STATE OF MINNESOTA
IN COURT OF APPEALS
A13-0008

Ridgeway Investments, LLC,
Appellant,

vs.

Glow Hospitality, LLC, et al.,
Respondents,

KAB Properties, Inc., d/b/a Holiday Inn Express in Bemidji, et al.,
Defendants,

United States Business Administration,
Respondent.

Filed August 19, 2013
Reversed and remanded
Peterson, Judge

Beltrami County District Court
File No. 04-CV-12-1301

Caren L. Stanley, Jon R. Brakke, Vogel Law Firm, Fargo, North Dakota (for appellant)

Boris Parker, Nicholas M. Wenner, Brandon Charles Meder, Parker & Wenner, P.A., Minneapolis, Minnesota (for respondents Glow Hospitality)

B. Todd Jones, United States Attorney for Minnesota, Roylene A. Champeaux. Assistant United States Attorney, Minneapolis, Minnesota (for respondent United States Business Administration)

Considered and decided by Chutich, Presiding Judge; Peterson, Judge; and Smith, Judge.

U N P U B L I S H E D O P I N I O N

PETERSON, Judge

In this appeal from summary judgment dismissing appellant mortgagee's foreclosure-by-action proceeding, appellant-mortgagee argues that the district court erred by invoking its equitable powers to (a) undo appellant's acceleration of the amounts due under the mortgage, (b) allow respondent-mortgagor to cure its defaults, and (c) rule that respondent's remaining defaults are not material. We reverse and remand.

FACTS

In January 2008, respondent Glow Hospitality, LLC, and Zion's First National Bank entered into a loan transaction approved by the Small Business Administration (SBA) that consisted of a construction-loan agreement and additional SBA funding for Glow to purchase and make improvements to a Holiday Inn Express Hotel. Glow executed in favor of the bank a promissory note for a loan of $2,177,506, a construction mortgage, a commercial security agreement, and an assignment of rents (hereinafter collectively, together with the construction-loan agreement, referred to as loan documents). Glow also executed a mortgage and a promissory note in favor of Prairieland Economic Development Corporation for loan proceeds of $1,517,000 received from the SBA. Respondents Devindar Khatkar and Harkrishan Khatkar personally guaranteed Glow's payment obligations to the bank and the SBA. Harkrishan Khatkar filed for bankruptcy in June 2010 and was granted a discharge of his debt.

In November 2010, respondent Baljinder Sandhu and Devindar Khatkar began a shareholder action against Glow and Harkrishan Khatkar and respondents Schivcharan

Singh and GIO Management, Inc. The same month, Harkrishan Khatkar and respondent Schivcharan Singh stopped making payments on the SBA loan on behalf of Glow, and, in February 2011, the development corporation accelerated the obligations due under the SBA note.

In March 2011, the bank and Glow entered into a forbearance agreement effective until September 11, 2011, under which the bank agreed to forebear from enforcing specified rights and remedies under the loan documents in exchange for Glow's agreement to cure payment defaults. In June 2011, the bank transferred its rights, title, and interest in the loan documents to Nick Klaers, who, on July 1, 2011, transferred them to appellant Ridgeway Investments, LLC, which owns a competing hotel across the street from the Holiday Inn Express.

On April 20, 2012, in the shareholder action, based on evidence that the defendants in that action had syphoned and usurped funds from the hotel, the district court appointed a receiver for the hotel. On June 25, 2012, the court entered a default judgment against the defendants and awarded Sandhu a 70% ownership interest in Glow.

Also in April 2012, Ridgeway brought this foreclosure action against respondents alleging the following events of default by Glow: failure to pay the SBA note, which had been accelerated by the SBA; failure to provide requested financial records and statements; failure to comply with the terms of the franchise agreement under which the hotel is operated; changes in Glow's ownership or officers and failure to notify Ridgeway of those changes; failure to provide annual personal financial statements of guarantors; commencement of the shareholder action and the resulting appointment of a receiver for

the hotel; failure to remove liens filed against the mortgaged property for labor done and materials furnished; and the bankruptcy of guarantor Harkrishan Khatkar. Glow and Sandhu assert that, before this action was commenced, neither the bank nor Ridgeway provided any respondent with written notice demanding cure of nonmonetary defaults as required by the loan documents.

Glow and Sandhu contend that they made the following efforts to cure the alleged defaults. After Sandhu was awarded an ownership interest in Glow, he signed a personal guaranty for the SBA loan, provided personal financial statements to the SBA, and deposited in the district court a check for $198,162 payable to the SBA on dismissal of this foreclosure action. In return, the SBA agreed to reinstate its loan with Glow. The receiver offered to let Ridgeway view all of Glow's financial records dating back to January 2008, but Ridgeway did not do so. Glow became current or made arrangements to become current on all of its obligations to the franchisor and is in good standing under the franchise agreement. The only lien against the hotel has been removed.

The changes in ownership resulted from the shareholder action, which was initiated before Ridgeway acquired its interest in the loan documents, and Ridgeway was present at the hearing when the district court appointed a receiver for the hotel. Glow asserts that Ridgeway was notified by court order of the changes in ownership resulting from the shareholder action but does not provide a citation to the record supporting that assertion. Glow states that Devindar Khatkar and Harkrishan Khatkar, the original guarantors of Glow, no longer are involved with the operations of Glow or the hotel and that Sandhu has provided a personal guaranty and personal financial statements to the

SBA. Glow asserts that Sandhu has offered to provide the same to Ridgeway but does not provide a citation to the record supporting that assertion. Harkrishan Khatkar's bankruptcy was filed before Ridgeway acquired its interest in the loan documents.

Ridgeway filed a motion for default judgment against the nonanswering defendants and a motion for summary judgment against Glow, Sandhu, Devindar Khatkar, and the SBA. Devindar Khatkar and the SBA did not file a response to Ridgeway's summary-judgment motion. Glow and Sandhu filed a cross-motion for summary judgment. The district court granted summary judgment in favor of Glow and Sandhu, denied Ridgeway's summary-judgment motion, and dismissed the foreclosure lawsuit. This appeal followed.

D E C I S I O N

Summary judgment is appropriate when "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that either party is entitled to a judgment as a matter of law." Minn. R. Civ. P. 56.03. On appeal from summary judgment, this court reviews de novo whether any genuine issues of material fact exist and whether the district court erred in applying the law. *McKee v. Laurion*, 825 N.W.2d 725, 729 (Minn. 2013). The evidence is viewed "in the light most favorable to the party against whom summary judgment was granted." *Id.*

Respondents do not dispute that appellant established a prima facie case for foreclosure by action. The issue presented is whether the district court erred in using its equitable powers to dismiss the action on respondents' motion for summary judgment.

The district court cited *Southtown Plumbing, Inc. v. Har-Ned Lumber Co.*, 493 N.W.2d 137, 140 (Minn. App. 1992), and *Peterson v. First Nat'l Bank*, 162 Minn. 369, 379, 203 N.W. 53, 56 (1925), to support its assertion that it has the equitable power to deny a foreclosure action if allowing the action would result in inequity or unjust enrichment. Those opinions do not support that assertion. In *Peterson*, the supreme court upheld an order relieving a party from a foreclosure sale under the doctrine of unilateral mistake. 162 Minn. at 379, 203 N.W. at 56-57. In *Southtown Plumbing*, this court held that subcontractors could not bring an unjust-enrichment claim against parties that provided financing for a construction project when the subcontractors had a legal remedy through the use of their mechanic's liens or in a breach-of-contract action. 493 N.W.2d at 141-42. This holding was based on the well-settled principle that "one may not seek a remedy in equity when there is an adequate remedy at law." *Id*. at 140. *See also ServiceMaster of St. Cloud v. GAB Bus. Servs., Inc.*, 544 N.W.2d 302, 306 (Minn. 1996) (party may not have equitable relief when adequate remedy at law is available); *Drobnak v. Andersen Corp*., 561 F.3d 778, 787 (8th Cir. 2009) (equitable remedies are available only when no adequate legal remedy exists).

The district court also cited principles of contract law and quoted a treatise and a restatement. The quoted treatise states:

> A party is not automatically excused from the future performance of contract obligations every time the other party commits a breach; if a breach is relatively minor and not of the essence, the plaintiff is still bound by the contract and may not abandon performance and obtain damages for a total breach by the defendant, though the nonbreaching party is entitled to damages caused even by the immaterial breach,

> albeit that these may be nominal in amount. Otherwise stated, a nonperforming party is liable for any breach of contract, but the other party is discharged from further performance, and is entitled to substantial damages only when there is a material breach. . . .
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> . . .Thus it has been said that a "material breach" is a failure to do something that is so fundamental to a contract that the failure to perform that obligation defeats the essential purpose of the contract or makes it impossible for the other party to perform under the contract. In other words, for a breach of contract to be material, it must "go to the root" or "essence" of the agreement between the parties, or be "one which touches the fundamental purpose of the contract and defeats the object of the parties in entering into the contract." A breach is "material" if a party fails to perform a substantial part of the contract or one or more of its essential terms or conditions, the breach substantially defeats the contract's purpose, or the breach is such that upon a reasonable interpretation of the contract, the parties considered the breach as vital to the existence of the contract. . . . Conversely, where a breach causes no damages or prejudice to the other party, it may be deemed not to be "material."
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> . . . .
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> The determination of whether a material breach has occurred is generally a question of fact.

23 Richard A. Lord, *Williston on Contracts* § 63:3, at 438-40 (4th ed. 2002).

The quoted restatement states:

> In determining whether a failure to render or to offer performance is material, the following circumstances are significant:
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> (a) the extent to which the injured party will be deprived of the benefit which he reasonably expected;
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> (b) the extent to which the injured party can be adequately compensated for the part of that benefit of which he will be deprived;
>
> (c) the extent to which the party failing to perform or to offer to perform will suffer forfeiture;

> (d) the likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of all the circumstances including any reasonable assurances;
>
> (e) the extent to which the behavior of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing.

Restatement (Second) of Contracts § 241 (1981).

Applying these contract principles, the district court determined that Glow had cured all of the defaults that it was possible to cure and the defaults that remained were immaterial, technical defaults. The district court also concluded that Ridgeway's conduct was contrary to the intention of the original parties who executed the loan documents and deemed the conduct to be in bad faith. Finally, the district court concluded that "it would be unjust and inequitable for the matter to proceed further and to allow the issuance of a foreclosure certificate."

When analyzing and applying the contract principles that it relied on, the district court did not consider the well-settled principle relied on by this court in *Southtown Plumbing* that "one may not seek a remedy in equity when there is an adequate remedy at law." 493 N.W.2d at 140. In Minnesota, a foreclosure by action is governed by the same rules and statutory provisions as civil actions. Minn. Stat. § 581.01 (2012). A defendant in a foreclosure by action may assert defenses and claims just as a defendant in any other civil action may, and, as in any other civil action, the defenses and claims will be considered by the district court according to the rules of civil procedure. Consequently, a foreclosure by action is an adequate remedy at law for a mortgagor asserting the defense that a breach is not a material breach, and the district court erred by asserting equitable

powers to address respondents' defense that there was no material breach. Because the determination whether any of Glow's breaches is a material breach is a question of fact, we reverse the summary judgment granted respondents and remand for further proceedings, including any necessary discovery. We express no opinion regarding the merits of the parties' claims.

Reversed and remanded.