

Case No. A07-183²

State of Minnesota
Supreme Court

The Business Bank,

Petitioner,

vs.

Kevin C. Hanson, et al.

Respondents,

Option One Mortgage Corporation,

Respondent,

The United States of America

Defendant.

**BRIEF OF MINNESOTA STATE BAR ASSOCIATION,
 REAL PROPERTY LAW SECTION,
 AS AMICUS CURIAE**

Barbara M. Ross (#182941)
 Edward P. Sheu (#312885)
 BEST & FLANAGAN LLP
 225 South Sixth Street, Suite 4000
 Minneapolis, MN 55402
 Telephone: (612) 339-7121
Attorneys for Respondent/Petitioner

Jonathan M. Bye (#148830)
 Karla M. Vehrs (#387086)
 LINDQUIST & VENNUM, PLLP
 80 South Eighth Street, Suite 4200
 Minneapolis, MN 55402
 Telephone: (612) 371-3211
*Attorneys for Respondent
 Option One Mortgage Corporation*

John M. Koneck (#57472)
 Patrick D.J. Mahlberg (#0388028)
 Joseph J. Cassioppi (#388238)
 Fredrikson & Byron, P.A.
 200 South Sixth Street, Suite 4000
 Minneapolis, Minnesota 55402
 Telephone: (612) 492-7000
*Attorneys for the Minnesota
 State Bar Association Real
 Property Law Section*

Scott A. Johnson (#124606)
 Todd M. Johnson (#52061)
 JOHNSON LAW GROUP LLP
 10850 Wayzata Boulevard, Suite 250
 Minnetonka, MN 55305
 Telephone: (952) 525-1224
*Attorneys for Respondents Kevin C.
 Hanson and Colleen L. Hanson*

TABLE OF CONTENTS

	<u>Page</u>
I. STATEMENT OF INTEREST	1
II. SUMMARY OF DISCUSSION	2
III. DISCUSSION	3
A. The Court of Appeals Misconstrued The Mortgage Registry Tax Statute.	4
1. The Court of Appeals Misinterpreted Minn. Stat. § 287.03.....	4
2. The Court of Appeals Misinterpreted This Court’s Precedent.....	8
B. The Court of Appeals’ Decision Threatens To Invalidate Countless Mortgages and Cause Unnecessary Litigation.....	10

TABLE OF AUTHORITIES

Page(s)

CASES

Engenmoen v. Lutroe, 153 Minn. 409, 190 N.W. 894 (1922).....9, 10

First State Bank of Boyd v. Hayden, 121 Minn. 45, 140 N.W. 132 (1913).....9

Staples v. E. St. Paul State Bank, 122 Minn. 419, 142 N.W. 721 (1913).....8, 9, 10

STATUTES

Minn. Stat. § 287.015

Minn. Stat. § 287.032, 4, 8, 10

Minn. Stat. § 287.0354, 11

Minn. Stat. § 287.055

Minn. Stat. § 287.105

Minn. Stat. § 287.136

Minn. Stat. § 507.34.....2, 7, 10, 11

Minn. Stat. § 645.176

Gen. Laws 1907, c. 328, § 1.....8

Gen. St. 1913, § 2301.....9

RULES

Minn. R. Civ. App. P. 129.031

I. STATEMENT OF INTEREST

The Minnesota State Bar Association Real Property Law Section (the “Real Property Law Section”) submits this brief as amicus curiae requesting reversal of the decision of the Minnesota Court of Appeals.¹

The Real Property Law Section’s interest is public in nature. With approximately 15,500 members, the Minnesota State Bar Association is the State’s largest voluntary organization of attorneys. Among its missions are to aid the courts in the administration of justice, to apply the knowledge and experience of the profession to the public good, and to provide a forum for discussion of subjects pertaining to the practice of law and law reform. The Real Property Law Section’s purpose is to further the Minnesota State Bar Association’s work in the field of real property law. The section also promulgated and updates the Minnesota Title Standards and White Pages, a comprehensive code of standards to guide attorneys examining real estate titles and documenting real property transfers. Additionally, the Real Property Law Section monitors court precedents and legislation that affects real estate and real estate transactions.

As the section that represents the lawyers that most often deal with the use and implications of the statutes at issue in this case, the Real Property Law Section has a valuable perspective that can assist this Court in deciding the issues in this appeal. As an organization of lawyers who most often handle mortgages and address legal issues

¹In accordance with Minn. R. Civ. App. P. 129.03, the Real Property Law Section hereby certifies that its counsel authored this brief and that no person or entity, other than the Real Property Law Section, has made a monetary contribution to the preparation or submission of this brief.

regarding real property, the Real Property Law Section is in a unique position to assist the Court in interpreting the statutes at issue in this matter. The Court of Appeals' holding in this case impacts the practice of all attorneys that practice in real estate law, including members of the Real Property Law Section.

II. SUMMARY OF DISCUSSION

Minnesota's Mortgage Registry Tax statute, Minn. Chap. 287, imposes a tax on the privilege of recording a mortgage in Minnesota and is purely a revenue measure. Section 287.03 provides that "[n]o instrument . . . relating to real estate shall be valid as security for any debt, unless the fact that it is intended and the initial known amount of the debt are expressed in it." In light of Chapter 287's status as a revenue measure, this Court has consistently rejected attempts to use section 287.03 as a means to invalidate or subordinate mortgages.

In this case, however, the Court of Appeals determined that a mortgage that states the amount of debt that it secures, but not the entire amount of the secured and unsecured debt, and upon which the proper tax has been paid, is invalid pursuant to Minn. Stat. § 287.03. This interpretation ignores the context of Chapter 287, which establishes a scheme of mortgage registry taxation designed only to ensure that the State of Minnesota collects the proper amount of mortgage registry tax. The Court of Appeals' interpretation also overlooks the Minnesota Recording Act, Minn. Stat. § 507.34, which determines the priority of interests in real estate. Viewed in the context of Chapter 287 and the Recording Act, the Court of Appeals misconstrued Minn. Stat. § 287.03 and should be reversed.

Moreover, practitioners and lenders have long relied on this Court's consistent holding that the Minnesota Mortgage Registry Tax statute is solely a revenue measure, and cannot be used by a junior lienholder to subordinate or render unenforceable an otherwise valid senior lien so long as the required tax has been paid. If this Court affirms the Court of Appeals, it will invalidate countless Minnesota mortgages and lead to an unnecessary surge of mortgage reformation actions.

III. DISCUSSION

In Minnesota, the issue of priority of interests in real estate is determined by the controlling statutes: namely, the Minnesota Recording Act. The Mortgage Registry Tax statute was not intended to determine priority or invalidate a mortgage that has been recorded properly and upon which the proper tax has been paid.

In this case, however, the Court of Appeals interpreted the Mortgage Registry Tax statute to subordinate The Business Bank's mortgage to Option One Mortgage's ("Option One") mortgage, even though The Business Bank had paid the proper registry tax and had properly recorded its mortgage more than one year before Option One's mortgage was recorded. As set forth below, the Court of Appeals' decision was based on a misinterpretation of the Mortgage Registry Tax statute and threatens to subordinate or render unenforceable numerous otherwise valid mortgages within this state. Accordingly, the decision of the Court of Appeals should be reversed.

A. The Court of Appeals Misconstrued The Mortgage Registry Tax Statute.

Read in context, Minn. Stat. § 287.03 is part of a statutory scheme designed to ensure proper determination and payment of the mortgage registry tax. Section 287.03 is part of Chapter 287, which is titled “Mortgage Registry Tax; Deed Tax.” Chapter 287, in turn, is in the Title, “Property Taxes.” Nothing in Chapter 287’s language implies that its provisions are intended as a tool for determining mortgage validity.

1. The Court Of Appeals Misinterpreted Minn. Stat. § 287.03.

Chapter 287 is a revenue measure designed to ensure the proper computation and collection of Minnesota’s mortgage registry tax. Accordingly, Chapter 287 imposes a mortgage registry tax, outlines how the tax is calculated, and provides a comprehensive scheme of penalties for non-compliance with its provisions.

Section 287.035 provides as follows:

A tax is imposed on the privilege of recording a mortgage. The tax rate is .0023 of the debt or portion of a debt that is secured by any recorded mortgage of real property located in this state. The person liable for the tax is the mortgagor. The tax is not imposed on the lawful interest amounts that may accrue with respect to a debt.

Section 287.035 imposes the mortgage registry tax only on the “debt or portion of a debt,” secured by the mortgage.

Section 287.03 provides that “[n]o instrument, other than a decree of marriage dissolution or an instrument made pursuant to it, relating to real estate shall be valid as security for any debt, unless the fact that it is intended and the initial known amount of the debt are expressed in it.” For purposes of the Mortgage Registry Tax statute,

“‘[d]ebt’ means the principal amount of an obligation to pay money that is secured in whole or in part by a mortgage of an interest in real property.” Minn. Stat. § 287.01, subd. 3.

Other provisions of Chapter 287 recognize that the amount of debt that is secured by a mortgage may be dynamic and, in some cases, may not even be known at the time the mortgage is recorded. *See* Minn. Stat. § 287.05, subs. 1, 1a, 3, 4, 5, and 6 (allowing mortgages to secure changing or unknown amounts of debt in various situations, including mortgages securing indeterminate amounts, revolving lines of credit, future advances, and reverse mortgages). In each of these situations, the initial known amount of debt is rarely stated on the mortgage, and, in some cases, it cannot be. And in each of these situations, pursuant to section 287.05, the mortgages are valid and enforceable.

Importantly, the Legislature has established consequences for failing to comply with Chapter 287. Section 287.10 governs the consequences of improperly calculating and paying the mortgage registry tax. It provides:

287.10 PREPAYMENT OF TAX; EVIDENCE; NOTICE.

A mortgage, or documents relating to its foreclosure, assignment, or satisfaction, must not be recorded unless the tax has been paid. Except as provided in section 582.25, a document or any record of the mortgage may not be received in evidence in any court, and is not valid notice, unless the tax has been paid. If the tax is paid, an error in computation or ascertainment of the amount does not affect the validity of the mortgage or the record or foreclosure. This section does not apply to a mortgage that is exempt from the tax imposed under section 287.035.

Section 287.13 establishes a full scheme of penalties for failing to pay the proper tax:

287.13 VIOLATIONS; CIVIL PENALTIES.

Subdivision 1. Failure to pay full amount.

Any person liable for the tax imposed by section 287.035 who fails to pay the full amount of mortgage registry tax imposed under this chapter, unless the failure is shown to be due to reasonable cause, is liable for a civil penalty of \$250 or 100 percent of the tax for each such failure, whichever is less.

Subd. 2. Additional penalty.

Any person who willfully attempts to evade or defeat the tax imposed under sections 287.01 to 287.12, or the payment thereof, shall, in addition to the penalty provided in subdivision 1, be liable for a penalty of 50 percent of the total amount of the underpayment of the tax.

Subd. 3. Payment to mortgagee.

If a mortgagee undertakes to collect from the mortgagor the amount of the tax due under sections 287.01 to 287.12 as provided in section 287.08, paragraph (e), the mortgagor is not subject to the penalties under this section and the mortgagee is subject to the provisions of this section.

The Minnesota Legislature did not intend a mortgagee's non-compliance with the provisions of Chapter 287 to invalidate or subordinate otherwise valid or prior mortgages, upon which the proper tax has been paid. Any interpretation to the contrary would render the remedial provisions of Chapter 287 impossible to execute and superfluous—because the mortgage would be invalid, not merely tax-deficient, results that the Legislature is presumed not to have intended. Minn. Stat. § 645.17, subs. 1 and 2.

In sum, Chapter 287 is a self-contained statutory scheme governing Minnesota's mortgage registry tax imposition and collection. It provides for the manner in which a party complies with the scheme, as well as the consequences for failing to comply therewith.

It is the Recording Act, Minn. Stat. § 507.34, that determines mortgage priority:

Every conveyance of real estate shall be recorded in the office of the county recorder of the county where such real estate is situated; and every such conveyance not so recorded shall be void as against any subsequent purchaser in good faith and for a valuable consideration of the same real estate, or any part thereof, whose conveyance is first duly recorded, and as against any attachment levied thereon or any judgment lawfully obtained at the suit of any party against the person in whose name the title to such land appears of record prior to the recording of such conveyance. . . .

In this case, the debt that was secured by The Business Bank's mortgage was "up to \$200,000." Pursuant to Chapter 287, the mortgage properly stated the amount of debt that was secured by the mortgage, and The Business Bank properly calculated and paid the registry tax when it recorded the mortgage. As a result, The Business Bank's mortgage is valid and, because it was recorded before Option One's mortgage, it has priority. The Court of Appeals erred when it determined that Chapter 287, despite the fact that it is purely a revenue measure, may be used by a subsequent lienholder as a method for determining mortgage validity and priority. As a result, its decision should be reversed.

2. The Court Of Appeals Misinterpreted This Court's Precedent.

This Court has previously considered, and consistently rejected, attempts to use the Mortgage Registry Tax statute as a means of invalidating or altering the priority of otherwise valid mortgages, upon which the proper mortgage registry tax has been paid.

Nearly 100 years ago, in *Staples v. E. St. Paul State Bank*, 122 Minn. 419, 142 N.W. 721 (1913), this Court considered whether a deed was invalid because it did not comply with section 287.03's predecessor. The Court determined that, because the Mortgage Registry Tax statute was a revenue measure, the deed was not invalid.

Section 287.03's predecessor provided that "[n]o instrument relating to real estate shall be valid as security for any debt, unless the fact that it is so intended and the amount of such debt are expressed therein." Gen. Laws 1907, c. 328, § 1. The deed at issue was given as security for a \$1,000 debt, but expressed only that it was given for \$1 "and other good and valuable consideration." *Id.* at 421-22, 142 N.W. at 722. Moreover, the deed did not express that it was intended for security. *Id.* at 422, 142 N.W. at 722.

Considering the effect of the deed's failure to comply with the Mortgage Registry Tax statute, the Court noted that

In applying this law, it is well to bear in mind that its apparently stringent provisions were not intended to change the law of contracts, except in so far as it became necessary to prescribe terms to be incorporated which would furnish information upon which the proper tax from every transaction could be secured.

Id. Continuing, the Court noted that "[t]he statute is purely a revenue measure, and we find nothing therein to indicate that it was the legislative intent to declare instruments

void for non-compliance therewith.” *Id.* (citing *First State Bank of Boyd v. Hayden*, 121 Minn. 45, 50, 140 N.W. 132, 134 (1913)). As a result, the Court held that the fact that the deed did not comply with the mortgage registry tax statute did not render the deed invalid. 122 Minn. at 423, 142 N.W. at 722.

A decade after deciding *Staples*, this Court again rejected the idea that a junior lienholder could use the Mortgage Registry Tax statute to invalidate or subordinate an otherwise valid and prior senior lien instrument. In *Engenmoen v. Lutroe*, 153 Minn. 409, 412, 190 N.W. 894, 895 (1922), the Court considered Gen. St. 1913, § 2301, which provided that “[n]o instrument relating to real estate shall be valid as security for any debt, unless the fact that it is so intended and the amount of such debt are expressed therein.” The plaintiff, a judgment lien holder, asked this Court to declare a prior deed invalid as to her, because it did not express that it was intended as security and the proper amount of mortgage registry tax had not been paid. *Id.* The Court rejected the plaintiff’s argument, instead holding that

The act is a revenue measure purely, and the only purpose of its prohibitive provisions is to compel the payment of the prescribed tax. A mortgage, whatever its form, is not rendered void by failure to comply with the requirements of the statute, but remains unenforceable, unrecordable, ineffective as notice and inadmissible as evidence until the tax is paid.

Id. (citations omitted). The Court also stated that the rights created by the mortgage “remain in abeyance or a state of dormancy and no affirmative proceeding to enforce them can be maintained until the purpose of the statute has been accomplished.” *Id.* The purpose of the statute is to compel payment of the proper tax. *Id.* The Court held that,

although the senior lienholder's rights were subject to the restrictions placed on mortgages upon which the proper tax has not been paid, the junior lienholder had not met her burden of showing that she did not have notice of the prior mortgage. *Id.* at 414, 190 N.W. at 896.

In this case, The Business Bank paid the proper mortgage tax and Option One is considered to have had constructive notice of The Business Bank's mortgage. Minn. Stat. § 507.34. As a result, Option One, as a subsequent lienholder with notice, may not seek to invalidate or subordinate The Business Bank's mortgage based upon its alleged non-compliance with Minn. Stat. § 287.03.

The Court of Appeals held that *Staples* and *Engenmoen* stand for the proposition that a mortgage that does not comply with Minn. Stat. § 287.03 "is invalid unless the noncompliance has been cured, such as by filing a proper mortgage . . . or by a district court judgment reforming the mortgage" However, *Staples* and *Engenmoen* actually stand for the proposition that a mortgage upon which the proper mortgage registry tax has been paid is valid and prior as against a subsequent lienholder's instrument. The Mortgage Registry Tax statute was "a revenue measure purely" then, and it is a "revenue measure purely" now, and its only purpose—to ensure that the State of Minnesota collects the proper amount of mortgage registry tax—remains.

B. The Court of Appeals' Decision Threatens to Invalidate Countless Mortgages and Cause Unnecessary Litigation.

The Court of Appeals issued its decision in this matter without considering the wide-ranging consequences of its holding. Countless mortgages have been prepared and

recorded in Minnesota pursuant to the long-established understanding, based upon decisions of this Court, that the Minnesota Mortgage Registry Tax statute (and its predecessors) is solely a revenue measure that does not affect the validity or enforceability of a mortgage so long as the proper tax has been paid. The Court of Appeals turned almost a century of practice on its head when it held that The Business Bank's failure to state the total amount of Hanson's indebtedness subordinated the mortgage to the junior mortgage held by Option One.

However, if this Court affirms the Court of Appeals, it will cause much more than an unfortunate result for The Business Bank. As an organization of lawyers who often prepare and file mortgages, the Real Property Law Section is concerned that an affirmance will invalidate mortgages throughout the state and lead to countless reformation actions.

It has long been common for real estate lawyers and lenders in Minnesota to state on the face of a mortgage only the dollar amount secured by the mortgage lien and not the total amount of the indebtedness, only a portion of which is secured by the mortgage lien. By doing so, and then filing the mortgage, a mortgagee is able to compute the appropriate mortgage registry tax and provide notice to subsequent lienholders of the amount of indebtedness secured by the property. *See* Minn. Stat. §§ 287.035 and 507.34. An affirmance by this Court will subordinate or render unenforceable numerous otherwise valid mortgages.

Additionally, lenders throughout the world who have loaned funds, a portion of which are secured by mortgages on real property in Minnesota, will be forced to review

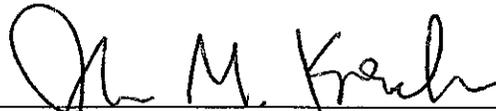
those mortgages to determine whether they comply with this new interpretation of the Minnesota Mortgage Registry Tax statute. All lenders holding mortgages that an affirmance would render non-compliant will be forced to pursue immediate reformation actions or face subordination or invalidation at the hands of subsequent lenders, mechanic's or judgment lien claimants, or other third parties. These junior lienholders could receive a windfall, even if they obtained their liens with actual knowledge of the senior secured indebtedness.

Rather than upsetting nearly a century's worth of practice and precedent, this Court should reaffirm that the Minnesota Mortgage Registry Tax statute is solely a revenue measure, and cannot be wielded by junior lienholders to render unenforceable or subordinate otherwise valid senior mortgages, where the proper mortgage registry tax has been paid.

CONCLUSION

For the foregoing reasons, the Real Property Law Section respectfully requests this Court reverse the decision of the Court of Appeals.

Respectfully submitted,



Dated: February 26, 2009

John M. Koneck (#57472)

Patrick D.J. Mahlberg (#0388028)

Joseph J. Cassioppi (#0388238)

FREDRIKSON & BYRON, P.A.

200 South Sixth Street, Suite 4000

Minneapolis, Minnesota 55402-1425

Telephone: (612) 492-7000

Fax: (612) 492-7077

*Attorneys for the Minnesota State Bar
Association Real Property Law Section*

4514919_3.DOC