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Commonwealth of Kentucky

Court of Appeals

NO. 2005-CA-002449-MR

REPUBLIC BANK & TRUST COMPANY — APPELLANT

v.

APPEAL FROM JEFFERSON CIRCUIT COURT
HONORABLE STEPHEN K. MERSHON, JUDGE
ACTION NO. 03-CI-009946

HERBERT VAN ARSDALE, II — APPELLEE

AND: NO. 2006-CA-001440-MR

HERBERT VAN ARSDALE, II — APPELLANT

v.

APPEAL FROM JEFFERSON CIRCUIT COURT
HONORABLE STEPHEN K. MERSHON, JUDGE
ACTION NO. 03-CI-009946

REPUBLIC BANK & TRUST COMPANY & HELENE GORDON WILLIAMS — APPELLEES

OPINION
AFFIRMING APPEAL NO. 2005-CA-002449-MR
AFFIRMING IN PART, REVERSING IN PART,
AND REMANDING APPEAL NO. 2006-CA-001440-MR

** ** ** ** **

BEFORE: COMBS, CHIEF JUDGE; ACREE AND TAYLOR, JUDGES.

TAYLOR, JUDGE: Republic Bank & Trust Company (Republic Bank) brings Appeal No. 2005-CA-002449-MR from a September 27, 2005, order of the Jefferson Circuit Court dismissing its complaint against Herbert Van Arsdale, II. Van Arsdale brings Appeal No. 2006-CA-001440-MR from April 18, 2006, and June 5, 2006, orders of the Jefferson Circuit Court awarding attorney fees to Republic Bank and dismissing his counterclaim against Republic Bank. We affirm the September 27, 2005, order in Appeal No. 2005-CA-002449-MR; we affirm in part, reverse in part, and remand the April 18, 2006, and June 5, 2006, orders in Appeal No. 2006-CA-001440-MR.

This action arises from a commercial loan transaction between Republic Bank and Van Arsdale. On November 17, 2000, Republic Bank loaned Van Arsdale $1,629,000.00 to refinance, repair, and renovate an apartment complex in Jefferson County, Kentucky. The indebtedness was evidenced by a promissory note executed and delivered by Van Arsdale to Republic Bank. The debt was secured by a mortgage against the real estate and improvements that comprised the apartment complex and an assignment of rents for the apartments.

The promissory note was for the principal amount of $1,629,000.00 and repayment was amortized for a fifteen-year period.[1] Under the terms of the note, an initial interest rate of 9.875% was assessed for the first five years of the note term with a monthly payment of $17,380.96. After the initial five-year period and beginning in the sixth year of the note, interest was to be adjusted annually to .375% above the prime rate of interest as published in *The Wall Street Journal*. The promissory note also contained a default provision. Van Arsdale was given a thirty-day grace period to cure any default under the terms of the note. The note also contained an acceleration clause whereupon Republic Bank could declare the entire balance of the note due and payable upon default by Van Arsdale. The default provision also provided for the assessment of an additional 4% interest (default interest) upon the principal balance of the note in the event of default. Additionally, if default occurred, the reasonable attorney fees and costs of collection incurred by Republic Bank were to be paid by Van Arsdale.

On August 20, 2003, a default was declared by Republic Bank due to payment being thirty-four days in arrears. Van Arsdale attempted to cure the default by making a payment on September 30, 2003, for the months of July and August. However, Van Arsdale failed to make the September payment. On November 12, 2003, Republic Bank filed a foreclosure action to enforce its mortgage in the Jefferson Circuit Court against, *inter alios,* Van Arsdale and the collateral securing the promissory note. Therein, Republic Bank alleged that Van Arsdale was in default pursuant to the

[1] Due to a mutual mistake of the parties concerning the monthly payment due under the promissory note, the promissory note was later revised by consent of the parties to reflect the proper monthly payment of $17,380.96.

provisions of the promissory note and demanded full payment of the outstanding balance on the note under the acceleration clause. Republic Bank also stated that the additional default interest rate of 4% was being applied to the outstanding balance of the loan. Republic Bank also sought attorney fees and costs incurred as a result of Van Arsdale's default.

By a written agreement dated December 15, 2003, Republic Bank agreed to hold the foreclosure action in abeyance for a period not exceeding six months if Van Arsdale made monthly payments of $17,380.96 on or before the 17th day of each month, with no grace period being extended. Van Arsdale continued to make timely monthly payments of $17,380.96 for some sixteen months until Van Arsdale secured a buyer for the collateral securing the debt.

At the closing conducted on April 28, 2005, Van Arsdale paid the balance owed on the promissory note to Republic Bank to permit the transfer of the collateral to the purchaser free of Republic Bank's mortgage lien. At closing, Republic Bank's payoff amount on the note exceeded Van Arsdale's estimate by $105,593.62. The discrepancy was later determined to be due in large part to Republic Bank's application of the default interest rate (4%) to the unpaid balance of the note effective October 17, 2003. According to Republic Bank, it "capitalized" the default interest every month from October 17, 2003, until the note was paid in full. Van Arsdale tendered the payoff amount of $1,471,789.62 under protest to Republic Bank.[2]

[2] The record reflects that the actual transfer of funds, including the disputed interest, occurred the week following the closing, on May 3, 2005.

On May 20, 2005, Republic Bank filed a motion to dismiss the foreclosure action since the promissory note had been paid in full and the mortgage released. Thereafter, on July 19, 2005, Van Arsdale filed a motion to file a counterclaim against Republic Bank. Van Arsdale's motion was granted by order entered August 23, 2005. In the counterclaim, Van Arsdale asserted that Republic Bank improperly assessed default interest of 4% upon the unpaid balance of the promissory note from October 17, 2003, until May 3, 2005. Van Arsdale alleged that "penalty interest is believed to be in excess of $100,000." Also, Van Arsdale further alleged that Republic Bank improperly added miscellaneous fees, costs, and attorney fees to the payoff amount of the promissory note.

Republic Bank then filed a "Withdrawal of Motion to Dismiss." Therein, Republic Bank attempted to withdraw its motion to dismiss in light of the circuit court's August 23, 2005, order granting Van Arsdale's motion to file a counterclaim.

By order entered September 27, 2005, the circuit court dismissed Republic Bank's action against Van Arsdale under Ky. R. Civ. P. (CR) 12.02 and CR 56. The court pointed out that the promissory note and mortgage held by Republic Bank had been satisfied and released. Thus, the court reasoned that there was "no cause of action upon which relief may be granted . . . ." Republic Bank filed a notice of appeal to this Court from the September 27, 2005, order of dismissal (Appeal No. 2005-CA-002449-MR).

Subsequently, Republic Bank filed a motion for summary judgment seeking to dismiss Van Arsdale's counterclaim. Republic Bank claimed that there existed no issue of fact and that under the promissory note it was entitled to the default interest from

the time of Van Arsdale's initial default until its payoff. Additionally, Republic Bank argued entitlement to attorney fees and costs related to the default under the promissory note. Republic Bank also filed a motion for attorney fees incurred from August 18, 2003, through December 28, 2005, in connection with the promissory note.

By order entered April 18, 2006, the circuit court denied Republic Bank's motion for summary judgment. The court specifically found that an issue of fact remained upon "whether Mr. Van Arsdale, because of the abeyance agreement, should have been charged the extra 4% penalty interest rate above the standard 9.875% rate . . . ." The court, however, concluded that Republic Bank was entitled to an award of attorney fees under the terms of the promissory note. Based upon an affidavit submitted by counsel, the court awarded Republic Bank $6,709.71 in attorney fees and expenses incurred from August 18, 2003, through December 28, 2005.

Both Republic Bank and Van Arsdale filed motions to vacate the April 18, 2006, order. In an Opinion and Order entered June 5, 2006, the circuit court granted Republic Bank's motion to vacate. The court concluded that Republic Bank was entitled to summary judgment and dismissed Van Arsdale's counterclaim. The circuit court reasoned:

> In reviewing its April 18th Opinion, it is apparent that the Court failed to appropriately review the abeyance agreement executed between the parties, as well as Republic's explanatory letter as to the terms of the abeyance. Reviewing this evidence along with the original promissory note, the Court finds that the four-percent interest penalty was a term provided for in the loan documents and the note was appropriately accelerated due to Mr. Van Arsdale's default.

> The Court finds that Republic Bank never waived its right to charge the penalty interest, despite agreeing to withhold prosecuting its foreclosure action for a limited period of time. As outlined in the promissory note, acceleration due to default included the charging of the penalty rate.

Van Arsdale filed a notice of appeal to this Court from the April 18, 2006, and January 5, 2006, orders (Appeal No. 2006-CA-001440-MR). Republic Bank and Van Arsdale's appeals were consolidated for the purpose of being heard by the same panel of this Court.

Appeal No. 2005-CA-002449-MR

Republic Bank contends that the circuit court erroneously dismissed its complaint against Van Arsdale. Republic Bank specifically argues that dismissal was improper under CR 41.01 and/or CR 41.02. However, Republic Bank ignores the fact that the circuit court stated that dismissal was "pursuant to the provisions of CR 12.02 and CR 56 . . . ." As the circuit court's order of dismissal was not premised upon either CR 41.01 or CR 41.02, we view Republic Bank's arguments to be without merit. More importantly, since Republic Bank has been paid in full, including disputed interest and attorney fees and the mortgage has been released, the relief sought in the complaint has been granted in full. The circuit court's dismissal of the complaint was proper.

Appeal No. 2006-CA-001440-MR

In this appeal, Van Arsdale contends that the circuit court erroneously rendered summary judgment dismissing his counterclaim against Republic Bank.

Summary judgment is proper where no genuine issues of material fact exist and the moving party is entitled to judgment as a matter of law. *Scifres v. Kraft*, 916 S.W.2d 779 (Ky. 1996). When ruling upon a motion for summary judgment, the circuit court is required to view the record in a light most favorable to the nonmoving party, and any doubts are resolved in his favor. *Steelvest, Inc. v. Scansteel Service Center, Inc.*, 807 S.W.2d 476 (Ky. 1991). As noted in *Steelvest*, "a party opposing a properly supported summary judgment motion cannot defeat it without presenting at least some affirmative evidence showing that there is a genuine issue of material fact for trial." *Id.* at 482 (citations omitted).

Van Arsdale has advanced various contentions of error. Essentially, we are called upon to address two legal issues: (1) whether the circuit court properly determined that Republic Bank was entitled to assess the additional default interest of 4% upon the unpaid balance of the promissory note from October 17, 2003, to May 3, 2005, and (2) whether the circuit court properly determined that Republic Bank was entitled to attorney fees in the amount of $6,709.71 for services rendered from August 18, 2003, through December 28, 2005. We shall address these issues seriatim.

As referenced, the promissory note provided for additional interest of 4% to be assessed in the event Van Arsdale defaulted. In its complaint, Republic Bank asserted that Van Arsdale defaulted upon the note and that said note was accelerated on October 17, 2003. Under the default provision of the promissory note, Republic Bank stated that the interest rate assessed upon the promissory note effective October 17, 2003, was

13.875% (regular interest rate of 9.875% plus default interest rate of 4%). Conversely, Van Arsdale cites to the agreement entered into by the parties on December 15, 2003, and believes that under its terms the parties agreed the default interest rate would not be assessed. Van Arsdale argues that the agreement essentially reinstated the note payment terms, including interest. This argument necessitates an examination of the December 15, 2003, agreement.

Under the terms of the December 15, 2003, agreement, Republic Bank agreed to "hold" the foreclosure action in "abeyance" if Van Arsdale made timely monthly payments of $17,380.96:

> 1. Republic Bank will hold the aforesaid action in abeyance as long as Van Arsdale makes payments of $17,380.96 on or before the 17th day of each month, beginning December 17, 2003, and continuing thereafter, on or before the 17th day of each month, for a period of time not exceeding six (6) months from the execution of this Agreement. Said payments must be received by Republic Bank before the close of business on the 17th day of each month.

The agreement provided no grace period to Van Arsdale, and the payments had to be received by Republic Bank before the 17th of each month. The agreement, however, was silent as to the default interest rate of 4% and curiously did not incorporate by reference or otherwise address the terms of the promissory note. Considering the terms of this agreement as a whole, we view the agreement as being ambiguous as to whether the default interest rate of 4% would apply under its terms. *See Warfield Natural Gas Co. v. Clark's Adm'x*, 257 Ky. 724, 79 S.W.2d 21 (1934).

It is well-established that interpretation and construction of a contract is a matter of law for the court. *Cinelli v. Ward*, 997 S.W.2d 474 (Ky. 1998). When interpreting a contract, the court is to be primarily guided by the intent of the parties. *Black Star Coal Corp. v. Napier*, 303 Ky. 778, 199 S.W.2d 449 (1947). Moreover, a contract is to be interpreted against the drafting party. *Warfield Natural Gas Co. v. Clark's Adm'x*, 257 Ky. 724, 79 S.W.2d 21 (1934).

To begin our analysis, we observe that the December 15, 2003, agreement was drafted by Republic Bank; thus, any ambiguity therein will be, if reasonable, resolved in favor of Van Arsdale. Under the terms of the December 15, 2003, agreement, Republic Bank specifically agreed not to proceed with its foreclosure action and to accept $17,380.96 from Van Arsdale as monthly payment upon the note if timely made. Republic Bank was aware, as well as Van Arsdale, that $17,380.96 was the original payment due under the terms of the promissory note and was calculated at the 9.875% interest rate, as opposed to the cumulative default interest rate of 13.875% (9.875% plus 4% default interest rate). We view the December 15, 2003, agreement as constituting a temporary modification of the promissory note. As the agreement expressly provided for Republic Bank's acceptance of a $17,380.96 monthly payment that was calculated at the 9.875% interest rate, we think the agreement impliedly excluded application of the default interest rate (4%) during the time the agreement was in effect. Thus, Republic Bank's assessment of default interest upon the balance of the promissory note during the

six-month term of the agreement was improper. The six month term of the December 15, 2003, agreement commenced on December 15, 2003, and ended on June 15, 2004.

Van Arsdale, however, argues that this six-month term was extended by Republic Bank's continued acceptance of the $17,380.96 monthly payment without objection for a total of sixteen months, until April 2005. We disagree.

The record reveals that Van Arsdale requested an extension of the December 15, 2003, agreement by letter to Republic Bank dated June 11, 2004. In response by letter dated June 23, 2004, Republic Bank expressly refused to extend the terms of the December 15, 2003, agreement because taxes were owed upon the property. Thus, Republic Bank clearly stated its intent to Van Arsdale that the December 15, 2003, agreement not be extended beyond June 15, 2004. As such, we hold that the December 15, 2003, agreement terminated by its own terms upon expiration of the six-month period on June 15, 2004. We also hold that Republic Bank's continued acceptance of the $17,380.96 monthly payment after expiration of the December 15, 2003, agreement was of no legal consequence under the unique facts of this case. The terms of the promissory note controlled as to any payments after the expiration of the agreement on June 14, 2004, and expressly provided that Van Arsdale remained liable for the debt, including default interest, regardless of any "act or omission" by Republic Bank with respect to the collection of the debt.

In sum, we are of the opinion that Republic Bank improperly assessed the additional 4% default interest only during the six-month term of the December 15, 2003,

agreement. Upon remand, Van Arsdale is entitled to reimbursement of the additional 4% default interest that cumulated during this period. The circuit court shall hold necessary proceedings to determine same.

Van Arsdale also challenges the circuit court's award of attorney fees and expenses to Republic Bank. The circuit court awarded Republic Bank attorney fees and expenses for a period beginning on August 18, 2003, through December 28, 2005. The total award was for the sum of $6,709.71. In so doing, the circuit court relied upon the terms of the promissory note and KRS 411.195.

Under the promissory note, the parties agreed:

> If default is made in the payment of this Note at maturity (regardless of how same may be brought about) Borrower agrees, upon expiration of the aforesaid curative period, to pay to the owner and holder hereof interest at a default rate equal to the annual rate for the principal hereof plus four percent (4%) until paid, together with all reasonable attorneys' fees and other costs of collection occasioned by any of the foregoing.

KRS 411.195 reads:

> Any provisions in a writing which create a debt, or create a lien on real property, requiring the debtor, obligor, lienor or mortgagor to pay reasonable attorney fees incurred by the creditor, obligee or lienholder in the event of default, shall be enforceable, provided, however, such fees shall only be allowed to the extent actually paid or agreed to be paid, and shall not be allowed to a salaried employee of such creditor, obligor or lienholder.

Thus, according to the plain language of the promissory note and KRS 411.195, Republic Bank is entitled to reasonable attorney fees and costs directly incurred as the result of Van Arsdale's default.

Under the facts of this case, we believe Republic Bank was entitled to attorney fees and other costs directly related to Van Arsdale's default which include all legal fees incurred for all legal matters in this litigation between the dates of August 18, 2003, through September 27, 2005, (the date the circuit court dismissed Republic Bank's foreclosure action). However, we do not view attorney fees incurred after the circuit court's dismissal of Republic Bank's foreclosure action as being directly incurred as the result of Van Arsdale's default. Rather, the attorney fees incurred by Republic Bank after that date were incurred in defense of Van Arsdale's counterclaim filed against Republic Bank. In the counterclaim, Van Arsdale essentially claimed that Republic Bank breached the terms of the December 15, 2003, agreement and the promissory note. As such, attorney fees incurred by Republic Bank in defense of the counterclaim after September 27, 2005, were not directly incurred as a result of Van Arsdale's default. Such attorney fees were incurred to defend against claims that Republic Bank breached the December 15, 2003, agreement and the promissory note. Consequently, we hold that Republic Bank is only entitled to reasonable attorney fees and costs incurred between the dates of August 18, 2003, through September 27, 2005. *See Ranier v. Gilford*, 688 S.W.2d 753 (Ky.App. 1985). Upon remand, the circuit court shall reconsider its award of attorney fees and costs and enter an order in conformity with our holding herein.

We view any remaining contentions to be without merit.

For the foregoing reasons, the September 27, 2005, order of the Jefferson Circuit Court is Appeal No. 2005-CA-002449-MR is affirmed; the April 18, 2006, and June 5, 2006, orders in Appeal No. 2006-CA-001440-MR are affirmed in part, reversed in part, and remanded for proceedings not inconsistent with this opinion.

ALL CONCUR.

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