

RESOLVING TITLE ISSUES IN BANKRUPTCY

By Steven W. Moglowsky

The Lou Jones Breakfast Club
October 12, 2010

Bass & Moglowsky, S.C.
501 West Northshore Drive
Suite 300
Milwaukee, WI 53217
Telephone No. (414) 228-6700

I. TITLE INSURANCE (OWNER'S POLICY)

- A. Indemnity agreement between owner or intended owner of real property and an insurer
- B. Insurer agrees either to pay or to defend any claim against the property at issue not reflected in the policy
- C. NOTE: case law reveals that a title commitment is not legally intended to describe the status of title; rather it is intended to notify the insured as to what the insurer agrees to defend against (Greenberg v. Stewart Title Guaranty Co., 171 Wis.2d 485, 492 N.W.2d 147 (Wis. 1992))
 - 1. Lawsuit involved claim by insured that title company was negligent in searching the records because they missed a mortgage
 - 2. Court held that claim was on the contract and did not involve the issue of negligence
- D. In case where undisclosed lienholder who was not foreclosed starts making demands on new property owner, title company must either or both:
 - 1. Defend the action;
 - 2. Pay the claim
- E. NOTE: title commitments have exceptions; read them
 - 1. Items not in the record
 - 2. Items that would be disclosed via a survey

II. TITLE ISSUES

- A. The WI Homestead Exemption and Rumage v. Gullberg
 - 1. Scenario - there is a nonpurchase money mortgage on the mortgagor's homestead, and the title commitment shows a docketed money judgment against the mortgagor which predates the mortgage on the property
 - 2. Statutes and Case Law
 - (a) **806.15 Lien of judgment; priority; statute may be suspended.**
 - (1) Every judgment properly entered in the judgment and lien docket ... shall, for 10 years from the date of entry, be a lien on all real property of every person against whom the judgment is entered which is in the county where the judgment is rendered, except homestead property that is exempt from execution under s.815.20, and which the person has at the time of entry of which the person acquires thereafter within the 10-year period.

(b) **815.20 Homestead exemption definition.**

(1) An exempt homestead as defined in s.990.01(14) selected by a resident owner and occupied by him or her shall be exempt from execution, from the lien of every judgment, and from liability for the debts of the owner to the amount of \$75,000.00, except mortgages, laborers', mechanics' and purchase money liens and taxes and except as otherwise provided....

(c) Rumage v. Gullberg, 2000 WI 53, par. 2, 235 Wis.2d 279, ___, 611 N.W.2d 458, 460 (Wis. 2000) (Wisconsin Supreme Court considered "whether a properly docketed judgment constitutes a valid lien against fully exempt homestead property at the time of sale.")

The Court held "that a judgment lien is not a valid lien against fully exempt homestead property," and determined that the property had, therefore, been sold free of the judgment lien without the need of a release. Id., 2000 WI 53 @ par. 47, 235 Wis.2d @ ___, 611 N.W.2d @ 469.

Using Section 815.18(9), Wis. Stats., the Court distinguished cases in which the judgment debtor's equity in the homestead exceeded \$40,000.00. "[W]hen a homestead is partially exempt, a docketed judgment is a lien upon the debtor's equity in excess of the amount sheltered by Wis. Stat. §815.20." Id., 2000 WI 53 @ par. 27, 235 Wis.2d @ ___, 611 N.W.2d @ 465-466.

NOTE: under the holding in Rumage, a judgment lien cannot attach to the homestead of the debtor if the debtor has less than \$75,000.00 in equity in the homestead

B. Judgments Discharged in Bankruptcy - s.806.19(4), Wis. Stats.

1. Scenario - there is a docketed judgment against the debtor in the county in which the debtor owns real property, but the debtor received a discharge in bankruptcy after the judgment was docketed

2. Statutes and Case Law

(a) S.806.15(1) - Every judgment property entered in the judgment and lien docket... shall, for 10 years from the date of entry, be a lien on all real property... which is in the county where the judgment is rendered, except homestead property....

- (b) S.806.19(4)
 - (1) Sub (a) - Any person who has secured a discharge of a judgment debt in bankruptcy and any person interested in real property to which the judgment attaches may submit an application for an order of satisfaction of the judgment and an attached order of satisfaction to the clerk of the court in which the judgment was entered.
 - (2) Sub (b) and (bm) create a statutory format for the application
 - (3) Sub (c) requires a creditor to mail a copy of the application to each judgment creditor affected "within 5 days **after** the date of submission." (emphasis added)
 - (4) Sub (d) states, in part, "Upon satisfaction, a judgment shall cease to be a lien on any real property that the person discharged in bankruptcy owns or later acquires."
- (c) S.806.21, Wis. Stats. **Judgment satisfied not a lien; partial satisfaction.** If a judgment is satisfied in whole or in part or as to any judgment debtor and the satisfaction is entered in the judgment and lien docket, the judgment shall, to the extent of the satisfaction, cease to be a lien. ...
- (d) Megal Development Corp. v. Shadof, 286 Wis.2d 105, 705 N.W.2d 645 (Wis. 2005) - Finding was:
 - (1) judgment debtors who obtained discharge of judgment in bankruptcy were entitled to both satisfaction of judgment and cessation of judgment lien, and
 - (2) state statute providing therefor was not preempted by federal bankruptcy law

C. Purchase Money Mortgages

1. Statutes

- (a) 708.09 **Purchase money mortgage defined.** A purchase money mortgage is one given as part of the transaction of purchase to the vendor or real estate for all or part of the purchase money or to a 3rd person who advances all or a part of the purchase money.
- (b) 706.02 **Formal requisites** ... (1)(f) Is signed, or joined in by separate conveyance, by or on behalf of each spouse, if the conveyance alienates any interest of a married person in a homestead under s. 706.01(7) except conveyances between spouses, but on a purchase money mortgage pledging that property as security only the purchaser need sign the mortgage;....

2. Case Law

- (a) In Weber v. Weber, 176 Wis.2d 1085, _____, 501 N.W.2d 413, 414 (Wis. 1993), the Wisconsin Supreme Court opined on "whether the signature requirement of the homestead provision of the statute of frauds can be waived by failure to plead it as an affirmative defense in a mortgage foreclosure action." There, only one spouse had signed the mortgage on the homestead. The Court ruled that the mortgage was void under the statute of frauds and further held that since Wisconsin had a "unique public policy favoring Wisconsin homesteads over other property interests," that the homestead exemption superseded the pleading requirements of sec. 802.03, Wis. Stats. Id., 176 Wis.2d @ _____, 501 N.W.2d @ 417.
- (b) "It is a recognized principle that a mortgage for the purchase money of land, which mortgage is executed at the time of the delivery of the conveyance of the legal title, has priority, as to the land conveyed, over existing judgments and executions against the vendee, whether the mortgagee is the vendor or a third person who furnishes the purchase price." Northern State Bank v. Toal, 69 Wis.2d 50, 55, 230 N.W.2d 153, 155 (Wis. 1975) quoting 46 Am.Jur.2d, Judgments, 503, sec. 301

D. Equitable Subrogation

1. Scenario - a title commitment shows a small mortgage in 1st lien position and a large mortgage in 2nd lien position; you know that your client's mortgage was primarily used to pay off a 1st mortgage on the property but there is no legal subordination agreement between the two mortgages that are now of record
2. Definition

Subrogation is an equitable doctrine designed to avoid unjust enrichment and may properly be applied whenever a person other than a mere volunteer pays a debt which in equity and good conscience should be satisfied by another. See Rock River Lumber Corp. v. Universal Mortgage Co., 82 Wis.2d 235, 240-41, 262 N.W.2d 114, 116 (1978).
3. History

Equitable, or legal, subrogation has its source in equity and arises solely by operation and application of equitable principles. Wisconsin Patients Compensation Fund v. Wisconsin Health Care Liab. Ins. Plan, 200 Wis.2d 599, 619, 547 N.W.2d 578, 585-86 (1996).
4. Purpose

It arises as a means of doing justice after a balancing of the equities of the case, Rock River, 82 Wis.2d at 242, 262 N.W.2d at 117, requiring courts to apply equitable principles to the facts of the case, Schulte v. Frazin, 176 Wis.2d 622, 628, 500 N.W.2d 305, 307 (1993).

5. Applicability

The remedy of subrogation is highly favored and the courts are inclined to give it a liberal application. Jindra v. Diederich Flooring, 181 Wis.2d 579, 599 n.11, 511 N.W.2d 855, 861 (1994).

In determining whether subrogation would be inequitable, the trial court is required to consider whether it would cut off the intervening rights of one who relied upon the extinguishment of the mortgage or who had innocently placed himself in a position of disadvantage and would be injured by, application of the doctrine. Rock River, 82 Wis.2d at 246, 262 N.W.2d at 119.

Equity will treat such a transaction as equivalent to an assignment of the original security. Id.

6. Negligence

Even in cases of negligence by the party requesting subrogation, one who is not a volunteer is entitled to equitable subrogation in the absence of intervening equities. Home Owners' Loan Corp. v. Papara, 241 Wis. 112, 3 N.W.2d 730 (Wis. 1942)

7. Excellent Bankruptcy Case Example: In re Larson, 346 B.R. 486 (Bankr. E.D. Wis. 2006)

E. Reformation of Legal Descriptions

1. Scenario - The legal description stated in the mortgage contains error(s) such as typographical mistakes in the name of the subdivision, a transposition of numbers in the lot or block numbers, or wrong directions in a metes and bounds description

2. Statutes & Case Law

(a) Definition of Reform - "To correct, rectify, amend, remodel. Instruments inter partes may be reformed, when defective. By this is meant that the court, after ascertaining the real and original intention of the parties to a deed or other instrument (which intention they failed to sufficiently express, through some error, mistake of fact or inadvertence), will decree that the instrument be held and construed as if it fully and technically expressed that intention." Black's Law Dictionary (5th Ed.), page 1152 (1979)

(b) Statutory Authority

(1) S.706.04, Wis. Stats.

Equitable relief. A transaction which does not satisfy one or more of the requirements of s.706.02 may be enforceable in whole or in part under doctrines of equity, provided all of the elements of the transaction are clearly and satisfactorily proved and, in addition:

(1) The deficiency of the conveyance may be supplied by reformation in equity....

(2) S.847.07, Wis. Stats. **Correction of description in conveyance.**

(1) The circuit court of any county in which a conveyance of real estate has been recorded may make an order correcting the description in the conveyance on proof being made to the satisfaction of the court that any of the following applies:

(a) The conveyance contains an erroneous legal description not intended by the parties to the conveyance....

* * *

(2) This section does not prevent an action for the reformation of any conveyance, and if in any doubt the court shall direct the action to be brought.

(c) Case Law

(1) Hine v. Vilter, 88 Wis.2d 645, 277 N.W.2d 772 (Wis. 1979) (action for specific performance of a contract for sale of land where contract failed to properly identify the parties)
"a transaction which does not satisfy the requirements [of the statute of frauds] may still be enforceable provided that all the elements of the transaction are clearly and satisfactorily proved and an equitable reason for enforcement is established."