STATE OF MINNESOTA
IN COURT OF APPEALS
A09-1897

Bank of New York, as Trustee,
on Behalf of the Certificate Holders CWABS, Inc.,
Respondent,

vs.

PK Investment Properties, LLC,
Appellant,

Paul Holmes, et al.,
Defendants.

Filed July 13, 2010
Affirmed
Bjorkman, Judge

Anoka County District Court
File No. 02-CV-08-457

Eric D. Cook, Wilford & Geske, P.A., Woodbury, Minnesota (for respondent)

Nathan M. Hansen, North St. Paul, Minnesota (for appellant)

Considered and decided by Worke, Presiding Judge; Halbrooks, Judge; and Bjorkman, Judge.

U N P U B L I S H E D O P I N I O N

BJORKMAN, Judge

Appellant challenges the district court's determination that respondent's interest in the subject real property is senior to its interest. Because the district court did not err in

determining that respondent's mortgage has priority over appellant's interest in the property, we affirm.

FACTS

In December 2004, Paul Holmes purchased a condominium located in the City of Ramsey in Anoka County. The legal description of the property is "Unit Number 113, CIC No. 187, Rivenwick Condominium, Anoka County, Minnesota" (the property). Holmes obtained a mortgage: the lender was Countrywide Home Loans d/b/a America's Wholesale Lender and the mortgagee was Mortgage Electronic Registration Systems, Inc. (MERS). The recorded mortgage contained the following legal description: "Unit 113, of Rivenwick Village, according to the recorded plat thereof, Anoka County, Minnesota." This description was incorrect because it omitted the CIC number and used the word "village" instead of "condominium." Because of this error, the mortgage appeared in the Anoka County grantor/grantee index, which lists properties by owners' names, but not in the tract index, which lists properties by legal description.

Beginning in April 2005, Holmes stopped paying his mortgage and went into default. He ceased paying his homeowners' association dues around the same time.

The homeowners' association placed a lien on the property, in the amount of $2,013.49, on October 10, 2005. The association recorded a notice of pendency to foreclose the lien with the correct property description on the same date, and a sheriff's sale was scheduled for January 31, 2006. Philip Rosar, chief manager of appellant PK

Investment Properties, LLC, purchased the property on behalf of appellant for $4,269.[1] Before purchasing the property, Rosar researched the property through the tract index. He did not review the grantor/grantee index. Rosar asserted at trial that he was not aware of the mortgage on the property until he met with Holmes after the sheriff's sale.[2]

On January 25, 2006, days before appellant purchased the property, MERS assigned its mortgage to respondent The Bank of New York, as trustee on behalf of the Certificate Holders of CWABS, Inc., Alternative Loan Trust 2004-15, Mortgage Pass-Through Certificates, series 2004-15. On January 30, respondent filed a notice of lis pendens under the correct legal property description announcing its intention to reform the legal description and foreclose on the mortgage. Respondent recorded the assignment of the mortgage on February 2, and initiated its foreclosure action on February 26. Respondent obtained judgment in its favor and purchased the property at the August 31 sheriff's sale for $163,056.71. An order confirming the sale to respondent was entered by the district court on October 9. But when the sheriff's certificate of sale was recorded on October 16, it incorrectly reflected that MERS purchased the property. Upon learning of this error, MERS quitclaimed any interest it had in the property to respondent on February 14, 2008.

[1] Appellant does not contest that Rosar acted as its authorized agent in this purchase.

[2] Holmes continued to live at the property after the sale and paid monthly rent to appellant.

Respondent commenced an action to evict Holmes in June 2007. Based on the ownership dispute between the parties, the district court dismissed the eviction action without prejudice.

Respondent commenced this declaratory-judgment action seeking to establish the priority of its interest in the property under the Minnesota Common Interest Ownership Act (MCIOA), Minn. Stat. § 515B.3-116(b)(ii) (2008), and under the Minnesota Recording Act, Minn. Stat. § 507.34 (2008). Appellant asserted its own priority under the recording act based on the legal errors in the recorded mortgage, and challenged respondent's existence and capacity to sue.

A trial was held on May 11, 2009. The district court granted judgment in respondent's favor, determining that its interest in the property is superior to appellant's interest. The district court concluded that appellant was not a bona fide purchaser under the recording act because appellant had constructive and inquiry notice of respondent's mortgage. The district court also concluded that the mortgage takes priority over the association lien under the MCIOA. This appeal follows.

D E C I S I O N

In reviewing declaratory judgments, we apply a clearly erroneous standard to the district court's findings of fact and review the district court's legal conclusions de novo. *Pestka v. County of Blue Earth*, 654 N.W.2d 153, 157 (Minn. App. 2002), *review denied* (Minn. Feb. 26, 2003). We do not reverse the district court's factual findings unless they are manifestly contrary to the weight of the evidence or not reasonably supported by the evidence as a whole. *Milbank Ins. Co. v. Johnson*, 544 N.W.2d 56, 59 (Minn. App.

1996). We give deference to the findings of the district court, which had the advantage of hearing the testimony and judging the credibility of the witnesses. *Hasnudeen v. Onan Corp*., 552 N.W.2d 555, 557 (Minn. 1996).

I. The district court did not err in finding that respondent is a legal entity and has capacity to seek declaratory relief.

From its first responsive pleading in this matter, appellant has challenged respondent's capacity to sue, arguing that respondent must prove that it exists as a New York corporation. While appellant may have legitimate concerns about and frustrations with the complexities and operation of the secondary mortgage market, these concerns do not translate into a successful legal challenge in this case.

The Minnesota Rules of Civil Procedure provide that a party's legal existence and capacity to sue are presumed, and the burden of overcoming these presumptions lies with the challenging party:

> It is not necessary to aver the capacity of a party to sue or be sued, the authority of a party to sue or be sued in a representative capacity, or the legal existence of a partnership or an organized association of persons that is made a party. A party who desires to raise an issue as to the legal existence of any party, the capacity of any party to sue or be sued, or the authority of a party to sue or be sued in a representative capacity shall do so by specific negative averment, which shall include such supporting particulars as are peculiarly within the pleader's knowledge.

Minn. R. Civ. P. 9.01. To successfully challenge a party's capacity to sue, the challenging party must provide evidence supporting its allegations that the challenged party lacks capacity. *See Lehigh Valley Coal Co. v. Gilmore*, 93 Minn. 432, 434, 101

N.W. 796, 797 (1904) (explaining that the production of evidence is an affirmative burden).

Apart from its bald assertions, appellant produced no evidence to defeat respondent's presumed existence and capacity to sue. The district court took judicial notice of the fact that respondent is registered with the FDIC and that its FDIC certificate number is 639. Public records show that respondent is duly registered as a corporation with the New York Secretary of State. Because appellant provided no evidence directly related to respondent's alleged lack of existence and legal capacity, the district court did not err in determining that respondent is a New York corporation that has capacity to proceed with this action.

Appellant also challenges the district court's finding based on the fact that respondent commenced this suit in January 2008, eight months after The Bank of New York merged with another entity to become The Bank of New York Mellon. Although appellant's factual assertion is accurate, under New York law, when a merger occurs, the new corporation may take up the liabilities and obligations of its premerger constituents. N.Y. Bus. Corp. Law § 906 (2010). And legal actions "may be enforced, prosecuted, settled or compromised *as if such merger or consolidation had not occurred*." *Id.* (emphasis added). Minnesota has a similar statutory provision. Minn. Stat. § 302A.691, subd. 2(b)(5) (2008). Respondent's decision to prosecute this action in its premerger name, the same name in which it pursued its February 2006 judicial foreclosure action, does not affect its capacity to bring this declaratory-judgment action.

II. The district court did not err in finding that respondent's mortgage is superior to appellant's interest in the property.

The district court concluded that appellant was not a bona fide purchaser under the Minnesota Recording Act because it had constructive and implied notice that a first mortgage encumbered the property. The district court also concluded that, pursuant to the MCIOA, respondent's mortgage has priority over the association lien on which appellant foreclosed. We agree.

Under the MCIOA, an association lien "is prior to all other liens and encumbrances on a unit except . . . (ii) any first mortgage encumbering the fee simple interest in the unit." Minn. Stat. § 515B.3-116(b). Appellant does not contest the district court's conclusion that respondent's mortgage has priority under the MCIOA.

But this court has determined that even when priority is granted to one party by the MCIOA, bona fide purchasers are entitled to the protection of the recording act. *Wash. Mut. Bank, F.A. v. Elfelt*, 756 N.W.2d 501, 509 (Minn. App. 2008), *review denied* (Minn. Dec. 16, 2008). The recording act provides that unrecorded conveyances "shall be void as against any subsequent purchaser in good faith and for a valuable consideration of the same real estate . . . whose conveyance is first duly recorded." Minn. Stat. § 507.34. The recording act is designed to protect bona fide purchasers, who, in reliance on the record, "give[] valuable consideration without actual, implied or constructive notice of inconsistent outstanding rights of others." *Miller v. Hennen*, 438 N.W.2d 366, 369 (Minn. 1989). The burden of proving bona fide purchaser status falls on the party claiming its protections. *Id.*

Appellant argues that it was a bona fide purchaser and thus entitled to the protection of the recording act. The issue before us is whether the district court clearly erred in finding that appellant had constructive and implied notice of the mortgage when appellant purchased the property. We address each of the district court's findings in turn.

Constructive Notice

"Constructive notice is a creature of statute, and as a matter of law, imputes notice to all purchasers of any properly recorded instrument even though the purchaser has no actual notice of the record." *Miller*, 438 N.W.2d at 369-70; *see also* Minn. Stat. § 507.32 (2008) ("The record, as herein provided, of any instrument properly recorded shall be taken and deemed notice to the parties."). Constructive notice of a mortgage arises as a presumption of law based on the mere existence of the record. *MidCountry Bank v. Krueger*, 782 N.W.2d 238, 245 (Minn. 2010). And although constructive notice is limited to "the facts appearing on the face of the record," *Miller*, 438 N.W.2d at 370 (quotation omitted), the record includes the entries in the recording index and the full documents to which the entries refer, *MidCountry Bank*, 782 N.W.2d at 249-50.

Appellant first argues that it did not have constructive notice of respondent's mortgage because the mortgage did not appear in the tract index, and appellant was not obligated to check the grantor/grantee index. We disagree.

Minnesota Statutes chapter 386 requires counties to keep both a tract index and a grantor/grantee index, through which searches for property records may be conducted.[3] Minn. Stat. §§ 386.03, .05, .19 (2008). The tract index lists recorded documents by the legal description of the property.[4] Minn. Stat. § 386.05. The grantor/grantee index lists the instruments by the last names of the seller and buyer. Minn. Stat. § 386.03. Purchasers of property are charged with notice of the entries in both indices and the contents of the full documents. *MidCountry Bank*, 782 N.W.2d at 251.

Appellant next argues that it cannot be charged with constructive notice of the mortgage recorded in the grantor/grantee index because of the errors in the legal description. Because of these errors, appellant asserts, the mortgage is not an instrument "properly recorded." Minn. Stat. § 507.32. We disagree.

Our supreme court recently rejected a strict interpretation of section 507.32, holding that "'properly recorded' requires a reference in the indexes sufficient to locate the document and a record of the document itself, and that between the indexes and the record, there is sufficient evidence that the document pertains to the property." *MidCountry Bank*, 782 N.W.2d at 250. A legal description provides constructive notice

[3] Counties are also required to keep a "consecutive index," which lists the documents by the number of the instrument and the time of its reception. Minn. Stat. § 386.32 (2008). This index is not at issue in this case.

[4] Prior to 2005, a county recorder's office was permitted, but not required, to keep a tract index. *See* 2005 Minn. Laws ch. 4, § 75, at 10, 40 (codified at Minn. Stat. § 386.05 (2008)) (changing the words "*may* procure . . . and keep . . . [a] tract index" to "*shall* procure . . . and keep . . . [a] tract index" (emphasis added)). But, "[i]f a county chooses to maintain a tract index, the county is required by law to make accurate and appropriate entries and the tract index is part of the record of which a purchaser is charged constructive notice." *Miller*, 438 N.W.2d at 370 (citation and quotation marks omitted).

if the property can be identified "with reasonable certainty," *Bank of Ada v. Gullikson*, 64 Minn. 91, 94, 66 N.W. 131, 132 (1896), or if it is apparent from the record that there is a defect in the description, *Howard, McRoberts & Murray v. Starry*, 382 N.W.2d 293, 296 (Minn. App. 1986).

The only errors in the mortgage's legal description were the omission of the CIC number and the substitution of the word "village" for "condominium." Respondent submitted substantial evidence that, despite these errors, the property could be identified with reasonable certainty. Sandra Ahles, a licensed abstractor, testified that the information contained in the tract and grantor/grantee indices was sufficient for potential purchasers to identify the property and accompanying mortgage with reasonable certainty. No mortgage appeared in the tract index, but that index contained the property owner's name, Paul Holmes. By searching the grantor/grantee index for any encumbrances associated with Holmes' name, Ahles found the mortgage. She noted that the legal description was very close to the one contained in the tract index, that the transaction dates were close, and that the street addresses were the same.

Even if Rosar were uncertain about the relationship between the mortgage and the property based on the legal description in the grantor/grantee index, the mortgage document on file with the county recorder contained the correct street address, which would have enabled him to definitively identify the property. On this record, we conclude that the district court did not clearly err in finding that appellant had constructive notice of the mortgage.

Implied Notice

Implied notice charges purchasers with knowledge of facts beyond the face of the written records. *Claflin v. Cmty. State Bank of Two Harbors*, 487 N.W.2d 242, 248 (Minn. App. 1992), *review denied* (Minn. Aug. 4, 1992). For example, "[i]f one is aware that someone other than the vendor is living on the land, one has a duty to inquire concerning the rights of the inhabitant of the property and is chargeable with notice of all facts which such inquiry would disclose." *Id.*

The district court determined that appellant had implied notice based on two grounds: (1) Rosar was an experienced property vendor/purchaser, and thus should have inquired further when he saw that the property had been owned for less than a year and had no mortgage listed and (2) appellant is charged with any knowledge it would have gained from speaking to the inhabitants of the property.

Holmes was living at the property at all times prior to appellant's purchase of the association lien. His trial testimony supports the district court's conclusion that "[a] cursory conversation with [Holmes] would have immediately led to the discovery that [Holmes'] interest in the property was subject to a mortgage." Appellant's reliance on Minn. Stat. § 325N.17 (2008) for the proposition that it is statutorily prevented from speaking with the inhabitants of a property subject to foreclosure before the sheriff's sale is misplaced. The statute contains no such prohibition. In fact, by prohibiting purchasers from making certain representations to and deals with homeowners prior to a sheriff's sale, the statute actually presumes that presale contact will occur. *See* Minn. Stat. § 325N.17(e) (defining impermissible contacts).

Further, the record evidence and common sense support the district court's finding that

> [i]t would be highly unusual for a parcel of property that had been owned less than one year to not have a mortgage *and* for the owner of a parcel of unencumbered property with a fair market value of over $150,000 to let the property be lost to foreclosure on a lien that was less than $2,500.

The discrepancy between the market value and foreclosure amount reasonably should have raised a red flag for an experienced property vendor such as Rosar, implicating his duty to inquire further into the status of the property. Our review of the record reveals no clear error in the district court's implied-notice finding.

Because appellant did not meet its burden of establishing that it was a bona fide purchaser, the district court did not err in finding that respondent's interest in the property is superior under the MCIOA and the recording act.

Affirmed.