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U.S. BANKRUPTCY COURT
NORTHERN DIST. OF CA.
SAN FRANCISCO, CA.

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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re)	
LAURENCE ELLIOT WHITING,)	Bankruptcy Case
)	No. 03-31927 DM
)	
Debtor)	Chapter 7
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E. LYNN SCHOENMANN, Trustee,)	Adversary Proceeding
)	No. 03-3697 DM
Plaintiff,)	
)	
v.)	
)	
KATHLEEN M. DE LEON and)	
L. MICHAEL DE LEON,)	
)	
Defendants.)	
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MEMORANDUM DECISION ON PLAINTIFF'S MOTION
FOR PARTIAL SUMMARY JUDGMENT

On March 11, 2004, this court held a hearing on the motion for partial summary judgment ("MSJ") filed by the Trustee E. Lynn Schoenmann ("Trustee"). Defendants Kathleen M. de Leon and L. Michael de Leon ("the de Leons") filed an opposition to the MSJ. For the reasons stated below, the court will deny the MSJ.¹

I. Relevant Undisputed Facts

This case concerns a "Tenancy in Common Agreement for 320-322

¹The following discussion constitutes the court's findings of fact and conclusions of law. Fed. R. Bankr. P. 7052(a).

1 Collingwood Street" ("TIC Agreement") between Laurence E. Whiting
2 ("Debtor") and the de Leons. At the time of the filing of the
3 bankruptcy petition, Debtor had a 32.14% or roughly one-third
4 interest, in property held as a tenant in common with the de
5 Leons.

6 In 2000, the de Leons purchased the entirety of property
7 located at 320-322 Collingwood Street, San Francisco, CA, 94114
8 ("Property"). The Property consists of a single parcel of land
9 with two dwellings. Since the time of the de Leons' purchase the
10 rear dwelling has been exclusively occupied by Debtor. The de
11 Leons have exclusively occupied the front dwelling. There is
12 separate access to each dwelling: the front dwelling has access
13 directly from the sidewalk up the front stairs, and the rear
14 dwelling has access from a separate stairway and walkway on the
15 South side of the Property.

16 In 2001, the de Leons and Debtor engaged in negotiations for
17 Debtor's purchase of an interest in the Property. The de Leons
18 and Debtor jointly sought and secured financing in the amount of
19 \$750,000. The Property loan was secured by a deed of trust which
20 was signed by the de Leons and by Debtor, and properly recorded.
21 In addition the de Leons and Debtor entered into the separate TIC
22 Agreement. The TIC Agreement provided that Debtor would be
23 responsible for 71.83% or roughly two-thirds of the loan
24 obligation (\$538,757), and the de Leons would be responsible for
25 the remaining one-third of the loan obligation (\$226,243). The de
26 Leons contend and Trustee does not dispute that Debtor agreed to
27 be responsible for a greater share of the loan obligation in lieu
28 of a down payment on the Property. The TIC Agreement set forth

1 the agreement between the de Leons and Debtor as to the division
2 of the loan obligation, areas of exclusive occupancy by each party
3 and further rights and obligations of each party relating to the
4 Property. Debtor and the De Leons also executed and signed a
5 "Memorandum of Agreement" which referenced the TIC Agreement. The
6 Memorandum of Agreement was to be recorded with the County
7 Recorder's office. Debtor and the de Leons failed to record the
8 Memorandum of Agreement or the TIC Agreement itself.²

9 On July 1, 2003, Debtor filed a chapter 7 bankruptcy
10 petition. As of the date of the filing of the bankruptcy petition
11 the TIC Agreement had not been recorded.

12 II. Issue

13 Whether Trustee can use Section 544(a)(3)³ to defeat the
14 effect of the TIC Agreement.

15 III. Discussion

16 A. Summary of Arguments

17 The de Leons argue that Trustee's MSJ must be denied because
18 triable issues of fact remain as to whether Trustee can use
19 Section 544(a)(3) to defeat the effect of the TIC Agreement. The
20 de Leons further argue that Trustee cannot establish that a
21 hypothetical buyer would have been without constructive notice of
22 the TIC Agreement and therefore cannot achieve the status of a
23 bona fide purchaser ("BFP").

24
25 ²For purposes of discussion, the TIC Agreement and the
26 Memorandum of Agreement will be treated as a single unrecorded
agreement referenced as "TIC Agreement".

27 ³Unless otherwise indicated, all chapter, section and rule
28 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330 and
the Federal Rules of Bankruptcy Procedure, Rules 1001-9036.

1 Trustee responds that the MSJ should be granted. Trustee
2 contends that there are no triable issues of fact as to whether
3 under Section 544(a)(3) she can use her status as a BFP to defeat
4 the effect of the unrecorded TIC Agreement. Trustee seeks to
5 defeat the effect of the TIC Agreement in order to sell the
6 Property under Section 363(h).⁴

7 Section 363(h) applies to property held as tenants in common.
8 11 U.S.C. § 363(h). A trustee can sell the entire property
9 despite the co-tenancy as long as the additional requirements of
10 subsections one through four are met. If Trustee's MSJ is granted
11 pursuant to under Section 544(a)(3) she can defeat the effect of
12 the TIC Agreement, and therefore avoid liability for two-thirds of
13 the loan obligation. If the TIC Agreement is defeated then the
14 net proceeds from the sale of the Property (after payment of costs
15 of sale and the loan on the Property) would be distributed with
16 the de Leons receiving two-thirds, and Debtor receiving the

17

18 ⁴Section 363(h) states:

19 (h) Notwithstanding subsection (f) of this section, [not
20 relevant here] the trustee may sell both the estate's interest,
21 under subsection (b) or (c) of this section, and the interest of
22 any co-owner in property in which debtor had, at the time of the
23 commencement of the case, an undivided interest as a tenant in
24 common, joint tenant, or tenant in entirety, only if-

25 (1) partition in kind of such property among the estate
26 and such owners is impracticable;

27 (2) sale of the estate's undivided interest in such
28 property would realize significantly less for the estate than
29 sale of such property free of the interest of such co-owners;

30 (3) the benefit to the estate of a sale of such property
31 free of the interests of co-owners outweighs the detriment,
32 if any, to such co-owners, and

33 (4) such property is not used in the production,
34 transmission, or distribution, for sale, of electric energy
35 or of natural or synthetic gas for heat, light, or power.

36 11 U.S.C. § 363(h).

1 remaining one-third. As set forth in paragraph 4.2 of the TIC
2 Agreement, Debtor is responsible for two-thirds of the loan
3 obligation. Therefore, if the TIC Agreement is given effect,
4 Trustee would not be entitled to one-third of the net sale
5 proceeds, but instead would be liable to the de Leons for two-
6 thirds of the loan obligation. As indicated at oral argument on
7 the MSJ, Trustee would not likely seek to sell the Debtor's
8 interest in the Property under Section 363(h) since the bankruptcy
9 estate would not realize any net proceeds from such a sale.

10 After careful consideration of the papers submitted and oral
11 arguments, the court agrees with the de Leons that triable issues
12 of fact remain as to whether Trustee can use Section 544(a)(3) to
13 defeat the effect of the TIC Agreement.

14 B. Summary of Law

15 1. 11 U.S.C. § 544

16 Section 544(a)(3)⁵ confers upon a trustee the status of a BFP
17 of real property. The court looks to applicable state law to
18 determine whether the trustee's BFP status can defeat the rights
19

20 ⁵Section 544(a)(3) states:

21 (a) The trustee shall have, as of the commencement of
22 the case, and without regard to any knowledge of the trustee
23 or of any creditor, the rights of and powers of, or may
24 avoid any transfer in property of the debtor or any
25 obligation incurred by the debtor that is voidable by-

26 (3) a bona fide purchaser of real property, other
27 than fixtures, from the debtor, against whom applicable
28 law permits such transfer to be perfected, that obtains
the status of a bona fide purchaser and has perfected
such transfer at the time of the commencement of the
case, whether or not such a purchaser exists.

11 U.S.C. § 544(a)(3).

1 of another party who claims an interest in the same property.
2 Marc Weisman v. Peters (In re Weisman), 5 F.3d 417, 420 (9th Cir.
3 1993); 5 Collier on Bankruptcy ¶ 544.08, at 544-15 (15th ed. Rev.
4 2003) ("State law governs who may be a bona fide purchaser and the
5 rights if such a purchaser for purposes of section 544(a)(3)").
6 In other words, for Trustee to achieve the status of a BFP here,
7 Trustee must meet the requirements as set forth in applicable
8 California state law.

9 2. Applicable California Law

10 California has established rules governing priority among
11 parties who claim an interest in the same property. 5 Miller and
12 Starr, California Real Estate § 11:1, at 7 (3rd ed. 2000) ("Laws
13 and rules establishing priorities were created to settle disputes
14 between various interests in real property by granting preference
15 to one interest or class of interests over another."). Therefore,
16 "a person who qualifies as a bona fide purchaser receives his or
17 her interest free and clear of prior unknown interests." Id.
18 §11.3 at 15. A person qualifies as a BFP who acted in good faith,
19 paid valuable consideration, was without notice of the other
20 party's interest in the property, and duly recorded that person's
21 interest. Gates Rubber Company v. Harry Ulman, 214 Cal.App 3d
22 356, 364 (Cal. Dist. Ct. App. 1989) (citations omitted); See also 4
23 Witkin, Summary of California Law, Real Property, § 206, at 411
24 (9th ed. 1998). "The status of a BFP is defeated if the
25 prospective purchaser has actual or constructive notice of the
26 other party's interest in the property. Id.; see also 5 Miller &
27 Starr, § 11.3, at 15. "The absence of notice is an essential
28 requirement in order that one may be regarded as a bona fide

1 purchaser. Carlo Basch v. Tidewater Associated Oil Company, 49
2 Cal.App.2d Supp. 743, 746 (Cal. App. Dep't Super. Ct. 1942).

3 IV. Application of Law to the Facts Presented

4 1. Standard for Summary Judgment.

5 Federal Rule of Civil Procedure 56(c) (incorporated by Rule
6 7056), provides that the "judgment sought shall be rendered
7 forthwith if the pleadings, depositions, answers to
8 interrogatories, and admissions on file, together with the
9 affidavits, of any, show that there is no genuine issue as to any
10 material fact and that party is entitled to judgment as a matter
11 of law."

12 "The proponent of a summary judgment motion bears a heavy
13 burden to show that there are no disputed facts warranting
14 disposition of the lawsuit without a trial." Younie v. Gonva (In
15 re Younie), 211 B.R. 367, 373 (9th Cir. BAP 1997), aff'd, 163 F.3d
16 (9th Cir.), (quoting Grazybowski v. Aquaslide 'N' Dive Corp. (In
17 re Aquaslide 'N' Dive Corp.), 85 B.R. 545 (9th Cir. BAP 1987)).
18 If the moving party adequately carries its burden, the party
19 opposing summary judgement must then "set forth specific facts
20 showing that there is a genuine issue for trial." Anderson v.
21 Liberty Lobby, Inc., 477 U.S. 242, 248 (1986).

22 All reasonable doubt as to the existence of genuine issue of
23 material fact must be resolved against the moving party. Liberty
24 Lobby, 477 U.S. at 248. "A 'material' fact is one that is
25 relevant to an element of a claim or defense or whose existence
26 might affect the outcome of the suit. The materiality of a fact
27 is thus determined by the substantive law governing the claim or
28 defense." T.W. Elec. Service v. Pacific Elec. Contractors Ass'n,

1 809 F.2d 626, 630 (9th Cir. 1986).

2 2. BFP.

3 In William R. Probasco v. Bill J. Eads (In re Probasco),
4 839 F.2d 1352, 1356 (9th Cir. 1988), the Ninth Circuit determined
5 that under California Civil Code section 19 constructive notice
6 can deny a trustee the status of a hypothetical BFP under Section
7 544(a)(3). California Civil Code section 19 provides:

8 Every person who has actual notice of circumstances
9 sufficient to put a prudent man upon inquiry as to
10 a particular fact, has constructive notice of the
fact itself in all cases in which, by prosecuting
such inquiry, he might have learned such fact.

11 California Civil Code § 19 (emphasis added). Stated differently,
12 a person is deemed to know facts that he or she could have
13 inquired about. Id. "[The] question is whether a prudent
14 purchaser, in light of the information reasonably available to him
15 . . . would have made [an] inquiry." Weisman, 5 F.3d at 420. If
16 a hypothetical buyer here had a duty to inquire about additional
17 facts, then Trustee is charged with constructive notice and fails
18 as a BFP.

19 3. Equal Rights of Possession and Tenants in Common.

20 It is well established that tenants in common are entitled to
21 use and possess the entire property. 5 Miller & Starr, § 12:2
22 (citations omitted). "Each cotenant is equally entitled to share
23 in the possession of the entire property and neither can exclude
24 the other from any part of it." 4 Witkin, § 264, at 465-466
25 (emphasis added). The de Leons' and Debtor's exclusive occupancy
26 of sections of the Property is inconsistent with property held as
27 tenants in common because "each tenant owns an equal interest in
28 all of the fee, and each has an equal right to possession of the

1 whole [property]." Swartzbaugh v. Sampson, 11 Cal. App. 2d 451,
2 454 (Cal. Dist. Ct. App. 1936).

3 There is nothing in any of the documents presented to this
4 Court to indicate that Debtor or the de Leons are able to occupy
5 the entire Property, i.e. both homes. The facts indicate
6 otherwise, namely that Debtor is only entitled to occupy his home,
7 and the de Leons theirs.⁶ For example, both residences have
8 separate entrances: access to the front dwelling is directly up a
9 set of stairs from the sidewalk and access to rear dwelling is by
10 a separate stairway and walkway along the front of the cottage.
11 Even when seeking ingress and egress to and from their respective
12 dwellings, Debtor and the de Leons do not occupy the same space.

13 4. Exclusive Occupancy is Inconsistent with Title

14 Debtor's and the de Leons' exclusive occupancy of sections of
15 the Property is inconsistent with property held as tenants in
16 common and would require a hypothetical buyer to inquire as to
17 whether there was an agreement and if so what were its terms.
18 This duty of inquiry would result in constructive notice and
19 defeat Trustee's status as a BFP.

20 Both the Ninth Circuit and the California Supreme Court have
21 recognized that "[t]here is no duty to inquire . . . regarding any
22 unknown claims or interests by a person in possession of real

23
24 ⁶The TIC Agreement allowed exclusive possession of parts of
25 the Property. Paragraph 3.2 "Assignments of Units and Exclusive
26 Use of Common Areas". The TIC Agreement expressly provides that
27 Debtor has "exclusive use" of "Unit 320" (his home) and the de
28 Leons will have "exclusive use" of "Units 322" (their home). Id.
The TIC Agreement further provides that Debtor has the exclusive
use of the adjacent deck common area and the de Leons have
exclusive use of the area below the rear exit stair and the entire
driveway. Id. This further supports that Debtor and the de Leons
did not intend for shared occupancy and use of the Property.

1 property where the occupant's possession is consistent with record
2 title." Weisman, 5 F.3d at 420; Philip Caito v. United California
3 Bank, 20 Cal. 3d 694, 702 (1978). For example, where a tenant's
4 possession is consistent with the terms of a recorded lease then
5 there is no duty on the part of the purchaser to inquire as
6 whether the tenant possesses other or additional rights. Gates
7 Rubber Company, 214 Cal.App 3d at 365.

8 A prudent purchaser is required to make an inquiry as to
9 another's interest in property only when the possession of the
10 property is inconsistent with the record title. Weisman, 5 F.3d
11 at 421 (emphasis added).

12 Where possession is inconsistent with the record title
13 and thereby creates a duty to inquire, a prospective
14 purchaser is charged with constructive notice of all
15 facts that would be revealed by a reasonably diligent
16 inquiry, regardless of whether the purchaser has ever
17 seen the property.

18 Weisman, 5 F.3d at 421. The de Leons argue that the exclusive
19 possession of the two dwellings on the Property was inconsistent
20 with property held as tenants in common.

21 As a hypothetical buyer, Trustee would have a duty to
22 inquire as to the nature of the agreement between the de Leons and
23 Debtor, because the occupancy was inconsistent with property held
24 as tenants in common. In Probasco, 839 F.2d at 1352, the Ninth
25 Circuit determined that the possession of a parcel property was
26 inconsistent with the record title and therefore the debtor-in-
27 possession ("DIP") had constructive notice of the non-debtor
28 party's interest in the land. Id. The DIP wanted to use Section
544(a)(3) to defeat Probasco's interest in a parcel of land. Id.
at 1354. The land in dispute consisted of three parcels of land

1 that appeared to be a single piece of property. Id. The entire
2 property was enclosed by a fence, staked and had roads running the
3 entire property, not each individual parcel of land. Id.

4 Probasco argued that the appearance of the property was such
5 that the entire property looked like a single parcel of land, and
6 therefore his interest in the property was apparent based on the
7 occupancy. The Ninth Circuit agreed with Probasco and stated:
8 "Such an interest in Parcel 1 was inconsistent with the record
9 title indicating that the Eads [DIP] were its sole owners." Id.
10 at 1356. The Ninth Circuit's analysis in Probasco, 839 F.2d at
11 1352, is applicable here. The de Leons' and Debtor's exclusive
12 occupancy of each of their respective homes is inconsistent with
13 property held as tenants in common because tenants in common have
14 a right to possess the entire property, not just sections of the
15 property. Swartzbaugh, 11 Cal. App. 2d at 454. As a result of
16 this inconsistency a hypothetical buyer would have a duty to
17 inquire as to the nature of the agreement between Debtor and the
18 de Leons.

19 In Gates Rubber, 214 Cal.App. 3d at 356, the Court of Appeal
20 affirmed the trial court's refusal to allow the plaintiff, Gates
21 Rubber Co., to purchase land based on an unrecorded option
22 purchase agreement contained in a recorded lease. Crucial to the
23 court's analysis was the fact that the plaintiff's continuous
24 operation of a factory on the premises was consistent with the
25 recorded short-form lease. Id. Here, unlike in Gates Rubber,
26 214 Cal.App. 3d at 356, the de Leons' and Debtor's exclusive
27 occupancy of separate dwellings was inconsistent with property
28 held as tenants in common.

1 A hypothetical purchaser would have a duty to inquire as to
2 the nature of the agreement between Debtor and the de Leons based
3 on their exclusive occupancy of sections of the Property. In
4 Basch, 49 Cal.App. 2d Supp. at 743, unbeknownst to the purchaser
5 of a gas station, an agreement existed to reduce the amount of
6 rent in the event traffic was diverted past the property. Id.
7 Prior to the purchase, the purchaser was shown by seller a copy of
8 an unrecorded lease agreement for the current gas station lessee.
9 Id. at 748. The purchaser did not inquire of the lessor as to
10 whether there were any other agreements with the property lessee.
11 Id. The court held that because the purchaser had a duty to
12 further inquire, the purchaser/new lessor was bound by the
13 reduction in rent.

14 [T]he tenant's possession is notice not only of his
15 rights under the lease, but also of any rights which
16 he may have under a subsequent agreement not incorporated
in the instrument of the lease, such as a contract for
the purchase of land.

17 Tidewater, 49 Cal.App. 2d Supp. at 750.

18 Similar to the unrecorded side agreement regarding the rental
19 price, a hypothetical purchaser would have a duty to inquire as to
20 the nature of the agreement between Debtor and the de Leons based
21 on their exclusive occupancy of sections of the Property. Id.
22 Tenants in common have a right to use and possess the entire
23 property. Swartzbaugh, 11 Cal. App. 2d at 454. Here, despite the
24 tenancy in common, there was no right to occupancy of the entire
25 Property which would have required a BFP to inquire as to the
26 nature of the agreement between Debtor and the de Leons. As a
27 result, Trustee is deemed to have constructive notice and cannot
28 defeat the effect of the TIC Agreement and achieve the status of a

1 BFP.

2 IV. Disposition

3 Based on Debtor's and the de Leons' exclusive occupancy of
4 their respective homes there remains a triable issue of fact as to
5 whether Trustee can use Section 544(a)(3) to defeat the effect of
6 the TIC Agreement. The court DENIES Trustee's MSJ.

7 Counsel for the de Leons should submit an order denying the
8 MSJ consistent with this memorandum decision. In doing so,
9 counsel should comply with B.L.R. 9021-1 and B.L.R. 9022-1.

10 Since the court cannot determine whether Trustee intends to
11 dismiss this adversary proceeding in light of the court's decision
12 and the apparent lack of any benefit to the estate in a sale under
13 Section 363(h), it will hold a status conference on May 28, 2004,
14 at 1:30 P.M.

15 Dated: April 28, 2004



16 _____
17 Dennis Montali
18 United States Bankruptcy Judge
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