SUPERIOR COURT OF NEW JERSEY

HUDSON VICINAGE

CHAMBERS OF
BARRY P. SARKISIAN
PRESIDING JUDGE
CHANCERY-GENERAL EQUITY

Brennan Courthouse
583 Newark Avenue
Jersey City, New Jersey 07306

NOT FOR PUBLICATION WITHOUT
THE WRITTEN APPROVAL OF THE COMMITTEE ON OPINIONS

LETTER OPINION

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Re: Citizens Bank, N.A. v. Victor Davis, et al
Docket No. HUD-F-18941-17
Date of Trial: June 5, 2018
Date of Decision: June 21, 2018

Dear Counsel:

This matter came before the Court for one day trial between Plaintiff Citizens Bank, N.A (hereinafter "Citizens"). and Co- Defendant Mortgage Electronic Registration Systems, Inc., as nominee for TD Bank, N.A., (hereinafter "MERS/TD") regarding Plaintiff's right to foreclose TD's interest as each party contested the priority of the other party's mortgage on the property. All other co-defendants, including the mortgagor, Victor Davis, had previously defaulted.

By way of procedural background, on August 10, 2017, Plaintiff Citizens Bank filed a complaint to foreclose on Defendant Victor Davis' property, located at 169 Wegman Parkway, Jersey City, New Jersey, in connection with a October 19, 2012 Home Equity Line of Credit Agreement (HELOC) and mortgage executed by Defendant in favor of Plaintiff Citizens Bank and secured by the subject property. Default was entered against Defendant Midland Funding LLC on October 30, 2017 and against Defendants Victor Davis and the State of New Jersey on December 29, 2017. Defendant MERS as nominee for TD Bank, the holder of a mortgage on the property, and on November 21, 2012, filed a contested answer alleging, inter alia, that Defendant's mortgage lien had priority over Plaintiff's mortgage lien under the doctrine of equitable subrogation

OPERATIVE FACTS

On or about September 23, 2011: Charlise Wright, Defendant Victor Davis' Aunt, and the previous owner of the property located at 169 Wegman Parkway, Jersey City (the property in question or "PIQ") since December 2010, executed a note and mortgage in the amount of $150,000, in favor of Sussex Bank, and secured by the subject property. The mortgage was recorded on October 14, 2011.

On or about October 27, 2011: Charlise Wright executed a Home Equity Line of Credit (HELOC) and mortgage for the"PIQ" in favor of TD Bank, N.A, for $80,000.00. The mortgage was recorded on November 22, 2011. The mortgage was "cancelled" (according to the document) on November 27, 2012.

On or about May 3, 2012: The "PIQ" was conveyed to the defendant Victor Davis by way of deed from Charlise Wright, and was recorded on September 12, 2012. Defendant also alleges that there was an "aborted mortgage closing", as demonstrated through a HUD-1 Statement, showing payoffs to Sussex Bank for $89,637 and to TD Bank for $55,363.00.

On or about October 19, 2012: Victor Davis executed a HELOC in the amount of $161,000.00 in favor of Plaintiff Citizens Bank, N.A secured by a mortgage on the PIQ. The mortgage was recorded on November 9, 2012 in Book 18022, Page 407. Plaintiff's one and only witness, Debbie Biddle, foreclosure operation manager for Citizens since 2015 testified that title searches conducted by Plaintiff revealed no prior mortgages on the property and believed they were getting a first mortgage position on the subject property for their Home Equity Loan. On cross examination by Defendant's attorney, she indicated she was unaware of how far back a search would be performed under then existing policy of Citizens Bank for a HELOC loan.

Seven (7) days later, on October 26, 2012, Victor Davis executed a mortgage in favor of Defendant MERS/TD in the amount of $224,169.00, and secured by the subject property. The mortgage was recorded on December 3, 2012, in Book 18033, Page 933.

Defendant's first witness, Kelly Poulin, TD's foreclosure specialist for the last five (5) years testified that after this loan had been in default for 120 days and prior to the filing of this foreclosure complaint, they received closing documents from the closing department of the title and mortgage closing which took place on October 26, 2012. The HUD 1 settlement statement disclosed that the borrower was Victor Davis, the seller was Charlise Wright and the settlement agent was attorney David Wecht. She testified that the same HUD-1 indicated that the proceeds of the TD loan were used, in part, to pay off a first mortgage in the amount of $149,416.56 and a second mortgage in the amount of $80,781.77. Her records also disclosed that the first mortgage paid off was issued by Sussex Bank and the second mortgage by TD bank. Both the seller and borrower issued Affidavits of Title to TD in customary form, both certifying there were no judgments or recognizances against them which would effect title and that title was being transferred on that day and that Mr. Davis intended to live at the subject property .On the same date, a corrective deed was issued from Ms. Wright to Mr. Davis, now containing correct tax record lot and block information that was not contained in the May 3, 2012 deed.

The October 26, 2012 closing took place approximately fourteen (14) days before the Plaintiff, Citizens' mortgage was recorded. Ms. Poulin testified that based on the documents she reviewed including the Affidavits of Title, TD bank believed they were in a first lien position.

Defendant TD's next and final witness was Kathryn Tiedemann, a Vice President of Sussex Bank now known as SB-One Bank for the last four (4) years. She testified that with respect to the PIQ, it had been brought to her attention this year that notwithstanding a loan that had been paid off in 2012, the mortgage was still of record. Acting upon that inquiry, she found no outstanding loan in the name of the borrower Charlene Wright and the records of Sussex Bank indicated that the loan had been paid in full in 2012 and that the subject mortgage had been endorsed for cancellation and sent to the attorney of record, Mr. Wecht.

The evidence before the Court brings the Court to the unmistakable conclusion that the proceeds of Defendant TD Bank's loan of October 26, 2012 were used for the purchase of the PIQ by Mr. Davis and the payoff of the pre-existing mortgages with Sussex Bank and TD Bank and that Mr. Wecht had failed to record the discharge of the Sussex mortgage which was not accomplished until Ms. Tiedemann's intervention resulting in the mortgage discharge of record on February 26, 2018.

DISCUSSION AND FINDINGS

Defendant TD Bank first argues that, although its mortgage was recorded after Plaintiff's mortgage, Defendant's mortgage should have priority pursuant to the doctrine of equitable subrogation since Defendant's mortgage was used to pay off two (2) prior liens on the property, namely, the Sussex and TD Bank mortgages, which were executed by the previous owner of the property, Charlise Wright, in 2011.

Alternatively, Defendant TD argues that its mortgage is a purchase money mortgage that is entitled to a super-priority lien vis a vis the Citizens Bank secondary loan mortgage. Defendant bases this contention on the premise that the first deed conveying Victor Davis the subject property from Charlise Wright on May 3, 2012 was defective in that it did not possess the proper lot and block number, and therefore, the October 26, 2012 closing of Defendant's mortgage also included a proper corrective deed that, for the first time, conveyed marketable title to Victor Davis. Defendant's argument hinges on that assertion that Plaintiff's mortgage was executed prior to Defendant taking title to the property. In opposition, Plaintiff contends that the May 3, 2012 deed validly conveyed title to Victor Davis.

Plaintiff argues that the Court should reject Defendant's theory under the doctrine of equitable subrogation. More specifically, Plaintiff argues that the TD Bank HUD-1 does not show which mortgage is being paid off, and that the check payable to Sussex Bank has the incorrect loan number on it and is dated October 29, 2012, which is in contrast to the October 26, 2012 date on the HUD-1. Moreover, Plaintiff argues that the application of equitable subrogation would materially prejudice Plaintiff as it intended for its mortgage to be a first mortgage and that its title searches on the property revealed no prior mortgages.

Absent the application of the doctrine of equitable subrogation, mortgage priority is typically governed by the recording statutes. See e.g. N.J.S.A. 46:21-1 and N.J.S.A. 46:22-1. New Jersey is a "race-notice" jurisdiction, and, as such, where parties are competing for priority over the other's lien or mortgage, the party that records its lien first will normally prevail as long as that party did not have actual knowledge of a previously acquired interest. Cox v. RKA Corp., 164 N.J. 487, 496 (2000) (citing Palamarg Realty Co. v. Rehac, 80 N.J. 446, 454, (1979)). Moreover, parties are generally charged with constructive notice of instruments that are properly recorded. Cox, supra, 164 N.J. at 496 (citing Friendship Manor, Inc. v. Greiman, 244 N.J. Super. 104, 108, (App. Div. 1990)). Properly recording such an interest properly is "notice to all subsequent judgment creditors, purchasers and mortgagees." N.J.S.A. 46:21-1.

Here, it is undisputed that the Citizens Bank Mortgage was recorded on November 9, 2012, before the Defendant TD Mortgage was recorded on December 3, 2012. Absent the application of the doctrine of equitable subrogation, the mortgage recorded first in time, the Citizens Bank mortgage would be given priority. In this case, Defendant TD claims priority over the Citizens Bank Mortgage by relying on the original priority of the Sussex Mortgage and TD Mortgage. In order to attempt to overcome the priority sequence established by the recording statutes, Defendant TD relies on the doctrine of equitable subrogation.

A court of equity has the inherent power to reform a contract so that it conforms to what the parties intended. Drake v. Town of Boonton, 106 N.J. Super. 79 (Law. Div. 1969). One equitable method is subrogation. Courts view equitable subrogation as “a device of equity to compel the ultimate discharge of an obligation by the one who in good conscience ought to pay it [and] … to serve the interests of essential justice between the parties.'" Culver v. Insurance Co. of North America, 115 N.J. 451, 455-456 (N.J. 1989) (quoting Standard Accident Ins. Co. v. Pellecchia, 15 N.J. 162, 171 (1954).

In 4 Pomeroy's Equity Jurisprudence (5th ed. 1941), § 1212, at pages 637-639, the author states that the grantee of the mortgage who takes the property subject to the mortgage and who pays off the mortgage may be subrogated to the rights of the mortgagee. The author states:

> Equity does not admit the doctrine of equitable assignment in favor of every person who pays off a mortgage. Such relations must exist towards the mortgaged premises or with the other parties, that the payment is not a purely voluntary act, but is equitably necessary or proper means of securing the interests of the one making it from possible loss or injury… in general, when any person having a subsequent interest in the premises, and who is therefore entitled to redeem for the purpose of protecting such interest, and who is not the principal debtor primarily and absolutely liable for the mortgage debt, pays off the mortgage, he thereby becomes an equitable assignee thereof … he is subrogated to the rights of the mortgagee to the extent necessary for his own equitable protection.

The doctrine provides that “if a third-party loans or advances funds to pay off an existing mortgage or other encumbrance in the belief that no junior liens encumber the subject premises, and it later appears that intervening liens existed, the new lender will be deemed to be substituted into the position of the prior mortgage holder by equitable assignment of the prior

mortgage to give effect to the new lender's expectation and to prevent unjust enrichment of the junior encumbrances." UPS Capital Business Credit v. Abbey, 408 N.J. Super. 524, 529 (Ch. Div. 2009).

"Subrogation rights are created in three (3) different ways: (1) by agreement; (2) by statute; or (3) judicially as an equitable device to compel the ultimate discharge of an obligation by the one who should in good conscience pay it." First Union Nat. Bank v. Nelkin, 354 N.J. Super. 557, 565 (App. Div. 2002). The Appellate Division, in Nelkin, described the operation of the doctrine of equitable subrogation as such:

> Generally, a new mortgagee is subrogated to the priority rights of an old mortgagee by either agreement or assignment. In the absence of such an agreement or assignment, a mortgagee who accepts a mortgage whose proceeds are used to pay off an older mortgage is equitably subrogated to the extent of the loan so long as the new mortgagee lacks knowledge of the other encumbrances. In that situation, the new mortgagee by virtue of its subrogated status can enjoy the priority afforded the old mortgagee. Equitable subrogation may still be afforded even though lack of knowledge on the part of the new mortgagee occurs as a result of negligence. On the other hand, the new lender is not entitled to subrogation, absent an agreement or formal assignment, if it possesses actual knowledge of the prior encumbrance.
>
> In addition to finding that the new mortgagee lacked knowledge of the preexisting encumbrance, application of the doctrine requires the court to find either: (1) the old mortgagee was unjustly enriched; or (2) the old mortgagee acted fraudulently. Being an equitable doctrine, "subrogation is applied only in the exercise of the court's equitable discretion."

Id. at 565-66 (internal citations omitted).

Where the new lender "knows of an encumbrance junior to the mortgage his money is used to discharge, the old mortgage will not be kept alive . . . unless there is a stipulation . . . or he obtains a formal assignment." First Fidelity Bank, Nat. Ass'n v. Travelers Mort. Services, Inc., 300 N.J. Super. 559, 569-70 (App. Div. 1997).

A recent federal case, Ricchi v. Am. Home Mortg. Servicing, Inc., 470 B.R. 715 (D.N.J. 2012) supports the proposition that actual knowledge does not defeat the right to equitable subrogation. In Ricchi, the court addressed a situation in which the lender attempting to apply the doctrine of equitable subrogation to claim first priority over a superior mortgage had knowledge of the existing mortgage. In that case, a representative of the lender had apparently been told about the existence of the mortgage, but the record was unclear as to whether the lender actually knew about the mortgage. The mortgage in that case did not appear on the lender's title report produced at closing. The Ricchi court, after analyzing New Jersey case law and concluding that there was a split in authority as to whether actual knowledge would bar subrogation, held that:

> It is within the realm of reasonableness to predict that the New Jersey Supreme Court would opt for a fact sensitive inquiry that focuses on unjust enrichment or prejudice to the junior mortgagee if equitable subrogation is imposed, rather than impose an absolute bar to the application of the doctrine where the new mortgagee had actual knowledge of the junior lien."

Id. at 723. The court ultimately concluded that the lender's successor could be subrogated to the higher priority, attributing the lender's failure to actually know of the existing lien to negligence that should not bar equitable relief. Id. at 724. While the federal Ricchi court determined that the Supreme Court would apply the restatement approach, the Appellate Division has twice refused to determine whether New Jersey will follow the rule of the Restatement (Third) of Prop. Mortgages § 7.6 comment (e). See Investors Sav. Bank v. Keybank Nat. Ass'n, 424 N.J. Super. 439, 446 n.3 (App. Div. 2012); Sovereign Bank v. Gillis, 432 N.J. Super. 36, 48-49 (App. Div. 2013). Under the Restatement approach, "the pertinent limiting factor is not the new lender's knowledge, but instead whether there has been 'material prejudice' to the intervening lienor." Gillis, supra, 432 N.J. Super. at 47.

The Restatement (Third) of Prop. Mortgages § 7.6 holds that a lender's actual knowledge of the pre-existing lien would not bar the application of the doctrine of equitable subrogation. Restatement (Third) of Prop. Mortgages § 7.6 comment (e) provides that "subrogation can be granted even if the payor had actual knowledge of the intervening interest." The pertinent part of that comment provides:

> Many judicial opinions dealing with a mortgagee who pays a preexisting mortgage focus on whether the payor had notice of the intervening interest at the time of the payment. Most of the cases disqualify the payor who has actual knowledge of the intervening interest, although they do not consider constructive notice from the public records to impair the payor's right of subrogation. Under this Restatement, however, subrogation can be granted even if the payor had actual knowledge of the intervening interest; the payor's notice, actual or constructive, is not necessarily relevant. The question in such cases is whether the payor reasonably expected to get security with a priority equal to the mortgage being paid. Ordinarily lenders who provide refinancing desire and expect precisely that, even if they are aware of an intervening lien. A refinancing mortgagee should be found to lack such an expectation only where there is affirmative proof that the mortgagee intended to subordinate its mortgage to the intervening interest.

Restatement (Third) of Prop. Mortgages § 7.6 comment (e). Notably, the Restatement approach has not been adopted by any court in this state.

Here, the Court finds that the doctrine of equitable subrogation applies to substitute Defendant TD Bank into the position of Sussex mortgage and thus, has higher priority than Plaintiff's Citizens bank's interest in the property. First, the Court is satisfied from the evidence presented that the proceeds of Defendant TD bank's loan of October 26, 2012 were used, in part, to payoff the preexisting mortgages with Sussex Bank and TD Bank. Defendant's foreclosure specialist, Kelly Poulin, testified that her records indicated that the first mortgage that was paid off was issued by Sussex Bank, in the amount of $149,416.56, and the second

mortgage by TD Bank, in the amount of $80,781.77, which is further supported by Defendant's HUD-1 settlement statement that reflects these payoffs. Defendant's second witness, Ms. Tiedemann, also testified that the Sussex bank records reflect that the loan had been paid in full in 2012 and the mortgage had been endorsed for cancellation that year. The Court finds that Plaintiff's arguments unconvincingly attempt to cast doubt on the transaction by placing emphasis on inconsequential details, like the date of the payoff check being four days later than the closing date, or that the closing instructions fail to instruct the closing agent to make a payment to Sussex Bank, which are used to mask Plaintiff's failure to present any evidence or argument that actually disproves that Defendant's mortgage paid off the prior mortgages.

Second, the Court finds that, regardless of whether the Court were to apply the traditional approach or the restatement approach of equitable subrogation, that both theories require the Court, using its equitable discretion, to find for Defendant TD Bank. Under the traditional approach, the Court must find that Defendant TD Bank did not have actual knowledge of Plaintiff's mortgage when it paid off the prior mortgages on the property. Here, it is undisputed that Defendant's mortgage was executed by Victor Davis on October 26, 2012, seven days after Mr. Davis executed a mortgage in favor of Plaintiff, on October 19, 2012, and approximately fourteen days before Plaintiff Citizen's mortgage was recorded. Accordingly, Defendant TD's mortgage was executed before Plaintiff's mortgage was recorded on the property and Plaintiff Citizen has failed to present any cognizable evidence of Defendant TD's actual knowledge of Citzens Mortgage.

Even if Plaintiff demonstrated that Defendant had actual knowledge of Plaintiff's prior mortgage, the Court finds that Defendant would still be protected by equitable subrogation under the restatement approach, as the pertinent factor is not the Defendant's knowledge, but rather whether there has been 'material prejudice' to the intervening lienor, or in this instance, Citizens Bank. The Court is not swayed by Plaintiff's arguments that it will be materially prejudiced because two title searches conducted on the property failed to reveal any prior mortgages on the property. While it is unfortunate that Plaintiff was the victim of a defective title search, the Court will not simply ignore the two (2) prior mortgages on the property because of a third-party's mistakes. While Plaintiff's witness, Ms. Biddle, testified that Plaintiff believed it was getting a first mortgage on the property, on cross-examination, Ms. Biddle stated that she was unaware of how far back a search would be performed under the then existing policy for Citizens for a HELOC loan. Plaintiff's title search was less than a 20-year search, and not even close to Defendant's 60-year search, which ultimately revealed the prior mortgages on the property. Thus, the Court finds that Plaintiff will not suffer prejudice by the imposition of equitable subrogation, and that any harm to the Plaintiff was caused by a third party, which is of no moment to the case at hand. In accordance with the principles of fairness and equity, that the Court will impose equitable subrogation on Defendant and finds that their mortgage is a first mortgage lien that is superior to Plaintiff's mortgage on the property.

While not germane to the Court's finding in favor of Defendant, in the interest of completeness, the Court will consider Defendant's alternative super priority lien argument. In order to qualify as a purchase money mortgage, the mortgage must be given at the same time as the conveyance of the property and the funds must actually be used to purchase the property.

See generally, Priority of purchase money mortgages, 29 N.J. Prac., Law of Mortgages § 110 (1st ed.). A purchase money mortgage has special priority over certain pre-existing claims. Specifically, the holder of a purchase money mortgage may assert priority over (1) judgments obtained against the purchaser prior to the time he or she acquired title to the mortgaged property; (2) mortgages executed by the purchaser prior to acquisition of title; (3) mechanics' liens relating to work performed prior to closing; and (4) claims of dower or curtesy by the purchaser's spouse. New Jersey Foreclosure Law & Practice 1-4; Defendant N.J.S.A. 46:9-8 provides that:

> Whenever real estate situate in this state is or shall be sold and conveyed, and a mortgage is given by the purchaser at the same time, on the real estate sold, to secure the payment of the purchase money or any part thereof, such mortgage shall be preferred to any previous judgment which may have been obtained against such purchaser.

N.J.S.A. 46:9-8 (emphasis added);

Descriptions in a deed often contain scrivener's errors … such descriptions are nevertheless usually sufficient to pass title. The problems can be cured, where it is necessary to so, by obtaining a corrective deed from the grantor who made the error. Commercial Real Estate Transactions in NJ § 4.6 (2010). Where a deed contains more than one description, one of which is clearly erroneous, the erroneous one usually may be disregarded. In Charette v. Fruchtman, 110 N.J. Eq. 256 (1932), the Chancery Court found that a misdescription of the land in the deed did not invalidate the conveyance of title. The Court held that if a tract of land intended to be conveyed is indicated with reasonable certainty, it will pass by conveyance, that the intent of the parties will prevail, although in some respects the description is erroneous. Id. at 258.

The Court finds that the May 3, 2012 deed sufficiently conveyed title to Victor Davis despite the scrivener's error in the description in the deed. The May 3, 2012 deed correctly stated that Charlise Wright, as grantor, was conveying the property located at 169 Wegman Parkway, Jersey City, NJ, to Victor Davis, as grantee, for $230,000. The error was in the tax map reference, and was corrected by the corrective deed, dated October 26, 2012, correcting the block and lot number. Defendant's argument hinges on its ability to demonstrate that the May 3, 2012 deed failed to convey marketable title and, therefore, Citizens Mortgage was issued at a time when Mr. Davis had not acquired title. The Court finds that the intent of the parties was to transfer title of the subject property from Charlise Wright to Victor Davis on May 3, 2012 despite the minor errors in the deed of conveyance. Therefore, the Court rejects Defendant's super priority lien argument.

CONCLUSION

The Court finds in favor of the Defendant Mortgage Electronic Registration Systems,, Inc as nominee for TD Bank, N.A., finding that their mortgage dated October 26, 2012 in the amount of $224,169.00, recorded on December 3, 2012, in Book 18033, Page 983 is a first mortgage lien that is superior to and prior to the Plaintiff's mortgage which is the subject of Plaintiff's foreclosure action.

SO ORDERED,

Barry P. Sarkisian

Hon. Barry P. Sarkisian, P.J.Ch.