

Western Caroline Trading Co. v. Fritz, 7 ROP Intrm. 264 (Tr. Div. 1998)
WESTERN CAROLINE TRADING COMPANY,
Plaintiff,

v.

HARRY FRITZ,
Defendant.

CIVIL, ACTION NO. 289-97

Supreme Court, Trial Division
Republic of Palau

Decided: December 1, 1998

Counsel for Plaintiff: David Shadel

Counsel for Defendant: Mark Doran

BEFORE: R BARRIE MICHELSEN, Associate Justice.

FACTS

In 1984, Harry Fritz leased property to Western Caroline Trading Company [“WCTC”]. The lease was set to expire in 2009, but Mr. Fritz desired an early termination. WCTC was willing to acquiesce to that request, provided the company was compensated for lost business income and for improvements and equipment on the property.

The terms were established in a promissory note signed by Mr. Fritz on June 1, 1994. In the note, Defendant promised to pay WCTC \$135,000 without interest. Payments are \$750 per month, due on the first day of each month, through the year 2009. The first payment was due July 1, 1994, but the note states “the first six (6) payments due hereunder do not need to be paid immediately but instead may be paid in one lump sum on or before June 1, 1999.” However, if the payments are not timely made, standard terms usually found in promissory notes become operative. **1265** Interest is charged from the date any payment is delinquent. The key term Plaintiff now sues to enforce is the acceleration clause:

In the event of default in the payment of any of the installments as herein provided, time being of the essence hereof, the holder of this note may, without notice or demand, declare the entire principal sum then unpaid, together with accrued interest thereon, immediately due and payable.

Mr. Fritz exercised his option not to make the first six payments when due. But in January 1995, he failed to make the seventh payment. Indeed, by October 1995 he had made no payments whatsoever, which meant he was ten payments behind. In a letter dated October 19, 1995, counsel for WCTC notified Mr. Fritz that the note was considered accelerated pursuant to

Western Caroline Trading Co. v. Fritz, 7 ROP Intrm. 264 (Tr. Div. 1998) the above-quoted acceleration clause and that payment should be made on the note through counsel. The letter gave Mr. Fritz a deadline of twenty days to pay the full amount then due (\$142,149.14) or suit would be commenced “promptly thereafter.”

This letter triggered the beginning of payments by Mr. Fritz, although the first payment was not made until December 1995, and it was only for one month’s payment of \$750. Mr. Fritz has continued to make monthly payments. WCTC did not carry out its intention to file suit as stated in its letter.

On September 26, 1996, counsel for WCTC sent another letter to Defendant requesting additional payments and informing him that the monthly payments were too low to even cover the accumulating interest. After receiving this letter, Defendant continued to make monthly payments in the amount of \$750. One year later, in September 1997, WCTC filed this lawsuit, and now requests that summary judgment be entered for the full amount of principal, plus interest, penalties, and reasonable attorney’s fees.

Defendant argues that by continuing to accept monthly payments for nearly two years without protest, WCTC has waived its rights under the acceleration clause, and is not entitled to judgment for the full amount, plus interest.

Because there are no statutes on point, and Palauan customary law does not address the law of commercial paper, American common law applies. 1 PNC § 303.

3. ACCELERATION CLAUSES GENERALLY

An acceleration clause

requires the maker, drawer or other obligator to pay part or all of the balance sooner than the date or dates specified for payment upon the occurrence of some event or circumstance described in the contract. Such clause operates when there has been a default such as nonpayment of principal, interest, or failure to pay insurance premiums.

Black’s Law Dictionary, 12 (6th ed. 1990). It “is a vehicle which permits a lender to protect against changes in credit risk which occur before maturity. Although acceleration clauses often serve the legitimate interests of holders, they also present the holder with potentially unfair power and are susceptible of misuse.” *WAMCO III Ltd. v. First Piedmont Mortgage Corp.*, 856 F. Supp. 1076, 1082 (E.D. Va. 1994). [Citations omitted]. Because of this potential, equitable principles apply to enforcement of such clauses. *Williamson v. Wanlass*, 545 P.2d 1145, 1148 (Utah 1976).

1266 Nonetheless, the determination of whether to invoke an acceleration clause is that of the creditor. *Browne v. Nowlin*, 570 P.2d 1246, 1248 (Ariz. 1977). Once all requirements for acceleration have been met, the creditor may demand full payment as per the agreement, and reject the usual monthly payments. *Salishan Hills. Inc. v. Kreiger*, 660 P.2d 160, 164 (Ore.

Western Caroline Trading Co. v. Fritz, 7 ROP Intrm. 264 (Tr. Div. 1998) 1983). However, depending on the circumstances a creditor may prefer to waive the acceleration clause, and the difficulties it may cause a debtor, if the payment schedule is placed back on track.

4. ACCELERATION CLAUSES AND WAIVER

When payments are accepted after default, there is often a question of whether acceptance of payments is a waiver of the acceleration clause. In this case Defendant argues that since he made nearly two years of payments subsequent to the notice of default and acceleration, and since WCTC took no further action to enforce its 1995 notice until filing this suit in 1997, the acceleration clause has been waived.

There are three relevant fact patterns concerning acceptance of payments and waiver of an acceleration clause:

- (1) Untimely payments are tendered, the creditor accepts the payments, accelerates the note based upon the untimeliness of the payments, then sues;
- (2) the creditor accelerates the note due to nonpayment of installment[s], then sues, and subsequently the debtor makes payments;
- (3) the creditor accelerates the note, payments are thereafter made and accepted, then the creditor sues;

With respect to the first scenario, if a debtor makes late payments, and the payments are accepted, those late payments cannot be a justification of a later acceleration. "Acceptance of a delinquent payment, prior to acceleration, cures the default and constitutes a waiver of the right to accelerate." *Browne v. Nowlin*, 570 P.2d 1246, 1248 (Ariz. 1977); accord, *Ashback v. Wenzel*, 346 P.2d 295, 297 (Colo. 1959). However, the creditor may renew an insistence on timely performance, and may enforce the acceleration clause against subsequent late payments. *Salishan Hills Inc. v. Krieger*, 660 P.2d 160, 163 (Ore. App. 1983).

Regarding the second fact pattern, if the note is accelerated, suit is thereafter instituted, and then the debtor tenders payments, such payments come too late. The acceleration clause being properly invoked and suit commenced, the debtor cannot claim it is inequitable to thereafter proceed. *Bank of Honolulu v. Anderson*, 654 P.2d 1370 (Hawaii App. 1982). *Commercial Sec. Bank v. Corporation Nine*, 600 P.2d 1000 (Utah 1979); *Puget Sound Bank v. Lillions*, 314 P.2d 935, 938 (Wash. 1957); *but see, Bisno v. Sax*, 346 P.2d 814, 819 (Cal. App. 1960) (acceleration considered waived by tender of all installments then due, at the time of trial).

When notice of default and acceleration is given because of non-payment but payments are thereafter made and accepted, "[s]peaking generally, the acceptance of payment of a delinquent installment of principal or interest cures that particular default and precludes a foreclosure sale based upon such pre-existing delinquency." *Bisno v. Sax*, 346 P.2d 814, 820 (Cal. Ct.App. 1960). However, if the tendered payments do not cure the entire default that existed at the time of the purported acceleration, there is no waiver. "For example, in *Oakland*

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Nat'l Bank v. 1267 Anderson, 81 Mich. App. 432, 265 N.W.2d 362, 364 (1978), the Court of Appeals of Michigan declined to consider an overdue payment made after acceleration a waiver, in part noting that the payment 'did not cure all the defaults which existed at the time.'" *FDIC v. Massengill*, 24 F.2d 768, 778 (5th Cir. 1994). However, a waiver may be found if the default that caused acceleration is rectified before commencement of litigation. In *Massengill*, the Fifth Circuit held that the creditor's acceleration clause was waived because the debtor corrected, and the creditor accepted, the actual default that had triggered the notice of acceleration. *Id.* at 778. Similarly, the Colorado Supreme Court held in *Barday v. Steinbaugh*, 272 P.2d 657 (Colo. 1954), that the acceptance of the very payments that caused the creditor to give notice of acceleration was a waiver of the acceleration. *Id.* at 658. "Manifestly, acceptance of payment of defaulted principal or interest cures that particular default." *Bisno v. Sax*, 346 P.2d 814, 820 (Cal.Ct.App. 1960).

In summary, the rules seem to be: 1) late payments which are accepted cannot be the basis of a later acceleration; 2) after acceleration, acceptance of all payments that caused the default is a waiver, and 3) payments accepted after institution of a civil action is not a waiver of the acceleration clause.

5. ANALYSIS

Applying these principles to the above case means that WCTC may proceed to deem the note accelerated, even if it accepted monthly payments afterward, unless the accepted payments cure the default that existed at the time of acceleration.

According to WCTC records, Mr. Fritz was in arrears \$14,649.14, including late payments and interest charges, on the date of acceleration; October 19, 1995. Subsequent payments prior to the filing of the lawsuit total \$16,500. Therefore, Mr. Fritz has cured the original default, and WCTC has waived its right to accelerate with respect to those payments. WCTC can rightly claim that Mr. Fritz is still in default because his payments are still behind. However, WCTC has not invoked the acceleration clause with respect to these later deficiencies.

This result is not inequitable. The note is not a repayment of a cash loan. It is part of a settlement reached regarding the early termination of a lease, to compensate WCTC for lost business income through the year 2009. WCTC remains entitled to receive \$135,000 pursuant to the note, and may charge interest on late payments. It has received \$27,000 to date, and no payments have been missed during 1996, 1997 or 1998. Plaintiff remains free to issue a new acceleration notice, or wait until the balloon payment is due next June to determine if Defendant is capable of meeting the terms of the note.

6. CONCLUSION

Acceptance of sums equal to or greater than the deficiency that was the reason for the acceleration waives the right to accelerate as to those amounts, if the payments were accepted before institution of litigation. Partial summary judgment is therefore granted to Defendant, because Plaintiff has waived notice of acceleration given in October 1995. Plaintiff may proceed

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to amend the complaint to seek recovery of the current delinquency only, or may dismiss without prejudice, reserving the right to file a subsequent complaint based upon a new acceleration at some later time during the remaining term of the note.