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STATE OF MINNESOTA
IN COURT OF APPEALS
A09-1960

Construction Mortgage Investors Co.,
Appellant,

vs.

Darrel A. Farr Development Corp., et al.,
Defendants,

Darrel A. Farr,
Respondent.

Filed August 10, 2010
Reversed and remanded
Bjorkman, Judge

Hennepin County District Court
File No. 27-CV-07-13740

Kay Nord Hunt, Keith J. Broady, Lommen, Abdo, Cole, King & Stageberg, P.A., Minneapolis, Minnesota (for appellant)

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Considered and decided by Larkin, Presiding Judge; Shumaker, Judge; and Bjorkman, Judge.

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

BJORKMAN, Judge

Appellant challenges the judgment denying enforcement of a personal guaranty against respondent. Because (1) the district court erred as a matter of law in concluding

that the personal guaranty is unenforceable because it is ambiguous and (2) the clear terms of the personal guaranty mandate entry of judgment in favor of appellant, we reverse and remand.

FACTS

Appellant Construction Mortgage Investors Co. (CMIC) lends money to land developers. Darrel A. Farr Development Corporation (DAFDC) is a residential land development company founded by respondent Darrel A. Farr. Farr chairs DAFDC's board of directors and owns 70% of the company's stock. Lucinda Gardner, Farr's daughter, is DAFDC's president, a minority shareholder, and is responsible for most of the corporation's daily operations.

This appeal concerns loan transactions related to DAFDC's development of land near Otsego. CMIC provided the initial funding for the development project in 2002. As the project continued, DAFDC obtained additional loans from CMIC. On May 24, 2005, DAFDC and CMIC agreed to restructure the various loans into a four million dollar "revolver loan." The revolver loan operated like a line of credit. As DAFDC continued development, it drew additional funds against the revolver loan. But DAFDC was obligated to make monthly interest payments on the borrowed funds.

In late 2006, the primary purchaser of lots in the Otsego development informed DAFDC that it would not purchase additional lots. Due to the resulting loss of cashflow, DAFDC sought to modify the terms of the revolver loan to suspend the monthly interest payments for one year. After several months of negotiations, CMIC provisionally agreed to suspend the interest payments, but only if Farr signed a personal guaranty and DAFDC

provided additional collateral in the form of a first mortgage on a property with a value of at least $400,000.

In February 2007, while the negotiations continued, CMIC drafted a personal guaranty to be signed by Farr. The personal guaranty contained the following recitals:

> WHEREAS, [DAFDC] has requested that [CMIC] suspend the requirement of payment of monthly interest, and [CMIC] has agreed to do so provided [Farr] provides [CMIC] with this Guaranty; and
>
> WHEREAS, [Farr] will derive a personal benefit from the agreement of [CMIC] to suspend the requirement of paying interest on a monthly basis and accordingly, is willing to execute this Guaranty.

The operative language of the personal guaranty did not reference any suspension or reduction of DAFDC's monthly interest payment obligation. Rather, the operative language bound Farr to the terms of the revolver loan and permitted CMIC to alter those terms without notice to Farr.

DAFDC was unable to locate a suitable property to provide additional collateral. Although the property that DAFDC offered met the $400,000 value requirement, it was subject to a $150,000 first mortgage. CMIC agreed to accept the property as collateral on the condition that DAFDC pay one-half of the monthly interest due on the revolver loan. Gardner agreed to this on behalf of DAFDC. CMIC prepared an amended loan agreement (loan amendment), which documented the parties' agreement:

> 1. All references in the loan documentation to the Note or the Loan Agreement will be deemed to refer to the Note or Loan Agreement as modified by this document, and all references in any of the loan documentation to a Guaranty

> or Guarantor shall be deemed to include Farr and the Guaranty provided in connection with this Agreement.
>
> 2. Farr agrees to execute and deliver to [CMIC] a Guaranty of the indebtedness evidenced by the Note and Loan Agreement in a form that is acceptable to [CMIC], and further agrees that the concessions being made by [CMIC] to [DAFDC] as part of this Agreement provide a distinct benefit to Farr and constitute adequate consideration to support the Guaranty.
>
> . . . .
>
> 4. [CMIC] agrees to extend the date of maturity of the Note to January 1, 2008 and further agrees to modify the Note to provide for monthly payments of one half the interest accruing under the Note, commencing in January, 2007. All unpaid interest will be compounded and will be added to the principal balance of the Note on a monthly basis.
>
> 5. Except as expressly amended and modified by the terms of this document, the Note and Loan Agreement are hereby ratified and confirmed and shall remain in full force and effect according to the originally stated terms.

Farr signed the personal guaranty and the loan amendment in April 2007. The recital portion of the personal guaranty had not been revised to reflect the fact that DAFDC was obligated to pay one-half of the monthly interest payments. Farr read the personal guaranty before he signed it, but did not read the loan amendment. He later testified that he would not have signed the personal guaranty if he knew that the loan amendment required DAFDC to pay one-half of the monthly loan interest.

In May 2007, the parties learned that CMIC could not obtain a second mortgage on the collateral property because Farr's ex-wife held the title. DAFDC admits that its failure to deliver the collateral breached the loan amendment.

CMIC commenced this action, alleging, among other claims, that Farr is personally liable for DAFDC's breach pursuant to the personal guaranty. CMIC moved for summary judgment against all defendants. The district court granted CMIC's motion as to DAFDC and Gardner, but denied summary judgment as to Farr. The district court concluded that, when read in conjunction, the personal guaranty and the loan amendment's interest-payment provisions were ambiguous, creating an issue for trial.

After a three-day bench trial, the district court determined that the personal guaranty is void because there was no meeting of the minds, and, if there were a contract, it is unenforceable because of mutual and unilateral mistake and the failure of CMIC to meet the condition precedent of suspending interest payments.

CMIC moved for amended findings of fact and conclusions of law under Minn. R. Civ. P. 52.02. The district court denied the motion, stating that "[CMIC's] motion does not make any new legal or factual arguments" and therefore was procedurally barred. This appeal follows.

D E C I S I O N

I. The issues of ambiguity and condition precedent are subject to review by this court.

Farr asserts that the issue of ambiguity is not appealable because it was disposed of when the district court denied CMIC's motion for summary judgment. CMIC contends that Farr did not properly plead the affirmative defense of condition precedent at trial. We disagree with both contentions.

Farr cites *Bahr v. Boise Cascade Corp.*, 766 N.W.2d 910, 919 (Minn. 2009), for the proposition that when a district court denies a motion for summary judgment, the issue presented in the motion is not within the scope of an appeal following entry of final judgment. This argument is unavailing. The *Bahr* court stated that if the denial of summary judgment was based on an issue of law, rather than fact, the issue is within the scope of appellate review of the final judgment. 766 N.W.2d at 919 n.9. And we are not persuaded by Farr's argument that CMIC was obligated to renew its argument at trial or bring a posttrial motion to preserve the ambiguity issue. Whether a contract provision is ambiguous is a legal issue CMIC properly raised in its summary-judgment motion. *See Hoffman v. N. States Power*, 764 N.W.2d 34, 53 (Minn. 2009). Therefore, a posttrial motion was not necessary. *See Alpha Real Estate Co. of Rochester v. Delta Dental Plan of Minn.*, 664 N.W.2d 303, 311 (Minn. 2003) ("[M]otions for a new trial pursuant to Minn. R. Civ. P. 59.01 are not a prerequisite for appellate review of substantive questions of law when a genuine issue of law is properly raised and considered at the district court level.").

CMIC contends that the condition-precedent issue is not properly before this court because Farr did not plead this affirmative defense with the specificity required by Minn. R. Civ. P. 9.03. But "[w]hen issues not raised by the pleadings are tried by express or implied consent of the parties, they shall be treated in all respects as if they had been raised in the pleadings." Minn. R. Civ. P. 15.02. While CMIC is correct that Farr did not initially plead this affirmative defense, it was the subject of cross-examination, Farr raised the issue in a posttrial motion, and CMIC had an opportunity to respond on the

merits. Because the issue was raised before the district court and CMIC had the opportunity to respond, we conclude that the issue is properly before this court.

II. Farr's personal guaranty is unambiguous and enforceable.

"Whether a contract is ambiguous is a question of law that we review de novo." *Carlson v. Allstate Ins. Co.*, 749 N.W.2d 41, 45 (Minn. 2008). Contract language is ambiguous if it is "reasonably susceptible to more than one interpretation." *Brookfield Trade Ctr., Inc. v. County of Ramsey*, 584 N.W.2d 390, 394 (Minn. 1998). "In interpreting a contract, the language is to be given its plain and ordinary meaning." *Id.* Recitals are not a part of the contract and are not legally binding. *Berg v. Berg*, 201 Minn. 179, 189, 275 N.W. 836, 842 (1937); *see also State by Crow Wing Envtl. Prot. Ass'n, Inc. v. City of Breezy Point*, 394 N.W.2d 592, 596 (Minn. App. 1986) (stating that contract recitals are statements of intent—they are not part of the contract itself), *review denied* (Minn. Dec. 17, 1986). But recitals may be used to resolve ambiguity in the operative provisions of the contract because they indicate the parties' intent. *Berg*, 201 Minn. at 189, 275 N.W. at 842.

The operative terms of the personal guaranty provide:

> 1. [Farr] absolutely and unconditionally guarantees to [CMIC] the full and prompt payment and performance of any and all indebtedness . . . to [CMIC] . . . under the Loan Documents or under any other loan, contract or agreement between [DAFDC] and [CMIC]. . . . In the event that [DAFDC] fails to observe or perform any terms or conditions to be kept or performed by [DAFDC] . . . [Farr] agrees to pay upon demand the Indebtedness together with any expenses or costs of collection . . . incurred by [CMIC]. . . .

. . . .

> 4. [CMIC] may take the following action without further authorization from or notice to [Farr] and without affecting or impairing the liability of [Farr]: . . . (c) modify or amend the terms and conditions of the Loan Documents. . . .

Farr does not argue that these terms themselves are ambiguous and we discern no ambiguity. The operative terms do not refer to monthly interest payments or any of the other payment terms contained in the loan amendment. Rather, the operative terms of the personal guaranty clearly state that Farr guarantees DAFDC's obligations under the loan amendment, whatever those terms may be. And the personal guaranty expressly authorizes CMIC to further alter the terms and conditions of the loan amendment at any time, without negating Farr's obligations under the personal guaranty.

The fact that Farr did not read the loan amendment before signing it is immaterial to our analysis. *See Huseman v. Life Ins. Co. of N. Am.*, 402 N.W.2d 618, 620 (Minn. App. 1987) (holding that a party signing a contract is bound by its terms whether the party read the contract or not, unless there is fraud, mistake, or unconscionable terms). Farr points out that the same principle should apply to CMIC—it should be charged with knowledge of the erroneous language in the recitals of the personal guaranty. But doing so does not alter Farr's legal responsibilities. Requiring CMIC to abide by the operative terms of both the personal guaranty and loan amendment would not change the fact that DAFDC is responsible for making the interest payments and providing the collateral required by the loan amendment.

Farr's argument that the personal guaranty's recitals are ambiguous or create ambiguity when read in conjunction with the loan amendment is unavailing. Although recitals may be useful in determining the intent of contracting parties when the operative terms of a contract are ambiguous, they cannot by themselves create ambiguity. *See Crow Wing*, 394 N.W.2d at 596. Farr relies on *Downing v. Indep. Sch. Dist. No. 9*, 207 Minn. 292, 301, 291 N.W. 613, 616 (1940), for the principle that recital language may create ambiguity. This reliance is misplaced. *Downing* involved a school-board resolution rather than a private contract, and the supreme court impliedly determined that the terms of the resolution were ambiguous and thus subject to construction. *Downing*, 207 Minn. at 301–02, 291 N.W. at 617–18.[1] Here, there is no ambiguity in the operative terms of either the personal guaranty or the loan amendment that would permit a court to look beyond the clear operative terms of the agreements.

Because the operative terms of the personal guaranty are unambiguous and clearly charge Farr with the responsibility for DAFDC's obligations under the loan amendment, the district court erred as a matter of law in denying relief to CMIC.

III. The district court clearly erred in finding that Farr may rescind his obligations under the personal guaranty due to mutual mistake, unilateral mistake, and the nonoccurrence of a condition precedent.

A district court's findings of fact are not reversed unless they are clearly erroneous. *Ebenhoh v. Hodgman*, 642 N.W.2d 104, 108 (Minn. App. 2002). "Findings of fact are clearly erroneous only if the reviewing court is left with the definite and firm

[1] The supreme court was divided in *Downing*. Three justices dissented on the basis that the operative terms of the resolution were clear and unambiguous. 207 Minn. at 305, 291 N.W. at 619 (dissenting opinion).

conviction that a mistake has been made." *Fletcher v. St. Paul Pioneer Press*, 589 N.W.2d 96, 101 (Minn. 1999) (quotation omitted). When reasonable evidence supports the district court's findings, we will not disturb them. *Rogers v. Moore*, 603 N.W.2d 650, 656 (Minn. 1999). But whether the findings of fact support the conclusions of law and judgment is a question of law that we review de novo. *Ebenhoh*, 642 N.W.2d at 108.

Mutual mistake of fact

"Where a mistake of both parties at the time a contract was made as to a basic assumption on which the contract was made has a material effect on the agreed exchange of performances, the contract is voidable by the adversely affected party unless he bears the risk of the mistake." Restatement (Second) of Contracts § 152(i) (1981), as quoted in *Winter v. Skoglund*, 404 N.W.2d 786, 793 (Minn. 1987). A mutual mistake only occurs when both parties have the same incorrect assumption about the terms of the contract. *Creative Commc'ns Consultants, Inc. v. Gaylord*, 403 N.W.2d 654, 657 (Minn. App. 1987). When parties merely disagree on the interpretation of a contract, there is no mutual mistake. *Id.*

CMIC argues that there was no mutual mistake of fact because CMIC and Farr had differing interpretations of the personal guaranty and the mutual-mistake doctrine only applies when the parties have the same erroneous belief as to a contract's provisions. We agree. It is undisputed that CMIC believed that the loan amendment eliminates only one-half of DAFDC's monthly interest obligations; but Farr believed that the interest payments were eliminated in full. Accordingly, Farr and CMIC had different understandings of what obligations the personal guaranty would secure. Because the

parties merely had differing interpretations of the loan amendment's terms rather than a shared misconception, the district court clearly erred in finding that there was a mutual mistake of fact.

Unilateral mistake

"A unilateral mistake in entering a contract is not a basis for rescission unless there is ambiguity, fraud, misrepresentation, or where the contract may be rescinded without prejudice to the other party." *Speckel by Speckel v. Perkins*, 364 N.W.2d 890, 893 (Minn. App. 1985). Farr does not allege, and the district court did not find, that CMIC engaged in fraud or misrepresentation or that either the personal guaranty or the loan amendment could be rescinded without prejudicing CMIC. The only claimed ground for rescission based on unilateral mistake is ambiguity. We have already concluded that the district court erred in determining that the personal guaranty is ambiguous. Accordingly, we conclude that the district court clearly erred in finding that Farr is entitled to rescind his obligations under the personal guaranty based on a unilateral mistake.

Condition precedent

A condition precedent is an act that must be performed or an event that must occur before a contractual right or duty accrues. *Carl Bolander & Sons v. United Stockyards Corp.*, 215 N.W.2d 473, 476 (Minn. 1974). If a condition precedent does not occur, the contract is unenforceable. *R.A., Inc. v. Anheuser-Busch, Inc.*, 556 N.W.2d 567, 570 (Minn. App. 1996), *review denied* (Minn. Jan. 29, 1997). Conditions precedent are

generally disfavored. *See Mrozik Constr., Inc. v. Lovering Assocs.*, 461 N.W.2d 49, 51-52 (Minn. App. 1990); *see also* Restatement (Second) of Contracts § 227 cmt. b (1981).

Recitals in a contract do not create binding obligations on a party. *Berg*, 201 Minn. at 189, 275 N.W. at 842. Because conditions precedent are binding obligations, it logically follows that they cannot be created in recital language. We conclude that if recitals cannot create binding obligations, they cannot create conditions precedent.

The district court erred in concluding that ambiguity precludes enforcement of the personal guaranty. The district court clearly erred in finding that the parties were operating under a mutual mistake of fact in connection with the personal guaranty. And because there is no ambiguity, the district court's conclusions of law relating to unilateral mistake and condition precedent are erroneous. Accordingly, we reverse and remand for entry of judgment in favor of CMIC.

Reversed and remanded.