PLUNKETT COONEY

Current Status of Equitable Subrogation in Michigan

November 22, 2013
Terra Firma Newsletter - Fall/Winter Edition 2013

While equitable subrogation has not yet achieved the status that it enjoys in other states, recent cases in Michigan have moved it closer.

In 2005, the Michigan Court of Appeals' decision in *Washington Mutual v Shorebank*, 267 Mich App 111 (2005) helped Michigan's cause for equitable subrogation. In this case, Washington Mutual was the lender who re-financed a prior (primary) mortgage to Option One. Shortly before the closing of the Washington Mutual mortgage, the borrower gave two smaller mortgages to Shore Bank and Standard Federal. Claiming that it was unaware of the two prior mortgages, Washington Mutual asked the appellate court to find that its subsequently recorded mortgage be given the prior priority status of the Option One mortgage of which its proceeds paid off, citing the doctrine of equitable subrogation. In denying the relief requested, the appellate court decided that since Washington Mutual was a new lender, it was a mere "volunteer" and was, therefore, not entitled to equitable subrogation, citing the older Michigan Supreme Court of *Lentz v Stoeffet*, 280 Mich 446 (1937), which said:

When plaintiffs loaned the money, they had no interest to protect …
it was voluntarily done on their part, and to grant it would not leave defendant in its former position. A mere volunteer is not entitled to subrogation". *supra* at 451.

In denying the application of equitable subrogation in the Washington Mutual case, the Michigan Court of Appeals left the door open by referring to *Schanhite v Plymouth United Bank*, 277 Mich 933 (1936). In *Schanhite*, the borrower gave the existing lender a new and larger mortgage of which additional proceeds were used to pay off property taxes that had gone into default. The appellate court allowed equitable subrogation over intervening mortgages because the lender had an existing interest in the property and the additional funds were required to protect that interest.

The idea of allowing equitable subrogation to an existing lender was found to be an accurate statement of Michigan law in the federal court case of *Van Dyk Mortgage Co v United States of America*, 503 Fed Supp 2d 876 (2007). In this case, the borrower re-financed a 2002 mortgage to Van Dyk with one that was $20,000 more in 2004. Five days before the closing of that replacement mortgage, the IRS recorded about $66,000 in federal tax liens. In citing *Shorebank,* the federal court afforded equitable subrogation to Van Dyk, stating that it was not a volunteer and at closing, it did not know about the IRS liens.

The suggestion of allowing equitable subrogation to an existing lender came further into fruition in the case of *Citimortgage, Inc. v Mortgage Electronic Registration Systems, Inc.*, 295 Mich App 72 (2001). There, the borrowers re-financed a 2001 ABN AMRO mortgage with a new one to ABN AMRO in late 2002. In the interim, the borrowers had given a mortgage to GMAC. In affording equitable subrogation to Citi, successor to ABN AMRO mortgage, the court referred to the Restatement of Property, third mortgage § 7.3 as well as *Shorebank, supra*. The court believed that equitable subrogation was affordable under these circumstances but remanded the case to the trial court for a finding as to whether or not the intervening lender was prejudiced by its application. Notably, the court indicated that a consideration of the equities is required for an analysis of equitable subrogation and, in this case, it was uncontradicted that the intervening mortgage had not been posted by the Wayne County Register of Deeds when the replacement mortgage was given to ABN AMRO and, therefore, was unknown to the replacement lender at the time of closing.

The equitable subrogation envelope was pushed further in the case of *National City Mortgage v Mercantile Bank of Michigan* (unpublished), 2012 WL 3101821. While reciting an amendment to the Michigan Recording Statute as a basis (which did not at all change the "race notice" statute, MCL 565.29), this panel of the Michigan Court of Appeals found that the facts were essentially identical to those of *Citimortgage v MERS, supra*. Yet, oddly, they were not. In *Citi*, the intervening mortgage was posted by the Register of Deeds when the replacement mortgage was given. In this case, the intervening mortgage had been recorded for seven months prior to the giving of the replacement mortgage!! Nevertheless, the appellate court's opinion was silent on that distinction.

Finally, the case of *MB Financial Bank N.A. v Thorn,* 2012 WL 4093617 (2012) goes on to analyze the further issue of any prejudice to the intervening lien holder, even if equitable subrogation is being considered. In this case, a third-party builder had an intervening mortgage that its lender had agreed to subordinate on two previous occasions to the owner's lender. On the third re-finance, the intervening lender would not subordinate, but the replacement lender went ahead anyway and closed the loan. The court held that the intervening lender was prejudiced and did not allow equitable subrogation.

This case also sets forth a good analysis of the present state of equitable subrogation in Michigan, and raises the question: if an intervening lender is known of and does not subordinate, is equitable subrogation available? It may even clash with *National City Mortgage v Merchantile Bank*, cited above.

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