

FEB 23 2007

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN RE:	:	CHAPTER 7
	:	
SANTRICE HUNT,	:	CASE NO. 04-77191-PWB
	:	
Debtor.	:	
<hr/>		
	:	
JANET G. WATTS, Chapter 7 Trustee	:	
for the Estate of Santrice Hunt,	:	
	:	
Plaintiff,	:	
	:	
vs.	:	ADVERSARY NO. 06-6235
	:	
ARGENT MORTGAGE COMPANY, LLC,	:	
	:	
Defendant.	:	
<hr/>		

**ORDER INCLUDING FINDINGS OF FACT
AND CONCLUSIONS OF LAW**

The chapter 7 Trustee seeks to avoid, as preferential transfers under 11 U.S.C. § 547(b), first and second priority purchase money security deeds held by the defendant lender on the Debtor's residence that were presented for recording some ten and six weeks, respectively, after their execution and funding and within 90 days of the Debtor's bankruptcy filing on October 18, 2004. The warranty deed from the seller by which the Debtor acquired the residence was recorded after recordation of the second priority security deed and at the same time as the first priority security deed.

The parties agree that three requirements for avoidance of the transfers set forth in

§ 547(b)(1), (3), and (5) have been met. The security deeds effected transfers of the interest of the Debtor (presumed to be insolvent under § 547(f)) in the residence to the lender that enabled the lender to receive more on its debt than it would have received in this case in the absence of the transfers. They dispute whether the transfers were on account of antecedent debts and whether they occurred within 90 days of the bankruptcy filing as required by § 547(b)(2) and (4).

Under 11 U.S.C. § 547(e)(2) as applicable here,¹ a transfer occurs for purposes of § 547(b) when it takes effect between the transferor and transferee if it is timely perfected; if it is not timely perfected, the transfer takes place when it is perfected. Under § 547(e)(1)(A), a transfer of real property is perfected “when a bona fide purchaser of such property from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest that is superior to the interest of the transferee.”

The controlling issue here² is whether a bona fide purchaser within the meaning of

¹The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPCPA”) amended § 547(e)(2) to extend the time within which perfection could occur for the date of the transfer to relate back to its effective date to 30 days from ten days. BAPCPA similarly amended § 547(c)(3), which provides that a purchase money security interest is not subject to avoidance if it is timely perfected after the debtor receives possession of the collateral, to extend the time for perfection from 20 to 30 days. The amendments do not apply in this case filed prior to BAPCPA’s effective date, but the different dates are immaterial to the issues.

²The Court’s analysis deals with the title record immediately prior to the first recordation of an Argent security deed. Thus, it is not dependent on the date that a security deed granted by the Debtor’s grantor, Bellwood Homes, LLC, in favor of United Community Bank (the “Bank”) was cancelled of record. Consequently, the Court need not address two theories Argent presents based on the existence of the Bank’s unsatisfied security deed. Argent’s first argument is that the Trustee cannot avoid Argent’s security deeds under § 547(c) because they qualify as purchase-money security deeds that were perfected on the closing date because the existence of the Bank’s unsatisfied security deed would put a bona fide purchaser on inquiry notice of Argent’s unrecorded interests. Argent asserts that, once its security deeds were perfected on this basis, the later satisfaction of the Bank’s security deed is immaterial. The second argument is that Argent is entitled to invoke the doctrine of equitable subrogation to assert the position of the

§ 547(e)(1)(A) of the Debtor's unrecorded title to the property would prevail over the unrecorded security deeds. If so, then the transfers under the security deeds were not perfected until they were presented for filing, those dates are the dates of the transfers, and the transfers were made within 90 days of the bankruptcy filing on account of antecedent debts. If not, then the transfers were perfected at the time of their execution and delivery, the transfers occurred at that time, and they were not made on account of antecedent debts.

After filing cross-motions for summary judgment, the parties stipulated that this adversary proceeding may be determined on the basis of the record before the Court, including the facts established in their summary judgment motions.³ Another bankruptcy trustee with a similar issue in another adversary proceeding before another judge has moved for leave to file an *amicus curiae* brief.⁴ The Court has considered the brief of the *amicus* trustee in addition to those of the parties.

This Court has authority to hear and determine this proceeding under 28 U.S.C.

Bank because loan proceeds from Argent's financing satisfied the Bank's security deed. The Trustee asserts that neither theory properly accounts for the fact that the Bank's security deed was satisfied within the preference period and prior to recordation of Argent's security deeds. Under this argument, Argent's debts were unsecured upon cancellation of the Bank's security deed and, consequently, perfection did not occur until the later recordation of Argent's security deeds. Because of the lapse in perfection, the Trustee contends that the transfers did not take place until recordation of Argent's security deeds, even if the Bank's unsatisfied deed has the effect Argent argues. The Court need not address these issues in view of its conclusion that Argent's interests were perfected at the time of closing without regard to when the Bank's security deed was cancelled.

³The stipulation was made in open court at the hearing on the motions for summary judgment on November 7, 2006.

⁴Tamara Miles Ogier, as Trustee for the Estate of Dana Pinkett, is the plaintiff in *Ogier v. Mortgage Electronic Registration Systems, Inc.*, Adv. No. 06-6234-CRM.

§ 157(b)(1) as a core proceeding under 28 U.S.C. § 157(b)(2)(F) within the District Court's jurisdiction under 28 U.S.C. § 1334(b) that the District Court has referred under 28 U.S.C. § 157(a) and L.R. 83.7, N.D.Ga.

I. FACTS

On July 8, 2004, the Debtor purchased a home in Henry County, Georgia, known as 120 Barrington Parkway, Stockbridge, Georgia, from Bellwood Homes, LLC ("Bellwood"). Prior to the purchase, a security deed executed by Bellwood in favor of United Community Bank (the "Bank") encumbered the property.

To pay for the property, the Debtor at closing executed two security deeds in favor of Argent Mortgage Company LLC ("Argent"), a first priority security deed to secure a loan of \$132,720 and a second priority deed to secure a loan of \$33,180. As expressly intended by Bellwood, the Debtor, and Argent, the proceeds from the two loans were used to pay the purchase price due to Bellwood and to pay \$116,802.53 to the Bank to satisfy its existing security deed. At the closing, Bellwood executed and delivered its warranty deed to the Debtor. The Debtor took possession of the property upon the closing of the purchase.

None of the documents relating to the title of the property were timely recorded in the Henry County real estate records. The security deed in favor of the Bank was not cancelled of record until August 15, 2004. The second priority security deed in favor of Argent was not presented for filing until August 19, 2004, and was not actually recorded until August 24, 2004. The warranty deed and the first priority security deed were not presented for filing until

September 22, 2004, and were not actually recorded until September 30, 2004.⁵

Under Georgia law, the controlling date for purposes of applying Georgia's real estate recordation statutes is the date a document is presented to the Clerk of the Superior Court for recordation in the county's real estate records, not the date on which the instrument is actually recorded. *E.g.*, O.C.G.A. § 44-2-2(b); *Pease & Elliman Realty Trust v. Gaines*, 160 Ga. App. 125, 286 S.E. 2d 448 (1981); 2 PINDAR'S GEORGIA REAL ESTATE LAW AND PROCEDURE, § 21-18 (6th ed. 2004). For convenience, the Court for purposes of this Order equates "recordation" of an instrument with its presentation to the Clerk of the Superior Court for filing.

II. DISCUSSION

Georgia law with regard to recordation of interests in real estate is based on a race-notice statute, O.C.G.A. § 44-2-1, which provides:

Every deed conveying lands shall be recorded in the office of the clerk of the superior court of the county where the land is located. A deed may be recorded at any time; but a prior unrecorded deed loses its priority over a subsequent recorded deed from the same vendor when the purchaser takes such deed without notice of the existence of the prior deed.

Under this statute, a purchaser of an interest in real property for value and without notice of a pre-existing but unrecorded interest acquires title unencumbered by the unrecorded interest. Its purpose is to protect purchasers of real property from having their rights defeated by a prior but

⁵The parties have stipulated that there is no evidence with regard to when the instruments at issue here were presented for filing other than the stamps on them that show the date of payment of the intangibles tax required for recordation. The Court finds that the instruments were presented for filing on those dates.

undiscoverable right that another might hold in the property. As noted in *Archer v. Kelley*, 194 Ga. 117, 127, 21 S.E.2d 51, 57 (1942):

It is by [the recording] statute made the plain duty of a grantee to record his deed, thereby giving constructive notice to every one of its existence and of his rights thereunder; and since it is thus made the duty of such grantee to supply notice, every one is justified in relying upon an examination of the record and believing that a purchase of land will convey all title which the record fails to disclose is in another.

A bankruptcy trustee's status as a bona fide purchaser is determined without regard to any actual knowledge of the unrecorded interest. For present purposes, the Court assumes, without deciding, that the real estate records here did not give constructive notice of the lender's security deeds at the required time to protect them as against a subsequent purchaser. Thus, whether a bona fide purchaser of the Debtor's unrecorded interest would take free of the security deeds depends on whether such a purchaser would be charged with notice based on a duty to inquire into the state of the title.

The Georgia Supreme Court set forth the standard for inquiry notice in *Price v. Watts*, 223 Ga. 805, 806, 158 S.E.2d 406, 407 (1967) (quoting *Gardner v. Granniss*, 57 Ga. 539, 541 (1876)):

Any circumstance which would place a man of ordinary prudence fully upon his guard, and induce serious inquiry, is sufficient to constitute notice of a prior unrecorded deed. And a younger deed, taken with such notice, acquires no preference by being recorded in due time.

If the duty of inquiry is triggered, Georgia law charges the purchaser with “notice of everything to which it is afterwards found such inquiry might have led.” *Collins v. Freeman*, 226 Ga. 610, 610-11, 176 S.E.2d 704, 705 (1970). This concept is codified in O.C.G.A. § 23-1-17:

Notice sufficient to excite attention and put a party on inquiry shall be notice of everything to which it is afterwards found that such inquiry might have led.

Ignorance of a fact due to negligence shall be equivalent to knowledge in fixing the rights of parties.

If the subsequent purchaser does not make an inquiry and does not explain why an inquiry would be futile, “it will be presumed that due inquiry would have disclosed the existent facts.” *Henson v. Bridges*, 218 Ga. 6, 10, 126 S.E.2d 226, 228 (1962).

Here, a purchaser’s search of record title to the property immediately prior to the recordation of the first of Argent’s two security deeds would have revealed record title in Bellwood and the cancelled security deed in favor of the Bank. The Debtor’s lack of record title was clearly sufficient to trigger a duty of inquiry on the part of a subsequent purchaser. A subsequent purchaser’s initial obvious question to Bellwood would be how the Debtor acquired the title, and the Trustee would have the duty to inquire stop there. But the discrepancy between the Debtor’s actual title and Bellwood’s recorded title poses a serious problem that underscores the need for more serious inquiry. Common sense would induce a person of ordinary prudence intent on conducting such a serious inquiry to go further and to ask Bellwood about the circumstances of the conveyance, including how the transaction was closed and how the purchase price was paid. Given the existence of the security deed in favor of the Bank and its satisfaction in these circumstances, the inquiry would have sought confirmation that it had

actually been paid. A reasonable inquiry would have led to discovery of the now known fact that the Debtor paid the purchase price to Bellwood as the result of a closing that including financing of the transaction by Argent, the execution and delivery of the two security deeds to secure that financing, and the use of those proceeds in part to satisfy the security deed held by the Bank.

Chestnut v. Weekes, 180 Ga. 701, 180 S.E. 716 (1935), is distinguishable from the situation here and does not establish a different principle. In that case, the purchaser had bought the property from a grantor who had acquired record title by defrauding the original owner. The original owner's son had been in possession of the property as a tenant when the purchaser bought it from the holder who had acquired it by fraud. After the original, defrauded owner died, her administrator sought to avoid the transfers to the fraudulent grantor and on to the purchaser, contending that the purchaser had a duty to inquire of the tenant son and that such inquiry would have revealed the fraudulent basis of the grantor's title. The court rejected this argument, ruling that "an inquiry of the tenant would have disclosed only that he was a tenant and claimed no title to the land." *Id.*, 180 S.E.2d at 720.

In *Chestnut*, the purchaser's grantor held record title and another possessed it as a tenant. The purchaser's duty of inquiry extended to determining the title of the possessor but not to investigating how the holder of record title had acquired it. In the situation here, in contrast, the grantor *does not* hold record title – it is in the original owner, Bellwood, from which the Debtor purchased the property. A purchaser of the Debtor's unrecorded title must find out how she acquired title, and it is reasonable to expect that the investigation include inquiries of Bellwood into how she paid for the property and of the Bank into how its security deed was paid. The

principle of *Chestnut* that possession does not give notice of facts other than the possessor's title does not limit the duty of inquiry when record title to the property is not in the grantor.

Under the inquiry requirement of Georgia law, a subsequent purchaser would have inquiry notice of Argent's security deeds. In a dispute between Argent and a purchaser of the Debtor's unrecorded interest in the residence, therefore, Argent as a matter of Georgia law would prevail.

Under this standard, Argent's security deeds were perfected within the meaning of § 547(e)(1)(A) from the time they were executed and delivered until the recordation of the warranty deed conveying the property to the Debtor. By the time the Debtor's title was recorded, Argent's second priority security deed had been recorded, and its first priority security deed was recorded at the same time. The recordation of the security deeds, of course, perfected Argent's interests under the security deeds for purposes of § 547(e)(1)(A). It follows that, because Argent's interests in the property under its security deeds were perfected when they were executed and delivered at the closing and remained perfected thereafter by virtue of their recordation prior to or simultaneously with recordation of the warranty deed to the Debtor, the transfers took place at closing under § 547(e)(2), and there was no antecedent debt. As such, the transfers are not avoidable under § 547(b).

The Trustee contends, however, that § 547(e)(1)(A) requires a different result. Noting that the statute provides that a transfer is perfected only when a bona fide purchaser *cannot* acquire an interest superior to the transferee, the Trustee reasons that perfection does not occur for purposes of § 547 if a subsequent purchaser could prevail under any set of circumstances. The Trustee contends, and Argent agrees, that, under Georgia law, a subsequent purchaser for

value who conducted an actual inquiry but did not discover the existence of Argent's security deeds because false information was supplied would prevail over the unrecorded security deeds. Because it is thus possible that an inquiring purchaser of the Debtor's unrecorded title who received false information would prevail over the unrecorded security deeds, the Trustee concludes that Argent's unrecorded security deeds are subject to the rights of a bona fide purchaser within the meaning of § 547(e)(1)(A). Under this view, Argent did not perfect its security deeds until they were recorded weeks after the transaction and, therefore, the transfers did not occur until those times and were on account of antecedent debt.

In support of the Trustee's position, the *amicus* trustee cites *Corn Exchange National Bank & Trust Co. v. Klaunder*, 318 U.S. 434 (1943), a case construing similar language in § 60 of the Bankruptcy Act, the predecessor of § 547. At issue there was the perfection of an assignment of the bankrupt's receivables under a secured lending arrangement. Because notice of the assignments had not been given to the bankrupt's account debtors, the assignments were ineffective against bona fide purchasers under state law. In determining that the failure to perfect the assignments in accordance with state law made them subject to avoidance by the trustee as preferences, the Court stated, *id.* at 436-37 (emphasis added):

[The statute's] apparent command is to test the effectiveness of a transfer, as against the trustee, by the standards which applicable state law would enforce against a good-faith purchaser. Only when such a purchaser is precluded from obtaining superior rights is the trustee so precluded. *So long as the transaction is left open to possible intervening rights to such a purchaser, it is vulnerable to the intervening bankruptcy.*

Focusing on the emphasized language, the *amicus* trustee asserts that *Klauder* requires the conclusion that, for purposes of § 547(e)(1)(A), a transfer of real estate is perfected only if there is no set of circumstances under which a subsequent purchaser could prevail over the unrecorded interest. Under this view, Argent's security deeds were not perfected until they were recorded because, as noted above, a subsequent purchaser receiving false answers to actual inquiries could acquire title unencumbered by Argent's unrecorded security deeds under Georgia law.

Klauder, however, did not involve a question of inquiry notice and did not address the question presented here. The case, therefore, is not controlling on this point, and its reasoning does not displace the concept found in other cases that a bankruptcy trustee's status as a bona fide purchaser under state law is determined by an objective standard without regard to what an actual purchaser did or did not do. The court in *Flatau v. Madonian (In re Sheetex, Inc.)*, 1999 WL 739628 at * 6 (Bankr. M.D.Ga. 1999), explained the status of a bankruptcy trustee as a bona fide purchaser of real estate under the "strong arm" statute, § 544(a)(3), as follows:

[B]efore exercising the rights and powers of a hypothetical bona fide purchaser, [a bankruptcy trustee] is obliged to take note of those same circumstances prevailing at the time of the petition that a hypothetical purchaser of Debtor's real property would be obliged to take note of, circumstances that would give the hypothetical purchaser notice of another person's pre-existing interest in Debtor's real property. If a hypothetical purchaser of Debtor's real property should have taken note of a superior interest existing in Debtor's real property, then the prospective purchaser could not have become a bona fide purchaser. It follows

that if circumstances would prevent any hypothetical purchaser from taking Debtor's property in good faith and without notice, then there exist no “shoes” of a hypothetical bona fide purchaser at the time of the commencement of the case for [the trustee] to step into.

Accord, Macleod v. SunTrust Bank Northwest Georgia (In re Henderson), 284 B.R. 515, 518 (Bankr. N.D. Ga. 2002).

The principle is that the status of a bona fide purchaser under state law for § 547(e)(1)(A) (or § 544(a)(3)) purposes is governed by application of the state law’s objective standards to the facts as they existed at the time in the light of what the facts are ultimately shown to be. The applicable Georgia law that determines whether a bona fide purchaser can acquire a superior interest to the transferee under § 547(e)(1)(A) imposes a duty of inquiry notice. If the inquiry duty arises and no inquiry has occurred, Georgia law establishes an objective standard for determining whether a reasonable inquiry would have led to discovery of the prior unrecorded interest. The bankruptcy statutes do not contemplate that a hypothetical bona fide purchaser be deemed to have conducted an inquiry without discovery of a prior unrecorded interest any more than they charge such a purchaser with actual knowledge of all the facts.

The Supreme Court in *Klauder*, 318 U.S. 434, 436-37, stated that the bankruptcy laws test the “effectiveness of a transfer, as against the trustee, by the standards which applicable state law would enforce against a good-faith purchaser.” Those standards under Georgia law include a duty to inquire and charge a subsequent purchaser with information that a reasonable inquiry would reveal. The Court does not interpret *Klauder*’s further statement – that a transaction is vulnerable if it is “left open to possible intervening rights” – as establishing a federal bankruptcy

rule that displaces the application of state law inquiry standards or as permitting determination of the rights of a good faith purchaser based on whether an actual inquiry could have failed to discover an unrecorded interest that a reasonable inquiry would have revealed. Rather, the Court reads this *dicta* as being generally declarative of the principle that the avoidance powers of a bankruptcy trustee, when determined by reference to a hypothetical bona fide purchaser standard, are not burdened by what actually did or did not occur.

The *amicus* trustee characterizes this result as improperly charging a bankruptcy trustee with negligence. Although it is true that the failure to conduct a required inquiry could be construed as negligence, it is also true that the statute makes state law rules determinative of the issue. The standard for bona fide purchaser status under Georgia law includes a requirement for inquiry and imposes consequences based on an objective determination of what that inquiry should have been and what it would have revealed. Section 547(e)(1)(A) incorporates those standards, whether or not they are characterized as “negligence.” In this sense, the statute does not attribute “negligence” to a bankruptcy trustee, but merely makes the § 547 claims she asserts subject to the same standards that would apply to determine the status of a bona fide purchaser under state law. The hypothetical status of the trustee cannot be augmented with an assumption that Georgia law does not make.

The Court is mindful of the Congressional policy embodied in the avoidance statutes against the recognition of “secret liens.” But Congress did not eliminate “secret liens” generally, only those that are not effective against a bona fide purchaser under applicable law in the case of real estate and against a judgment creditor in the case of personal property. The proper Congressional policy to apply in considering the issue here is the recognition that parties are

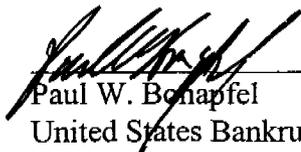
entitled to the same rights with regard to the enforceability of their property rights as against a bankruptcy trustee as they have under applicable nonbankruptcy law.

III. CONCLUSION

Argent's security deeds were perfected within the meaning of § 547(e)(1)(A) at the time they were executed and delivered because, under Georgia law, a bona fide purchaser would have had inquiry notice of them at all times prior to their recordation based on the Debtor's absence of record title and the existence of the cancelled security deed on the property in favor of the Bank. As such, the transfers took place under § 547(e)(2)(B) at the time of their execution and delivery, and the transfers were not for or on account of an antecedent debt and were not made within 90 days of the bankruptcy filing as required by § 547(b)(2) and (4) for the Trustee to prevail. Accordingly, Argent is entitled to judgment in its favor. A separate judgment will be entered.

The motion of the *amicus* trustee for leave to file an *amicus curiae* brief is granted. The request of Argent for leave to respond to the *amicus* brief is denied as moot.

It is SO ORDERED this 23 day of February, 2007.


Paul W. Bonapfel
United States Bankruptcy Judge