

11 U.S.C. § 544

28 U.S.C. § 157

O.R.S. 88.070

O.R.S. 88.075

Election of remedies

Mortgage foreclosure

Knight v. Boese, Adv. No. 91-6190-R

In re Gordon & Bonnie Knight, Case No. 690-63779-R11

6/26/92

Radcliffe, J.

Unpublished

This matter came before the court on the plaintiffs' (debtors-in-possession) motion for summary judgment in this adversary proceeding to determine that a mortgage held by the defendants was invalid and therefore avoidable under 11 U.S.C. § 544. The court granted the plaintiffs' motion.

In 1984 the parties entered into an exchange agreement whereby the Boeses exchanged their Deschutes County property for the Knights' Lane County property. The agreement provided that Knights would attempt to sell the Lane County property for Boeses. Knights also executed a mortgage on the Deschutes property in favor of the Boeses to secure Knights obligation to obtain a buyer for the Lane County property. After the Knights failed to find a buyer the Boeses' brought three different actions to enforce their rights and/or recover damages. The first alleged breach of contract and sought foreclosure of the mortgage; it was dismissed. The second alleged breach of contract and unjust enrichment and sought specific performance of the contract; the Boeses prevailed at trial and on appeal. The third was a malpractice lawsuit by the Boeses against their former attorney who had prepared the exchange agreement.

Applying Oregon law, the court held that the Boeses, by proceeding to recover a judgment against Knights in the suit for

specific performance, breach of contract and unjust enrichment elected their remedy, and the mortgage had therefore become unenforceable. In other words, because the Boeses brought an action against the Knights on the debt secured by the mortgage, they are precluded from seeking to foreclose the mortgage; they waived their lien and the Knights may avoid it. The court granted the Knights' motion for summary judgment.

E92-4 (14)

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

IN RE)	
)	
GORDON BOYD KNIGHT and)	Case No. 690-63779-R11
BONNIE KAY KNIGHT,)	
)	
_____ Debtors.)	
)	
GORDON BOYD KNIGHT and)	Adversary Proceeding
BONNIE KAY KNIGHT,)	No. 91-6190-R
)	
Plaintiffs,)	
)	
v.)	
)	
RALPH W. BOESE and)	MEMORANDUM OPINION
GLENNYS BOESE,)	
)	
_____ Defendants.)	

This matter comes before the court upon the plaintiffs' motion for summary judgment. Plaintiffs, the debtors-in-possession herein, (Knights) have brought this adversary proceeding seeking a determination that a mortgage held by the defendants (Boeses) on property owned by the Knights in Deschutes County, Oregon

(Deschutes County property) is invalid and therefore avoidable under 11 U.S.C. § 544.

FACTUAL BACKGROUND

The parties have been involved in extensive litigation for years. This adversary proceeding is at least the fourth suit between the same parties concerning an exchange agreement entered into by and between the parties on or about December 12, 1980 as hereinafter more fully explained. A review of the pleadings herein indicates that facts are essentially agreed upon. In addition, many, if not all of the facts have already been judicially determined in litigation between the parties, See Boese v. Knight, 104 Or. App. 559, 802 P2d 675 (1990). The parties disagree as to the legal conclusions and inferences that should be drawn from the facts. The operative facts are as follows.

In 1980 the Boeses owned a ranch in Deschutes County, Oregon (Deschutes County property). They were approaching retirement and they wanted to sell the ranch; Knights wanted to buy it. The parties agreed to a selling price for the ranch of \$264,000. Since the Knights lacked the funds with which to buy the ranch, the Knights and the Boeses executed an "exchange agreement" on December 12, 1980. Under the exchange agreement the Knights received title to the Deschutes County property and the Boeses received title to two parcels of land in Lane County owned by the Knights (the Lane

County property). The Boeses had not seen the Knights' land, apparently did not want it, and so advised the Knights.

The exchange agreement, prepared by Boeses' attorney, provided in part as follows:

1. At closing Boese shall convey Deschutes Property, including all improvements thereon to Knight by statutory warranty deed. . .

2. At closing Knight shall convey Lane Property, including all improvements thereon, to Boese by statutory Warranty deed. . . Knight shall be entitled to maintain possession of Lane Property until it is sold as provided for below. . .

Following conveyance of Lane property by Knight, Knight shall use best efforts to sell Lane property for Boese at a price of \$264,000. No broker's fee, commission or other sales costs shall be paid by Boese in connection with the sale.

. . . In the event Knight fails to sell Lane property within twelve (12) months of the date of this agreement, Knight shall promptly execute a sales agreement in which Knight agrees to buy Lane property under the terms and conditions described in (i)-(v) above.

As security for Knights' obligation to obtain a buyer for Lane property Knight shall execute a mortgage on Deschutes property naming Boese as mortgagee. Boese shall release this mortgage upon execution of a satisfactory sales agreement for Lane property.

As part of the exchange agreement, the Knights, as mortgagors, executed a mortgage of the Deschutes County property in favor of the Boeses. The mortgage was given to secure the ". . . performance of certain obligations of mortgagor set forth in that contract between Mortgagee and Mortgagor dated December 12, 1980."

The Knights never found a buyer for the Lane County property. After the time provided by the exchange agreement, the Boeses demanded that Knights execute a land sale contract according to the exchange agreement. Knights have repeatedly refused to do so. After the Boeses attempted unsuccessfully to sell the Lane County property for the Knights, litigation followed.

LITIGATION BACKGROUND

First Lane County Lawsuit

On November 9, 1984, the Boeses sued the Knights in the Circuit Court of the State of Oregon for Lane County (the "first Lane County lawsuit"). The Boeses complaint alleged breach of contract and sought foreclosure of the mortgage and damages for fraud. The Knights filed two motions against the complaint. The first was a motion to dismiss the first claim for relief (breach of contract/foreclosure of mortgage) on the ground that it failed to state facts sufficient to constitute a claim. The second was a motion to dismiss the second claim for relief (fraud) because it was not commenced within two years after the fraud was discovered. The court granted both motions.

After further pleading, Boeses' third amended complaint asserted only a breach of contract claim. It alleged that Knights had breached the exchange agreement by failing to purchase the Lane County property for the sum of \$264,000 and by failing to use their best efforts to sell the Lane County property. It sought damages of \$232,343.30 plus attorneys' fees, costs and disbursements.

The trial on Boeses' third amended complaint was conducted on November 25, 1986. After Boeses had presented their case, Knights moved for a judgment of dismissal. The court dismissed the action without prejudice.

Deschutes County Lawsuit

On October 4, 1985, Boese's commenced an action in the Circuit Court of the State of Oregon for Deschutes County ("Deschutes County Lawsuit") seeking to reform the mortgage and to foreclosure upon it. Boeses subsequently amended their complaint to seek merely reformation of the mortgage. The principal allegation was that due to a mutual mistake and an oversight in drafting, the mortgage did not say that it had been executed as security for the payment of \$264,000.¹

Knights filed a motion for summary judgment which the Court granted. The Court's final judgment stated in part as follows:

The court grants the motion [for summary judgment] on the basis that (1) the antecedent agreement alleged in the amended complaint is not shown to be the agreement of the parties, (2) the exhibit AA exchange agreement attached to the amended complaint was incorporated in the mortgage, and (3) the exhibit AA exchange agreement is the antecedent agreement of the parties. The granting of the motion decides all issues in controversy and the court expressly directs the entry of final judgment.
Case #85-CV-0562-19 July 24, 1986, Mosgrove, J.

Second Lane County Lawsuit

On May 19, 1987, Boeses brought a second action in Lane County Circuit Court ("second Lane County lawsuit") against Knights for

¹ The complaint in the first Lane County lawsuit was dismissed, in part, on the grounds that the mortgage as drafted was invalid under Oregon law. In their motion to dismiss, the Knights contended that to be valid under Oregon law the mortgage must secure payment of a debt or money equivalent obligation. Bruckman v. Breitenbush, 272 Or. 1, 15, 534 P2d 971 (1975). Because the exchange agreement provision secured by the mortgage merely obligated the Knights to find a buyer for the plaintiffs' property for a stated price, it only secured an obligation to perform a duty, not the payment of a debt.

specific performance, breach of contract and unjust enrichment. They eventually recovered a judgment against the Knights which was entered on September 21, 1989. It stated (in part) as follows:

1. The judgments entered December 8, 1988 and June 22, 1989 are set aside.

2. Plaintiffs shall have and recover judgment against the defendants, and each of them, in the sum of \$264,000, plus interest thereon at the rate of 12% per annum, from December 12, 1981, until paid, on plaintiffs' first claim for relief.

3. Defendants, and each of them, are hereby ordered and directed to satisfy the aforementioned judgment by entering into a contract to purchase from plaintiffs the real property (the Lane County property). . . upon the terms and conditions as set forth in the form of Contract of Sale, . . . and make all payments due thereon, within thirty (30) days from the date of the entry of this judgment, and in the event that the defendants do not enter into such Contract of Sale, and make the payments which are due hereunder, the Sheriff of Lane County is directed to sell at public auction, in the manner provided by law on execution the real property (the Lane County property). . . with the proceeds of said sale to be applied to the payment of the judgment against the defendants. In the event that the amount received from the sale of said real property is not sufficient to satisfy the amount of the plaintiffs' judgment, plaintiffs shall have a judgment against the defendants, and each of them, for the deficiency. (parenthesis added)

4. Plaintiffs shall have and recover judgment against the defendants, and each of them, for their costs and disbursements incurred herein to include a reasonable attorney's fee.

5. Plaintiffs' second and third claims for relief are dismissed as moot.

6. Defendants' counterclaim for attorney fees is dismissed.

Case #16-87-04332, September 21, 1989, Spencer, J.

Knights appealed this judgment but it was affirmed by the Oregon Court of Appeals on December 12, 1990, one decade after the parties first executed the exchange agreement. Knight v. Boese, 104 Or.App. 559, 802 P2d 675 (1990).

Malpractice Lawsuit

On November 27, 1990, Boeses filed a legal malpractice lawsuit against their former attorneys who had drafted the exchange agreement. They allege that the attorneys were negligent in their representation of Boeses in preparing the exchange agreement documents. Specifically, they maintain that the attorneys were negligent in failing to advise plaintiffs that the mortgage was useless and that it provided security only for the Knights obligation to find a buyer for the Lane County property. That lawsuit is still pending.

BANKRUPTCY PROCEEDING

Knights filed their petition for relief under Chapter 11 of the Bankruptcy Code herein, on October 15, 1990. On June 12, 1991 they commenced this adversary proceeding seeking a determination that the mortgage on the Deschutes County property is invalid and therefore avoidable under 11 U.S.C. § 544. Knights allege that the mortgage is invalid because enforcement of it is barred:

1. By the 10 year statute of limitations to bring an action on a mortgage provided by Oregon law;
2. By the doctrine of res judicata or collateral estoppel
3. The mortgage has been satisfied and discharged by the last Lane County Circuit Court judgment (election of remedies);

4. The original mortgage was invalid because it did not describe a debt and/or;
5. The original mortgage was invalid because it secured an obligation other than one to pay a debt.

Boeses have alleged four affirmative defenses:

1. The bankruptcy court does not have jurisdiction to invalidate the mortgage;
2. That the complaint does not state a claim for relief;
3. Enforcement of the mortgage is not barred by the statute of repose because the filing of the petition in bankruptcy on October 15, 1990, suspended the limitation period; and
4. Knights have come into this court with unclean hands.

DISCUSSION

All statutory references are to the Bankruptcy Code, Title 11 U.S.C. unless otherwise indicated.

Jurisdiction

Boeses contend, in their first affirmative defense, that this court lacks jurisdiction to invalidate the mortgage on the Deschutes County property. Knights are, however, acting as the debtors-in-possession in this Chapter 11 proceeding.

Generally, § 1107(a) provides that a debtor-in-possession shall have all of the rights, powers and duties of a trustee other than the right to seek compensation under § 330.

Knights seek to use the provisions of § 544 in bringing this adversary proceeding. An examination of the parties' pleadings indicates that the Boeses have admitted the jurisdiction of this court and the fact that this adversary proceeding is a core

proceeding by admitting paragraphs 1-3 of plaintiffs' complaint (See defendants' answer filed July 12, 1991).

Even if the pleadings are read to assume a dispute on these matters, 28 U.S.C. § 157(b)(2)(K) clearly provides that a complaint to determine the validity, extent or priority of liens is clearly a core proceeding. This is such an adversary proceeding, hence this court concludes that this adversary proceeding is a core proceeding as defined in 28 U.S.C. § 157 and that this court has jurisdiction to resolve the issues brought before it herein.

Motion for Summary Judgment

Rule 56(c) of the Federal Rules of Civil Procedure, as incorporated by Bankruptcy Rule 7056, provides that summary judgment shall be rendered if the record shows that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. If the moving party meets its initial burden of identifying for the court portions of the record that it believes show the absence of any genuine issue of material fact, the non-moving party may not rely on the mere allegations in the pleading to preclude summary judgment. In re R & T Roofing Structures and Commercial Framing, Inc., 887 F2d 981 (9th Cir. 1989). Thus the burden is shifted to the non-moving party to show that there is a genuine issue of material fact. Celotex Corp. v. Catrett, 477 U.S. 317 (1986). The non-moving party must set forth facts showing that there is a genuine issue for trial. Anderson v. Liberty Lobby, Inc., 477 U.S. 242 (1986). Where the parties agree on all of the material facts relevant to the issue raised by the motion for summary judgment, the case can be resolved as a matter of law. Summary judgment is the proper procedural device. Ferguson v. Fly Tiger line, Inc., 688 F2d 1320 (9th Cir. 1982); Smith v Califano, 596 F2d 152 (9th Cir. 1979).

Based on the record and facts set forth above, this court concludes that there are no genuine issues of material fact.

Election of Remedies

This case is resolved by an application of the doctrine of election of remedies as established by Oregon law.

The state of Oregon has long provided, by statute, that a creditor may not obtain a deficiency judgment against a debtor/borrower after the creditor elects to foreclose its interest in property under a purchase money mortgage.

O.R.S. 88.070 provides as follows:

When a decree is given for a foreclosure of any mortgage given to secure payment of the balance of the purchase price of real property, the decree shall provide for the sale of the real property covered by such mortgage for the satisfaction of the decree given therein, but the mortgagee shall not be entitled to a deficiency judgment on account of the mortgage or note or obligation secured by the same.

This is one of the so called anti-deficiency statutes.

As early as Wright v. Wimberly, 184 Pac. 740 (Or. 1919), the Supreme Court of Oregon recognized that the anti-deficiency statutes were intended to be remedial in nature, to avoid a situation in which a purchase money mortgagee or trust deed beneficiary might foreclose upon the property subject to their lien for a sum less than the debt and execute upon the personal obligation of the debtor for the balance, jeopardizing the debtor's future financial prospects.

Accordingly, the Supreme Court of Oregon developed the doctrine of election of remedies as a necessary corollary to the anti-deficiency statutes. Thus, a purchase money mortgagee or trust deed beneficiary has an election upon default. It may either elect to (1) foreclose upon the property encumbered by its mortgage or trust deed in the manner provided by law, or in the alternative, it may (2) bring an action at law against the parties personally liable for the debt secured by the mortgage or trust deed. Once one remedy has been elected, the creditor is barred from pursuing the other remedy. Wright v. Wimberly, supra.; Marshall v. Middleton, 100 Or. 247, 296

Pac. 830 (1921); Lutz v. Blackwell, 128 Or. 39, 273 Pac. 705 (1929); Wright v. Nothnagal, 163 Or. 156, 96 P2d 228 (1939); Ward v. Beem Corp., 244 Or. 204, 437 P2d 483 (1968); Bantier v. Harrison, 259 Or. 182, 485 P2d 1073 (1971); See also Family Bank of Commerce v. Nelson, 72 Or. App. 739, 697 P2d 216 (1985).

One obvious reason for the development of this doctrine lies in the rationale that the mortgagee or trust deed beneficiary should be prevented from doing indirectly what the anti-deficiency statutes prohibit, directly. In other words, if the statutes prohibit the obtaining of a deficiency after foreclosure, a creditor should not be able to obtain a judgment, execute thereon and then collect the deficiency, if any, by way of foreclosure. This would permit a creditor to obtain a deficiency judgment so long as the creditor elected to sue the parties personally liable on its debt first and to execute upon any judgment obtained prior to attempting foreclosure on the property subject to a purchase money mortgage or trust deed. "If the purchase money mortgagee elects to foreclose the mortgage, he is barred from bringing an action on the mortgage debt, or he may obtain a judgment on the mortgage debt, in which case he loses his mortgage lien." Bantier v. Harrison, 259 Or. 182, 485 P2d 1073, 1075 (1971).

Woodward v. U.S. Creditcorp, (In re Woodward), Adv. No. 685-6147-R; (slip op.)., (Radcliffe, J., 1986) (unpublished)

The application of O.R.S. 88.070 and the doctrine of election of remedies in this case depends upon whether the mortgage on the Deschutes County property is a purchase money mortgage. O.R.S. 88.075 defines a purchase money mortgage as follows:

A mortgage entered into after September 13, 1975, is a purchase money mortgage if the mortgage is given to a vendor to secure the unpaid balance of the purchase price of real property or if the mortgage is given to a lender or any other person to secure up to \$50,000 of the unpaid balance of the purchase price of real property used by the purchaser as the primary or secondary single family residence of the purchaser.

Boeses argue that this court should not interpret the mortgage as a purchase money mortgage. They argue that it was not given to secure the payment of the unpaid balance of the purchase price, but other obligations. In support of this argument they point out that the Circuit Court in the Deschutes County case refused to reform the mortgage to include language that "it is intended to secure the payment of \$264,000 plus interest"

The facts in this case clearly demonstrate that the mortgage on the Deschutes County property was given by the Knights as part of and incident to the exchange agreement.

This court is not free to adopt its own interpretation of what the mortgage was intended to secure, the Oregon Court of Appeals has ruled on what the parties intended.

In the second Lane County lawsuit, Boeses sought and received a money judgment for \$264,000, against the Knights (the amount of the original sales price of the Deschutes County property). The Lane County Circuit Court and the Oregon Court of Appeals have both found that Boeses are entitled to recover the amount of the original debt obligation.

The Court of Appeals stated:

Here, it is clear what the parties intended. Plaintiffs (Boeses) wanted to sell their property for \$264,000 and defendants (Knights) agreed to buy it for that amount. Defendants were to pay plaintiffs by selling the Lane County property for that amount; if they sold it for less, they were to pay plaintiffs the difference so that plaintiffs would receive \$264,000. If defendants sold the Lane County property for more, they were entitled to

the excess, leaving Boese with \$264,000. If they were unable to sell the Lane County property within 1 year, they were required to purchase it under a land sale contract under the terms in the exchange agreement. (parenthesis added)

104 Or.App. 559, 563.

Since the mortgage was given to secure the Knights obligations under the exchange agreement, it is clearly a purchase money mortgage based upon the conclusion of the Oregon Court of Appeals set forth above.

Boeses further contend, however, that even if the mortgage is considered as a purchase money mortgage under Oregon law, they have not made an election of remedies, since the filing of this bankruptcy by the Knights has prevented them from executing upon the judgment they have obtained by virtue of the operation of § 362.

Under Oregon law, this argument is without merit. The Oregon Court of Appeals has stated: "As a general rule, an election is not made until a judicial proceeding has gone to judgment." Family Bank of Commerce v. Nelson, 72 Or. App. 739, 697 P2d 216, 218 (1985). (See also, Woodward v. U. S. Creditcorp, Adv. No. 685-6147-R (Radcliffe, J., 1986) (unpublished)).

Here, it is clear that Boeses have proceeded to recover a judgment against Knights in the second Lane County lawsuit brought for specific performance, breach of contract and unjust enrichment. In other words, Boeses have elected to bring an action against the

parties personally liable for the debt secured by the mortgage, precluding a suit to foreclose the mortgage for the reasons set forth above. The Boeses have elected their remedy, the mortgage has become unenforceable. The Boeses have, in effect, waived the mortgage lien and it may be avoided by the Knights in this proceeding.

CONCLUSION

Due to the foregoing, this court need not consider the other issues raised by the parties. Plaintiffs' motion for summary judgment should be granted, an order consistent herewith shall be entered. This opinion shall constitute the court's findings of fact and conclusions of law pursuant to Bankruptcy Rule 7052; they shall not be separately stated.

ALBERT E. RADCLIFFE
Bankruptcy Judge