NO. 23441

IN THE INTERMEDIATE COURT OF APPEALS

OF THE STATE OF HAWAIʻI

REALTY FINANCE, INC., Plaintiff-Appellee, v.
THOMAS FRANK SCHMIDT; LORINNA JHINCIL SCHMIDT; and AMERASIAN LAND CO., a Nevada corporation, Defendants-Appellants, and KALOKO TWO PARTNERSHIP, a Hawaiʻi limited partnership; ASSOCIATION OF APARTMENT OWNERS OF THE MARCO POLO APARTMENTS, an unincorporated condominium association; LAWHN & KEEVER, a Law corporation; JOHN RAPP; DOUGLAS J. IGE; INVESTORS FINANCE, INC., a Hawaiʻi corporation; STATE OF HAWAIʻI, by and through the Chief, Oahu Collections Branch; JOHN DOES 1-50; JANE DOES 1-50; DOE PARTNERSHIPS 1-50; DOE CORPORATIONS 1-50; DOE ENTITIES 1-50; and DOE GOVERNMENTAL UNITS 1-50, Defendants; and TURLINGTON CORPORATION, as Successor-in-Interest to Defendant John Rapp, Party-In-Interest-Appellant

APPEAL FROM THE FIRST CIRCUIT COURT
(CIV. NO. 97-1235-03)

MEMORANDUM OPINION
(By: Burns, C.J., Watanabe and Lim, JJ.)

In this foreclosure case brought by Plaintiff-Appellee Realty Finance, Inc. (Plaintiff or Realty Finance), Defendants-Appellants Thomas Frank Schmidt (Schmidt) and Lorinna Jhincil Schmidt (collectively the Schmidts) and Amerasian Land Co.,[1] a Nevada corporation, (Amerasian), and Party-In-Interest-Appellant

[1] In the Declaration of Thomas Schmidt signed by Defendant-Appellant Thomas Frank Schmidt (Schmidt) on December 21, 1999, Schmidt states that he is "the Vice President of Amerasian Land Company, Inc."

Turlington Corporation (Turlington),[2] (collectively Appellants), appeal from "Plaintiff's Final Deficiency Judgment Based Upon Order Granting Plaintiff Realty Finance, Inc.'s Motion for Order Allowing Additional Attorneys' Fees and Costs and for Deficiency Judgment Against Thomas Frank Schmidt and Lorinna Jhincil Schmidt" entered by Circuit Court Judge Kevin S. C. Chang on June 9, 2000.[3] We affirm.

BACKGROUND

In 1991, Investors Finance, Inc. (Investors), loaned money to the Schmidts and, in return, received two promissory notes (Promissory Notes).

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[2] Attorney John Rapp (Rapp) was named a defendant as holder of a judgment lien on account of judgments entered in his favor against Schmidt and Defendant-Appellant Lorinna Jhincil Schmidt (collectively the Schmidts). Rapp assigned his judgments to Appellant Party-In-Interest Turlington Corporation (Turlington).

[3] For purposes of appeal, foreclosure cases are bifurcated into two, not three or more, separately appealable parts. Sturkie v. Han, 2 Haw. App. 140, 627 P.2d 296 (1981). The first part is the decree of foreclosure. Hawaii Rules of [Appellate Procedure Rule 4(a)'s] thirty-day appeal period begins to run upon its filing. Moreover, if, as in this case, the order of sale is included in the decree of foreclosure or if, as in Powers v. Ellis, 55 Haw. 414, 520 P.2d 431 (1974), an order of sale is entered subsequent to a decree of foreclosure and thereafter a party files an appeal which is timely as to both, then the decree of foreclosure and the order of sale are treated as a single final order for purposes of appeal.

The second part includes all other orders. With rare exception, all other orders are appealable upon the entry of the last of the series of orders which collectively embrace the entire controversy. Sturkie, supra. In foreclosure cases which result in a deficiency, the last and final order which starts the clock running is usually the deficiency judgment.

Hoge v. Kane I, 4 Haw. App. 246, 246-47, 663 P.2d 645, 647 (1983) (footnotes omitted).

The June 10, 1991 promissory note (June Note) states, in relevant part, that the Schmidts "promise to pay you, [Investors], on or before" June 15, 1996, the sum of $140,000, plus "simple interest figured on the unpaid balances of it at the initial simple annual rate of 13.5%[,]" in 60 payments of $1,821.05 per month commencing July 15, 1991, and concluding with a balloon payment of $121,411.77 on June 15, 1996, or "whenever you demand it before that date." It also states: "Late Charge: If a payment or part of a payment is late, I will be charged 5% of the amount that is late." This June Note was secured by a mortgage on a commercial condominium in the Marco Polo Apartments.

The July 11, 1995 promissory note (July Note) states, in relevant part, that the Schmidts promise to pay $225,000, plus interest, "to the order of the Lender. The Lender is INVESTORS FINANCE, INC., a Hawaii corporation. I understand that the Lender may transfer this Note. The Lender or anyone who takes this Note by transfer and who is entitled to receive payments under this Note will be called the 'Note Holder.'" The Schmidts promised to make payments of $2,250 per month commencing August 11, 1995, and to make a final balloon payment on April 10, 1996. The Schmidts also promised that

> [i]f the Note Holder has not received the full amount of any payment by the end of ten (10) calendar days after the date it is due, I will pay a late charge to the Note Holder. The amount of the late charge will be five percent (5%) of the overdue amount. I will pay this late charge only once on any late payment.

This July Note was secured by a mortgage on vacant Lot 4 in the Kaloko II Subdivision, Increment I, and vacant Lot 5 of the Kaloko II Subdivision, Increment II.

In October 1995, Investors transferred/assigned its interest in the Promissory Notes and mortgages to Realty Finance. On March 27, 1997, after the Schmidts defaulted, Realty Finance filed this foreclosure action and, pursuant to Hawaii Revised Statutes (HRS) §§ 501-151 and 634-51 (1993), filed a notice of pendency of action. HRS § 634-51 (1993) states, in relevant part, that "[f]rom and after the time of recording the notice, a person who becomes a purchaser or incumbrancer of the property affected shall be deemed to have constructive notice of the pendency of the action and be bound by any judgment entered therein if the person claims through a party to the action[.]"

On July 18, 1996, Realty Finance and the Schmidts executed a Loan Extension and Modification Agreement, allowing the Schmidts to pay the $121,134.18 balance due on the June Note, plus interest at the annual percentage rate of 13.50% per annum, at the rate of $1,821.05 per month commencing August 15, 1996, provided that the entire balance due would be paid on or before July 15, 1997.

On May 16, 1996, Realty Finance and the Schmidts executed a Loan Extension and Modification Agreement, allowing the Schmidts to pay the $224,968.67 balance due on the July Note,

plus interest at the annual percentage rate of 12% per annum, at the rate of $2,250 per month commencing June 15, 1996, provided that the entire balance due would be paid on or before May 15, 1997.

On December 17, 1997, Realty Finance moved for a summary judgment and an interlocutory decree of foreclosure.

On January 14, 1998, the Schmidts, Amerasian, and Defendant Kaloko Two Partnership (Kaloko Two) filed an answer and a counterclaim. The answer stated "that said note and mortgage is in default due to the fraud and misappropriation and/or misapplication of the construction loan proceeds which prevented the sale of the house which was pre-sold and for which the proceeds from the sale of such house would have paid [Realty Finance] in full."

The counterclaim alleged that:

1. Realty Finance is liable for its own acts and the acts of Investors.

2. Amerasian guaranteed the Schmidts' obligation to pay Realty Finance.

3. Schmidt had an approximate twenty-six-year business relationship with Investors.

4. Schmidt wanted

> 7. . . . a construction loan for a subdivision development of at least 16 homes with an initial loan to construct a home that was a pre-sold 3 acre parcel . . . to a Terry Llewellyn (Llewellyn) for the one (1) acre portion of a proposed CPR [Condominium Property Regime] and a pre-sale to a Dennis Smith

> for $200,000.00 for the two (2) acre portion of the same lot. SCHMIDT represented that all he had to do was complete the house and the CPR approval for said 3 acre parcel and needed about $225,000 to do so.
>
> 8. SCHMIDT also offered an additional three (3) acre lot as extra collateral and represented that he could sell off one (1) acre of that lot for $150,000.00 on another CPR (SCHMIDT had pre-sold the 1 acre CPR lot to a G. Helsinga for $150,000.00). If the house and CPRs were finished SCHMIDT was to receive $590,000.00 in sales proceeds, which was enough to retire the $225,000.00 loan and the remaining land costs.

5. Investors agreed to the loan, to a schedule for the withdrawal of funds, and to reduce the interest rate on the June Note from "13% to 9%."

6. Investors agreed that Cal Anglin, President of Molokai Supply, Inc., would coordinate the construction of Llewellyn's house, and Nelson Rapoport, a licensed contractor, would do timely inspections for $2,500.

7. Investors agreed that the performance guaranty by Molokai Supply, Inc., would be acceptable in lieu of a performance bond.

8. Investors violated the agreement in various ways, such as by asserting absolute control over the construction loan proceeds, failing to facilitate the CPR applications or construct the Llewellyn's house, and using some of the funds to construct "the Hartsock's house" because Investors needed the money for that project.

9. Investors admitted that the performance guaranty was unenforceable.

10. Realty Finance, in July 1996, falsely represented that "the loan purchased by [Realty Finance], was a 'very well secured land loan' and not a construction loan."

11. Upon the demand of Investors, the Schmidts agreed to an additional loan of $60,000, and Investors agreed to finish the Llewellyn house in 90 days.

12. Investors failed to pay for the items they agreed to pay with the $60,000 and instead, "misappropriated or embezzled" approximately $10,000 and "fraudulently modified the note and mortgage documents."

13. Llewellyn canceled the purchase of his house.

Copies of three documents were attached to the counterclaim. One document was a letter from Investors to the Schmidts signed by Investors[4] and the Schmidts. It was dated July 11, 1995, and states, in relevant part, as follows:

> RE: Your Loan No. REL/16743, Dated 7/11/95 in the amount of $225,000.
>
> In regards to the mortgage loan referred to above, the mortgage document . . . which secures the promissory note for this loan, provides for a requirement, . . . that you must receive prior written consent from [Investors] before you may construct improvements on the premises of the mortgaged property.
>
> You have provided IFI with a copy of the plans and specifications for the single family house you will build on the mortgaged property from funds advanced from the subject loan. You have agreed to furnish IFI with a guarantee from Molokai Supply Company for the sum of $100,000 required to pay for all labor and materials to construct this house to completion. IFI has set aside in a savings account the sum of $115,000 from the proceeds

[4] This document was signed for Defendant Investors Finance, Inc., by its President, David D. Hill.

> of the loan, which will be used to disburse funds in several increments, as approved by IFI, for the purpose of paying for labor and materials in the construction of the dwelling.
>
> . . . Borrowers are aware that IFI has provided for a contingency amount of $15,000 over the guaranteed amount of $100,000 provided to complete the house, and borrowers agree that IFI may rely upon this contingency to disburse funds to Molokai Supply Co. to pay for certain expenses in advance for which no actual work has been completed. . . . It is not intended that such disbursements will increase the total cost above $100,000, but simply be available for costs not ordinarily paid out until work has been completed.
>
> In consideration of the above, please be advised that [Investors] grants permission for borrowers to proceed with the construction of the single family house on the mortgaged property.

Another document, also dated July 11, 1995, was signed by the Schmidts and stated, in relevant part, as follows:

> IRREVOCABLE COLLATERAL AGREEMENT
> ASSIGNMENT OF PASSBOOK ACCOUNT
>
> TO: INVESTORS FINANCE, INC.
>
> [The Schmidts] hereby assign to [Investors] the PASSBOOK ACCOUNT . . . with an original balance of $115,000 as of July 11, 1995, deposited with [Investors]. . . .
>
> It is understood that the funds deposited in this account were disbursed from the proceeds of the mortgage loan . . . for the purpose of providing funds for the construction of a single family dwelling to be constructed on Lot 4, Koloko II Subdivision, Increment I, ...
>
> . . . .
>
> In executing this assignment, we authorize any officer of [Investors] to disburse funds from this account as required to promptly pay all appropriate billings submitted to [Investors] by Molokai Supply Co. . . .
>
> In executing this assignment, we also agree that should our loan become delinquent 30 days or more, you are authorized, at your discretion, to withdraw funds that may be in excess of funds needed to complete the construction of the dwelling to pay any such balances due, including late charges.

After a hearing on January 26, 1998, the circuit court entered a February 24, 1998 Judgment deciding that the Schmidts owed Realty Finance (a) a principal balance of $121,123.18, plus $9,363.82 interest, plus interest at the rate of $44.8031 per day

accruing from and including February 13, 1997, and (b) a principal balance of $224,968.67, plus $15,098.99 interest, plus interest at the rate of $73.9623 per day accruing from and including February 13, 1997, and:

> 4. That [Realty Finance] is entitled to foreclose its mortgages.
>
> 5. That the subject properties shall be sold at foreclosure free and clear of all liens and encumbrances whatsoever, and subject to confirmation of said sale by this Court. . . .
>
> 6. That this Court reserves jurisdiction to confirm the foreclosure sale and to determine the following: (1) the amount of real property taxes due, if any; (2) the fees, costs and expenses to be awarded to the Commissioner and the attorneys; (3) any additional sums owed to [Realty Finance] under its mortgages, including interest and advances under the mortgages subsequent to the entry of this Judgment; (4) if applicable, the amount of any deficiency judgment to be entered against [the Schmidts], jointly and severally; and (5) if applicable, the disposition of any surplus from the proceeds of the foreclosure sale.

(Emphasis added.) This February 24, 1998 Judgment contained language that finalized it in accordance with Hawai‘i Rules of Civil Procedure (HRCP) Rule 54(b).[5]

On March 6, 1998, the Schmidts, Kaloko Two, and Amerasian filed a motion for reconsideration, HRCP Rule 59(e), and for relief, HRCP Rule 60(b)(6). The memorandum in support of this motion alleges, in relevant part, as follows:

> [Realty Finance] participated in distributing said construction loan funds directly or under the direction of [Investors] who had taken over the sole custody and distribution of said construction funds. The ledger of **financial transactions is clearly under Plaintiff Real Estate Finance's business logo** and **takes place prior to October 31, 1995**, the closing date of the purchase of the loans from [Investors].

[5] Utilization of Hawai‘i Rules of Civil Procedure (HRCP) Rule 54(b) was unnecessary. See footnote 3 above.

(Emphasis in the original.) This motion was denied by an order entered on June 3, 1998.

The Schmidts had thirty days after June 3, 1998, to file a notice of appeal. They did not do so. The February 24, 1998 Judgment was not appealed. Therefore, the matters decided therein are res judicata. Sturkie v. Han, 2 Haw. App. 140, 146-47, 627 P.2d 296, 301-02 (1981).

On June 9, 1998, the court entered its "Order Granting Plaintiff Realty Finance, Inc.'s Motion to Authorize Commissioner to Conduct Auction Without Open Houses." Similar orders were entered on October 12, 1999, and on November 2, 1999.

On June 12, 1998, well within the thirty days allowed for the appeal of the June 3, 1998 order and the February 24, 1998 Judgment, the circuit court entered "Findings of Fact and Conclusions of Law."[6] This document states, in relevant part, as follows:

> **CONCLUSIONS OF LAW**
>
> A. Pursuant to the June and July Assignments, and H.R.S. § § 490:3-302 and 490:3-305(a), [Realty Finance], as a holder in due course, may enforce the subject Notes and Mortgages free of any personal defenses [the Schmidts] may have or may assert.
>
> B. As of February 13, 1997, there was due and owing from [the Schmidts] to [Realty Finance] under the June Note, . . . the principal balance of $121,134.18 . . . ; plus interest as of February 13, 1997, in the amount of $9,363.82 . . . . Interest continues to accrue at the rate of $44.8031 per day, from and including February 13, 1997, together with such other and further amounts as the Court shall subsequently

[6] The same findings and conclusions had been filed on February 24, 1998, but that document was signed by the "Attorneys for Plaintiff" who had prepared and presented it, rather than the court.

> determine to be lawfully chargeable . . . , including interest, costs, expenses, other charges, and attorneys' fees, as the Court shall determine.
>
> C. As of February 13, 1997, there was due and owing from [the Schmidts] to [Realty Finance] under the July Note, . . . the principal balance of $224,968.67 . . . ; plus interest as of February 13, 1997, in the amount of $15,098.99 . . . . Interest continues to accrue at the rate of $73.9623 per day, from and including February 13, 1997, together with such other and further amounts as the Court shall subsequently determine to be lawfully chargeable . . . including interest, costs, expenses, other charges, and attorneys' fees, as the Court shall determine.

(Emphases added.)

On July 10, 1998, Realty Finance filed its motion to confirm a private sale to Waikiki Investments 418, Inc. (Waikiki 418), for the following prices:

Kaloko II Subdivision, Increment I, Lot 4	$135,000
Kaloko II, Subdivision, Increment II, Lot 5	$135,000
Marco Polo Apartments Commercial Unit 2	$160,000

On September 4, 1998, Realty Finance moved "for an order granting summary judgment and dismissing the Counterclaim[.]" This motion was based on the court's decision that Realty Finance was a holder in due course. This motion was granted by order entered on August 16, 1999, dismissing the counterclaim with prejudice. The judgment was entered on September 8, 1999, and finalized as authorized by HRCP Rule 54(b). This judgment was not appealed. Therefore, the matters decided therein are res judicata.

On October 15, 1998, Turlington, represented by attorney Jerry A. Ruthruff, purchased from John Rapp for $348,000

two recorded judgments against the Schmidts and all rights and claims in Civil No. 94-0903-03, First Circuit Court, State of Hawai‘i, including attorney fees, costs and interest.

"[E]ffective as of the 31st day of December, 1998," Realty Finance, as Seller, and Waikiki 418, as Purchaser, entered into a Purchase and Sale Agreement[7] that states, in relevant part, as follows:

> A G R E E M E N T
>
> For valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:
>
> 1. Purchase and Sale of Interest. [Realty Finance] agrees to sell to [Waikiki 418], and [Waikiki 418] hereby agrees to purchase from [Realty Finance], the Loan Documents[8] at the purchase price and pursuant to the terms and conditions set forth in this Agreement.
>
> 2. Purchase Price. The Purchase Price to be paid by [Waikiki 418] to [Realty Finance] for the Loan Documents is [$450,000] (the "Purchase Price"). The Purchase Price shall be consideration for full and complete value of the Loan Documents as and at the Closing without regard to the actual outstanding loan balance due seller, under the Loan Documents . . . .

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[7] This December 31, 1998 Purchase and Sale Agreement was signed for Plaintiff-Appellee Realty Finance, Inc. (Realty Finance), by its President Richard Henderson and its Treasurer Michael S. Chagami. It was signed for Waikiki Investments 418, Inc. (Waikiki 418), by its President, Peter G. Fredericksen. We note that the certificate of service of the December 22, 1999 "Supplemental Memorandum of Turlington Corporation, as Successor in Interest to Defendant John Rapp, in Opposition to Plaintiff Realty Finance, Inc.'s Motion for Order Approving Commissioner's Report and for Distribution of Proceeds and Allowing Attorneys' Fees and Expenses (Motion Filed December 14, 1999)" was signed as follows:

> [signature]
> PETER G. FREDERICKSEN
> Assistant to JERRY A. RUTHRUFF
> Attorney for
> TURLINGTON CORPORATION

[8] The December 31, 1998 Purchase and Sale Agreement describes the "Loan Documents" as "The June Note, June Mortgage, July Note, July Mortgage, Assignment of Rents, June Assignment, July Modification Agreement, Corrected July Mortgage, July Assignment and May Modification Agreement[.]"

> 3. Payment of Purchase Price. A sum of $100,000.00 shall to be paid to [Realty Finance] on or before January 8, 1999. The remaining balance of the Purchase Price shall bear interest at 10% per annum. The balance of the Purchase Price due shall be payable . . . by June 30, 1999 . . . . Should [Waikiki 418] make a payment of not less than $200,000.00 (the "Second Installment") prior to June 30, 1999, [Realty Finance] shall extend the repayment period for the remaining sums payable for a further three months or until September 30, 1999, whichever is sooner. Upon the payment of the Second Installment, [Realty Finance] shall consent to [Waikiki 418's] release of the lien as to Lot 4 of the Kaloko Property.
>
> 4. Security. As security for the payment of the Purchase Price, [Waikiki 418] shall assign the Loan Documents to [Realty Finance].
>
> 5. Release of Claims by Schmidts. [Waikiki 418] shall obtain the written Release of Claims against [Realty Finance] in a form provided by [Realty Finance], by no later than thirty (30) days from Closing as provided in paragraph 7 herein.
>
> 6. Default. In the event of [Waikiki 418's] default in payments pursuant to paragraph 3 herein . . . , (a) [Realty Finance] shall have the right to retain all monies paid to [Realty Finance], (b) [Realty Finance] shall have the right to immediately record the Assignment of Notes and Mortgages, to be executed by [Waikiki 418] concurrently herewith, (c) [Waikiki 418] shall have no further rights pertaining to the Loan Documents (d) [Realty Finance] shall proceed with any foreclosure action pertaining to the Properties described in the Loan Documents and (e) [Realty Finance] shall exercise any other right or remedy [Realty Finance] may have at law or in equity by reason of the default.
>
> 7. Closing. Subject to the satisfaction or waiver of all conditions to the obligations of the parties to consummate the transactions contemplated hereby, the purchase and sale of [Realty Finance's] right, title and interest in, to and under the Loan Documents shall take place (the "Closing") on December 31, 1998 (Hawaii standard time), or at such earlier date as may be mutually agreed upon by the parties hereto (the "Closing Date"), at such location as shall be mutually agreed upon.

(Footnote added.)

On December 31, 1998, Realty Finance executed an Assignment of Notes and Mortgages, which stated that Realty Finance "does hereby, without recourse sell, assign, transfer, set over and deliver unto [Waikiki 418] . . . those certain mortgages . . . together with the notes described therein and the

money due or to become due thereon with the interest provided therein[.]"

On December 31, 1998, Waikiki 418 executed the Assignment of Notes and Mortgages as Security and Security Agreement mentioned in the Purchase and Sale Agreement. This document states, in relevant part, as follows:

> WHEREAS, [Realty Finance] is the current holder of two Simple Interest Notes, ...
>
> . . . .
>
> . . . (The June Note, June Mortgage, July Note, July Mortgage, Assignment of Rents, June Assignment, July Modification Agreement, Corrected July Mortgage, July Assignment and May Modification Agreement, shall be referred to collectively hereinafter as the "Loan Documents").
>
> . . . .
>
> WHEREAS, Pursuant to the Purchase and Sale Agreement dated December 31, 1998 ("Sale Agreement"), [Waikiki 418] has purchased the Loan Documents for the consideration of $450,000.00; and
>
> . . . .
>
> NOW, THEREFORE, . . . in order to secure the timely payment pursuant to the Sale Agreement . . . , [Waikiki 418] does hereby assign to [Realty Finance] all of the right, title and interest of [Waikiki 418] in, to and under the Loan Documents.
>
> TO HAVE AND TO HOLD the same unto [Realty Finance], its successors and assigns, absolutely and forever.
>
> TOGETHER WITH all sums payable under the Loan Documents, including without limitation, principal and interest, as they respectively become due, and the right to enforce the Loan Documents.
>
> PROVIDED, HOWEVER, if [Waikiki 418] shall pay in full said Sale Agreement, . . . this assignment shall cease to exist and [Realty Finance] will, upon request of [Waikiki 418] re-assign to [Waikiki 418] the property and rights assigned to [Realty Finance] hereunder; AND, PROVIDED FURTHER, that so long as [Waikiki 418] shall not be in default under the Sale Agreement, under this instrument, or under any other instrument or agreement evidencing or securing the Sale Agreement . . . , [Waikiki 418] shall have a revocable license to collect the sums accruing by virtue of the Loan Documents, and to enforce said instrument. Said license shall be automatically revoked without notice upon the occurrence of any event of default.

Realty Finance did not sign this document. Waikiki 418 paid the $100,000 payment, and Realty Finance "applied this payment towards the outstanding loan balances."

The undated Receipt states, in relevant part, as follows:

RECEIPT

Waikiki Investments 418, Inc. acknowledges receipt of $534,000[.]00 from:

Phoenix Investments 418, Inc./Lulani Properties, LLC/Amerasian Land Co., Inc. on promissary [sic] notes and Mortgages assigned to Waikiki Investments 418, Inc. by:

Assignment Of Notes And Mortgages
Recorded January 7, 1999 as document Number _____

WAIKIKI INVESTMENTS 418, INC.

[signature]
ROBERT J. AUSTIN
President

Each check ($225,000 and $309,000) is dated June 23, 1999. The $225,000 check is on James L. Watson's account at the Bank of Hawaii. The $309,000 check is on a Bank of Hawaii account of an unidentified person or entity of Charles Schwab.

On May 13, 1999, Realty Finance filed and served by mail on all parties in the case[9] "Plaintiff Realty Finance Inc.'s Notice of Transfer of Real Party in Interest" giving notice "that, on December 31, 1998, the Real Party in Interest as defined by HRCP Rule 17(a) for the above captioned matter became [Waikiki 418] in place of [Realty Finance] and [Waikiki 418's] attorney of record is Jerry A. Ruthruff, Esq."

[9] George K. Noguchi, who was then the attorney for the Schmidts, Defendant Kaloko Two Partnership and Defendant-Appellant Amerasian Land Co., a Nevada corporation, was one of those who was served.

Waikiki 418 did not make the payment it owed Realty Finance on June 30, 1999, and it did not make any subsequent payment to Realty Finance.

On October 25, 1999, Realty Finance filed a motion for order approving confirmation of private sale of subject properties. The memorandum in support of the motion stated, in relevant part, as follows:

> 1. [The Schmidts] are the owners in fee simple of the Kaloko Properties and the leaseholders of the Marco Polo Property.
>
> . . . .
>
> 4. On October 15, 1999, pursuant to the DROA [Deposit Receipt Offer and Acceptance], [the Schmidts] and buyers, [Amerasian] entered into a contract for the purchase and sale of the Marco Polo Property and the Kaloko II Lot 5 Properties, for a total purchase price of $200,000. . . .
>
> 5. On October 18, 1999, pursuant to the DROA, [the Schmidts] and buyers, Lulani Properties LLC [(Lulani)] entered into a contract for the purchase and sale of the Kaloko II Lot [4] Property for a total purchase price of $300,000. . . .
>
> . . . .
>
> III. ANALYSIS
>
> Realty Finance requests that this Court approve the sale of the Subject Properties, as the price appears to be fair for the Subject Properties, and is most likely greater than the price that would be obtained if the Subject Properties were sold in foreclosure. Therefore, confirming this sale, [sic] is in the best interests of [the Schmidts], Realty Finance and the creditors of [the Schmidts].
>
> IV. CONCLUSION
>
> Based on the foregoing, Realty Finance respectfully asks that this Court issue an order confirming the sale of the Subject Properties pursuant to the Sales Contracts, without prejudicing Realty Finance's right to seek a deficiency on the sale.

This memorandum is misleading. The October 15, 1999 DROA is initialed only by the buyer (Amerasian) and is only an offer to buy. The October 18, 1999 DROA is initialed only by the

buyer (Lulani) and is only an offer to buy.[10] The October 15, 1999 DROA states, in relevant part, as follows:

> **OTHER SPECIAL TERMS** . . .
> 1) [Amerasian] acknowledges and agrees that it is purchasing the properties by way of a foreclosure sale with a standard Commissioner's deed, with no warranties or representations and that the properties are being conveyed "As Is". 2) [Amerasian] shall pay for closing costs and escrow fees per standard foreclosure practice. 3) Sale is subject to court approval. 4) Buyer understands and agrees the Commissioner is making no warranties or representations regarding asbestos or hazardous wastes on the subject property. 5) [Amerasian] understands that, subject to Court order, [Amerasian] may forfeit or lose some or all of the down payment should [Amerasian] default on the transaction herein.

On October 27, 1999, the Commissioner's Report was filed recommending acceptance of the private offers. On November 1, 1999, the court entered its "Order Denying Motion of Lulani Properties, LLC, for Leave to Intervene in Proceeding, Filed September 10, 1999." The primary concerns were "judicial economy and judicial efficiency" and "timeliness of the motion to intervene." At a hearing on December 2, 1999, the court stated, in relevant part, that "the court will grant and approve the private sale of the subject properties as set forth and described in the motion for order approving confirmation of private sale of subject properties filed on October 25, 1999, and as further amended on the record this morning by counsel[.]"[11]

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[10] Not all of the pages of Lulani Properties, LLC's (Lulani) October 18, 1999 Deposit Receipt Offer and Acceptance are in the record.

[11] It appears that the amendment pertained to an understanding that purchaser Lulani would satisfy a mechanic's lien on Lot 4.

On December 14, 1999, "Realty Finance, Inc.'s Motion for Order Approving Commissioner's Report and for Distribution of Proceeds and Allowing Attorneys' Fees and Expenses" was filed. This motion noted that as of December 8, 1999, the Schmidts owed the following amounts for the following loans:

Loan No. 204-16089 (secured by Marco Polo condo unit)	
Principal Balance	$ 70,549.63
Interest	24,653.83
Loan No. 204-16743 (secured by Kaloko properties)	
Principal Balance	$224,968.67
Interest	61,830.21

This motion sought allocation of the $500,000 as follows:

Commissioner	$ 4,078.67
Realty Finance: costs and attorney fees	83,830.19
Realty Finance: June Note	95,437.83
Realty Finance: July Note	299,381.08
Escrow Fees and Closing Costs	unspecified
Balance subject to court order	unspecified

The December 18, 1999 Declaration of Robert Austin states, in relevant part, as follows:

> 1. On June 23, 1999, I was the President and general manager of [Waikiki 418]. From and after that date, I was solely and exclusively in charge of its business activities and financial affairs.
>
> . . . .
>
> 4. As of June 23, 1999, I believed (and still believe) that Waikiki 418 had the absolute right to collect the amounts owed on the notes and mortgages which are the subject matter of this action as assignee and licensee of [Realty Finance] based on the express language of the agreements between [Waikiki 418] and [Realty Finance] . . . .
>
> 5. On June 23, 1999, in its capacity as the assignee of [Realty Finance's] interest in the notes and mortgage documents described in the Purchase and Sale Agreement which are the subject

matter of this action, Waikiki 418 collected $309,000 from [Amerasian] and $225,000 from [Lulani] and signed a receipt for said sums, ...

6. As part of the transaction whereby [Amerasian] paid $309,000 to Waikiki 418, I represented to Thomas Schmidt and others, that after [Lulani] paid $225,000 for the other Kaloko lot, Waikiki 418 would obtain and record a release of the mortgages encumbering the Marco Polo Commercial Unit and Lot 5 of the Kaloko Subdivision . . . .

7. As part of the transaction whereby [Lulani] paid $225,000 to Waikiki 418, I represented to James L. Watson, Larry White and others that after [Amerasian] paid $309,000 for the Marco Polo Commercial Unit and Kaloko Lot 5, Waikiki 418 would obtain and record a release of the mortgage encumbering Lot 4 of the Kaloko Subdivision . . . which [Lulani] was purchasing.[12]

8. As of June 23, 1999 and at all times thereafter, it was my understanding and belief that no additional payments were owed to [Realty Finance] until June 30, 1999, and accordingly that between June 23, 1999 and June 30, 1999, Waikiki 418 had the absolute right to utilize and invest the $534,000 in mortgage proceeds it had collected, for its own business purposes.

9. As of June 23, 1999, and at all times thereafter, I intended that Waikiki 418 pay at least $200,000 to [Realty Finance] on or before June 30, 1999.

10. Between June 23, 1999 and June 29, 1999, I traveled to Singapore and Korea as part of a short term investment of the $534,000 of mortgage proceeds. I had arranged to travel to Los Angeles to partially liquidate this investment by June 29, 1999 so that Waikiki 418 could pay Realty Finance at least $200,000 by June 30th.

11. While I was on that trip, the $534,000 in mortgage proceeds (plus additional funds) was wrongfully diverted by a long time friend of mine or his associates, who have thus far refused to return the funds and/or to deliver the investments which were to be purchased with said funds.

12. As of this date, it is uncertain when or to what extent Waikiki 418 and I will be able to recover the monies which are owed to Waikiki 418.

13. I never at any time disclosed in any way or discussed with Thomas Schmidt or anyone else acting on behalf of Amerasian or to James Watson, Larry White or anyone else acting on behalf of [Lulani], the intention of Waikiki 418 and me to utilize the $309,000 it was collecting from [Amerasian] and the $225,000 it

[12] On June 23, 1999, court approval was required before Lulani could purchase Lot 4 of the Kaloko Subdivision, and Lulani had no assurance that such court approval would be given.

was collecting from [Lulani] for a short term investment until June 30, 1999, instead of immediately paying the amounts owed to [Realty Finance].

. . . .

15. I have no business or social relationship with Thomas Schmidt, Larry White, James Watson or anyone else who acted on behalf of [Amerasian] or [Lulani] and have had no other conversations or meetings with any of them except as set forth herein.

(Footnote added.)

In his December 19, 1999 declaration, attorney Jerry A. Ruthruff stated, in relevant part, as follows:

2. I represented Waikiki 418 in connection with the transaction evidenced by said agreements, ... I personally supervised the transaction between Waikiki 418 and [Realty Finance] and was handling all details thereof with [Realty Finance] on behalf of Waikiki 418, until June 23, 1999, when Robert Austin took sole control of Waikiki 418.

3. All of the Loan Purchase Agreements were drafted by counsel for [Realty Finance], and not by me or anyone acting on behalf of Waikiki 418. All of the documents were drafted and signed at the same time as part of a single transaction.

4. On May 13, 1999, [Realty Finance's] Notice of Transfer Of Real Party In Interest was filed in this action and served on the parties thereto to give notice that Waikiki 418 was the real party in interest.

. . . .

7. Neither James Watson, Larry White, Tom Schmidt nor anyone else associated with or acting on behalf of [Lulani] or [Amerasian] was ever informed by me or by anyone else in my presence, or to my knowledge by anyone at any time, that Waikiki 418 intended to or would utilize the $309,000 it was collecting from [Amerasian] and $225,000 it was collecting from [Lulani], for an investment, rather than immediately paying [Realty Finance] the remaining $350,000 plus interest which was owed pursuant to the Loan Purchase Agreements.

8. To the best of my knowledge, [Amerasian] and [Lulani] were not informed that [Realty Finance] had not been paid the remaining $350,000 owed to it, until at least August, 1999.

9. On behalf of Waikiki 418, I obtained the release required by paragraph 5 of the Purchase and Sale Agreement, in form and substance approved by counsel for [Realty Finance], and delivered same to counsel for Plaintiff, in the time period specified therein.

In his December 21, 1999 declaration, Schmidt states, in relevant part, as follows:

> 1. I am the Vice President of [Amerasian]. In that capacity, I handled the purchase of Lot 5 of the Kaloko Subdivision . . . and the Marco Polo Commercial Unit . . . and the payment of the $309,000 to [Waikiki 418] in order to obtain a release of the mortgage encumbering those properties.
>
> 2. I was introduced to Mr. Austin by telephone by Jerry Ruthruff on June 18, 1999. In a subsequent conversation, Mr. Ruthruff stated that he had known Mr. Austin for many years, that Mr. Austin was a good guy who had adopted a number of kids and was someone who Mr. Ruthruff trusted.
>
> 3. I was told by Robert Austin around June 18, 1999 that Lot 5 and the Marco Polo Unit could be purchased by [sic] for $309,000 if and only if that sum was paid no later than June 23, 1999. I was already very familiar with those properties as a result of my prior involvement in the ownership and mortgaging thereof.
>
> 4. I already knew . . . that [Waikiki 418] had to pay a total of $350,000 plus interest to [Realty Finance] by June 30, 1999. . . .
>
> 5. Mr. Austin told me that the mortgage which [Waikiki 418] had purchased from [Realty Finance] could not be released simultaneously with the payment of the $309,000 by [Amerasian] but would be released after [Waikiki 418] received the proceeds from the sale of Lot 4 to [Lulani], which I understood would be closed before June 30, 1999.
>
> 6. Since I knew that Lot 4 was worth $200,000 or more, I never thought that [Amerasian] was taking a risk by agreeing to pay the $309,000 purchase price without simultaneously receiving a release of the mortgage, . . . and did not think it necessary to utilize an escrow for that purpose.
>
> 7. On June 23, 1999, I arranged for [Amerasian] to pay $309,000 to [Waikiki 418] in satisfaction of the mortgage on Lot 40[.]

On December 21, 1999, the court entered its "Order Granting Realty Finance, Inc.'s Motion for Order Approving Confirmation of Private Sale of Subject Properties Filed October 25, 1999" (December 21, 1999 Order). This order approved the sale of Kaloko Lot 4 to Lulani for $300,000, the sale of

Commercial Unit 2, Marco Polo Apartments to Amerasian for $30,000, and the sale of Kaloko Lot 5 to Amerasian for $170,000.

On December 21, 1999, Turlington[13] and the Schmidts/Amerasian each filed a memorandum seeking, in the words of Schmidt, "that the $534,000 paid to [Waikiki 418] in June 1999, be credited to instant [in]debtedness owed by the Schmidts to Realty Finance[.]"

On January 6, 2000, Realty Finance filed a memorandum in which it argued that it was not obligated to credit the $534,000 payment because it properly filed a lis pendens on March 27, 1997. This memorandum states that "the Lis Pendens conclusively forecloses any claims that subsequent purchasers are entitled to proper title to the properties." An accompanying footnote 3 states that "Turlington is claiming that the amounts paid to Waikiki 418 should be credited by Realty Finance. Essentially, this would result in an extinguishment of the Mortgages and a sale of the property to the parties that paid Waikiki 418. This result is foreclosed by virtue of the Lis Pendens."

[13] On December 21, 1999, Turlington, as successor-in-interest to Rapp, filed a memorandum stating, in relevant part, that the question "[w]hether [Realty Finance] must credit said payments totaling $534,000 paid to its assignee, against the amount allegedly now owing to [Realty Finance] on the Mortgage Indebtedness is the most important issue which remains to be resolved in this case." Turlington was represented by attorney Jerry A. Ruthruff.

On January 31, 2000, after a hearing on January 13, 2000, the court entered its "Findings Of Fact, Conclusions Of Law And Order Granting Plaintiff Realty Finance, Inc.'s Motion For Order Approving Commissioner's Report And For Distribution Of Proceeds And Allowing Attorneys' Fees And Expenses," proposed by Realty Finance. This document states, in relevant part, as follows:

FINDINGS OF FACT

. . . .

19. Waikiki 418 timely paid Realty Finance the initial $100,000.00 payment down payment, and Realty Finance applied this payment towards the outstanding loan balances.

20. Waikiki 418 thereafter failed to make the June 30, 1999 balloon payment as required by the Conditional Sale Agreement.

21. Realty Finance received no other payments from Waikiki 418 or any other party.

22. Pursuant to the Conditional Sale Agreement and an Assignment and Security Agreement, Realty Finance recorded an executed Assignment of Notes and Mortgages and revived the foreclosure proceedings against all Defendants, all with notice to the parties herein.

. . . .

24. Lulani's Motion for Leave to Intervene in Proceeding was denied on November 1, 1999.

25. Realty Finance has received an offer to purchase both subject properties from Lulani and [Amerasian]. Lulani offered to purchase Lot 4 of the Kaloko II Subdivision, . . . for $300,000.00.

26. Amerasian submitted an offer to Realty Finance to purchase the Marco Polo condo unit and Lot 5 of the Kaloko Subdivision, . . . for $200,000.00. . . .

. . . .

30. As of December 31, 1999, Realty Finance is owed $128,997.51 pursuant to the Marco Polo [June] Note and Mortgage. . . . As of December 31, 1999, Realty Finance is owed $346,408[.]80 pursuant to the Kaloko [July] Note and Mortgage. . . .

29.[sic] Interest continues to accrue after December 31, 1999, to the date of closing at the per diem rate of $14.12 . . . and $61.63. . . .

. . . .

CONCLUSIONS OF LAW

A. Under HRS § 634-51, the properly filed Lis Pendens serves as notice to any subsequent encumbrances or purchasers. Any purported purchaser of property after the filing of a lis pendens "shall be deemed to have constructive notice of the pendency of the action and be bound by any judgment entered therein if the person claims through a party to the action." Thus, pursuant to this Court's Order entered November 1, 1999,[14] the Lis Pendens conclusively forecloses any claims that any subsequent purchasers are entitled to either title to the properties or credit for any payments allegedly made to any other party except Realty Finance.

. . . .

G. [Realty Finance] is entitled as a matter of law to receive the amounts due and owing pursuant to the valid, subsisting and unpaid Marco Polo Note and Mortgage and Kaloko Note and Mortgage from the distribution of proceeds . . . .

. . . .

ORDER

. . . .

2. That as of December 31, 2000 there is due and owing to [Realty Finance] from Defendants [the Schmidts] the following amounts:

Loan No. 204-16089 (secured by Marco Polo condo unit)

. . . .

Total for Loan No. 204-16089	**128,997.51**

Loan No. 204-16743 (secured by Kaloko properties)

. . . .

Unpaid Late Charges	11,248.43

. . . .

Total for Loan No. 204-167431	**$346,408.80**
Total for both loans:	**$475,406.31**

[14] We did not find a relevant November 1, 1999 Order in the record.

. . . .

GOOD CAUSE APPEARING THEREFOR, IT IS HEREBY ORDERED, ADJUDGED AND DECREED:

. . . .

5. That, with respect to the sum of $500,000.00, the aggregate total purchase price of the properties, the Commissioner pay:

a Any unpaid real property taxes, pro rated as of the date of closing.

b To GEORGE K. H. LAU, as Commissioner, the sum of $4,078.67 representing his fee plus expenses.

c To ASHFORD & WRISTON, attorney for [Realty Finance], the sum of $86,277.24 for services rendered.

d Any escrow fees and closing costs not otherwise chargeable to the Purchasers or Purchasers' respective nominees and;

e The remainder, if any, to be held in escrow, subject to further order of this Court.

. . . .

10. There being no just reason for delay, this shall be an express direction that judgment be entered, pursuant to Rule 54(b), H.R.C.P., as to all claims determined by this Order.

(Footnote added, emphases added.)

On April 11, 2000, the court entered its "Judgment Based Upon Realty Finance's Order Granting Plaintiff Realty Finance, Inc.'s Motion For Order Approving Confirmation of Private Sale of Subject Properties Filed October 25, 1999." The language in this judgment appeared to have finalized the judgment as authorized by HRCP Rule 54(b).[15]

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[15] At least one "claim" or all of the rights and liabilities of at least one party must be decided before the lower court can apply HRCP Rule 54(b). FFG, Inc. v. Jones, 6 Haw. App. 35, 708 P.2d 836 (1985). As noted in footnote 3 above, foreclosure cases are bifurcated into two separately appealable parts. The first part is the decree of foreclosure.

(continued...)

On May 10, 2000, the court entered its "Judgment Based Upon the Findings of Fact, Conclusions of Law and Order Granting Plaintiff Realty Finance, Inc's Motion for Order Approving Commissioner's Report and for Distribution of Proceeds and Allowing Attorneys' Fees and Expenses." The language in this judgment appeared to have finalized the judgment as authorized by HRCP Rule 54(b).[16]

On June 9, 2000, the court entered "Plaintiff's Final Deficiency Judgment Based Upon Order Granting Plaintiff Realty Finance, Inc.'s Motion for Order Allowing Additional Attorneys' Fees and Costs and for Deficiency Judgment Against Thomas Frank Schmidt and Lorinna Jhincil Schmidt." The amount was $9,662.50.

DISCUSSION

A.

Pursuant to the December 31, 1998 Purchase and Sale Agreement, Waikiki 418 had purchased from Realty Finance the Promissory Notes and the Mortgages for $450,000. It had paid $100,000 and it owed the balance, plus interest at 10% per annum, by June 30, 1999. If it made the payment, it would stand in the shoes of Realty Finance in the foreclosure case.

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[15](...continued)
The second part is usually the deficiency judgment. Thus, HRCP Rule 54(b) did not authorize finalization of the April 11, 2000 judgment.

[16] See footnote 15 above.

On June 23, 1999, Amerasian and Lulani paid a combined total of $534,000 to purchase from Waikiki 418 what Waikiki 418 had purchased from Realty Finance. Realty Finance also gave Waikiki 418 "a revocable license to collect the sums accruing by virtue of the Loan Documents, and to enforce said instrument."

In their opening brief, Appellants contend that the payments allegedly received by Waikiki 418 from Amerasian and Lulani reduced the amount owed on the mortgage indebtedness. They state the following question: "Where Plaintiff assigned the Mortgage Indebtedness to Mortgage Purchaser and authorized Mortgage Purchaser to collect the amounts due on the Mortgage Indebtedness, should payments collected by the Mortgage Purchaser be deducted from the remaining balance owed on the Mortgage Indebtedness?" Appellants further contend that

> the Loan Purchase Documents gave Mortgage Purchaser an additional right which led to the present situation ---- the right to collect the Mortgage Indebtedness at any time between January 1, 1999 and June 30, 1999 without a corresponding obligation to make any additional payments to [Realty Finance] until June 30, 1999[.]

We disagree with the assertion that Waikiki 418 had "the right to collect the Mortgage Indebtedness at any time between January 1, 1999 and June 30, 1999 without a corresponding obligation to make any additional payments to Plaintiff Realty until June 30, 1999[.]" In this case, Waikiki 418 wore two hats. First, it was the buyer from Realty Finance in the December 31, 1998 Purchase and Sale Agreement and the seller to Amerasian/Lulani in the June 23, 1999 Purchase and Sale

Agreements. Second, it was Realty Finance's limited and special agent to collect the sums due on the Promissory Notes. Which hat was Waikiki 418 wearing when Waikiki 418 collected $309,000 from Amerasian and $225,000 from Lulani? As noted above, the December 18, 1999 Declaration of Robert Austin states, in relevant part, that:

> 4. As of June 23, 1999, I believed (and still believe) that Waikiki 418 had the absolute right to collect the amounts owed on the notes and mortgages which are the subject matter of this action as assignee and licensee of [Realty Finance] based on the express language of the agreements between [Waikiki 418] and [Realty Finance] . . . .
>
> 5. On June 23, 1999, in its capacity as the assignee of [Realty Finance's] interest in the notes and mortgage documents described in the Purchase and Sale Agreement which are the subject matter of this action, Waikiki 418 collected $309,000 from [Amerasian] and $225,000 from [Lulani] and signed a receipt for said sums, ...
>
> . . . .
>
> 8. As of June 23, 1999 and at all times thereafter, it was my understanding and belief that no additional payments were owed to [Realty Finance] until June 30, 1999, and accordingly that between June 23, 1999 and June 30, 1999, Waikiki 418 had the absolute right to utilize and invest the $534,000 in mortgage proceeds it had collected, for its own business purposes.
>
> 9. As of June 23, 1999, and at all times thereafter, I intended that Waikiki 418 pay at least $200,000 to [Realty Finance] on or before June 30, 1999.

If Waikiki 418 was wearing its "collection agent" hat when engaging in the June 23, 1999 transaction, then Waikiki 418 collected the money as collection agent for Realty Finance and was a fiduciary holding the money in trust for its principal, Realty Finance, and it did not have the right to do anything with the money collected other than to pay it to Realty Finance.

3 AM. JUR. 2D Agency § 222 (1986). HRS § 708-830(6)(a) (1993) states, in relevant part, as follows:

> A person commits theft if the person does any of the following: . . . Failure to make required disposition of funds. . . . A person intentionally obtains property from anyone upon an agreement, or subject to a known legal obligation, to make specified payment or other disposition, whether from the property or its proceeds or from the person's own property reserved in equivalent amount, and deals with the property as the person's own and fails to make the required payment or disposition.

On the other hand, if Waikiki 418 was wearing its "buyer/seller" hat when engaging in the June 23, 1999 transaction, Waikiki 418 did not collect the money for Realty Finance. It collected the money for itself as "buyer" from Realty Finance and "seller" to Amerasian and Lulani. In this situation, payments collected by Waikiki 418 should not be deducted from the remaining balance owed to Realty Finance on the Promissory Notes secured by the mortgages.

Clearly, the fact that Austin, the president of Waikiki 418, collected the money while thinking that "Waikiki 418 had the absolute right to utilize and invest the $534,000 in mortgage proceeds it had collected, for its own business purposes" proves that Waikiki 418 was wearing its "buyer/seller" hat rather than its "collection agent" hat when engaging in the June 23, 1999 transaction with Amerasian and Lulani. Thus, Waikiki 418 did not collect the money for Realty Finance. It collected the money for itself, and the money it collected should not be deducted from the remaining balance owed on the mortgage

indebtedness as if the payment had been received by an agent of Realty Finance.

B.

Assuming Waikiki 418 was acting as "collection agent" for Realty Finance when it collected the $534,000 from Amerasian and Lulani, Realty Finance presents two grounds why the payments received by Waikiki 418 were properly not credited toward the amounts owed on the Promissory Notes.

1.

The first ground is stated in the answering brief as follows:

> Realty Finance also demonstrated that it possessed the Promissory Notes. Appellants did not object to the representations of fact from Realty Finance's counsel that Realty Finance never relinquished possession of the Promissory Notes to Waikiki 418 and that the assignment was only conditional. . . . Appellants thus waived their challenge to Realty Finance's possession of the Promissory Notes, and there existed no substantial injustice which would warrant the application of the civil plain error doctrine based on HRAP Rule 28(b)(4). Shanghai Investment Co., Inc. v. Alteka Co., Ltd., 92 Hawai'i 482, 993 P.2d 516 (2000) (ruling that objections not timely made below are waived on appeal and refusing to consider as plain error the improper comments made below).
>
> Additionally, the Affidavit of Harris Hirata, Dated December 16, 1997 ("the Hirata Affidavit"), supported Realty Finance's position. As Executive Vice-President of Realty Finance, Mr. Hirata had personal knowledge about the Promissory Notes and Mortgages, had access to the original documents (thereby indicating that Realty Finance had possession of the original documents), and provided authenticated copies of the documents as Exhibits to Realty Finance's December 17, 1997 Motion for Summary Judgment Against All Defendants, and for Interlocutory Decree of Foreclosure. . . .
>
> Appellants have cited no on-point, supporting authority. In Hanalei, BRC Inc. v. Porter, 7 Haw. App. 304, 760 P.2d 676 (1988), there was enough evidence to reasonably infer that the creditor had possession of the note. . . . Here, Waikiki 418 did not pay Realty Finance the entire outstanding debt on the Promissory

> Notes, and, after Waikiki 418's default, Realty Finance was therefore entitled to collect the remaining amount from the Schmidts and Amerasian.

(Emphasis in original, record citations omitted.)

Simply stated, Realty Finance contends that (a) Waikiki 418 cannot deny that Realty Finance "never relinquished possession of the Promissory Notes to Waikiki 418" and (b) Hanalei is authority that Realty Finance's possession of the Promissory Notes precluded payments to Waikiki 418 from being credited to the outstanding balances due on the Promissory Notes.

In a joint reply brief, Appellants respond as follows:

> Appellants then showed that under standard contract law, and the legal principles applicable to agency and to assignments of contracts and judgments, payments made to [Waikiki 418], as [Realty Finance's] assignee, reduced the amount owed on the Mortgage Indebtedness which [Realty Finance] was entitled to collect when the Mortgage Indebtedness was reassigned to [Realty Finance] by [Waikiki 418].
>
> . . . Appellants respectfully submit that the Joint Amended Opening Brief amply demonstrated that payments made to an assignee of a contract or judgment must be credited to the amount owed on the contract or judgment and that the alleged failure of [Waikiki 418] to pay the amount it owed to [Realty Finance], is a separate dispute solely between [Realty Finance] and [Waikiki 418] which is not relevant to the resolution of the issues raised in this appeal. [Realty Finance's] lack of meaningful argument can only be interpreted as a virtual concession of this issue.

(Footnotes omitted.)

In other words, Appellants rely on the following three documents:

1. The December 31, 1998 Purchase and Sale Agreement, whereby Waikiki 418 agreed to purchase the June Note and the July Note and the other Loan Documents.

2. The December 31, 1998 Assignment of Notes and Mortgages, whereby Waikiki 418 acquired "the notes . . . and the money due or to become due thereon with the interest provided therein[.]"

3. The December 31, 1998 Assignment of Notes and Mortgages as Security and Security Agreement, whereby Waikiki 418 conveyed to Realty Finance, as security for the payment of the $450,000, all right to the Loan Documents and the right to enforce the Loan Documents, but retained the following right:

> PROVIDED FURTHER, that so long as [Waikiki 418] shall not be in default under the Sale Agreement, under this instrument, or under any other instrument or agreement evidencing or securing the Sale Agreement . . . [Waikiki 418] shall have a revocable license to collect the sums accruing by virtue of the Loan Documents, and to enforce said instrument. Said license shall be automatically revoked without notice upon the occurrence of any event of default.

However, the HRS (1993) state, in relevant part, as follows:

> **§490:3-102 Subject Matter.** (a) This Article applies to negotiable instruments. . . .
>
> . . . .
>
> **§490:3-104 Negotiable Instrument.** (a) . . . "[N]egotiable instrument" means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:
>
> (1) Is payable to bearer or to order at the time it is issued or first comes into possession of a holder;
>
> (2) Is payable on demand or at a definite time; and
>
> (3) Does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money, ...
>
> . . . .

§490:3-201 Negotiation. (a) "Negotiation" means a transfer of possession, whether voluntary or involuntary, of an instrument by a person other than the issuer to a person who thereby becomes its holder.

(b) Except for negotiation by a remitter, if an instrument is payable to an identified person, negotiation requires transfer of possession of the instrument and its indorsement by the holder. If an instrument is payable to bearer, it may be negotiated by transfer of possession alone.

. . . .

§490:3-203 Transfer of instrument; rights acquired by transfer. (a) An instrument is transferred when it is delivered by a person other than its issuer for the purpose of giving to the person receiving delivery the right to enforce the instrument.

(b) Transfer of an instrument, whether or not the transfer is a negotiation, vests in the transferee any right of the transferor to enforce the instrument, including any right as a holder in due course, ...

. . . .

§490:3-301 Person entitled to enforce instrument. "Person entitled to enforce" an instrument means (i) the holder of the instrument, (ii) a nonholder in possession of the instrument who has the rights of a holder, or (iii) a person not in possession of the instrument who is entitled to enforce the instrument pursuant to section 490:3-309 [had rightful possession but instrument was lost, destroyed, or stolen] or 490:3-418(d) [recovery of mistaken payment]. A person may be a person entitled to enforce the instrument even though the person is not the owner of the instrument or is in wrongful possession of the instrument.

. . . .

§490:3-418 Payment or acceptance by mistake. . . .

(b) Except as provided in subsection (c), if an instrument has been paid . . . by mistake . . . , the person paying . . . may, to the extent permitted by the law governing mistake and restitution, (i) recover the payment from the person to whom or for whose benefit payment was made . . . .

(c) The remedies provided by subsection (a) or (b) may not be asserted against a person who took the instrument in good faith and for value or who in good faith changed position in reliance on the payment . . . .

. . . .

§490:3-602 Payment. . . . [A]n instrument is paid to the extent payment is made (i) by or on behalf of a party obliged to pay the instrument, and (ii) to a person entitled to enforce the instrument.

Hanalei is authority that "[s]ince possession is requisite to the status of a 'holder' of a negotiable instrument, generally, a person without actual possession of the instrument is not a 'holder' entitled to maintain an action for its collection." 7 Haw. App. at 308, 760 P.2d at 679.

In the instant case, Appellants have not disputed Realty Finance's allegation that Realty Finance possessed the Promissory Notes when Waikiki 418 allegedly received the payments on them. The December 31, 1998 Assignment of Notes and Mortgages as Security and Security Agreement states that Realty Finance was the current holder of Promissory Notes.

Thus, we have a situation where Realty Finance agreed to sell to Waikiki 418, and Waikiki 418 agreed to purchase from Realty Finance the loan documents, including the two Promissory Notes. Pursuant to this agreement of sale, Waikiki 418 assigned the loan documents back to Realty Finance as security for the payment of the purchase price. This assignment back noted that Realty Finance was the current holder of the two Promissory Notes. If Waikiki 418 defaulted, Realty Finance was authorized to record the assignment and proceed with the foreclosure. If Waikiki 418 made the payments, Realty Finance was obligated to execute a reassignment to Waikiki 418. Realty Finance conveyed to Waikiki 418 "a revocable license to collect the sums accruing

by virtue of said Loan Documents, and to enforce said instrument."

In the case of The Equity Bank v. Gonsalves, 44 Conn. Supp. 464, 691 A.2d 1143 (Conn. Super. Ct. 1996), on May 29, 1987, Gonsalves executed a negotiable instrument promissory note (G-PN) in favor of Laurora in the amount of $150,000, secured by a mortgage on property in the town of Wethersfield. On September 21, 1993, Laurora assigned the G-PN and the mortgage to the bank as collateral security for a loan made by the bank to Laurora. The assignment was recorded in the Wethersfield land records. The bank never informed Gonsalves of the assignment or made any demand on Gonsalves for payments after the assignment. Gonsalves continued to pay monthly payments to Laurora. On May 27, 1994, Gonsalves paid Laurora the balance due on the G-PN. Laurora executed a release of the mortgage and the release was recorded in the Wethersfield land records, but Gonsalves neither asked for nor did Laurora turn over the original G-PN. The bank asserted its right to payment by commencing a foreclosure action in October 1995. The bank was not able to produce the original G-PN. It presumed it was lost. The court concluded, in relevant part, as follows:

> "The rule as to the payment and discharge of negotiable instruments is that payment of the bill or note must be made to the rightful holder or his authorized agent. It is payment in due course which discharges an instrument . . . and one of the elements of payment in due course is payment to the holder of the instrument, that is, to the payee or indorsee of the instrument who is in possession of it, or the bearer thereof."

. . . .

> As for negotiable instruments, notice to the maker of the transfer of the note is not required. The reason given is that the maker can protect himself by demanding production of the instrument and refusing to pay a party not in possession of it.

Id. at 467, 691 A.2d 1145-46 (citations omitted).[17]

In the case of Lambert v. Barker, 232 Va. 21, 348 S.E.2d 214 (Va. 1986), in 1978, the Barkers executed a negotiable instrument promissory note (B-PN) in favor of Davis, secured by a deed of trust on real estate. Davis conveyed the B-PN to Lambert. This B-PN, indorsed in blank by Davis, was in the possession of Lambert. Davis and Lambert agreed that the monthly payments on the B-PN would be payable to Davis while any

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[17] The Superior Court of Connecticut also opined that:

> To this court that reason does not make sense as to a mortgage note payable monthly. A mortgagor cannot be expected every month he makes a payment to ask a mortgagee bank to prove [its] possession of the note. Moreover, if the mortgagor pays monthly to the mortgagee a self-amortizing mortgage note to the date of maturity, should not payment in full in that manner fail to be a complete defense to an action by an assignee of the mortgagee who never gave notice of the assignment?
>
> Despite the good sense and fairness of allowing such a defense, the rule appears to be "the maker of a negotiable note secured by a mortgagee cannot discharge his liability by payment to one not the holder . . . and a mortgagor is not justified as against an assignee of the mortgage in making payments to a mortgagee who does not have possession of the instrument. . . ."
>
> Foreclosure is an equitable action, however, and a court can consider all the equities in deciding whether to enter a foreclosure. In the present case, the court would be inclined on that ground to decide for [Gonsalves], but a consideration of all the equities gives rise to questions of fact. Consequently, the court must deny [Gonsalves'] motion for summary judgment.

The Equity Bank v. Gonsalves, 44 Conn. Supp. 464, 467-68, 691 A.2d 1143, 1146 (Conn Super. Ct. 1996).

We are not as inclined as the court in The Equity Bank to ignore the command of an unambiguous statute.

prepayment was payable to Lambert. The Barkers conveyed the property to Beloff, who conveyed it to the Harwoods who agreed to pay the B-PN. When the Harwoods conveyed the property to the Buggs, Davis falsely asserted at closing that he was the note holder but that the B-PN was lost. The balance due on the B-PN was paid to Davis. Thereafter, Lambert sued the Barkers and the Harwoods to recover the amount for the balance due on the B-PN. The trial court ruled that Lambert had failed her duty to give notice to both the Barkers and the Harwoods of the pledge of the B-PN. On appeal, the Barkers contended that payment to Davis discharged their liability as makers of the B-PN. The Supreme Court of Virginia disagreed with the Barkers. It noted that

> [t]he right of a party to payment . . . depends upon his status as a holder. A holder is one who is in possession of an instrument issued or indorsed to him or his order, to bearer, or in blank. Payment or satisfaction discharges the liability only if made to the holder of the instrument. Because payment in satisfaction of the instrument must be made to a party in possession in order to discharge the payor's liability, no notice is required for the protection of the payor. Rather, the payor may protect himself by demanding production of the instrument and refusing payment to any party not in possession unless in an action on the obligation the owner proves his ownership.
>
> Payment to an authorized agent of the holder will also satisfy the requirement of payment to the holder, resulting in discharge. But the burden of proving an agency relationship rests on the party claiming payment as a defense.

Id. at 24-25, 348 S.E.2d at 216 (footnote and citations omitted).

Based especially on HRS § 490:3-301 and the above precedent, we conclude that the fact that Waikiki 418 had "a revocable license to collect the sums accruing by virtue of the Loan Documents, and to enforce said instrument" did not cause

Waikiki 418 to be a "[p]erson entitled to enforce" the Promissory Notes. Therefore, assuming Amerasian and Lulani paid Waikiki 418 $534,000, the payment was not a payment on the Promissory Notes.

2.

The second ground is stated in the January 31, 2000 Conclusions of Law as follows:

> A. Under HRS § 634-51, the properly filed Lis Pendens serves as notice to any subsequent encumbrances or purchasers. Any purported purchaser of property after the filing of a lis pendens "shall be deemed to have constructive notice of the pendency of the action and be bound by any judgment entered therein if the person claims through a party to the action." Thus, pursuant to this Court's Order entered November 1, 1999, the Lis Pendens conclusively forecloses any claims that any subsequent purchasers are entitled to either title to the properties or credit for any payments allegedly made to any other party except Realty Finance.

It is not necessary for us to decide the merits of this ground and, therefore, we do not do so.

C.

Appellants contend that Realty Finance is not entitled to collect late fees because "the February 24, 1998 Judgment does not require the [Appellants] to pay or entitle Realty Finance to collect late charges[.]" We disagree. The February 24, 1998 Judgment states that the "Court reserves jurisdiction to confirm the foreclosure sale and to determine the following: . . . ; (3) any additional sums owed to [Realty Finance] under its mortgages[.]" Those additional sums include late fees.

D.

Appellants contend that Realty Finance's attorney fees and costs are not secured by the mortgages and do not constitute a first lien on the property. We disagree.

E.

Appellants contend that Realty Finance is not a holder in due course and is subject to personal defenses asserted by the Schmidts and is not entitled to collect on the Kaloko Note and Mortgage. We disagree.

CONCLUSION

Accordingly, we affirm the circuit court's June 9, 2000 "Plaintiff's Final Deficiency Judgment Based Upon Order Granting Plaintiff Realty Finance, Inc.'s Motion for Order Allowing Additional Attorneys' Fees and Costs and for Deficiency Judgment Against Thomas Frank Schmidt and Lorinna Jhincil Schmidt[.]"

DATED: Honolulu, Hawai‘i, June 27, 2002.

Jerry A. Ruthruff for
Party-In-Interest/Appellant.

Chief Judge

Thomas P. Dunn and
for Defendants-Appellants.

Associate Judge

Francis P. Hogan
(David C. Farmer, Jody
Kaulukukui-Li, and Keith M.
Yonamine (Ashford & Wriston,
of counsel) on the brief)
for Plaintiff-Appellee.

Associate Judge