

When Mistakes Are Made in Mortgage Documents, Courts Will Not Use Equitable Subrogation to Reform

For title companies issuing title insurance policies and attorneys who defend these companies, a recent case from the Eighth Circuit should serve as a reminder that, if mistakes in legal descriptions are made, they should be corrected as soon as possible. When a mistake is made, discovered, and left uncorrected, the doctrine of equitable subrogation cannot be used to reform a flawed mortgage.

In *Ocwen Loan Servicing, LLC v. Summit Bank, N.A., (In re Francis)*, 750 F.3d 754 (8th Cir. 2014), a recent Eighth Circuit case, the Francises (the "Debtors") owned a 22-acre parcel of land that was divided into two portions: a 10.5-acre parcel ("Parcel A") and an 11.5-acre parcel ("Parcel B"). GMAC Mortgage Corporation ("GMAC") refinanced a first mortgage loan on the Debtors' home and full 22 acres, but inadvertently described the adjacent 11 acres on the mortgage document, which was signed and filed. Mr. Francis realized the error and attempted to bring it to GMAC's attention, but GMAC did not modify the loan documents.

Subsequently, the Debtors mortgaged Parcel A to Summit Bank ("Summit") to secure a new loan. The Debtors told Summit about their intent to grant GMAC a first mortgage, but that GMAC had not corrected its error in the mortgage. Summit therefore concluded that it held a first mortgage on Parcel A. The Debtors then mortgaged all 22 acres to Southern State to secure two additional loans after Southern State also concluded that GMAC had no mortgage lien on the property.

Without GMAC's Mortgage Lien

Parcel A(1) Summit (2) Southern State	Parcel B(1) Southern State
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With GMAC's Mortgage Lien

Parcel A(1) GMAC (2) Summit (3) Southern State	Parcel B(1) GMAC (2) Southern State
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After the Debtors filed for bankruptcy, GMAC's successor in interest ("Ocwen") argued that it should be entitled to equitable subrogation under Arkansas law because GMAC satisfied the prior first mortgage on the property and the Debtors intended GMAC to have a first mortgage lien. The Eighth Circuit concluded that the doctrine of equitable subrogation should not apply in this context because "equity will only intercede provided it can be done without working hardship or injustice to innocent parties." Not only would allowing Ocwen to revive GMAC's first mortgage be unfair to Summit and Southern State, but GMAC's position was also a product of its own negligence. GMAC's agents prepared the flawed loan documents and did not heed the Debtors' warnings to correct the legal description of the property. As such, the court refused to stretch the doctrine of equitable subrogation to revive Ocwen's lien.

When mistakes in legal descriptions occur, it is important to take immediate steps to correct the problem. The Ocwen court emphasized that GMAC was to blame for its own position; the Debtors warned GMAC of the error, but the problem went uncorrected. Without this carelessness, the court may have been more sympathetic to Ocwen's position. Additionally, it is important to note that an attempt to revive a mortgage lien like GMAC's with an equitable subrogation argument may not succeed for the reasons discussed by the Eighth Circuit. Equitable subrogation must not work hardship or injustice on innocent parties, and the party seeking subrogation must be without fault. In situations such as this in which a party failed to correct a mistake in a mortgage document, the doctrine cannot be used to salvage a lien.

If you have any questions about equitable subrogation, please contact your Reinhart attorney or any member of Reinhart's [Business Reorganization group](#).

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