



## The Docket: The Meaning of the Word 'Is': Title Insurer as a Creditor in Bankruptcy Court

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*The Docket is a monthly TitleNews Online feature provided by ALTA's Title Counsel Committee, which reviews significant court rulings and other legal developments, and explains the relevance to the title insurance industry.*

Today's review of a recent U.S. Court of Appeals case concerning an insurer's claim against an allegedly fraudulent borrower was provided by Lance Pomerantz, a sole practitioner in New York focusing exclusively on land title issues. He can be reached at [Lance@LandTitleLaw.com](mailto:Lance@LandTitleLaw.com).

**Citation:** *Pazdzierz vs. First American Title Insurance Company* (In re Pazdzierz), No. 11-2398/2441 (6th Cir., June 10, 2013)

**Facts:** The debtor had previously obtained loans secured by mortgages on properties he claimed to own but, in fact, did not. First American, acting through a policy-writing agent, insured the mortgages. Following closing, the lender immediately assigned the notes and mortgages to Bayview Financial.

After the debtor defaulted on the loan payments, Bayview discovered the debtor did not have title to the property and filed claims against First American. In settling the claims, Bayview assigned 75 percent of its interest in the notes to First American.

The debtor commenced a voluntary Chapter 7 bankruptcy proceeding. First American sought an order holding the debt was not dischargeable pursuant to 11 U.S.C. 523(a)(2)(b). Debtor argued that Michigan law prohibits assignment of claims for fraud, precluding First American from pursuing its claims under the notes. In addition, he claimed that First American could not show reliance upon the false information that Debtor had provided to the original lender.

**Holding:** The Court of Appeals panel quickly determined that the claims were "grounded in tangible property rights," i.e., the notes (assignable under Michigan law), rather than merely "naked claims of fraud" (which are not assignable).

The reliance argument turned on the meaning of the word "is" in §523(a)(2)(b) ("a statement ... on which the creditor to whom the debtor is liable for such money, ... reasonably relied")(emphasis supplied). Debtor argued that, because of the assignment, First American was the "creditor to whom the debtor is [presently] liable" for purposes of the Chapter 7 proceeding, and that the allegedly false representations were made to the original lender. Following precedent from the Ninth and Seventh Circuits, the court held that if the original lender relied on false information, the debt became non-dischargeable at the time the original lender advanced the funds. The subsequent assignment did not alter this status.

**Relevance to the Title Industry:** Following the economic crisis of recent years, many instances of mortgage fraud have come to light. When these schemes result in title claims, insurers need to seek recovery from the perpetrator. This decision promotes sound public policy prohibiting dishonest debtors from escaping liability.

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