRST NATIONAL BANK,
Defendant and Respondent.

11671

APPELLANT'S BRIEF

Appeal from the Judgment of the
Third District Court for Salt Lake County
Honorable Merrill C. Faux, Judge

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Clerk, Supreme Court, Utah

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APPELLANT'S BRIEF

STATEMENT OF THE NATURE OF THE CASE

This is an action involving a contest between the Third Party Plaintiffs-Appellants and Defendant-Respondent as to a priority of mortgage between the Appellants, who were vendors of the property and took back a first mortgage to secure the unpaid balance of the purchase price, and the Defendant-Respondent, who as a lender, loaned part of the money for the purchase price and received back a Deed of Trust or mortgage to secure the payment of the moneys advanced for part of the purchase price and other moneys loaned.

DISPOSITION IN LOWER COURT

The case was tried to a jury and submitted on two special interrogatories. The lower court rendered its decision in favor of the Defendant-Respondent and denied Plaintiffs - Appellants' Motion for a New Trial. From the judgment for the Defendant-Respondent, Third Party Plaintiffs-Appellants appeal.

RELIEF SOUGHT ON APPEAL

Third Party Plaintiffs-Appellants seek reversal of the judgment of the lower court.

STATEMENT OF FACTS

LaVell Kemp and Thelma Alice Kemp, his wife, Appellants, were owners either in fee or by virtue of purchasers on a real estate contract, of certain tracts of land located at Draper, Utah. They were lay people and inexperienced in the handling of real estate transactions being more experienced in the egg producing business. They sold their property to Dr. Joseph W. Noble in whom they had confidence, for the sum of \$40,000.00 payable at \$11,000.00 cash and the remaining \$29,000.00 to be paid in monthly installments evidenced by a Promissory Note and a first mortgage on the property. Relying upon the agreement and representations of Dr. Noble, they executed and delivered a Warranty Deed to Dr. Noble and received back the Promissory Note and the mortgage; these documents having been prepared by Dr. Noble's attorney. This transaction took place in the latter part of November 1964.

Dr. Noble in turn made an application to Zions First National Bank to borrow money, part of which was to pay the down payment owed to the Kemps, part of which was to pay the costs of moving certain improvements from Holladay to the Draper property and part of which was to be used for his own use in the sum of \$35,000.00 total. Zions First National Bank also received a mortgage to secure its note which purportedly was also a first mortgage. Zions First National Bank prepared the closing statement for the parties. Zions First National Bank also handled certain moneys held by them for the paying of placing certain improvements on the Draper property. Dr. Noble in turn sold the property to a Ferroll Fullmer on a contract for \$64,000.00. Due to survey and title problems, Zions First National Bank made disbursements on or about December 4, 1964 and recorded its mortgage on that day. The Kemps, not knowing that they had to record their mortgage, did not record their mortgage until 1966, nearly two years later.

The dates on the Noble-Kemp transaction, to-wit: The Deed, Mortgage and Note are apparently filled in by Dr. Noble in that the Deed has a date of November 30, but referring to a Mortgage made of even date.

The jury unanimously found that Zions First National Bank reasonably should have been aware of the unpaid balance on the purchase price owed by Dr. Noble to the Kemps.

ARGUMENT

WHICH MORTGAGE HAS PRIORITY, AN UNRECORDED PURCHASE MONEY MORTGAGE OR A RECORDED MORTGAGE OF A THIRD PARTY LENDER WHO DID NOT HAVE ACTUAL KNOWLEDGE OF THE UNPAID BALANCE BUT HAD ENOUGH INFORMATION THAT IT SHOULD HAVE BEEN AWARE OF AN UNPAID BALANCE?

Plaintiffs contend that their mortgage is prior to Zions First National Bank in two ways:

- A. By virtue of a purchase money mortgage; and
- B. Constructive notice on the part of Zions First National Bank or notice of inquiry.

A. Purchase money mortgage: This type of purchase money mortgage where a seller, pursuant to a prior contract or without one, conveys title to a buyer and received at that time part of the purchase money and receives as part of the same transaction, a mortgage upon the property to secure the balance of the purchase money. Zions First National Bank's position is also a form of a purchase money mortgage who advances part of the purchase price and a mortgage back to secure not only the part of the money loaned for the purchase property, but also for the balance of the money loaned. This type of situation presents a most difficult question

as to the priority of these purchase money mortgages. Because of this type of problem, your writer respectfully urges the court to read very carefully, the dissertation on this subject in 4 American Law of Property 219-226. Because of the manner in which this subject has been treated in the aforesaid reference, this writer wishes to quote from this reference those matters which he wishes to be stressed. Each quote will be followed by the page or pages wherein the quote will be found, to-wit:

"... It is familiar learning that a purchase money mortgage, executed at the same time as the deed of purchase of land, or in pursuance of agreement *as part of one continuous transaction*, takes precedence over any other claim or lien attaching to the property through the vendee-mortgagor. This is so even though the claim antedates the execution of the mortgage to the seller. It will also have priority if it is in favor of a third person who advanced the purchase money paid to the vendor, provided the money was loaned for this purpose only." (Emphasis added) Page 220.

"... Where the contest is between a purchase money mortgage to a third person who advances part of the purchase price and a purchase money mortgage to the vendor for the balance, the latter is given preference even if he had notice of the former." Pages 221-222.

"... Several rationales have been advanced for this favoritism of the law for the purchase money mortgagee. The most venerable and frequently stated explanation is that of transitory seizure. The idea is that title shot into the grantee and out of him again into the purchase money mort-

gagee so fleetingly — quasi uno flatu, in one breath, as it were — that no other interest had time to fasten itself to it: the grantee-mortgagor must be regarded as a mere conduit. Such a theory breaks down in lien states where the fee remains permanently in the grantee-mortgagor. It also is inconsistent with the cases of quite common occurrence in which some considerable time elapses between the conveyance to the mortgagor and the execution of the mortgage. If the reason were to be taken literally it would require the execution of the deed of purchase and the execution of the mortgage to be practically simultaneous, something that is ordinarily not feasible and not required by the cases. As was said by an able judge in a leading case, "An examination of the cases will show that the real test is not whether the deed and mortgage were in fact executed at the same instant, or even on the same day, but whether they were parts of one continuous transaction, and so intended to be, so that the two instruments should be given contemporaneous operation in order to promote the intent of the parties." Pages 222-223.

"... A better statement of the reason for the rule is that the title comes to the purchaser already charged with the encumbrance in favor of the grantor-mortgagor; that regardless of the form all that the transaction ever transfers is the redemption right. While such a conclusion would square with the decisions where the purchase money mortgage goes to the vendor, it is more difficult to apply it to the mortgage going to a third party lender of the purchase price, although it has been advanced in such a case. Furthermore, it would seem that the opposite conclusion could

have been reached just as easily. Indeed it would have been easier to do so, since in form there is a transfer of the full title without reservation, and the grantee then by a separate mortgage instrument creates the charge on it. So, unless the matter is dug into more deeply, one is left unsatisfied as to why this one of two perfectly possible conclusions has been chosen.

A little delving, though, does give more illuminating answers. One is somewhat technical and legalistic. The other more satisfactorily deals with it as a matter of intrinsic fairness based upon the just expectations on the part of the purchase money mortgagee. The first answer suggests that the purchase money mortgage always takes the place of an equitable interest in the property that precedes any lien or interest of any kind attaching to the purchaser's estate at the time of acquiring title. Where there is a prior contract of sale this equitable interest consists of a specifically enforceable contract right to have the purchase money mortgage given on taking title, and the equitable estate under the purchase contract is subject to this right. Where there is no prior contract the vendor has left in him on conveying title without receiving payment an equitable vendor's lien. When the purchase money mortgage is given it merely replaces and takes the priority of one of the other of these prior equities, and this is so whether it is given at once or subsequently, provided it is part of the same transaction. The priority of the third party lender of the purchase money is an extension of this. He is said to be in the position of an assignee of prior equitable rights of the vendor, a theory similar to one advanced when the question was as to the applica-

bility of the Statute of Frauds to a promise to give a mortgage on lands to be acquired with money loaned for that purpose by the promisee.

The other answer justifies the doctrine on the equity and justice of protecting one who has parted with his property on the faith of having a security interest in it until the money for which he was exchanging it is received, as against persons who, for different reasons, have inferior claims." Pages 224-225.

"... As against other mortgagee claimants to the property, especially those who have made their loan for the purpose of paying part of the purchase price, the question is closer. These, unlike the others, have relied upon getting paid out of the same specific property and have parted with value on that reliance. Even so, the vendor has the edge because the property he is relying on for payment was previously his up to the time of sale and mortgage back. There was never an instant when he relinquished a hold on it. And he would never have parted with it at all except upon the belief and faith that if his buyer defaulted he could either recapture his property or get paid out of it. And this is normally so even though he may know that his buyer is going to finance the deal in part by borrowing some of the purchase money from another and by giving him a mortgage on the property. Other mortgages, on the other hand, even including lenders of purchase money, parted only with money in which they retained no interest whatsoever, and placed their reliance for repayment of their debts on getting a security interest in other property not only never previously owned by them but not even owned by the mortgagor at the time the

money was loaned, even though they might not have known that fact. This difference in attitude toward the hazard of losing property previously owned and that of not getting an interest in property which had never before belonged to the claimant is an old and important one." Pages 225-226.

The lower court in its Memorandum Decision, has cited a Utah case, *State vs. Johnson*, 268 Pac. 561, for the premise that the mortgage for purchase money must be executed simultaneously with the deed of conveyance from the vendor. A reading of this case was dicta and that the case turned on uncontroverted facts that the purchase money mortgage was in fact intended to be a second mortgage and the seller is the one who procured the borrowed money and handled the complete transaction. It is also important to note that there was nearly a month's time elapsed from the date of the deed and the mortgage. In a much later Utah case, *McMurdie vs. Shugg*, 107 P2d 163, the court discussed the vendors lien as being valid even though there were only promissory notes executed at a much later time.

It is the writer's opinion that the reasoning set forth in the American Law of Property justly sets forth the reason for equity favoring the owner of the property. It could also be stated that irrespective of the dates shown on the document, it is certainly obvious that the overall intent was one continuous transaction and that both Kemps and Zions First National Bank were intentionally misled by the fraud on the part of Dr. Noble.

B. Constructive notice of inquiry notice. It is elementary that a person is charged with having notice of all matter reflected in a properly recorded document in a recorder's office whether or not he has actual knowledge or not. This is constructive notice. One form of constructive notice is, "inquiry notice."

"... It exists when the circumstances are such that a purchaser is in possession of facts which would lead a reasonable man in his position to make an investigation that would advise him of the existence of prior unrecorded rights. He is said to have constructive notice of their existence whether he does or does not make the investigation. The authorities are unanimous in holding that he has notice of whatever the search would disclose." No. 4 *American Law of Property*, paragraph 17.11 pages 565 and 566. Also see *Reilly vs.*

McLean, 84 Utah 551, 563, 37 P.(2d) 799 (1934; *Corey vs. Roberts*, 82 Utah 445, 25 P.(2d) 940 (1933), *LeVine vs. Whitehouse*, 37 Utah 260, 109 Pac. 2.

If Kemps had of recorded their mortgage in the recorder's office prior to the recording of Zions First National Bank's mortgage, there can hardly be a question that Kemp's mortgage would be prior whether Zions First National Bank had actual notice or had not actual notice of the recording; this is constructive notice. By the same token, if Zions First National Bank has constructive notice by virtue of the knowledge of the facts that it had, as found by the jury, they have constructive

notice of the seller's rights in the property. When a bank has, or should have, knowledge that a person is selling property, the bank can very easily protect itself by merely asking the Kemps at the time they signed the closing statement as to whether or not there is an unpaid balance on the purchase price and as between experienced real estate mortgage personnel as opposed to inexperienced chicken ranchers, the owner of the property should be favored.

CONCLUSION

In conclusion, it is Appellants' contention that the vendor purchase money mortgage has priority over a lenders purchase money mortgage, and secondly, the bank had constructive notice of the vendors mortgage and was the bank's responsibility to make inquiry. Either one of the two theories gives the Kemps priority, and a combination of the two, should create little problem in giving relief to the Kemps.

Respectfully submitted,

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Plaintiffs Appellants