

NO. A11-1521

**STATE OF MINNESOTA
IN COURT OF APPEALS**

Amos Graves,

Appellant,

vs.

Michael Wayman, et al., Respondents, REA Group, Inc., Respondent, C&M Real Estate Services, Inc., Respondent, Trademark Properties Group, LLC, Respondent, First Minnesota Bank, Respondent,

APPELLANT'S REPLY BRIEF

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STATEMENT OF FACTS IN REPLY

In this case, the relevant facts are clear and undisputed, despite Respondent First Minnesota Bank's ("FMB") lengthy discussion in its brief.

Charles Blair testified FMB had a "master loan agreement" with C&M and "that multiple transactions were funded underneath to redeem specific properties out of sheriff sale." (Trans. 142:16-24) He conceded knowing C&M was in the business of redeeming sheriff's certificates. (Id.)

One of these properties was the Subject Property in question. C&M faxed the unrecorded quit claim deed and purchase agreement to Bryan Guse. Guse was the loan officer for this particular loan and C&M was his banking customer. (Trans. 143:6-10) FMB knew C&M was owned by Cori and Michael Wayman. (Id. 143:17-18) Blair knew REA was "common ownership with Wayman" and that it would have been reasonable for a lender to know the relationship between C&M and REA. (Trans. 183:21-23)

Blair testified FMB knew C&M was not going to occupy the Subject Property. (Id. 144:15-18) Aside from this fact, he did not know what C&M's intentions were with respect to the Subject Property. (Id. 144:19-25; 145:1-3) Blair never asked because he was not the loan officer. (Id. 145:1-6) Notably, he agreed that "only the loan officer [Bryan Guse] would likely know" C&M's intentions on the house. (Id. 145:6-7)(emphasis added) Thereafter, Blair testified as follows:

Q. Based on your review of the files, did anyone from First Minnesota Bank go to the property at 1221 at any time during the year 2007?

A. I'm not qualified to answer that.

Q. You don't know, is that correct?

A. I don't know.

(Id. 146:22-25; 147:1-2) He does not disagree that a passerby could have visualized Appellants' possession if the property were inspected. (Id. 147:3-9)

On September 11, 2007, two days before the end of the redemption period, REA executed a \$100.00 mortgage to C&M, secured by the Subject Property and recorded the same day. (Id. 181:11-23)

The Court found it was “clear that the only purpose of the \$100.00 mortgage was to create a mortgage so that C&M could redeem the subject property as junior creditor.” (A35, ¶30) Even Blair, a 44 year veteran, admitted the \$100 mortgage was not typical in the industry. (Trans. 183:2-19) The same day, a Notice of Intention to redeem was recorded. These September 11th documents identified Mr. Wayman as the CEO of REA and C&M. (APP79-81)

FMB produced a two page fax from its files during discovery. (A35-36) Considering Blair had no personal involvement, he could neither admit nor deny that this fax was received by FMB on September 23, 2007, as reflected on the fax header. (Trans. 155:3-14) This included a copy of the unrecorded quitclaim deed from the Graves and a purchase agreement. (A35-36)

Blair testified “we review the documents” for title examination. (Id. 143:23-25; 144:1-2) He also testified FMB relies “heavily on the opinions of the title company.” (Id.) However, FMB offered no written title opinion and did not call this elusive “title company.” He testified that FMB determines a borrower has clear title by title insurance.

On September 13, 2007, Guse closed the loan. (Trans. 160:14-18) Blair testified as follows:

- Q. Do you know whether Mr. Guse inquired about any interest or possessors in the property in the month of September 2007?
- A. I don't know what he did or didn't do in those regards.
- Q. You would be guessing, correct?
- A. I would be.
- Q. You personally never asked or checked on the property to see if anyone is possessing it, correct?
- A. Not in that timeframe.
- Q. You would agree that –
- A. I wasn't a lender on staff in September of '07. I was on the board of directors.

When asked about Mr. Guse's actual knowledge, he testified as follows:

- Q. So you don't know what Bryan Guse actually knew, is that correct, in terms of if anyone occupied this property?

A. Yeah, I don't know everything that he knew.

(Trans. 173:13-16)

It was Mr. Guse's responsibility, as the loan officer, to ensure all "exceptions" on the title policy were reviewed and taken care of prior to funding a loan.

Mr. Blair testified he had nothing in its files to show the Graves received \$182,000. (Trans. 163:1-4)

Mr. Blair testified that he did not know whether Mr. Guse ever inquired about possessors of the Subject Property during September of 2007. (Id. 161:4) Mr. Blair never checked at that time. (Id.)

ARGUMENT

I. THE DISTRICT COURT ERRED IN APPLYING THE BONA FIDE PURCHASER DEFENSE WHEN APPELLANT REVOKED THE OFFER OR CANCELLED THE TRANSACTION A MONTH BEFORE FMB'S PURPORTED INTEREST.

A. FIRST MINNESOTA, AS SUCCESSOR TO REA/C&M'S INTEREST, CANNOT TURN A VOID INTEREST INTO AN ACTUAL INTEREST.

The thought of creating *something* out of *nothing* is certainly intriguing. Much like a fairytale, FMB fanaticizes of transforming its void, *non-interest* from C&M, REA and Mr. Wayman ("Wayman Entities") into a real title interest. Only then, as FMB concedes, does the bona fide purchaser defense have any bearing on this matter.

However, it is black letter law that an assignee, such as the Wayman Entites, "cannot, by assigning...give his assignee any greater rights than he himself had." *American Baptist Missionary Union v. Weeks*, 72 Minn. 484, 488, 75 N.W. 713, 714 (Minn. 1898). For this reason, it is axiomatic that an assignee "stands exactly in the shoes of his assignor." *Id.*; *See also, e.g., State ex rel. Southwell v. Chamberland*, 361 N.W.2d 814 (Minn. 1985)(assignment operates to vest in the assignee the same right, title, or interest that the assignor had in the thing assigned). The central question, then, whether the Wayman Companies held any interest.

First, the quitclaim deed was not delivered by the Graves as noted in Appellants Brief. Even if it were delivered, the transaction was void upon the Graves's cancellation. "Cancellation occurs when the homeowner delivers." Minn. Stat. § 325N.13(b). "If cancellation is mailed, delivery is effective upon mailing." *Id.* Because the Graves' cancellation predated any interest of FMB, this effectively left REA/C&M without any interest to convey or mortgage. FMB cannot create an interest out of a non-interest and has failed to cite any supporting case.

Rather than addressing this issue, FMB digresses to arguments of "equity." Albeit a \$375mm banking empire, FMB claims it would be unfair if Appellant is declared the fee title owner of his own house or be paid the amount due under the purchase agreement. (Trans., 142: 4-15) As the record reflects, FMB already received a full damages judgment against the Wayman Entities in its covert action against Mr. Wayman and C&M. It even refused to serve the summons and complaint upon the Graves, despite being required to do so by statute. Minn. Stat. § 582.041, subd. 1 (homestead designation notice must be included in a summons and complaint and "served on the person in possession of the real property")

More than a year into litigation in the above-entitled matter, FMB incorporated its "bona fide purchaser" defense into its answer. Around the same point in litigation, Respondents claimed Appellant must make an "election of theories" as to whether he will try the case as an equitable mortgage or a sale absolute. Appellant made an "election" as ordered by the court, with objection and in protest, proceeding under the sale theory.¹

¹ The "election of theory" claim was a convoluted and frivolous one concocted by Respondents during the district court action. Thereafter, Appellant made a motion in limine to force the issue onto the table, claiming it was a frivolous argument. (Trans., 4-11) By its nature, an equitable mortgage is a *sale in form*, but a *mortgage in substance*. That issue has not been appealed because correct resolution of the BFP issue will eliminate FMB's interest. It is unclear what FMB is attempting to raise with this foolish "election of theory" argument and it cites no case in support.

II. RESPONDENT FIRST MINNESOTA BANK – NOT APPELLANT - AFFIRMATIVELY RAISED THE BONA FIDE PURCHASER DEFENSE AND THEREFORE WAS REQUIRED TO PROVE ITS BONA FIDE PURCHASER DEFENSE.

First Minnesota concedes, as it must, that the sole burden of its bona fide purchaser defense rests on its shoulders. The district court agreed FMB could have learned of the Graves' interest in the Subject Property had it made inquiry of the Graves. (A49) However, it believes that if it had, FMB:

would have only been made aware of the limited extent of Graves' interest in the property. A title search would have shown that a previous foreclosure had occurred, the redemption period had expired, the property had been redeemed, and that Graves continued to occupy the premises pursuant to a Rent Back Agreement. Under the circumstances of this case, First Minnesota's status would not have been affected by these disclosures. On this record, this Court finds nothing that should disqualify First Minnesota from its status as bona fide purchaser. Accordingly, the Court declares that Plaintiff's interest in the premises is subject to that of First Minnesota.

There is no question that FMB would have been made aware of the Graves' interest had it inquired as required by law. FMB could have been made aware that the Graves continued to occupy the premises pursuant to a Rent Back Agreement. If so, there is no reason FMB could not have learned the Graves exercised their right to cancel. In fact, Mr. Graves testified he and his wife had personal knowledge of this detail.

III. RESPONDENT FIRST MINNESOTA BANK FAILED TO ESTABLISH IT LACKED ACTUAL, CONSTRUCTIVE OR IMPLIED NOTICE OF APPELLANT'S INTEREST AND THEREFORE WAS NOT A BONA FIDE PURCHASER FOR VALUE.

FMB called a single individual to testify on its BFP defense. Rather than calling Guse, who had actual knowledge because he worked on the loan, it called Blair, who testified he was clueless on what facts Guse knew. He conceded Guse may have known of the possessors and their interests.

As an employee, FMB is charged with notice of Guse's factual knowledge and of any inquiry he made. Guse's total knowledge remains a mystery. However, it will be established that FMB failed to prove the BFP doctrine applies in this case.

A. CHARLES BLAIR'S APPEAL TO IGNORANCE DOES NOT ESTABLISH THAT FIRST MINNESOTA LACKED KNOWLEDGE OF THE GRAVES' POSSESSION.

FMB called a single witness – Charles Blair – to testify as the organization's knowledge of the Graves' possession. Not surprisingly, Mr. Blair testified he had no knowledge at the time. This is because he had no involvement in the transaction and was therefore ignorant on the subject. Mr. Blair agreed only Bryan Guse could testify as to known and unknown facts at the time. To be sure, Mr. Blair conceded he was clueless about Mr. Guse's knowledge, agreeing Mr. Guse may have known of the Graves' possession. Naturally, if an ignorant person is called to testify as his actual knowledge, what will the record reflect?

This is a textbook *argumentum ad ignorantiam* – i.e., appeal to ignorance. This is the fallacy of assuming something is true simply because it has not been proven false. For example, one could argue UFOs exist because nobody has *disproven* them. In doing so, the proponent seeks to shift the burden of proof upon the opposing party to disprove it. But the truth of this statement cannot be proven by appealing to ignorance. It is a logical fallacy.

This is probably why the district court shifted the burden upon Appellant to *disprove* BFP status. But the burden does not shift. *Errett v. Wheeler*, 109 Minn. 157, 162-163, 123 N.W. 414, 415 (1909). In *Errett*, the defendant attempted a nearly identical “appeal to ignorance” strategy. *Id.* at 415. The defendant claimed it purchased the property in the ordinary course of business for valuable consideration, free from suspicious circumstances, and without notice of the prior deed to plaintiff. *Id.* Appealing to ignorance of Plaintiff's deed, defendant claimed the burden shifted to the plaintiff to *disprove* his knowledge of the deed. *Id.* However, “the learned trial

court correctly disposed of this point” and rejected this theory. *Id.* In contrast, the district court in the present case did not.

If Mr. Blair was ignorant as to Mr. Guse’s knowledge of facts, it certainly does not follow that Mr. Guse or FMB lacked knowledge. As an employee, Mr. Guse’s knowledge is imputed to FMB. *SCI Minnesota Funeral Services, Inc. v. Washburn-McReavy Funeral Corp.*, 795 N.W.2d 855 (Minn. 2011)(“a corporation is charged with constructive knowledge...of all material facts of which its officer or agent...acquires knowledge while acting in the course of employment within the scope of his authority”). It remains a mystery as to whether Mr. Guse knew of the Graves’ possession, the contents of his discussions with the Waymans and whether he spoke to the late Carol Graves.

Findings and conclusions must be justifiably sound and based on reasonable inferences. *LaFavor v. American Nat. Ins. Co.*, 279 Minn. 5, 155 N.W.2d 286 (Minn. 1967). An inference is a logical, permissible deduction of proven or admitted facts - not pure conjecture. *Wilder v. W.T. Grant Co.*, 270 Minn. 259, 260-261, 132 N.W.2d 852, 853 (Minn. 1965).

Mr. Blair’s testimony that he has no knowledge of Mr. Guse’s understanding as to the Graves’ interest, it does not follow that FMB had no knowledge. As to Mr. Guse’s knowledge – which is imputed to FMB – it remains a mystery because FMB offered nothing. If an organization could prove BFP status by calling someone who is ignorant due to non-involvement, this would ostensibly shift the burden of proof, which was prohibited under *Errett*.

B. FIRST MINNESOTA BANK NEVER PROVED IT LACKED ACTUAL KNOWLEDGE; IN FACT, RECORD SHOWS THE OPPOSITE.

For the most part, FMB offered little evidence to support its claim that it lacked knowledge. All that can be discerned is that Mr. Blair claimed he had no knowledge, which was

explained by his testimony that he was not involved in the transaction. As stated above, Mr. Guse may have knowledge of possession or suspicious circumstances.

To be clear, Appellant has no burden of proving what FMB knew and did not know. This was purely FMB's burden. Nevertheless, the record certainly shows an abundance of actual knowledge that (1) the transaction violated Minn. Stat. §§ 325N.10-.18 and (2) that the Graves had a written purchase agreement entitling them to \$182,000 of gross consideration.

The Transaction Violated Minn. Stat. §§ 325N.10-.18

Minn. Stat. §§ 325N.10-.18 applies to a "foreclosure reconveyance" transaction between a "foreclosed homeowner" and a "foreclosure purchaser." FMB never claimed to be ignorant that the scheme violated Minn. Stat. §§ 325N.10-.18.

First, FMB never claimed – or even proved – it lacked actual notice that the Graves were "foreclosed homeowners," as defined in Minn. Stat. § 325N.10, subd. 2 (defined as "an owner of residential real property...that is the primary residence of the owner and whose mortgage on the real property is or was in foreclosure"). FMB offered no testimony that it did not know the Graves were the owner of the property, that it was the Graves primary residence, and that the mortgage is or was in foreclosure. Mr. Blair concedes he does not know whether Guse knew about the transaction or possession. FMB failed to call Guse to testify as to any supposed lack of knowledge of these facts. In fact, Blair conceded Guse might have had actual knowledge, which would be imputed to FMB. Accordingly, FMB has not met its burden.

Second, FMB never claimed – or even proved - it lacked actual notice that Mr. Wayman, C&M and REA were "foreclosure purchaser," as defined in Minn. Stat. § 325N.10, subd. 3 (defined as "a person that has acted as the acquirer in a foreclosure reconveyance," which "includes a person that has acted in joint venture or joint enterprise with one or more acquirers in

a foreclosure reconveyance”). FMB offered no testimony that it did not know the REA and C&M companies were alter egos of Mr. Wayman, which would be disregarded. In fact, Blair testified he knew these were affiliated and that the \$100.00 mortgage at the very end of redemption was not typical. Both the C&M and REA names appeared on the purchase agreement that FMB had in its possession before it extended the loan. The district court even found it “clear that the only purpose of the \$100.00 mortgage was to create a mortgage so that C&M could redeem the subject property as junior creditor.” (A-35) These facts were also clearly disclosed in the title insurance commitment “heavily relied upon” by FMB. FMB failed to call Guse to testify as to any supposed lack of knowledge of these facts. In fact, Blair conceded Guse might have had actual knowledge, which would be imputed to FMB.

Third, FMB never claimed – or even proved - it lacked actual notice the August 15th transaction was a “foreclosure reconveyance,” as defined in Minn. Stat. § 325N.10, subd. 3 (defined as a two-step transaction involving (1) transfer of title, either by transfer of an interest from the homeowner or by creation of a mortgage or lien that allows for redemption as a junior lienholder, and (2) a subsequent conveyance, or promise of a subsequent conveyance, of an interest back to the foreclosed homeowner allowing him to possess the house, such as a “purchase agreement, option to purchase, or lease”). FMB never claimed to lack actual notice of the quit claim deed at the time of its mortgage to C&M. In fact, this instrument was in its possession and noted in the title insurance commitment it “heavily relied upon.” This was in FMB’s file and contains a fax header date that predated closing. FMB never claimed to lack actual notice of the option to purchase described in the Rent Back Agreement. It never claimed to lack actual notice of the lease received into evidence. FMB had actual notice that an assignment of rents was drafted by it, by which rents were assigned to FMB. Like the quit claim

deed, FMB's file held a copy of the faxed purchase agreement, bearing a fax date that predated closing. The purchase agreement disclosed the Graves had a right to live in the house through October 1, 2007 and beyond by paying a "per diem of \$150.00." FMB failed to call Guse to testify as to any supposed lack of knowledge of these facts. In fact, Blair conceded Guse might have had actual knowledge, which would be imputed to FMB.

Fourth, FMB failed to prove it had actual notice of violations of Minn. Stat. § 325N.10-.18. FMB failed to prove it lacked actual notice that the quit claim deed was executed before a compliant contract was fully executed, violating Minn. Stat. § 325N.11. The plain language of the quit claim deed and purchase agreement plainly disclose the violation and were in FMB's possession. FMB failed to prove it lacked actual notice that the contract omitted mandatory terms, violating Minn. Stat. § 325N.12. Again, the plain language of the quit claim deed and purchase agreement plainly show a violation. FMB failed to prove it lacked actual notice of that the contract omitted the notice of cancellation, violating Minn. Stat. § 325N.14. It is clear that FMB failed to prove it lacked actual notice of each of the other violations of Minn. Stat. § 325N.17 that were found. Specifically, FMB failed to prove it lacked notice that the Graves were never paid the statutory amount stated in Minn. Stat. § 325N.17(b).² Again, FMB failed to call Guse to testify as to any supposed lack of knowledge of these facts. More important, Blair conceded Guse might have had actual knowledge, which would be imputed to FMB.

The Graves Held a Vendor's Lien

As noted in Appellant's brief, a vendor's lien is simply a lien for unpaid proceeds for a conveyance. If title vested in C&M, FMB's interest would be subordinate to the Graves' lien – and subject to foreclosure. As noted above, FMB knew C&M was obligated to pay the Graves

² Much like a vendor's lien, the Graves would have a statutory lien for this amount.

\$182,000 as stated in the purchase agreement. It knew C&M understood it had an obligation to pay the Graves \$182,000 even after the supposed redemption period. This is reflected on the settlement statement, which clearly identifies an amount due to the Graves. More important, FMB failed to prove it lacked notice that the Graves were never paid \$182,000. FMB failed to call Guse to testify as to any supposed lack of knowledge of these facts. More important, Blair conceded Guse might have had actual knowledge, which would be imputed to FMB.³ FMB never proved it lacked actual notice, conceding truly may have.

C. FIRST MINNESOTA'S CONSTRUCTIVE KNOWLEDGE

On **page 34** of its responsive brief, FMB believes constructive notice only applies to recorded instruments. *See, e.g., Anderson v. Graham Inv. Co.*, 263 N.W.2d 382, 384 (Minn. 1978). However, a person is also deemed to have constructive notice of title if another person is in actual possession:

[P]ossession of real estate is *constructive* notice of the title of the possessor. Such notice is the same in effect as the notice which is imputed by the recording acts. Possession is not only prima facie evidence of title, but is also notice of whatever rights the possessor has, which would be disclosed upon reasonable inquiry. *This is a branch of the doctrine of constructive notice. Such possession in order to be sufficient to constitute notice, must be actual, open, visible, and exclusive possession inconsistent with the title of the apparent owner by the record.*

Farmers' State Bank of Eyota v. Cunningham, 182 Minn. 244, 246, 234 N.W. 320, 321 (1931)(emphasis added).

FMB claims “[c]onstructive notice is not at issue here because there is no testimony on record that there was ever a recorded instrument...setting forth Appellant’s claimed interest in the Property.” FMB is naturally confused over the distinction between *constructive* notice and

³ Rights in real property can continue after the end of a supposed redemption period under § 325N and case law. *See, e.g., Oertel v. Pierce*, 116 Minn. 226, 271-272, 133 N.W. 797, 799-800 (Minn. 1911).

implied notice. Apparently, its confusion trickled over to the district court when it changed its findings.

It was undisputed that the Graves were in actual, open possession of the Subject Property and it was their sole home. Even Blair “testified that First Minnesota made no inquiry of the Graves regarding their possession of the premises.” (A49) As *Cunningham* holds, the Graves’ possession is “the same in effect as the notice which is imputed by the recording acts.” 182 Minn. at 246, 234 N.W. at 321.

The *Daml* case cited by Respondent is inapposite. *Daml v. Meyers*, 2010 WL 7326389 (D. Minn. 2010). In that case, the court found it important that the foreclosure purchaser “gave the mortgage to [the bank] at the same closing at which he received the deed to the Property from the [foreclosed homeowner].” *Id.* at *3. Whether correct or incorrect in its analysis, a key difference is that the Graves continued to live in the Subject Property for approximately a month after signing the quit claim deed. FMB also had a copy of the quit claim deed and purchase agreement. It knew of C&M’s business. It is unnecessary to state all the distinctions.

FMB failed to prove it lacked constructive notice of the Graves’ interest. The recorded instruments show a foreclosed home, occupied by the Graves, with a quit claim deed to REA for \$500.00 or less of consideration during the redemption period. Two days before the end of redemption, REA gave a \$100 mortgage to C&M and C&M redeemed. The recorded instruments show Michael Wayman was the CEO of both entities. This, combined with the actual notice of the Purchase Agreement, is sufficient to show a violation of Minn. Stat. §§ 325N.10-.18 and that Appellant holds a vendor’s lien for non-payment.

D. FIRST MINNESOTA'S IMPLIED KNOWLEDGE

For implied notice, the Supreme Court has stated the following rule for implied notice cases:

One is not a bona fide purchaser entitled to protection of the recording act, though he paid a valuable consideration and did not have actual notice of a prior unrecorded conveyance from the same grantor, if he had knowledge of facts which ought to have put him on an inquiry that would have led to knowledge of such conveyance.

Henschke v. Christian, et al., 228 Minn. 142, 146-47, 36 N.W.2d 547, 550 (1949). If a person is in actual, open possession of real property, this operates as constructive notice, as explained by *Cunningham*. 182 Minn. at 246, 234 N.W. at 321. If a person is not in actual, open possession, but has notice of suspicious facts which would have triggered an inquiry leading to knowledge of an unrecorded interest. *Henscke*, 228 Minn. at 146-47, 16 N.W.2d at 550.

As FMB notes, *implied* notice requires knowledge of suspicious facts. But it apparently confused implied notice with constructive notice. Now that its confusion is lifted, it should follow that FMB concedes to Appellant's superior interest.

Although this should dispose of the matter, FMB nevertheless failed to prove it lacked knowledge of facts which required an inquiry. It had actual knowledge that the Graves were owners, had been foreclosed, and executed a quit claim deed for \$500 or less during the redemption period. Blair agreed the \$100 mortgage from REA to C&M was not typical. After all, the mortgage's recording fee was \$46 and recording a satisfaction would cost another \$46, leaving nothing greater than a few dollars of benefit. FMB knew the Graves signed a purchase agreement for \$182,000, despite deed representing \$500 or less of consideration. It knew the Graves had a right to continue living in the house because this was stated clearly in the purchase agreement. It knew C&M acknowledged it owned the Graves funds on the settlement statement.

Adding up all distributions, it knew it lacked documentation that C&M paid the Graves \$182,000. In fact, the settlement statement strongly suggests missing money. Blair testified that Guse closed the loan. If so, FMB would know – as the court found – that the Graves had not been paid over \$70,000. It never proved it lacked notice that the Graves were foreclosed homeowners or that the Wayman Entities were a foreclosure purchaser.

It is unnecessary to restate all of the facts of which FMB concedes having actual knowledge of, many of which are restated above. However, FMB knew the Graves owned and occupied the Subject Property, had been foreclosed, signed a quit claim deed for \$500 or less of consideration, signed a purchase agreement the same day for \$182,000 of gross consideration, that REA and C&M were entities owned by Mr. Wayman, that the clear purpose of the \$100 mortgage from REA to C&M was simply to redeem as a junior creditor, that the settlement statement shows C&M and FMB understood the Graves were entitled to payment as a “payoff,” and that the purchase agreement allowed the Graves to continue living in the Subject Property well past the date on which FMB gave a mortgage to C&M.

Under the implied notice rule, it is true that it applies “if” the purported BFP had actual notice of suspicious facts that would lead to knowledge of an unrecorded interest. It is clear that FMB’s actual notice of these facts would have led to knowledge that (1) the transaction violated §§325N.10-.18 and (2) the Graves had not been paid \$182,000. Perhaps FMB inquired during the “underwriting” performed by Guse. But Blair had no idea whether inquiry was made or any results.

On these facts, FMB bears the burden of proving it could not have led to any knowledge of the Graves’ interest in the Subject Property. In fact, the district court agreed FMB could have learned of the Graves’ interest through inquiry.

Beginning on **page 35** of its responsive brief, FMB evidences confusion over the distinction between *actual possession* as constructive notice and *actual knowledge of suspicious facts* as triggering implied notice. For instance, on **page 36** of its brief, FMB implies *Hauger v. J.P. Rodgers Land Co.*, 156 Minn. 45, 194, N.W. 95 (Minn. 1923) only involved implied notice. Instead, it considered both implied and constructive notice. The facts were clear that the out-of-state lender had no *actual knowledge* that a person openly possessed the property. Instead, the court noticed that plaintiff's *actual possession* served as constructive notice of plaintiff's rights, stating "had [the out-of-state lender] visited the house and made inquiry of the plaintiff and his wife, he would in all probability have learned much more about the transaction" even though "plaintiff was not awakened to a realization of the fraud that had been practiced upon him." *Id.* at 50. It noted *actual possession* (not *actual knowledge* of possession) is notice to all the world of the title and rights of the person in possession. *Id.* This operates as constructive notice, which is equivalent to a recorded interest as *Cunningham* notes.

As the court agreed, FMB could have learned of the Graves' Rent Back Agreement if it made inquiry. If it reviewed that document, it certainly would have known the Graves had a right to purchase the property and, because the notice of cancellation form was part of the agreement, would have seen that the Graves cancelled the same. FMB could have learned much more about the transaction had they inquired as the constructive and implied notice rules command.

On **page 37** of its responsive brief, FMB implies the purported BFP actually received a copy of the lease *before* receiving its interest in the property. *Ludowese v. Amidon*, 124 Minn. 288, 144 N.W. 965 (Minn. 1914). Rather, the court noted "[i]t does not appear when this lease and the deed to Rebecca came into her possession." *Id.* at 294. There was no showing that the

purported BFP had any *actual knowledge* of the lessee's possession. Even then, it still found the purported BFP never met its burden because "without inquiry [of an actual possessor] no one can claim to be an innocent purchaser." *Id.*; *Sheerer v. Cuddy*, 85 Cal. 270, 273, 24 P. 713 (Cal. 1890) (reversing trial court BFP finding because "[w]hether the respondent knew of appellant's [actual] possession, or not, is immaterial" to constructive notice).

Regardless, FMB offered no evidence that it did not know of the Graves' possession or rights. Instead, Blair testified Guse could have known and that FMB was unsure of his knowledge, which is imputed to FMB.

E. OTHER POINTS MADE BY FIRST MINNESOTA

On **page 27** of its responsive brief, citing section 325N.17(f)(3), FMB misleads the court in claiming its mortgage is "not 'defeated or affected' unless the bona-fide purchaser had 'notice of a violation of sections 325N.10 to 325N.18.'" (Emphasis added) This statement implies its mortgage is presumably valid unless it Appellant affirmatively shows FMB had notice of a violation. As stated above, FMB's framing of the issue is an erroneous attempt to shift the burden to Appellant. Even the statute places the burden solely and squarely on FMB's shoulders:

A foreclosure purchaser shall not...(f) do any of the following until the time during which the foreclosed homeowner may cancel the transaction has fully elapsed... (3) transfer or encumber or purport to transfer or encumber any interest in the residence in foreclosure to any third party, provided no grant of any interest or encumbrance is defeated or affected against a bona fide purchaser or encumbrance for value and without notice of a violation of sections 325N.10 to 325N.18, and knowledge on the part of any such person or entity that the property was "residential real property in foreclosure" does not constitute notice of a violation of sections 325N.10 to 325N.18. This section does not abrogate any duty of inquiry which exists as to rights or interests of persons in possession of the residential real property in foreclosure..."

Minn. Stat. § 325N.17(f)(3)(emphases added).

By statute, FMB was obligated to prove (1) it was a bona fide encumbrancer for value AND (2) it lacked notice of a violation of sections 325N.10 to 325N.18. It failed to do so and the district court never reached any affirmative findings showing FMB *lacked* notice of these items, finding only that FMB must be innocent because Appellant did not affirmatively show FMB had notice. Under the correct standard, FMB failed to affirmatively *lacked* notice and the district court never made such a showing.

On **page 28** of its responsive brief, FMB once again seeks to shift the burden upon Appellant, stating “[t]he record is absolutely void of any evidence that First Minnesota had such notice prior to this litigation, and Appellant cannot make such a showing.” As noted above, FMB bears the sole burden and it does not shift to Appellant – ever. The issue is not whether FMB had “such notice prior to this litigation.” Instead, the issue is whether FMB *lacked such notice* at the time of its mortgage. This is a vital distinction. Appellant has no burden of proving FMB had notice. FMB must prove it lacked notice.

Also on **page 28** of its responsive brief, FMB simply outs out that a title search would have yielded nothing of the Graves’ right in the property. First, this finding only relates to *constructive* notice. If inquired up on, FMB would have learned the Graves cancelled the transaction, which left C&M with nothing. Even if the transaction were not cancelled, the Graves were entitled to \$182,000, which was not terminated by the foreclosure. This obligation was ratified by C&M and memorialized into the settlement statement. The fact that FMB could have learned the Graves gave a quit claim deed during redemption and, after expiration of the redemption period, “continued to occupy the premises pursuant to a Rent Back Agreement” simply affirms that FMB knew or could have known that the transaction involved a foreclosure reconveyance violating §§ 325N.10-18. This language does not marginalize what could have

been learned. If anything, it clarifies that FMB could have learned of the important facts necessary to reach a legal conclusion as to the Graves' interest.

On **page 29** of its responsive brief, FMB claims if the transaction was void before the redemption period expired, the property would have been lost. However, the district court found the Graves were not without options. Also, the foreclosure reconveyance statute was specifically designed to protect this situation. *See* Minn. Stat. § 325N.10, subd. 3 (protecting junior mortgages or liens created for the purpose of redeeming as junior lienholders).

On **page 30** of respondent's brief, it believes the incorrect burden of proof is a "harness error." As noted, the district court presumed FMB was an innocent purchaser and looked upon Appellant to offer evidence to disprove the theory.

It never affirmatively found FMB produced evidence it lacked actual, constructive or implied notice. Instead, it found Appellant failed to prove FMB had actual, constructive or implied notice. By default – rather than by evidence – the court reached its decision.

If the district court applied the correct burden, it would have presumed FMB had actual notice. In doing so, it would have assumed Guse had actual notice of the Graves' interest, absent a showing to the contrary. Because FMB refused to call him, the default conclusion is that he must have had actual notice. Perhaps FMB may have proven actual notice by calling persons who had discussions with Guse, such as Mr. Wayman. But one cannot deny that FMB never proved it lacked actual notice. It only proved Blair lacked actual notice. Even more important, the district court never affirmatively found FMB lacked actual notice. Instead, it merely found "nothing that should disqualify First Minnesota" from being a BFP. (A50)

If the district court applied the correct burden, it would have presumed FMB had constructive notice. In doing so, FMB would be presumed to have notice unless it produced

conclusive evidence to overcome the presumption. *Hauger v. J.P. Rodgers Land Co.*, 156 Minn. 45, 50, 194 N.W. 95, 97 (Minn. 1923). The court actually found FMB did not produce conclusive evidence, noting FMB could have learned of the Graves' interest had it inquired. But then the court proceeded to speculate on what FMB would have learned had it inquired of the Graves, which was erroneous because:

The court will not speculate in cases of this character upon what might happen or be discovered if inquiry were made, but will presume, in the absence of evidence conclusively showing the contrary, that upon inquiry the true situation and claims of the possessor would be made known. The only way of overcoming this presumption is to produce the conclusive evidence, or make the inquiry. The conclusive evidence does not appear, and as no inquiry was made, the presumption must be applied.

Id., 156 at 50, 194 N.W.at 97 (emphasis added). Considering the court agreed FMB made no inquiry, it could have only found in favor of FMB if conclusive evidence were shown otherwise. Because of this rule, it is unnecessary to remand because the district court agreed FMB could have learned of the Graves' interest. The speculation on what it could have learned must be stricken.

Considering the entire burden was incorrectly applied at the beginning, this is not a "harmless error." But it is unnecessary to remand for additional findings because the record does not show conclusive evidence.

On **page 32** of respondent's brief, FMB believes applying § 325N would be unfair to a sophisticated, \$345mm banking institution because the Graves would have supposedly lost their modest house at the end of redemption the following month. But § 325N.10-.18 is an action at law – not equity – and the equities theme has no bearing. Under FMB's theory, anyone who redeems a foreclosure should keep its interest because the owner would otherwise lose the

property. In other words, it believes equities under the foreclosure purchaser statute favor the predator and its successors, rather than the prey.

But this is the type of conduct the legislature sought to prohibit. It made most of the practices in this action amenable to criminal action. Minn. Stat. § 325N.18, subd. 4 (up to one year imprisonment). FMB, having aided and abetted the Wayman Companies with the scheme, is out on the preverbal limb claiming equities are somehow in its favor. The record shows FMB received a full judgment against C&M for the amount due in its foreclosure by action. Had FMB asked the Graves, it would have learned the transaction was cancelled. In all likelihood, it knew of the Graves' interest vicariously through Guse, which is why it chose not to call him.

Although irrelevant in this instance, equity favors allowing Appellant his family home and the memory of his late wife, particularly when they cancelled the transaction. FMB is in the business of lending and taking risk. It lent money to C&M knowing the funds were earmarked for a foreclosure purchasing operation. Moreover, the district court would be responsible for weighing any equities even if they were, available. The district court's initial findings found no equities in favor of FMB and, contrary to FMB's belief, the amended findings were not based upon "equities." Instead, it was based upon an erroneous application of BFP law made at FMB's insistence on its motion to amend. The court found the Graves were not without options. Because FMB is not a BFP, the law views this situation as though Wayman funded the deal directly, since an assignee takes subject to the equities of the assignor. Moreover, the law follows equity, and §§ 325N.10-.18 was designed to protect vulnerable foreclosed purchasers.

On **page 37** of its responsive brief, FMB claims "it did not ignore the language of the title insurance exceptions." To support this claim, it states "Blair testified that the initials on the side of each listed exception to the title insurance policy indicated that the matters had been

addressed and resolved at the time of the closing of the loan.” This testimony says nothing about what the language “taken care of” or “resolved” means. (Trans, 180:5-12). If FMB purports it engaged a third party title company as its agent for inquiry, the title company’s knowledge would be imputed through ordinary agency rules just like Guse’s knowledge. FMB never called a title company. What FMB calls “initials” on the list of exceptions is, instead, the word “on.” Each item on the listed exceptions is “on” – vis-à-vis – “off.” This means the policy will insure the list unless they were “taken care of to [the insurer’s] satisfaction.” (APP92) FMB did not even attempt to speculate on what “taken care of” consisted of – to wit visiting the property, discussing with the late Carol Graves, nothing, etc.

On **page 38** of its responsive brief, FMB claims *Appellant* failed to explain how FMB would have known the Graves had not been paid the \$182,000 listed in the purchase agreement when it reviewed the Settlement Statement at closing. First, Appellant does not have to explain anything. This is FMB’s sole burden of explaining the Settlement Statement did not trigger inquiry notice. Second, basic math shows the disbursements do not reflect \$182,000. Third, Blair testified Guse closed the transaction and his knowledge would be imputed to FMB. Fourth, FMB relied upon the title company, who Blair testified was authorized and engaged to handle title issues, and the title company’s knowledge of non-payment would also be imputed through agency principles. Fifth, Line 101 of the Settlement Statement contains a place for stating the total sales price. This line was suspiciously omitted, triggering a duty of inquiry. If \$182,000 had been included, then the “gross amount due from borrower” on Line 120 would have been much higher – unless a down payment or earnest money check was credited on the intervening lines. Blair testified C&M might have had banking accounts at other institutions, but he did not

know. He also testified he had access to C&M's bank account information at FMB, but never checked to see if C&M ever made a single payment to the Graves.

FMB concedes the purchase agreement did not state the date on which the Graves were to be paid. It could have been after the September 2007 loan according to the purchase agreement, which FMB acknowledges on page 38 of its responsive brief. On **page 39** of its responsive brief, FMB acknowledges the Graves had a right to \$182,000 "within 150 days" of eviction or dispossession. This would be equivalent to a vendor's lien. FMB knew the Graves had to be paid. Had it inquired based on these circumstances, it would have known the Graves had not been paid and retained a vendor's lien for any sale and/or had a statutory right to payment under section 325N.17(b).

IV. FIRST MINNESOTA BANK'S ARGUMENTS AGAINST A VENDOR'S LIEN IGNORE THAT APPELLANT WAS ALSO ENTITLED TO PAYMENT NOT ONLY BASED ON EQUITY, BUT ALSO STATUTE.

FMB's argument against a vendor's lien is mostly based on blaming the victim for being prey in the first place. FMB purports the vendor's lien, being equitable in nature, should allow anyone supplying the financial ammunition should be protected.

Assuming, for the sake of argument, the Graves delivered title, the transaction had not been cancelled and FMB truly proved it lacked notice of violations of §§325N.10-.18, then FMB would still be subject to a vendor's lien because it is not a BFP. It never proved it lacked actual, constructive and implied notice of the Graves' right to \$182,000 of proceeds. It knew the Graves were entitled to this amount. If a sale truly occurred, then any valid foreclosure by FMB would vest title in its name. However, its title interest would be inferior to Appellant's vendor's lien for the unpaid amount. Equity does not allow FMB to make a total profit at the Graves' expense. An assignee takes subject to the equities of its assignor. *See, e.g., MacDonald v. Kneeland*, 5 Minn. 352, 6 Gil. 283 (Minn. 1861).

FMB's "blame the victim" is disingenuous and does not comport with ordinary principles of equity.

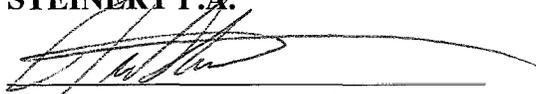
The fact that the Graves were uneducated in these matters and were victims of an equity stripping scheme does not place any equities in FMB's favor.

CONCLUSION

Summarily, FMB concedes the district court incorrectly imposed the burden upon Appellant. This is no surprise, considering that FMB has pressed – even in this Court – a rule that Appellant must *disprove* FMB's supposed status. FMB failed to prove it lacked actual notice and refused to call anyone (e.g., Guse) who worked on the loan at the time. The record shows it did. FMB failed to prove it lacked constructive notice. The Graves were in actual possession and, if it made no inquiry, this forced FMB to provide conclusive evidence, which it has not. Finally, FMB failed to establish its actual knowledge of suspicious facts were reasonably investigated. The record is quiet on what FMB did because it refused to call anyone with real knowledge on the matter. FMB is not a BFP and it takes subject to Appellant's rights.

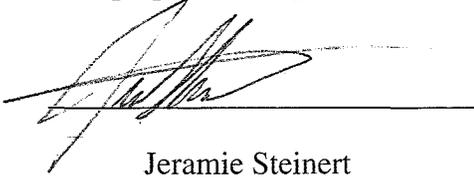
Dated: 2/16/12

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CERTIFICATE OF COMPLIANCE

I hereby certify that this brief complies with the type-volume limitations of Minn. R. App. P. 132.01, subds 1 and 3, contains 8005 words and was prepared using Microsoft Word 2010.



Handwritten signature of Jeramie Steinert over a horizontal line.

Jeramie Steinert