

UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF MICHIGAN

In re:

FREDERICK ALLAN STANKUS and
MICHELLE MARIE STANKUS,

Case No. SG 04-10024
Chapter 13

Debtors.

BRETT N. RODGERS,

Adversary Proceeding
No. 05-80738

Plaintiff,

v.

COUNTRYWIDE HOME LOANS INC.,

Defendant.

MEMORANDUM ORDER

At a session of said court, held in and for said District, at the United States Bankruptcy Court, One Division, Grand Rapids, Michigan this 1st day of June, 2006.

PRESENT: HONORABLE JO ANN C. STEVENSON
Chief United States Bankruptcy Judge

The Plaintiff having filed a Motion for Summary Judgment with Brief in Support; and the Defendant having filed a Response to the Motion with Brief in Support; and a hearing having been held; and the court being duly advised in the premises;

WHEREAS, on November 10, 2000, the Debtors signed a first mortgage on their home in the principal amount of \$125,600.00 in favor of Countrywide Home Loans ("Defendant"). On the same day, the Debtor executed a second mortgage on the same property with the Defendant for \$23,550.00. The first mortgage was properly recorded on November 22, 2000. The second mortgage was never recorded.

On September 4, 2001, Debtors signed a third mortgage for \$10,000.00 for the same property

with Capital One. This mortgage was properly recorded on September 21, 2001. It was later assigned to Sherman Acquisition which recorded its assignment on April 15, 2004.

The Debtors filed bankruptcy on August 16, 2004. They listed the Defendant as a secured creditor based upon its first and second liens on the property. They listed the Defendant's claim as \$136,236.96, based upon the amount of its first lien.

The Debtors' Schedule D was later amended to show the Defendant's second lien as totaling \$23,550.00. The value of the property was listed as \$152,200.00.

On August 4, 2005, Plaintiff filed a Complaint to Avoid Unrecorded Mortgage on Real Property alleging that the second mortgage was unrecorded and therefore unperfected. In response, the Defendant alleged that the liens on property became effective at the point of origination, not recording; parties other than the Defendant might be liable for the failure of the recordation of the mortgage; the Plaintiff had constructive notice of the lien; and the avoidance of the lien would not benefit the estate.

The Trustee filed his Motion for Summary Judgment on March 31, 2006, requesting a ruling in his favor and arguing that he did not have constructive notice of the Defendant's lien; that actual knowledge is irrelevant; and that the Defendant's affirmative defenses had no merit. The Defendant filed a Response on April 21, 2006, arguing that the Trustee could not be a bona fide purchaser because he had constructive notice.

11 U.S.C. §544(a)(3) states:

(a) The Trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee of any creditor the rights of and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by –

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

This court must defer to state law in determining the nature and priority of interests in property. Butner v. United States, 440 U.S. 48, 99 S.Ct. 914 (1979). The priority of liens is to be determined by reference to nonbankruptcy law. United States v. Darnell (In re Darnell), 834 F.2d 1263 (6th Cir. 1987).

Under Michigan law, a bona fide purchaser is a buyer without actual notice of competing claims or knowledge of facts which would lead a reasonable man to make further inquiries. Lakeside Associates v. Toski Sands, 131 Mich. App. 292 (1983). The priority of liens created under state law is governed by a race/notice recording scheme. In re Warren Estates Mobile Home Park, Inc., 811

F.2d 608 (6th Cir. 1986). Consequently, in Michigan a mortgage that is not recorded as provided by law is void as against any subsequent purchaser in good faith and for a valuable consideration of such real estate whose conveyance is recorded before such mortgage. M.C.L.A. §565.29.

The Defendant admits that its mortgage is unrecorded. There is no genuine issue of fact in this case as to any of the elements of 11 U.S.C. §544(a)(3). Therefore, unless the Defendant's affirmative defenses have merit, the Trustee is entitled to judgment on his complaint.

The first defense advanced by the Defendant is that the lien became effective at the point of origination, not recording. This argument is irrelevant since the lien, no matter what date it became effective, was not recorded. "If the intentions of the original contracting parties are not reflected in the public record, a subsequent bona fide purchaser who has relied upon the public record cannot be bound by those unrecorded intentions." Lakeside Associates v. Toski Sands, 131 Mich. App. at 298.

Next, the Defendant argues that parties other than the Defendant may be liable for the failure of the recordation of the mortgage. This argument also fails in that the burden of perfection is on the parties creating a mortgage. "When the court is faced with giving validity to a mortgage between two parties who failed to follow the law and a subsequent party who did, the negligent parties should bear the consequences of their actions. Holding less would make a mockery of mortgage laws and jeopardize the rights they were designed to protect." Thackery v. United Companies Lending Corp., 256 B.R. 724, 730 (W.D. Ky. 2000).

As for the argument that the Trustee had constructive notice of the lien, 11 U.S.C. §544(a)(3) permits a trustee to avoid any transfer of property of the debtor, or obligation incurred by the debtor, that would be voidable by a bona fide purchaser of the property. Actual knowledge of the unrecorded interest is irrelevant because the trustee "shall" be able to avoid an encumbrance that would be voidable by a bona fide purchaser without regard to any knowledge of the trustee or of any creditor. Simon v. Chase Manhattan Bank (In re Zaptocky), 250 F.3d 1020 (6th Cir. 2001); Sandy Ridge Oil Co., Inc. v. Centerre Bank National Association (In re Sandy Ridge Oil Co., Inc.), 807 F.2d 1332 (7th Cir. 1986); Kohut v. Quicken Loans, Inc. et al. (In re Wohfeil), 322 B.R. 302 (Bankr. E.D. Mich. 2005).

Last, the Defendant argues that the avoidance of the lien would not benefit the estate. If the Defendant's lien were avoided by the Trustee, making the second mortgage completely unsecured, the bankruptcy estate would receive a greater dividend for unsecured creditors. This is clearly a benefit.

NOW, THEREFORE, IT IS HEREBY ORDERED that the Plaintiff's Motion for Summary Judgment is GRANTED;

IT IS FURTHER ORDERED that this Memorandum Order shall be served pursuant to Administrative Order 2004-06 (Mandatory Electronic Filing) upon Brett Rodgers, Esq., Chapter 13 Trustee, Frederick Allan and Michelle Marie Stankus, Countrywide Home Loans Inc., and John P. Kapitan, Esq.