Not For Publication

UNITED STATES BANKRUPTCY COURT
DISTRICT OF CONNECTICUT

IN RE:	)	CASE NO.	01-32463 (LMW)
GARRY KLINGER,	)	CHAPTER	7
DEBTOR.	)	DOC. I.D. NOS.	755, 768

APPEARANCES

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MEMORANDUM OF DECISION AND ORDER RE: CLAIM NO. 48

Lorraine Murphy Weil, United States Bankruptcy Judge

There is a surplus (the "Surplus") in this chapter 7 case after payment of timely-filed claims. Stewart Title Guaranty Company ("Stewart") has filed a late proof of claim (the "POC") with respect to Claim No. 48 in the amount of $71,500.00 seeking distribution from the Surplus pursuant to 11 U.S.C. § 726(a)(3). The above-referenced debtor (the "Debtor") has filed an objection (Doc.

I.D. No. 755, the "Objection")[1] to the POC. This court has jurisdiction over this matter as a core proceeding pursuant to 28 U.S.C. §§ 157 and 1334 and that certain Order dated September 21, 1984 of the District Court (Daly, C.J.).[2] This memorandum constitutes the findings of fact and conclusions of law required by Rule 7052 of the Federal Rules of Bankruptcy Procedure (made applicable here by Rule 9014 of the Federal Rules of Bankruptcy Procedure).

I. PROCEDURAL BACKGROUND

The Debtor commenced this case by a chapter 11 petition filed on May 11, 2001. The case was converted to a case under chapter 7 on November 15, 2001. (*See* Doc. I.D. No. 313.) March 11, 2002 was set as the last day for filing proofs of claim in this case. (*See* Doc. I.D. No. 314.) The Debtor was denied a discharge in this case by judgment dated October 22, 2003. (*See* Doc. I.D. No. 680.) Stewart filed the POC on April 10, 2006[3] and the Debtor filed the Objection on June 26, 2006. The chapter 7 trustee (the "Trustee") serving in this case filed her Final Dividend Distribution Report (Doc. I.D. No. 781) on September 8, 2006; that report establishes the existence of the Surplus.[4]

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[1] References herein to the docket of this chapter 7 case appear in the following form: "Doc. I.D. No. ___." Stewart's response to the Objection appears in the record as Doc. I.D. No. 768.

[2] That order referred to the "Bankruptcy Judges for this District" *inter alia* "all proceedings arising under Title 11, U.S.C., or arising in . . . a case under Title 11, U.S.C. . . . ." References herein to title 11 of the United States Code or to the Bankruptcy Code are references to the same as they appeared prior to the effective date of their amendment by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

[3] The POC asserts a general unsecured claim in the amount of $71,500.00 with respect to a certain note (described with more particularity below, the "Note") which Stewart claims to hold by assignment (endorsement). A copy of the endorsed Note is annexed to the POC.

[4] The Debtor has standing to object to claims against the Surplus. *See* 11 U.S.C. § 726(a)(6).

The Objection first came on for a non-evidentiary hearing on August 30, 2006. The Debtor participated in that hearing telephonically.[5] This court issued an Order Requiring Further Briefing on September 6, 2006. (*See* Doc. I.D. No. 778.) Both parties submitted briefs in compliance with that order. (*See* Doc. I.D. Nos. 786 (Stewart's Initial Brief), 789 (the Debtor's Answer Brief).) The court subsequently scheduled this matter for an evidentiary hearing (the "Hearing") to be convened on March 6, 2007.[6] The Hearing was convened as scheduled. Albert Strazza, Esq. testified at the Hearing for Stewart and Stewart introduced documentary evidence into the record.[7] At the conclusion of the Hearing the court took the matter under advisement and the matter now is ripe for decision.

II. FACTS[8]

Prior to the commencement of this case, the Debtor was a paralegal. Prior to the commencement of this case, the Debtor also was in the business of buying, selling and leasing real property. The Debtor purchased certain real property (the "Property") in West Haven, Connecticut known as 91 Meloy Road in March of 1998 for $95,000.00. (*See* Hearing Exh. A1.) It is undisputed that the Debtor executed the Note as maker on or about June 8, 1999. The Note was in the stated principal amount of $71,500.00 and was made payable to Chase Manhattan Mortgage Corporation ("Chase") as payee. It is undisputed that the loan evidenced by the Note was fully funded. It is

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[5] The Debtor is incarcerated.

[6] The court issued a *Pro Se* Writ of Habeas Corpus Ad Testificandum to enable the Debtor to appear at the Hearing in person. (*See* Doc. I.D. No. 795.)

[7] References herein to the Hearing exhibits appear in the following form: "Hearing Exh. ___." A transcript of the Hearing is in the record as Doc. I.D. No. 800 and references herein to that transcript appear in the following form: "Transcript at ___."

[8] The facts stated below and elsewhere in this opinion are taken from the record made at the Hearing and the record of this entire case.

undisputed that the Note was secured by a mortgage (the "Mortgage") on the Property.[9] It is uncontested that, on or about June 9, 1999, Chase obtained an ALTA Loan Policy of title insurance (the "Policy") from Stewart with respect to the Mortgage. Among other things, the Policy stated that the Mortgage had been "recorded [on] June 9, 1999 at 2:45 p.m. in the West Haven Land Records." (*See* Doc. I.D. No. 786 (copy of Policy annexed as Exhibit A to the Affidavit (the "Affidavit") of Pamela Butler O'Brien, Regional Litigation Counsel for Stewart).) The Policy insured Chase against loss or damage sustained or incurred by Chase by reason of "[t]he invalidity or unenforceability of the lien of the insured mortgage upon the title . . . ." (*Id.*) The Policy also provides that "[i]n case of a claim under this policy, [Stewart may] . . . [p]urchase the . . . [Note]." (*Id.* § 6.) The Mortgage is not of record in the Town of West Haven.[10]

The Policy issuing attorney (the "Attorney") was Pacific T. Giordano, Esq. The Attorney was the limited agent of Stewart "only for the purposes of issuing title policies in the name of STEWART . . . ." (Doc. I.D. No. 786 (Exhibit B (as amended in 1997, the "Retainer Agreement") annexed to the Affidavit).) The Retainer Agreement provides in relevant part:

> DIVISION OF LOSS AND LOSS EXPENSE: The term "Loss" shall include the amount paid to or for the benefit of the insured, as well as loss adjustment expense including any cost of defending the claim resulting in the loss.
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> (b) The relationship between ATTORNEY and STEWART under this Agreement is that of Attorney and Client, and the responsibility and liability of each party to the other shall be governed by the law relating to Attorney and Client; however, without limiting liability of the ATTORNEY, the ATTORNEY shall be liable to STEWART for any loss which STEWART

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[9] During the period April, 1998 through January, 2000, the Debtor encumbered the Property with other mortgages. (*See* Hearing Exh. B.) The status (existence) of those other mortgages as of the commencement of this case is unclear.

[10] *See* Transcript at 8 (testimony of Attorney Strazza); Hearing Exh. A6 (copies of grantor and grantee indices).

> may sustain or incur under any policy issued pursuant to this Agreement occasioned by any fraud[,] intentional act, or omission or negligence of ATTORNEY in performing of his undertaking hereunder, including, but without limiting the generality of the foregoing any loss resulting from any error in abstracting which was not performed by an abstractor approved by STEWART, any loss resulting from an error in the examination of the title, or any loss resulting from any error in closing of the transaction, or any loss resulting from a violation of this Agreement, or a violation of the instructions given by STEWART. ATTORNEY does not and shall not represent that ATTORNEY is closing the transaction on behalf of STEWART.
>
> (c) The liability of ATTORNEY hereunder shall survive and remain in the event of the termination of this Agreement for any cause, including the expiration thereof.
>
> (d) In all instances in which ATTORNEY is liable as defined in this paragraph, ATTORNEY shall be liable to STEWART for all reasonable costs and expenses incurred in connection therewith, and the fee of any associate counsel retained by STEWART. STEWART shall have no obligation to defend ATTORNEY.
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> (e) ATTORNEY is expressly not appointed as an agent of STEWART for purposes of providing abstracting and/or escrow services, and STEWART shall have no liability or responsibility for any claims or losses due to ATTORNEY acting in his own capacity as principal in providing such abstracting and/or escrow services. . . .

(Retainer Agreement ¶ 7.)[11]

By deed dated July 9, 1999, the Debtor quitclaimed the Property to Tomarra Dawn Klinger. (*See* Hearing Exh. A2.) By deed dated January 17, 2000, Ms. Klinger quitclaimed the Property back to the Debtor. (*See* Hearing Exh. A3.) As noted above, the Debtor commenced this case on May 11, 2001. Chase obtained relief from stay to foreclose the Mortgage by order dated January 23, 2002. (*See* Doc. I.D. No. 478, the "R/S Order.") The Trustee abandoned the estate's interest in the

[11] An amendment to the Retainer Agreement struck a formerly existing paragraph (a) in its entirety. The amendment claimed to modify paragraph (b) above but no changes were made to that paragraph.

Property in April, 2002. (*See* Doc. I.D. No. 566.)[12] The Debtor sold the Property to Susan Arnold for $183,000.00 in April, 2003. (*See* Hearing Exh. A4, the "Warranty Deed.") That transfer was effectuated by the Warranty Deed dated April 22, 2003 which contained no exception for the Mortgage (or any other mortgage). (*See id.*) Substantially contemporaneously, Ms. Arnold encumbered the Property with a mortgage (the "DBNTC Mortgage") in favor of People's Choice Home Loan, Inc. (together with its assigns, "DBNTC"). (*See* Hearing Exh. A5.) Some time in 2004, DBNTC commenced foreclosure proceedings on the DBNTC Mortgage. (*See id.*) Title to the Property became absolute in DBNTC pursuant to those proceedings in February, 2005. (*See id.*)

Some time after entry of the R/S Order, Chase discovered that the Mortgage was not of record and made a claim (the "Policy Claim") under the Policy. (*See* Affidavit.) After investigation of the Policy Claim, Stewart purchased the Note for $71,500.00 and Chase endorsed the Note over to Stewart. (*See id.*; POC (attachments).) Chase never filed a proof of claim in this case. As noted above, Stewart filed the POC as a late claim.

III. ANALYSIS

A. Legal Standard

> A proof of claim, if it is executed and filed in accordance with the Federal Rules of Bankruptcy Procedure, constitutes *prima facie* evidence of the validity and amount of that claim, Fed. R. Bankr. P. 3001(f), and is deemed allowed unless a party in interest objects under 11 U.S.C. § 502(a).
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> . . .
>
> [T]he burden of persuasion under the bankruptcy claims procedure always lies with the claimant, who must comply with Fed. R. Bankr. P. 3001 by alleging facts in the proof of claim that are sufficient to support the claim. If the claimant satisfies these requirements, the burden of going forward with the evidence then shifts to the objecting party to produce evidence at least equal in probative force to that offered

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[12] Accordingly, the automatic stay has not applied to the Debtor personally or property that is not property of the estate since denial of the Debtor's discharge, and has not applied to the Property specifically since its abandonment. *See* 11 U.S.C. § 362(c)(1), (2).

> by the proof of claim and which, if believed, would refute at least one of the allegations that is essential to the claim's legal sufficiency. *See Lundell v. Anchor Const. Specialists, Inc. (In re Lundell),* 223 F.3d 1035, 1041 (9th Cir. 2000); *Sherman v. Novak (In re Reilly),* 245 B.R. 768, 773 (2d Cir. BAP 2000) . . . . If the objecting party meets these evidentiary requirements, then the burden of going forward with the evidence shifts back to the claimant to sustain its ultimate burden of persuasion to establish the validity and amount of the claim by a preponderance of the evidence. *See In re Consumers Realty & Development Co.,* 238 B.R. 418 (8th Cir. BAP 1999); *In re Allegheny International, Inc.,* 954 F.2d 167, 173-74 (3d Cir. 1992).

In re Rally Partners, L.P., 306 B.R. 165, 168-69 (Bankr. E.D. Tex. 2003).

The POC (together with its attachments) is regular on its face and otherwise complies with Rule 3001. Accordingly, the burden of going forward at the Hearing with contrary evidence was on the Debtor. However, even if the foregoing were not true (and the burden of going forward and the burden of persuasion were on Stewart at the Hearing (except with respect to the Debtor's affirmative defenses)), the result would be no different here.

B. Objections

The Debtor objects to the POC on various grounds considered below.

1. Late-Filed Claim

The Debtor argues that the POC must be disallowed because it was filed late and no motion for allowance as a late claim was filed. For the reasons set forth below, that argument is not persuasive.

Section 502(b)(9) of the Bankruptcy Code provides in relevant part that a claim be disallowed if "proof of such claim is not timely filed, except to the extent tardily filed as permitted under paragraph . . . (3) of section 726(a) of this title . . . ." 11 U.S.C.A. § 502(b) (West 2005). Section 726(a)(3) provides that late-filed claims may be paid but on a subordinated basis as provided for therein. *See* 11 U.S.C.A. § 726(a). Stewart confirms that it is seeking only payment on a subordinated basis (i.e., as a late-filed claim) in accordance with Section 726(a)(3). No motion for

permission to file a Section 726(a)(3) claim is required. Accordingly, if otherwise appropriate the POC may be allowed as a late-filed claim (against the Surplus) and the Debtor's timeliness objection cannot prevail.

2. Payment

The Debtor argues that Stewart paid (*i.e.,* discharged) the Note when it paid Chase. Payment is an affirmative defense on which the Debtor bears the burden of proof in all events. *See Selvaggi v. Miron,* 60 Conn. App. 600, 601 (2000) ("The burden of proving the special defense of payment rests upon the defendant.").

> A third person's payment of a debtor's obligation differs from the third person's purchase of the debt in that payment discharges the debt while purchase does not discharge the debt, which is enforceable by the third person. Ordinarily, the intention of the parties determines whether a transfer of money by a third person to a creditor constitutes a discharge or purchase of an underlying debt.

60 Am. Jur. 2d *Payment* § 5 (2007) (footnotes omitted). Here, the only evidence of Chase's and Stewart's intent is Chase's endorsement of the Note over to Stewart. That endorsement is consistent with a Note purchase and inconsistent with a discharge of the Note. The Debtor produced no evidence of a "payment" intent (or of any other form of payment). Accordingly, the court concludes that the Note was not paid by Stewart.[13]

3. Laches

The Debtor argues that, although the Mortgage may have been unrecorded, it still was enforceable as against him (even if unenforceable against third parties). That is true. The Debtor further argues that, if Chase had foreclosed in a timely fashion, it could have fully satisfied the Note

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[13] Any argument that Stewart should be required to marshal its security (i.e., its unperfected mortgage) (*see* Conn. Gen. Stat. § 52-380i) is irrelevant because (as noted above) the Mortgage was foreclosed out by DBNTC and there is no security left to marshal.

in those foreclosure proceedings. Construing the foregoing in the light most favorable to the Debtor, he has alleged the defense of laches with which Stewart may be chargeable as Chase's assignee.

"Laches consists of an inexcusable delay which prejudices the defendant . . . . Delay alone is not sufficient to bar a right; the delay in bringing suit must be unduly prejudicial." *Cummings v. Tripp,* 204 Conn. 67, 88 (1987) (citations and internal quotations omitted). The burden is on the party alleging laches (*i.e.,* the Debtor) to establish that defense. *See id.* at 88. Here there is no persuasive evidence in the record that the Debtor was prejudiced by the non-foreclosure. Arguably, one piece of evidence in the record (the Warranty Deed) is inconsistent with the Debtor's laches argument. That is because the Warranty Deed could be interpreted as evidence that the Debtor himself used the "delay" as an opportunity to extract from the Property the value which should have been attributed to the (unrecorded) Mortgage. In any event, the court finds and/or concludes that the Debtor has not satisfied his burden of proof with respect to laches.

4. Improper Payment of the Policy Claim

The Debtor argues (on various grounds) that the Policy Claim was not a good claim under the Policy and Stewart should not have paid it. The Debtor does not explain why that should be relevant here (even if it is true, a matter upon which the court makes no findings or conclusions). Stewart purchased the Note from Chase and Chase's endorsement of the Note over to Stewart merely substituted Stewart for Chase. Accordingly, this particular objection cannot prevail.

5. Retainer Agreement ¶ 7

The Debtor argues that Stewart must proceed against the Attorney under paragraph 7 ("Paragraph 7") of the Retainer Agreement rather than against the Debtor himself (or at least before proceeding against him.) The Debtor does not explain how Paragraph 7 waives (or defers) Stewart's rights with respect to the Note (and its maker) under Section 6 of the Policy. Those two sets of

rights are alternatives and not inconsistent as a matter of law. Accordingly, the court will not find a waiver or deferral without proof of Stewart's intent to waive or defer. No such proof was offered by the Debtor at the Hearing. Accordingly, this particular objection cannot prevail.

6. RESPA

The Debtor argues that various alleged failures to comply with the provisions of the Real Estate Settlement Procedures Act (12 U.S.C. §§ 2601 *et seq.*, "RESPA") bar Stewart's enforcement of the Note. As an initial matter, RESPA applies only to consumer transactions (*i.e.,* for personal, family or household use). *See* 12 U.S.C.A. § 2606 (West 2007) ("This chapter does not apply to credit transactions involving extensions of credit – . . . primarily for business, commercial, or agricultural purposes . . . ."). The record supports the finding that the Debtor's 1998 purchase of the Property was not a consumer transaction. (*See* Transcript at 16:15-25, 19:3-14 (summary of record by Stewart's counsel).) Accordingly, RESPA does not apply on its face.

Moreover, failure to comply with RESPA does not adversely affect the validity or enforceability of the Note. *See* 12 U.S.C. § 2615 (West 2007). *See also G.E. Capital Mortgage Services, Inc. v. Baker,* No. CV 980167089S, 1999 WL 511156, at *4 (Conn. Super. Ct. July 7, 1999) (applying Section 2615); *Security Pacific Nat'l Bank v. Robertson,* No. CV 920124622S, 1997 WL 561235, at *4 (Conn. Super. Ct. Aug. 28, 1997) (same).[14]

The Debtor's RESPA defense is unpersuasive for the foregoing reasons.

[14] There is no reason in this case to graft an equitable exception onto Section 2615. *Cf. Bibler v. Arcata Investments 2, LLC,* No. 263024, 2005 WL 3304127 (Mich. Ct. App. Dec. 6, 2005).

7. Demand

The Debtor argues that the POC must be disallowed because no valid demand for payment of the Note was made on him or the Trustee. The POC constitutes a demand upon the Trustee with respect to the Note. The Debtor admits that "[d]emand for satisfaction, absent relief from stay, was made on the incarcerated [D]ebtor]in] January [,] 2006." (Objection ¶ 5.) As noted above, the Debtor has not been protected by the automatic stay in this case since October 22, 2003, and he received no discharge in this case. Accordingly, to the extent that demand upon the Trustee and the Debtor is necessary for allowance of the POC (and the court makes no conclusions in that regard), such demand has been made.

8. State Licensing Requirements

The Debtor argues that Stewart cannot lawfully hold the Note because it is not licensed under Connecticut law as either a bank or a mortgage company. It is true that a mortgage loan made by an applicable lender without compliance with the licensing requirements of Title 36a, Chapter 668, Part I of the Connecticut General Statutes is unenforceable. *See Solomon v. Gilmore,* 248 Conn. 769 (1999). However, the applicable licensing requirements, like RESPA, apply only to consumer transactions. *See* Conn. Gen. Stat. §§ 36a-485(6) (definition of "first mortgage loan"), 36a-510(10) (definition of "secondary mortgage loan"). Moreover, those licensing requirements apply only to "the . . . making [of] . . . mortgage loans." Conn. Gen. Stat. Ann. §§ 36a-486(a), 36a-511(a) (West 2007).[15] It is not contended that Chase was unlicensed when the subject loan was made.

[15] It appears that the state licensing statutes might not have applied to Chase (and consequently to Stewart, as its assignee). *Cf. Wachovia Bank, N.A. v. Burke*, 414 F.3d 305 (2d Cir. 2005), *cert. denied*, 127 S. Ct. 2093 (2007) (holding that Connecticut state licensing statutes do not apply to national banks because such statutes are preempted by the National Bank Act, 12 U.S.C. § 21 *et seq.*). *Cf. also Walters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559 (2007). The issue was not raised by the parties.

Furthermore, there is nothing in the state licensing requirements which prevents an unlicensed entity from enforcing by assignment a loan originally extended by a licensed lender.

For all of the reasons stated above, the Debtor's "licensing" defense is unpersuasive.[16]

IV. CONCLUSION

For the reasons set forth above, the court concludes that the Objection must be overruled and that the POC should be allowed as a claim for distribution under Bankruptcy Code § 726(a)(3). It is **SO ORDERED.**

Dated: June 21, 2007

BY THE COURT

Lorraine Murphy Weil
United States Bankruptcy Judge

[16] The court has considered all of the Debtor's remaining arguments and concludes that they are unpersuasive.