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# Tender by a worthless document: McElroy v Chase Manhattan Mortgage, 2005

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**Debtor's tender of document (purporting to pay off loan) worthless on its face does not prevent foreclosure or give rise to creditor's obligation to object to tender.**

*McElroy v Chase Manhattan Mortgage Co.* (2005) 134 CA4th 388, 36 CR3d 176

After defaulting on a loan secured by a deed of trust on their property, the McElroys tendered full payment of the loan to their lender (Chase) in the form of a Bonded Bill of Exchange Order (the Bill). Attached to the Bill were processing instructions stating that the Bill was a negotiable instrument and should be processed as a check and sent by certified mail to the Secretary of the Treasury. Chase, ignoring the Bill and a letter sent later with further redemption instructions, sold the property at a nonjudicial foreclosure sale. The property was subsequently purchased by Finicle.

The McElroys' amended complaint against Chase and Finicle alleged several causes of action, including:

- Quiet title to the property, on the theory the foreclosure was fraudulent because of Chase's refusal to process the Bill; and
- Fraudulent foreclosure.

The cause of action for declaratory relief asked the court to:

- Declare the McElroys' debt discharged by Chase's lack of response to the tender; and
- Set aside the foreclosure sale.

Demurrers to the amended complaint were sustained without leave to amend.

The court of appeal affirmed, holding that the demurrers were properly sustained because the Bill was worthless on its face. The Bill was not a negotiable instrument because it was not made "payable to bearer or to order." Com C §3104(a)(1). Although a check qualifies as a negotiable instrument even if not payable to bearer or order (§3104(c)), the Bill was not a check because it was not drawn on a bank (§3104(f)).

Moreover, although the Bill expressly provided that the Secretary of the Treasury's obligation to honor it arose under a Joint Resolution of Congress and *Guaranty Trust Co. v Henwood* (1939) 307 US 247, 83 L Ed 1266, 59 S Ct 847, nothing therein creates any such obligation. Because the Bill purported to identify the source of the obligation to honor the Bill, and the cited source does not establish an obligation, the Bill was a worthless piece of paper.

The court also rejected the McElroys' argument, in reliance on CC §1501 and CCP §2076, that the trustee sale was tainted by fraud because Chase's failure to respond effectively waived any objections to the tender and discharged the debt by operation of law. The purpose of these code sections is to allow a debtor to know what its creditor demands so that the debtor may make a conforming tender. They do not apply when the amount of the creditor's demand is known to the debtor and the amount of the tender is wholly insufficient. The McElroys knew the precise amount of their creditor's demand, but tendered a worthless piece of paper. The tender of a worthless document does not pay off a debt because the creditor fails to object to the tender.

Moreover, the McElroys knew their tender was not acceptable to Chase for several months before the foreclosure, but did not reinstate the loan by bringing the delinquent payments, as provided in CC§2924c(a)(1). The court noted the tender date alleged in the complaint and took judicial notice of the recording dates of the notices of default and sale and of the deed upon sale in order to conclude that the McElroys had ample opportunity to cure the defective tender.

Because the Bill was worthless on its face, and the McElroys did not make a proper tender to cure the default, foreclosure was proper. Therefore, the McElroys had no adverse claim to the property and thus failed to state quiet title or declaratory relief causes of action.

***THE EDITOR'S TAKE:*** Of the two arguments made by the debtors in this case, the first was probably a known loser from the start, but the second one could have really messed up the lending industry had it been given any credence.

The contention that the 1933 repeal of the gold standard entitled private parties to pay their debts by draws on the U.S. Treasury could be taken seriously only by the lunatic fringe of society that believes all government is a communist or atheistic plot. (Most of those types would have been hard put to draft a document as legal-sounding as this "Bonded Bill of Exchange Order"—although the failure to add "or order" to make it at least look negotiable was pretty careless, even for fanatics.) I think the debtors knew all along that no court would treat the document as payment; their real hope was that they could make some headway by arguing that the lender did not properly respond to their "tender" of payment.

Literal readings of CC §1501 and CCP §2076 do seem to say that a bad tender is nevertheless effective if the "tenderee" (I hope there is such a word) fails to correctly object to it. A good many of the decisions dealing with those provisions involve the courts in trying to find some way around applying those sections too literally. But this decision was almost overkill in holding that the tender of a worthless instrument does not constitute payment of debt, and it includes some rather dubious arguments that may someday come back to haunt judges.

First, the court said that an obligation to object would not serve the purpose of those code sections because these debtors actually knew how much they owed. But a debtor's knowledge of how much is due hardly makes it unnecessary for the creditor to tell the debtor what is wrong with the manner of payment. A creditor should not be excused from informing its debtors that their check bounced just because the debtors knew how much the check had been written for.

Second, the court held that tender of the document was "wholly insufficient" and therefore not a tender at all (thereby apparently dispensing with any need to object to it). But can the bar live under a rule that wholly insufficient tenders are not subject to the objection requirement? Will the definition of tender now include a requirement as to the amount or the validity of the payment offered? If so, will the standard be objective or subjective? This ruling will not be helpful to "tenderors" or "tenderees" as to when and how to respond to questionable tenders.

Third, the court "noted" that the debtors knew their tender was bad because they received notices of default and sale thereafter. But while subsequent receipt of these notices may inform the debtors that their tender was rejected, it does not advise them of the grounds for rejecting it, which is what the statutes really are aiming at.

Furthermore, the opinion makes a large leap in getting from the fact that these notices were recorded to the conclusion that the debtors knew about them. Recording is only constructive, rather than actual, notice; it does not usually apply to those who already own the property. A finding that the debtors had actually received those notices would have carried far more weight on that issue. (The opinion also names the trustee deed as a third basis of knowledge, but that clearly came too late in the process to serve as a timely objection.)

We can all agree that such "Bonded Bills" will not and should not work, and that commercial lenders should not have to waste resources in drafting and sending formal rejection responses to crazy schemes concocted by lunatic borrowers. However, I wish better reasons had been given for reaching that sane result.—*Roger Bernhardt*