STATE OF MINNESOTA
IN COURT OF APPEALS
A07-1789

James Klapmeier, et al.,
Appellants,

vs.

Peoples National Bank of Mora,
Respondent.

Filed August 5, 2008
Reversed and remanded
Hudson, Judge

Kanabec County District Court
File No. 33-CV-06-176

Jon C. Saunders, Anderson Larson Hanson & Saunders, P.L.L.P., 331 Southwest Third Street, P.O. Box 130, Willmar, Minnesota 56201 (for appellants)

D. Sherwood McKinnis, Grant W. Lindberg, Lindberg & McKinnis, P.A., 200 Third Avenue Northeast, Suite 300, Cambridge, Minnesota 55008 (for respondent)

Considered and decided by Schellhas, Presiding Judge; Shumaker, Judge; and Hudson, Judge.

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

HUDSON, Judge

On appeal in this mortgage dispute, appellants-mortgagors argue that the district court erred in denying a motion for amended findings or a new trial because respondent-

bank's deduction of $60,000 from the proceeds of the sale of appellants-mortgagors' real property, and use of those proceeds to apply against a new debt to satisfy a mortgage debt that had previously been paid, constituted conversion of those funds. Respondent-bank filed a notice of review claiming that the district court abused its discretion in denying its motion for attorney's fees. We reverse and remand.

FACTS

In September 1993, appellants James Klapmeier and his wife borrowed $60,000 from respondent Peoples National Bank of Mora (PNB) to finance the purchase of commercial real property for $80,000. The loan was secured by a mortgage in favor of PNB. The parties identified the property as the "Land-O-Lakes" property, and PNB recorded the mortgage in the Kanabec County Recorder's Office.

In April 1998, Klapmeier made the final payment to PNB on the 1993 mortgage loan; however, no satisfaction of mortgage was filed at the county recorder's office, nor did Klapmeier request a satisfaction of the mortgage. According to PNB's president, Roger Rinerson, PNB did not close the loan file or issue a satisfaction because Klapmeier wanted to keep the mortgage in place on the property to protect his assets from other creditors. After paying off the mortgage, Klapmeier transferred the Land-O-Lakes property to Klapmeier Investment Limited Partnership (KILP).

Over the next few years, Klapmeier allegedly used the 1993 mortgage to secure future lines of credit for his business operations. Whenever Klapmeier's business obtained a line of credit from PNB, Klapmeier signed a personal guaranty as security for the indebtedness to PNB, and the personal guaranty referenced the 1993 mortgage as

security for the guaranty. Rinerson stated that over a period of time, Klapmeier provided different guaranties, and as the amount of the line of credit increased, old guaranties were returned to Klapmeier in exchange for new guaranties to secure new loans or credit lines.

In March 2002, Klapmeier sold his yacht-manufacturing business, American Marine, Ltd., to his son and nephew who operated the business under the name BWHC, LLC. The sale did not include the Land-O-Lakes property. As part of the sale and financing conditions required by PNB, on March 28, 2002, Klapmeier signed a personal guaranty of the debt of BWHC for $1.5 million. The guaranty states that it is secured by "real estate mortgages dated 12-31-96 and September 16, 1993."[1] The 1996 mortgage secured debt of $400,000 and was not related to the Land-O-Lakes property; the September 16, 1993 mortgage secured the original $60,000 loan used to purchase the Land-O-Lakes property. Although the total debt consisted of $1.5 million, Rinerson testified that PNB accepted a "partial guarant[y]" as a "compromise in restructuring the debt and/or the purchase by BWHC."

On February 16, 2006, KILP sold the Land-O-Lakes property to Kanabec State Bank for $300,000. Attorney Robert Lindig attended the closing on behalf of KILP, and Stephanie Keyser attended on behalf of Kanabec State Bank. From the sale proceeds, PNB deducted $60,000 on the basis that it had a $60,000 mortgage against the property, securing Klapmeier's guaranty of BWHC, LLC's debt. This deduction was documented

[1] The record is unclear as to whether Klapmeier transferred title in the Land-O-Lakes property to KILP before executing this personal guaranty. The record is clear that he signed the guaranty individually and that KILP did not grant PNB a mortgage in the Land-O-Lakes property.

in the "Seller's Closing Statement" signed by Lindig. PNB does not dispute that without receiving $60,000 from the sale proceeds, the closing would not have proceeded.

As part of the closing, Keyser sent a letter to PNB with the $60,000 payment and requested that PNB provide her office with the satisfaction of the mortgage for recording. PNB received the $60,000 "mortgage payout" and applied the funds to the principal owed on the $1.5 million BWHC loan secured by Klapmeier's personal guaranty. Rinerson signed the satisfaction of mortgage on February 15, 2006. Rinerson subsequently sent a fax to Klapmeier with a copy of the guaranty and the signed mortgage satisfaction. The fax cover sheet includes a note that states in part: "your guarant[y] is for $1,500,000 and present debt is less than that."

After the closing, Klapmeier demanded that the $60,000 be returned to him on the basis that he satisfied the 1993 Land-O-Lakes mortgage in 1998. PNB refused to return the money, and Klapmeier brought suit asserting a single claim of conversion by PNB of the funds received from the February 16, 2006 closing. Following a bench trial, the district court issued its order concluding that no evidence was offered to contradict the assertion made by PNB that Klapmeier wanted the 1993 "mortgage to appear to remain in place after the final payment on the loan" was made in 1998, "both to avoid possible encumbrance on the property by other creditors and to use the property as collateral for subsequent indebtedness." The court also stated that:

> The mortgage on the property sale from which [PNB] received payment was used as for security on the debt owed by [Klapmeier] to [PNB]. [Klapmeier's] agent at the closing properly made the payment to [PNB]. [PNB] fully credited [Klapmeier's] payment on the underlying debt. [PNB]

> promptly provided the satisfaction when properly requested to do so.

Thus, the district court held Klapmeier failed to establish an act of conversion because PNB was entitled to payment from Klapmeier.

On May 23, 2007, PNB filed a motion for attorney's fees and disbursements pursuant to the April 2007 order. The next day, Klapmeier filed a motion for amended findings of fact and conclusions of law or, alternatively, a motion for a new trial. Klapmeier claimed that there was no basis for the conclusion that PNB was entitled to the $60,000 mortgage payout because the 1993 mortgage had been satisfied in full in 1998. The district court denied Klapmeier's posttrial motion, concluding that:

> [Klapmeier] ask[s] that the Court "apply the law" to the facts of this case; i.e. strict application of the terms of mortgages to the $60,000 at issue. This request of [Klapmeier] is like asking the court to describe the scenery on the North Shore of Lake Superior solely by visiting Duluth. Although [Klapmeier] frame[s] the argument with a sole focus on the $60,000 mortgage, this viewpoint denies the longstanding relationship between these parties and the hundreds of thousands of dollars that were exchanged. This Court, in issuing its ruling, viewed the totality of the relationship of the parties.

The court also denied PNB's motion for attorney's fees. Klapmeier subsequently filed this appeal, and PNB sought review of the district court's denial of attorney's fees.[2]

[2] On April 10, 2008, Klapmeier moved to (a) stay the appeal and (b) remand to the district court for consideration of a new motion under Minn. R. Civ. P. 60.02 concerning issues not raised in this appeal. This court denied Klapmeier's motion but did not preclude the district court from considering the motion during the pendency of this appeal.

D E C I S I O N

On appeal from the denial of a motion for a new trial, this court gives great deference to the district court's findings of fact and will not set them aside unless clearly erroneous. Minn. R. Civ. P. 52.01. "Findings of fact are clearly erroneous only if the reviewing court is left with the definite and firm conviction that a mistake has been made." *Fletcher v. St. Paul Pioneer Press*, 589 N.W.2d 96, 101 (Minn. 1999) (quotation omitted). If there is reasonable evidence to support the district court's findings, this court will not disturb them. *Rogers v. Moore*, 603 N.W.2d 650, 656 (Minn. 1999). We review the district court's determination of questions of law de novo. *Rice Lake Contracting Corp. v. Rust Env't & Infrastructure, Inc.*, 549 N.W.2d 96, 98–99 (Minn. App. 1996), *review denied* (Minn. Aug. 20, 1996).

Conversion is "an act of willful interference with personal property, done without lawful justification by which any person entitled thereto is deprived of use and possession." *DLH, Inc. v. Russ*, 566 N.W.2d 60, 71 (Minn. 1997) (quotation omitted). "To make out a prima facie claim for conversion, a party must show it had a right to the use, possession, or ownership of the property converted." *Gen. Cas. Co. of Wis. v. Mid-Continent Agencies, Inc.*, 485 N.W.2d 147, 149 (Minn. App. 1992), *review denied* (Minn. July 16, 1992).

Klapmeier argues that the district court erred in denying his motion for amended findings or a new trial because PNB's deduction of $60,000 from the sale of the Land-O-Lakes property, and use of those funds to satisfy a debt that had previously been paid,

constituted conversion of those funds. To support his claim, Klapmeier relies on the contractual language of the 1993 mortgage. This language provides:

> That if the said mortgagors . . . shall pay to the said mortgagee . . . the sum of sixty thousand dollars ($60,000.00) according to the terms of one principal promissory note . . . with interest . . . executed by the said mortgagors and payable to said mortgagee, at its office in Mora, Minnesota, and shall repay . . . all sums advanced in protecting the lien of this mortgage, . . . then this deed to be null and void, and to be released at the mortgagor's expense.

Klapmeier argues that because he repaid the loan in 1998, the mortgage on the Land-O-Lakes property was no longer valid. Thus, Klapmeier argues that PNB had no legal basis for taking the $60,000 from the sale of the Land-O-Lakes property.

Under longstanding Minnesota law, once a mortgage debt has been paid in full, and evidence thereof is surrendered to the mortgagor, the mortgage is completely extinguished because "it was a mere incident of the debt." *Hendricks v. Hess*, 112 Minn. 252, 256, 127 N.W. 995, 997 (1910). Moreover, even if a mortgage that was paid in full was not satisfied of record, the mortgage is still completely extinguished. *See id.* (holding that "it is well settled that an assignee of a mortgage takes it subject to the defense that it has been paid, even though not discharged of record").

Here, it is undisputed that the 1993 mortgage was paid in full by Klapmeier in April 1998. Thus, under *Hendricks*, the mortgage was completely extinguished. *See id.* Moreover, the mortgage contract unambiguously provides that after the $60,000 is paid to PNB, the deed becomes "null and void." Therefore, when Klapmeier paid the mortgage

in full in April 1998, the 1993 mortgage became null and void and could not be used as security for subsequent debt.

PNB concedes that Klapmeier satisfied the mortgage in full in 1998. But PNB argues that because Klapmeier did not request that a satisfaction of mortgage be recorded, and in fact specifically requested that the bank not file a satisfaction of the mortgage, the parties' subsequent conduct rendered the 1993 mortgage still enforceable. We disagree. Minnesota law is clear that once a mortgage has been paid in full, the mortgage is completely extinguished and unenforceable. *See id.* Although we acknowledge that Klapmeier specifically requested that PNB not file a satisfaction of mortgage, Klapmeier's request simply relieved the bank of any liability for not filing the satisfaction of mortgage. *See* Minn. Stat. § 507.41 (2006) (stating that when a "mortgagee . . ., upon full performance of the conditions of the mortgage, . . . fail[s] to discharge [the mortgage] within ten days *after being thereto requested* and after tender of the mortgagee's reasonable charges therefor, that mortgagee shall be liable to the mortgagor . . . for all actual damages" (emphasis added)); *see also* Minn. Stat. § 47.208 (2006) (imposing liability on a lender for failing to comply with the requirement that "[u]pon written request, a good and valid satisfaction of mortgage in recordable form shall be delivered to any party paying the full balance of a mortgage indebtedness that is secured by Minnesota real estate").[3] Moreover, mortgages fall within the statute of frauds. *Hatlestad v. Mut. Trust Life Ins. Co.*, 197 Minn. 640, 643, 268 N.W. 665, 667 (1936)

[3] Absent a request, a bank is under no legal obligation to sua sponte file a satisfaction of mortgage when a mortgage has been paid in full.

(stating that mortgages fall within the statute of frauds and cannot be created by oral agreement). Thus, any oral agreement to resurrect an extinguished mortgage and use it as security for Klapmeier's revolving line of credit, and later the 2002 personal guaranty, would be invalid under the statute of frauds because it would be an attempt to (re)create a mortgage based on an oral agreement.[4]

Finally, we acknowledge the parties' longstanding business relationship. But the parties simply cannot do, under the law, that which they did. Because the mortgage became null and void when the underlying debt was paid in full in 1998, it could not be used as security for the personal guaranty signed by Klapmeier in 2002. We agree with appellant that if the bank wanted to use a mortgage on the Land-O-Lakes property as security for the personal guaranty, it should have created a new mortgage. Although the record reflects that Klapmeier's hands are not entirely clean, the fact is that PNB could not collect on the $60,000 from the sale of the Land-O-Lakes property because the mortgage was no longer valid due to Klapmeier's payment in full of the mortgage in

[4] We note that the parties did not argue, and we do not address, whether or to what extent partial performance of the parties' oral agreement might take this case out of the statute of frauds. *Cf. Rosenberg v. Heritage Renovations, LLC*, 685 N.W.2d 320, 325–26 (Minn. 2004) (noting general rule that partial performance can take an oral agreement out of the statute of frauds). We also note that an agreement to use an old mortgage to secure a new debt or revolving line of credit, rather than satisfying the old mortgage and creating a new mortgage to secure the new debt or credit line, appears to run afoul of Minnesota tax law, which imposes a tax on the amount of debt that is secured by the recorded mortgage of real property. *See* Minn. Stat. § 287.035 (2006).

April 1998. Accordingly, we reverse and remand for proceedings consistent with this opinion.[5]

Reversed and remanded.

[5] PNB filed a notice of review claiming that the district court erred in denying its request for attorney's fees. Because we are reversing the district court's decision, PNB's attorney's-fee argument is moot.