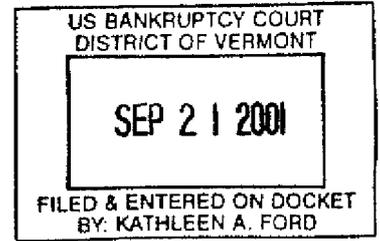


UNITED STATES BANKRUPTCY COURT
DISTRICT OF VERMONT



In re:

Stanley and Susan Potter,
Debtors.

Chapter 13 case
00-10595

Jan M. Sensenich, as Chapter 13 Trustee
of the Estate of Stanley and Susan Potter;
Stanley Potter and Susan Potter,
Plaintiffs,

v.

Mortgage Lenders Network, USA
dba Family Credit Connection,
Defendant.

Adversary Proceeding
01-01031

#171

Appearances: Christopher O'C. Reis, Esq.
Randolph, VT
Counsel for Defendant

Rebecca Rice, Esq.
Rutland, VT
Counsel for Debtors

Jan Sensenich, Esq.
White River Junction, VT
Chapter 13 Trustee

**AMENDED¹ MEMORANDUM OF DECISION
DENYING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT AND
GRANTING PLAINTIFFS' CROSS-MOTION FOR SUMMARY JUDGMENT**

On July 25, 2001, the defendant, Mortgage Lenders Network, USA dba Family Credit Connection (hereafter "Mortgage Lenders") filed a Motion for Summary Judgment [Dkt. #7-1] accompanied by an Undisputed Statement of Facts and Memorandum of Law, seeking a determination that the filing of its Foreclosure Complaint in the applicable clerk's office under 12 V.S.A. § 4523 constituted constructive notice sufficient to prevent the chapter 13 trustee from avoiding its purported lien on the debtors' homestead property. In response, the chapter 13 trustee and the debtors, Stanley and Susan Potter, filed Plaintiffs' Cross-Motion for Summary Judgment on August 28, 2001 [Dkt. #13-1] seeking a judgment in their favor that the subject mortgage fails to constitute a perfected lien on the debtors' property because

¹This Amended Memorandum of Decision supercedes the Memorandum of Decision entered September 20, 2001. The only change made is that reference to the recording of the state court foreclosure judgment issued on or about March 31, 2000 is deleted as a basis for this decision.

it was not witnessed as required under Vermont law. The plaintiffs' cross-motion was accompanied by a response to the defendant's statement of undisputed facts and a memorandum of law. The defendant timely filed a Reply to the Cross-Motion for Summary Judgment. This Court has jurisdiction under 28 U.S.C. §§ 157 and 1334. For the reasons set forth below, the defendant's Motion for Summary Judgment is denied and the plaintiffs' Cross-Motion for Summary Judgment is granted.

THE FACTS

On May 22, 2000, the debtors filed for relief under chapter 13 of title 11 U.S.C. ("the Bankruptcy Code"). Prior to the commencement of the case, the defendant had initiated a foreclosure action against the Potters in state court and filed a copy of its Foreclosure Complaint in the Rutland, Vermont Clerk's Office on January 24, 2000. At the time the subject mortgage between Mortgage Lenders and the Potters was recorded in the land records, it lacked the signature of one or more witnesses as required by 27 V.S.A. § 341 (amended in 1994 to require one witness). The state court issued a Judgment Order and Decree of Foreclosure in favor of Mortgage Lenders on March 31, 2000. No corrective mortgage was filed prior to the entry of the order for relief in this case. The plaintiffs initiated this adversary proceeding on June 28, 2001 seeking to avoid any lien upon the debtors' property in favor of Mortgage Lenders. The defendant's Answer and Affirmative Defenses admitted the material factual allegations of the Complaint, including the allegation that there are no witnesses to the signatures on the mortgage, but denied that the subject mortgage between the parties failed to constitute a valid, perfected mortgage and also denied that the chapter 13 trustee was empowered to avoid the subject mortgage under 11 U.S.C. § 544. Mortgage Lenders interposed the sole affirmative defense of constructive notice. The parties each contend that the foregoing undisputed facts support a judgment in their favor.

THE LAW

a. Summary Judgment Standard

Summary judgment is proper only if the record shows that there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c); Fed. R. Bankr. P. 7056. A genuine issue exists only when "the evidence is such that a reasonable [trier of fact] could return a verdict for the nonmoving party."

Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S.Ct. 2505, 2510, 91 L.Ed.2d 202 (1986); *see also* Celotex Corp. v. Catrett, 477 U.S. 317, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). The substantive law will identify which facts are material. Only disputes over facts that might affect the outcome of the suit under the governing law will properly preclude the entry of summary judgment. Liberty Lobby, 477 U.S. at 247, 106 S.Ct. at 2509. Factual disputes that are irrelevant or unnecessary are not material. Id. Furthermore, materiality is determined by assessing whether the fact in dispute, if proven, would satisfy a legal element under the theory alleged or otherwise affect the outcome of the case. Id. Furthermore, the court must view all the evidence in the light most favorable to the nonmoving party, Valley Liquors, Inc. v. Renfield Importers, Ltd., 822 F.2d 656, 659 (7th Cir.), *cert. den.*, 484 U.S. 977 (1987), and draw all inferences in the non-movant's favor. Santiago v. Lane, 894 F.2d 218, 221 (7th Cir. 1990). In making its determination, the court's sole function is to determine whether there is any material dispute of fact that requires a trial. *See* Waldridge v. American Hoechst Corp., 24 F.3d 918 (7th Cir. 1994).

b. Constructive Notice Under Vermont Law

The defendant relies solely upon 12 V.S.A. 4523 as the basis for its argument that the filing of its Foreclosure Complaint in the city clerk's office constitutes constructive notice upon the chapter 13 trustee and precludes the trustee from avoiding its lien. That statute states in pertinent part:

- b. The plaintiff shall file a copy of the complaint in the town clerk's office in each town where the mortgaged property is located. The clerk of the town shall minute on the margin of the record of the mortgage that a copy of foreclosure proceedings on the mortgage is filed. The filing shall be sufficient notice of the pendency of the action to all persons who acquire any interest or lien on the mortgaged premises between the dates of filing the copy of foreclosure and the recording of the final judgment in the proceedings. Without further notice or service, those persons shall be bound by the judgment entered in the cause and be foreclosed from all rights or equity in the premises as completely as though they had been parties in the original action.

The defendant asserts that pursuant to this Vermont statute it provided *lis pendens* constructive notice of its interest in the Potters' real property and also bound all purchasers, lienholders or other parties in interest, including the chapter 13 trustee, to the terms of the unrecorded judgment order issued by the state court after the Foreclosure Complaint had been recorded in the Rutland clerk's office. On the other hand, the plaintiffs argue that a mortgage deed that is imperfectly executed essentially constitutes a nullity and is incapable of giving constructive notice to others.

It should be noted that under Vermont law, the doctrine of *lis pendens* is not a favorite of the courts and as a general rule the courts construe it strictly and against extending its operation without strict necessity. Cole v. Cole, 91 A.2d 819, 823 (Vt. 1952). Furthermore, it has been observed that the statutory language of 12 V.S.A. 4523(b) binds “persons who acquire their interest between the time of filing the copy of the petition for foreclosure with the town clerk and the recording of the final judgment.” Schott v. Baker, 326 A.2d 157, 158 (Vt. 1974); compare Green Mountain Bank v. Bruehl, 536 A.2d 554, 556 (Vt. 1987)(“the filing of a foreclosure complaint in the town clerk’s office constitutes notice to all persons who subsequently acquire ‘any interest’ in the mortgaged premises”). Under federal law, a bankruptcy trustee has the status of a *bona fide* purchaser of real property who purchased the property in a hypothetical transaction at the commencement of the bankruptcy case. See 11 U.S.C. § 544 (a)(3); see also In re Ryan, 851 F.2d 502, 505 (1st Cir. 1988).

DISCUSSION

After reviewing the statements of undisputed facts and the very thorough memoranda of law filed by counsel for each of the parties and the applicable case law, this Court finds that there are no material facts in dispute and hence that summary judgment is appropriate.

As to the merits, the Court bases its determination that the plaintiffs are entitled to judgment in their favor upon both state and federal law. Of particular significance is the First Circuit decision of In re Ryan, *supra*². In that case, the First Circuit Court of Appeals construed Vermont law as providing that an original deed was not an effective or valid recording, even though the deed and a subsequent valid mortgage assignment were placed in the records of the town clerk, where the deed lacked the requisite signatures of witnesses; and that in such circumstances Vermont law requires that the deed be treated as if it had never been recorded. Id. at 505-507. A deed or mortgage that fails to comply with the statutory witness requirement creates no legal incumbrance on the premises. See Lakeview Farm, Inc. v. Enman, 166 Vt. 158, 689 A.2d 1089 (1997); Day v. Adams, 42 Vt. 510 (1869); see also In re SSL Corporation, 26 F.3d 302, 303

² The defendant cites to the bankruptcy court decision in In re Ryan, 70 B.R. 509 (Bankr. D. Mass. 1987) for the proposition that the lack of a witness on a Vermont mortgage deed provides constructive notice to the trustee. However, as pointed out by the plaintiffs, the bankruptcy court in In re Ryan was subsequently reversed by the district court in In re Ryan, 80 B.R. 264 (D. Mass. 1987), which was affirmed by the First Circuit in In re Ryan, 851 F.2d 502 (1st Cir. 1988), on this very point.

(2nd Cir. 1994); In re Davis, 109 B.R. 633, 637-38 (Bankr. D.Vt. 1989); Merchants Bank v. Bouchard, 568 A.2d 412 (1989).

The majority of jurisdictions that have addressed the issue hold that instruments that are deemed defective because of a missing signature fail to impart constructive notice to a subsequent purchaser. See In re Ryan, 851 F.2d at 510. These cases deal with the very issue raised herein and defeat Mortgage Lenders argument that the trustee had constructive notice of the mortgage because it filed the Foreclosure Complaint in the Rutland clerk's office. Vermont law is clear that an invalid mortgage is not sufficient to put someone on notice and that a deed or mortgage that is improperly witnessed or acknowledged is deemed to be invalid. Lakeview Farm, Inc. v. Enman, *supra*; Day v. Adams, *supra*. Moreover, Vermont courts construe the doctrine of *lis pendens* strictly and against extending its operation without strict necessity. The simple act of recording a copy of foreclosure proceedings based upon an invalid mortgage as described in 12 V.S.A. 4523(b) cannot by *legerdemain* somehow cure the fatal defect and create a valid instrument for purposes of constructive notice. The unpublished decision of Orf v. First NH Bank of Lebanon, AP Case No. 90-0066 (Bankr. D. Vt., Conrad, J., May 11, 1991) is equally compelling and is additional cause to deny the relief sought by the defendant. Significantly, other than constructive notice, the defendant fails to raise any other alternative legal basis in its summary judgment motion or affirmative defenses in support of the relief it seeks herein.

This Court has considered the case law cited by the defendant regarding Washington statutes and a repealed California state curative statute and finds that these enactments, with language materially different from 12 V.S.A. sec. 4523(b), are inapposite and distinguishable from Vermont law.

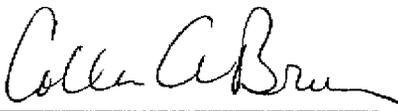
In conclusion, the Court finds that the defendant has failed to raise any persuasive legal argument that warrants a decision different from the holdings of the foregoing Vermont legal authorities, or the In re Ryan case, *supra*. The Court finds that the plaintiffs' position is consistent with state and federal law on this point and therefore holds that the plaintiffs are entitled to summary judgment.

In granting the plaintiffs' summary judgment motion avoiding the subject mortgage lien, it should be noted that a dismissal of this bankruptcy case prior to completion of all payments under the debtors' plan reinstates any avoided lien under 11 U.S.C. § 349(b)(3). In order to ensure that the operation of § 349(b)(1)(B) is not impaired and the subject property is not irreparably compromised during the pendency of this case, this Court will require that the order of lien

avoidance provide that it shall not be entered upon the real estate records relating to the subject property until an order of discharge has been entered in this bankruptcy case and that the property not be transferred or encumbered in the interim without further order of this Court. *See In re Prince*, 236 B.R. 746, 750 (Bankr. N.D. Okla 1999); *In re Stroud*, 219 B.R. 388, 390 (Bankr. M.D. N.C. 1997). The debtors are entitled to a fresh start, including the avoidance of this defective mortgage lien, but only once they have successfully completed their plan and receive a discharge.

Based upon the foregoing, the defendant's Motion for Summary Judgment is denied and the plaintiffs' Cross-Motion for Summary Judgment is granted. Any lien on the subject premises arising from the defendant's invalid mortgage is avoided upon the terms set forth in this decision.

September 21, 2001
Rutland, Vermont



Colleen A. Brown
U.S. Bankruptcy Judge

NOTE:

Although the movant may have designated additional parties to receive this document, the court has served copies of this document only on the parties named below. If a designated party is not listed, they are not in the court's database as a party to this case.

Notice sent to:

Rebecca A Rice
26 West St, Ste 1
Rutland, VT 05701-3274

Christopher O'C Reis
6 N Main St
Randolph, VT 05060

Jan M. Sensenich
6 Palmer Court
White River Jct., VT 05001

U S Trustee
74 Chapel St, Ste 200
Albany, NY 12207-2190

11400 Commerce Park Drive
Suite 600
Reston, Virginia 22091-1506

CERTIFICATE OF SERVICE

District/off: 0210-1
Case: 01-01031

User: kaf
Form ID: #07

Page 1 of 1
Total Served: 4

Date Rcvd: Sep 21, 2001

The following entities were served by first class mail on Sep 23, 2001.
aty-def +Christopher O'C Reis, 6 N Main St, Randolph, VT 05060-1127
pla +Jan M. Sensenich, 6 Palmer Court, White River Jct., VT 05001-3323
aty-pla +Rebecca A Rice, 26 West St, Ste 1, Rutland, VT 05701-3274
cr U.S. Trustee, 74 Chapel St #200, Albany, NY 12207

The following entities were served by electronic transmission.
NONE.

TOTAL: 0

***** BYPASSED RECIPIENTS *****

NONE.

TOTAL: 0

Addresses marked '+' were corrected by inserting the ZIP or replacing an incorrect ZIP.
USPS regulations require that automation-compatible mail display the correct ZIP.

I, Joseph Speetjens, declare under the penalty of perjury that I have served the attached document on the above listed entities in the manner shown, and prepared the Certificate of Service and that it is true and correct to the best of my information and belief.

Date: Sep 23, 2001

Signature:

