

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF OHIO

IN RE: \*  
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VEND INVESTMENT, INC., \*  
\* CASE NUMBER 02-41565  
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Debtor. \*  
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VEND INVESTMENT, INC., \*  
\* ADVERSARY NUMBER 04-4062  
\*  
Plaintiff, \*  
\*  
vs. \*  
\*  
MAHONING COUNTY TREASURER, \*  
et al., \*  
\* HONORABLE KAY WOODS  
Defendants. \*  
\*

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M E M O R A N D U M O P I N I O N  
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Vend Investment, Inc. ("Debtor") filed a voluntary petition pursuant to Chapter 11 of the Bankruptcy Code on April 15, 2002. This case was converted to a case under Chapter 7 of the Bankruptcy Code on August 24, 2004. Michael D. Buzulencia is the duly appointed Chapter 7 Trustee ("Trustee") for the case.

Prior to conversion of the case, Debtor initiated this adversary proceeding seeking a determination of the validity, extent and priority of liens, encumbrances and interests in certain real property known for street numbering purposes as 267 W. Main Street, Canfield, Ohio 44406 ("267 W. Main"). Pursuant to Order of this Court dated October 29, 2003, Debtor sold 267 W. Main to Shani M. Murphy for the sum of One Hundred Ten Thousand Dollars (\$110,000.00), with all liens, encumbrances and other interests

transferring to the proceeds of sale. The adversary proceeding required that each of the named defendants, *i.e.*, Mahoning County Treasurer, Dean W. Fried ("Fried"), Farmers National Bank of Canfield ("Farmers"), and American Mortgage Solutions, Inc. ("AMS") set forth its interest in 267 W. Main. On June 1, 2004, Chase Manhattan Bank, as Indenture Trustee for the IMC Home Equity Loan Asset Backed Notes, Series 1998-7A and Series 1998-7B ("Chase") moved to intervene in the adversary proceeding.<sup>1</sup> Chase argued that it was a party in interest and that Chase, not AMS, was the holder of the mortgage on 267 W. Main. On October 21, 2004, this Court granted the motion to intervene.

AMS filed American Mortgage Solutions, Inc's Answer and Cross Claim to Plaintiff's Complaint on June 4, 2004. On June 23, 2004, this Court (Judge William A. Clark, presiding) entered an Order (the "June 23, 2004 Order") that the two following issues would be tried to the Court before all other issues, which other issues were stayed until that time:

1. Who is the legal owner of the AMS mortgage filed for record on April 27, 1998?
2. Who is the legal owner of the AMS judgment lien filed for record on November 8, 2000?

This Order also set a discovery cutoff of October 14, 2004. Fried filed an answer to the AMS cross claim on July 3, 2004. Chase filed

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<sup>1</sup>In subsequent pleadings, Chase is identified as JP Morgan Chase, but the Court will use the designation of Chase to refer to this entity both before and after the name change.

its Answer of Chase Manhattan Bank, as Trustee, to Cross-Claim of American Mortgage Solutions, Inc. on July 9, 2004. On September 20, 2004, the Trustee was substituted as the real party in interest for the Debtor as plaintiff. The Trustee continues to hold the proceeds of the sale of 267 W. Main, pending an order of this Court.

After several extensions of the discovery period (through September 15, 2005), a final pretrial was held in this case on November 21, 2005. The Court issued a Trial Order on November 22, 2005, which set a trial date of February 13, 2006. The parties submitted pretrial briefs and filed motions in limine, which motions the Court ruled on prior to the beginning of trial.

At the beginning of trial, counsel for AMS represented that AMS and Fried had settled their disputes regarding ownership of the AMS judgment lien, thus resolving Issue No. 2 in the June 23, 2004 Order. As a consequence, the trial was, in essence, a two-party dispute between AMS and Chase on the cross claim asserted by AMS to resolve Issue No. 1 in the June 23, 2004 Order.<sup>2</sup> Trial lasted two days, with each side presenting witnesses and exhibits.

This Court has jurisdiction of this case pursuant to 28 U.S.C. § 1334 and 28 U.S.C. § 157. This is a core proceeding

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<sup>2</sup>The judgment lien of Farmers was filed later and comes behind both the mortgage and the AMS judgment lien in priority. Since the Trustee is not holding sufficient funds from the sale of 267 W. Main to satisfy all of the liens, Farmers will not receive anything in payment of its lien. Farmers did not participate in the trial. The Mahoning County Treasurer also did not participate at trial. It is not clear whether the tax liens have already been paid from the proceeds of sale, but, since the tax liens have a statutory priority pursuant to 11 U.S.C. § 507(A)(8), there is no question that the Mahoning County Treasurer is to be paid before payment is made on the mortgage.

pursuant to 28 U.S.C. § 157(b)(2)(N). The following constitute this Court's findings of fact and conclusions of law as required by FED. R. Civ. P. 52, as incorporated by FED. R. BANKR. P. 7052.

For the reasons set forth below, this Court finds that Chase is the legal owner of the AMS mortgage.

### **FACTS**

The facts are generally not in dispute. AMS originated some loans and acted as a mortgage broker for other loans. In or about late 1997, AMS entered into the first of several notes and mortgages with Raymond L. Lonsway ("Lonsway"). Stephen Lambert, sole shareholder and CEO of AMS, testified that he believed that AMS had fewer than ten (10) loans with Lonsway. Lambert testified that AMS directly loaned money to Lonsway and also brokered some of the loans.<sup>3</sup> Lonsway executed a Balloon Note dated April 24, 1998 in the amount of Sixty-Two Thousand Two Hundred Fifty Dollars (\$62,250.00) in favor of AMS (the "Note"). (Chase Ex. 1.) On that same date, Lonsway executed an Open-End Mortgage for 267 W. Main in favor of AMS (the "Mortgage"). (Chase Ex. 3.)

It is customary in the real estate mortgage industry to buy and sell notes and mortgages. Entities, such as AMS, sell to other mortgage brokers at a premium over the face value of the note. Lambert testified that some notes/mortgages are sold as

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<sup>3</sup>Heather Urban, a former AMS employee responsible for all of the "backroom operations," including sending files to purchasers such as IMC Mortgage Company, testified that she believed there were six transactions involving AMS and Lonsway and at least one of those was for commercial, rather than residential, property.

single files,<sup>4</sup> but most are sold as bulk transfers. When a file is sold (either singly or in bulk), it contains the original note, original mortgage and an allonge evidencing transfer of such documents. According to Karen Kettle, Manager of Contract Compliance with Ocwen Federal Bank, collateral files do not contain wire transfer or other payment documentation.

Starting in the fall of 1997, AMS began to transact with IMC Mortgage Company ("IMC"). Lambert testified that the value of the bulk sales by AMS to IMC ranged from \$1.5 Million to \$3 Million. In total, AMS sold approximately ten (10) bulk transactions to IMC. Lambert testified that AMS tried to sell a loan as close to its execution date as possible so that it was "fresh" and so that the purchaser would not think that it had been rejected by some other purchaser as an undesirable loan. Pursuant to a transaction sometime in April, May or June 1998,<sup>5</sup> AMS transferred a bulk of files containing original notes, mortgages, allonges and other relevant documents to IMC. The bulk in question contained the Note, Mortgage and allonge (collectively the "Documents") all relating to 267 W. Main. (Chase Ex. 2.) Lambert acknowledged that all of the Documents relating to 267 W. Main were signed by himself

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<sup>4</sup>These are called collateral files.

<sup>5</sup>AMS elicited testimony from its own witnesses regarding various dates for the bulk transaction that included 267 W. Main. AMS cannot pinpoint when the Documents relating to 267 W. Main were transferred to IMC, but because the original Note, Mortgage and allonge relating to 267 W. Main were all transferred by IMC to Chase as part of a securitization in December 1998, the evidence is only unclear about when the transaction occurred, not whether it occurred.

or an authorized signor for AMS. Lambert also acknowledged that such Documents were negotiable.

AMS asserts that although the properly signed and negotiable Documents relating to 267 W. Main were sent to IMC, such was done only as a bailment. Despite the contention of AMS that the transfer was done as a bailment and that the bailee letter was a critical part of such transaction, AMS did not - and stated that it could not - produce the bailee letter covering the bulk transfer that included 267 W. Main. Lambert and Urban each testified that AMS had a three year retention policy for documents, but that AMS no longer had the bailee letter covering the transfer of Documents for 267 W. Main to IMC. Lambert further testified that the bailee letter was just as important to the transfer as the Note and the Mortgage, yet - inexplicably - AMS could not produce the bailee letter.<sup>6</sup> AMS contends that unless and until IMC paid AMS for the Documents relating to 267 W. Main, AMS retained sole ownership of the Note and Mortgage. AMS insists that the transfer of Documents relating to 267 W. Main was a "failed bailment" because IMC never paid AMS for the Note and Mortgage.<sup>7</sup> AMS asserts that it was paid

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<sup>6</sup>Lambert testified that if he had known there would be litigation over this issue, he would have retained the bailee letter. The unusual circumstances of this bulk transfer should have alerted AMS to potential litigation.

<sup>7</sup>AMS makes this same argument regarding two other notes and mortgages signed by Lonsway, which relate to: 8981 Mahoning Avenue, Youngstown, Ohio and 3160 Meridian Road, Youngstown, Ohio. There is no dispute that Chase also has the original notes, mortgages, allonges and collateral files relating to these other two properties. These two properties are not before the Court since the dispute at issue is the validity, priority and extent of liens relating only to 267 W. Main. The parties agree, however, that the other two Lonsway loans were part of the same bulk transfer as 267 W. Main. AMS contends that, like 267 W. Main, it was not paid for these other two collateral files; Chase maintains that it acquired those files through the December 1998

for the other files in the bulk transfer that included the Documents for 267 W. Main, but that IMC did not pay for the Lonsway loans.<sup>8</sup> Lambert testified that IMC "kicked out" the Lonsway loans from the bulk and paid for the remainder of the loans in the bulk at that time. Lambert conceded that there is no documentation to indicate that IMC "kicked out" the Lonsway loans. The customary practice is for a purchaser to return a collateral file if it is not going to be purchased. Lambert said that he thought IMC would continue to evaluate the Lonsway loans and perhaps purchase them at a later time. Despite the allegation that AMS was not paid for the Lonsway loans, AMS continued to deal with IMC. Lambert testified that, of AMS's ten (10) transactions with IMC, three (3) or four (4) of them occurred subsequent to the bulk transfer that included 267 W. Main.

Lambert stated that he was not concerned about IMC's failure to pay for the Lonsway loans because AMS still owned the loans. He said that this continued ownership was the reason AMS did not file suit against IMC for either return of the files or payment. Lambert testified that he never transferred a file without AMS either (i) being paid for the file or (ii) receiving the file back from the purchaser.<sup>9</sup> AMS contends that, because it never received payment for the Lonsway loans, including the Documents relating to

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securitization, along with Documents relating to 267 W. Main. There is no bailee letter for 267 W. Main or the other two properties.

<sup>8</sup>AMS did not provide any evidence of payment for the rest of the notes and mortgages in the bulk transfer that included 267 W. Main.

<sup>9</sup>Although this was Lambert's testimony, the Court believes he meant this was true for all cases except the Lonsway loans in question.

267 W. Main, AMS kept such loans as assets on its books. AMS further contends that it continued to be in contact with Joan Lonsway (mother of Raymond Lonsway) in an effort to collect on the Lonsway loans.<sup>10</sup> Lambert testified that he made efforts to get IMC to return the Lonsway files or pay for them until IMC "shut its doors" some time in the fall of 1998. Lambert admits that AMS did not initiate a lawsuit or take any other legal action against IMC.

Chase has the original Documents relating to 267 W. Main and the other Lonsway loans in its possession. Chase claims that it acquired such Documents through a securitization transaction in December 1998 (the "Securitization") that involved IMC as the Seller, IMC Securities, Inc. as the Depositor, IMC Home Equity Loan Owner Trust 1998-7 as the Issuer, Ocwen Federal Bank as the Servicer and Chase as the Indenture Trustee. (Chase Exs. 17, 18, 20 and 22.) The Securitization was registered with the Securities Exchange Commission ("SEC"). The ultimate result of this transaction was a transfer of certain collateral files containing negotiable instruments to Chase, with Chase acquiring the interest in such collateral files as Trustee for certain noteholders. Chase contends that the representations and warranties in the Securitization documents provide the basis for Chase to be a holder, as defined in Article 3 and Article 9 of the Uniform Commercial Code

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<sup>10</sup>Although Lambert testified that Joan Lonsway was the person at Vend Investment, Inc. that collected rent and generally ran operations, Joan Lonsway is not mentioned in Debtor's petition. Debtor's petition was signed by Raymond Lonsway as President. Counsel for AMS stated that Joan Lonsway was in attendance at the first morning of trial, but it is not clear what relationship, if any, exists between Joan Lonsway and AMS or what relationship, if any, Joan Lonsway has or had with Debtor.

("UCC") and, as a consequence, it has good title in and to the Note and the Mortgage and AMS has no rights or interests therein.

#### **APPLICABLE LAW**

As the parties acknowledged at the end of the trial, they essentially argued two separate cases. The parties do not agree on the law that governs the dispute and each of the parties insists that its view is controlling. AMS postulates that the common law of bailment governs a transfer of notes, mortgages and allonges in bulk from one mortgage broker to another. AMS states that when it transferred the Documents to IMC, it did so through a bailment, as was usual and customary in the industry. Chase, on the other hand, asserts that the UCC governs the transaction because Chase acquired the Note and Mortgage for 267 W. Main in a securitization and that it is either an innocent *bona fide* purchaser for value or a holder in due course.

#### **DISCUSSION OF AMS'S ARGUMENT**

Although AMS characterized the transaction as a "failed bailment," the Court believes that AMS's use of this term includes both a breach of contract for bailment and a breach of contract for sale. The Court will first focus on whether the transaction constitutes a bailment.

Black's Law Dictionary defines bailment as: "A delivery of personal property by one person (the *bailor*) to another (the *bailee*) who holds the property for a certain purpose under an express or implied-in-fact contract. Unlike a sale or gift of personal property, a bailment involves a change in possession

but not in title." BLACK'S LAW DICTIONARY 151-52 (8th ed. 2004). In order to prove a *prima facie* case against a bailee in an action for breach of bailment contract, a bailor must prove: (1) the contract for bailment; (2) delivery of the bailed property to bailee and (3) failure of the bailee to redeliver the undamaged bailed property at the end of the bailment. *Morgenstern v. Eastman Kodak Company*, 569 F. Supp. 474, 476 (N.D. Ohio 1983) (citing *David v. Lose*, 7 Ohio St. 2d 97; 218 N.E. 2d 442 (1966)).

The only evidence AMS offered regarding transfer of the Documents as a bailment was testimony referencing a bailee letter. Lambert and Urban testified that AMS had a three year retention period for documents, but that AMS no longer had the bailee letter and therefore could not produce the letter. The absence of the bailee letter is problematic because there is no other evidence that the transaction was a bailment. Furthermore, even assuming, *arguendo*, that the bailee letter once existed, the Court has no way of knowing the terms of the alleged bailment. AMS failed to provide the bailee letter for 267 W. Main or a generic bailee letter. Without proof of a contract for bailment, AMS fails to meet its burden.

Furthermore, a bailment requires the bailed property to be redelivered to the bailor at a later date. As evidenced by Lambert's testimony, the bulk transfer in question involved a sale to IMC rather than a transaction that required IMC to redeliver the original collateral files to AMS at a later date. Lambert testified that bulk sales by AMS to IMC ranged from \$1.5 Million to

\$3 Million. Lambert further testified that AMS sold approximately ten (10) bulk transfers to IMC. AMS elicited testimony from its own witnesses who admitted that AMS sold the Documents for 267 W. Main to IMC in a bulk transaction sometime in April, May or June of 1998. Finally, the Corporation Assignment of Real Estate Mortgage/Deed of Trust document (the "Corporation Assignment Document") states that the loan for 267 W. Main was sold to IMC. (Chase Ex. 4.) Since a sale does not require the purchaser to redeliver the purchased item, a sale cannot be classified as a bailment. See BLACK'S LAW DICTIONARY 151-52. As a result, and despite the contention of AMS that the Documents were delivered based on a bailment, this Court finds that AMS delivered the negotiable Documents to IMC based on a contract for sale.<sup>11</sup>

Consequently, the Court will address whether AMS met its burden to prove breach of contract. "A contract is a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty." RESTATEMENT (SECOND) OF CONTRACTS § 1 (1981). A breach of contract occurs when a party fails to perform according to the agreement. The party asserting the breach of contract bears the burden of proving the breach and damages relating thereto. See *Kissinger v. Singh*, 304 F. Supp. 2d 944, 951 (6th Cir. 2003).

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<sup>11</sup>Lambert testified that this type of transaction was a bailment based on industry practice, but AMS failed to provide adequate testimony on industry practices to prove this allegation. The fact that AMS expected IMC to return any files for which IMC did not pay is consistent with a contract of sale.

In the instant case, the transaction required (i) AMS to deliver the Documents to IMC, and (ii) IMC to pay AMS the agreed upon price. There is no question that AMS delivered the Documents.<sup>12</sup> Therefore, AMS performed its legal duty under the contract. Here, however, in order to resolve this case in favor of AMS under its theory of the case, AMS must prove that IMC failed to perform its legal duty under the contract by failing to pay for the Lonsway loans, in particular the Documents relating to 267 W. Main. AMS has the burden of proving IMC did not perform its duty. AMS has failed to meet its burden.

The Corporation Assignment Document states:

**FOR VALUE RECEIVED**, the undersigned hereby grants, assigns and transfers to IMC MORTGAGE COMPANY . . . all the rights, title and interest of undersigned in and to that certain REAL ESTATE MORTGAGE/DEED of TRUST dated April 24, 1998, executed by Raymond L. Lonsway . . . to American Mortgage Solutions, Inc.

(Chase Ex. 4 (emphasis added).) The Corporation Assignment Document describes the transferred property as 267 W. Main. The Corporation Assignment Document was notarized on April 24, 1998 and was signed by AMS's Closing Department Manager, Teri Westerviller.<sup>13</sup> (*Id.*) This document, which was executed by AMS, expressly states that AMS received "value" for the 267 W. Main Mortgage. Although the "value" is not described or specified, the Corporation Assignment Document

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<sup>12</sup>See *supra* at n.5.

<sup>13</sup>Lambert's testimony states that all of the documents in question were signed by himself or someone who was authorized by AMS to sign such documents. Urban testified that Westerviller had the authority to sign the Corporation Assignment Document.

provides that the value received was sufficient to cause AMS to transfer all of its rights, title and interest in and to the Mortgage relating to 267 W. Main. As a result, AMS has a heavy burden to refute its own express acknowledgment of receipt of value in the Corporation Assignment Document.

AMS attempted to contradict the Corporation Assignment Document and establish that IMC did not pay for the Lonsway loans through testimony that AMS continued to carry the Lonsway loans on its books as an asset. AMS's auditor, Kyan Kraus, CPA, testified that AMS continues to carry the Lonsway loans on its books, but he also said that he could not match payments with any particular loan. Lambert testified that there were loans to Lonsway in addition to the three in question<sup>14</sup> and that the commercial loans were not and could not be transferred in a bulk. AMS has only the testimony of Lambert and Kraus that the loan for 267 W. Main is still carried on the AMS books.

The fact that AMS kept the Lonsway loans on its books as assets is some indication of non-payment, but that fact, alone, does not establish that IMC did not pay for the Note and Mortgage for 267 W. Main. Specifically, that fact, alone, is insufficient to contradict the express acknowledgment of AMS that it received value for the Mortgage, as set forth in the Corporation Assignment Document. Rand Smith, counsel for AMS, in questioning Karen Kettle, insisted that there were only two outcomes in a bailment - either the bailee paid the bailor for the goods that were bailed or the

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<sup>14</sup>See *supra* at n.7.

bailee returned the goods.<sup>15</sup> Despite that unequivocal statement, AMS argues here that there is a possible third outcome - a "failed bailment" - even though Lambert testified that he had never before seen a failed bailment.<sup>16</sup> AMS has the burden of proof that the transaction was, indeed, a "failed bailment." Karen Kettle testified that possession of original negotiable documents does not establish ownership, but a bulk transfer required a purchaser to either pay for the notes or return the notes. Consequently, if a purchaser has possession of the notes it is *prima facie* proof it has ownership thereof. IMC had possession of the collateral file containing the Documents relating to 267 W. Main and did not return it; hence, IMC's possession of those Documents is *prima facie* evidence that it paid for the collateral file for 267 W. Main and, accordingly, owned the Documents.

In addition, AMS continued to send bulk transfers to IMC after the alleged failed bailment. AMS alleges that it did not initiate any legal action against IMC on the theory that AMS still owned the Note and Mortgage. AMS acknowledges that a failed

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<sup>15</sup>Since the Court determines that the transaction did not constitute a bailment, the Court interprets AMS's use of the "bailment" to mean contract, the use of the "bailee" or "bailor" to mean party and the phrase "failed bailment" to mean breach of contract. Smith's argument is consistent with Lambert's testimony regarding the experience of AMS with "bailments" (see p. 7 and n.9, *supra*); however, insistence that there are only these two outcomes is contrary to AMS's version of the facts in the instant case. The Court believes that AMS intended to argue, instead, that there were only two legal obligations under this type of contract, *i.e.*, the recipient of a file had to pay for the file or return the file. Failure to perform either action constitutes a breach of contract.

<sup>16</sup>Lambert testified that he had never seen a failed bailment. See *supra* p. 7. Property is either bailed or not bailed. Therefore, a failed bailment must mean a breach of a bailment contract. IMC was, therefore, required to either pay for the Note and Mortgage or return the Note and Mortgage to AMS; failure to perform either action is a breach of contract. See *supra* at n.15.

bailment is extremely unusual, yet AMS failed to keep a copy of the bailee letter despite Lambert's testimony that he would have kept the letter if he had anticipated litigation.<sup>17</sup>

In order to overcome the presumption in the Corporation Assignment Document that AMS received value from IMC, AMS needed to show more than the fact that AMS - a privately held company - continued to carry the loan for 267 W. Main on its books. This is especially true here because the outside accountant for AMS could not match payment to any particular loan. Thus, there is no evidence that the existence of the loan as an asset on the books of AMS demonstrates that IMC failed to pay for the Note and Mortgage. As a result, AMS failed to prove that IMC did not pay for the collateral file relating to 267 W. Main.

AMS failed to meet its burden to establish that (i) the transaction was a bailment, and (ii) IMC breached the contract for sale.

#### **DISCUSSION OF CHASE'S ARGUMENT**

*Arguendo*, even if AMS met its burden in proving a breach of contract, Chase would still prevail on its argument that the UCC applies and that Chase is a holder in due course.<sup>18</sup>

Chase contends that the UCC governs this dispute. The Court agrees with Chase. See *supra* pp. 9-11 (The Court's ruling

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<sup>17</sup>See *supra* at n.6.

<sup>18</sup>Since AMS did not meet its burden in proving a breach of contract, AMS cannot collect on the Note and Mortgage for 267 W. Main from any other entity. To permit such recovery would permit AMS to receive double compensation for the sale of the loan for 267 W. Main - once from IMC and again from the Trustee.

that the dispute is not governed by bailment law.). Chase relies on UCC Article 3 (negotiable instruments) and Article 9 (secured transactions), but Article 3 is the governing body of law.<sup>19</sup>

There is no question that the Note for 267 W. Main is a negotiable instrument as defined in O.R.C. § 1303.03 (UCC 3-104). In fact, Lambert testified that the Note is a negotiable instrument.

Section 3-104 of the UCC states, in pertinent part:

(A) Except as provided in divisions (C) and (D) of this section, "negotiable instrument" means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it meets all of the following requirements:

(1) It is payable to bearer or to order at the time it is issued or first comes into possession of a holder.

(2) It is payable on demand or at a definite time.

(3) It does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money, but the promise or order may contain any of the following:

(a) An undertaking or power to give, maintain, or protect collateral to secure payment;

(b) An authorization or power to the holder to confess judgment or realize on or dispose of collateral;

(c) A waiver of the benefit of any law intended for the advantage or protection of an obligor.

(B) "Instrument" means a negotiable instrument.

. . .

(D) A promise or order other than a check is not an instrument if, at the time it is issued or first comes into possession of a holder, it contains a conspicuous statement,

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<sup>19</sup>Article 3 is set forth in Chapter 1303 of the Ohio Revised Code. Article 9 is set forth in Chapter 1309 of the Ohio Revised Code.

however expressed, to the effect that the promise or order is not negotiable or is not an instrument governed by this chapter.

(E)(1) "Note" means an instrument that is a promise.

First, the Note for 267 W. Main involves an unconditional promise to pay the fixed amount of Sixty-Two Thousand Two Hundred Fifty Dollars (\$62,250.00) with an interest rate of 12.25%. (Chase Ex. 1.) Second, the Note was payable to the order of AMS when it was first issued and was payable to "anyone who takes this note by transfer." (*Id.*) Third, the Note is payable on the first of every month from June 1, 1998 through May 1, 2013. (*Id.*) The Lonsways did not have to perform any act but to pay money to the holder of the Note. Finally, the holder of the Note has the power to "confess judgment or realize on or dispose of the collateral." (*Id.*) As a result of the aforementioned, the Note is a negotiable instrument as defined by UCC 3-104. Accordingly, Article 3 of the UCC is the controlling body of law.

Since the Note is a negotiable instrument, the Court must determine if Chase is a holder in due course. If Chase qualifies as a holder in due course, it takes free of competing claims of property or possessory rights in the instrument or its proceeds. O.R.C. § 1303.36(C) (UCC 3-306). For Chase to establish itself as a holder in due course it must prove: (i) it is a holder, (ii) of a negotiable instrument, (iii) taken for value, (iv) in good faith, and (v) without notice that the negotiable instrument has been dishonored, contains an unauthorized signature, a party has a defense as stated in O.R.C. § 1303.35 (UCC 3-305), or a party has

a claim in the instrument pursuant to O.R.C. § 1303.36 (UCC 3-308, 3-306). O.R.C. § 1303.32 (UCC 3-302).

Chase became the holder of the Note - which as stated above is a negotiable instrument - through the Securitization. IMC transferred and sold all of its interest in the 267 W. Main collateral file and other collateral files worth more than \$70 Million to Chase through the Securitization. During the Securitization process, IMC represented: that (i) it had a clear title to the 267 W. Main loan, (ii) after the Securitization, Chase would have a valid and perfected security interest in the 267 W. Main loan, and (iii) IMC did not sell the subject loan with the intent to hinder, delay or defraud any of its creditors. (Chase Ex. 18.) Therefore, Chase bought the loans in good faith and did not have notice that any other party had an interest in the Note and Mortgage.<sup>20</sup> As a result, Chase is a holder in due course and holds the Note and Mortgage free of competing claims of property or possessory rights in the Note and Mortgage and their proceeds. O.R.C. § 1303.36(C) (UCC 3-306).

AMS argues that, because IMC did not pay AMS for the Documents, IMC did not have clear title to the loan. As a consequence, AMS argues that Chase does not hold an interest in the Mortgage and that Chase's recourse is against IMC for breach of warranty. It was incumbent upon AMS, however, to preserve its

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<sup>20</sup>AMS did not assert that (i) Chase was excepted from being a holder in due course (O.R.C. § 1303.32 (UCC 3-302)) per O.R.C. § 1303.32(C), (ii) AMS held a defense pursuant to O.R.C. § 1303.35 (UCC 3-305), or (iii) a party has a claim in the instrument pursuant to O.R.C. § 1303.36 (UCC 3-308, 3-306).

rights to assert a claim (O.R.C. § 1303.36) or defense (O.R.C. § 1303.36) regarding the Documents by timely bringing suit against IMC for breach of contract. This AMS failed to do.

AMS asserts that it conducted an annual title search on 267 W. Main, which failed to disclose that Chase recorded any interest in the property. Since Chase did not record the Mortgage, AMS contends that it had no knowledge of the Securitization.<sup>21</sup> AMS further contends that the failure of Chase to record the assignment is fatal. This argument is flawed. Recordation is applicable only for subsequent purchasers of the subject property. Lack of recording is of no moment as between AMS and Chase under O.R.C. § 1303.32 (UCC 3-302).

#### **CONCLUSION**

The governing law for the dispute between AMS and Chase is the UCC; even under a breach of contract theory, however, AMS loses. AMS has not established the essential element of its claim - *i.e.*, that IMC did not pay for the Documents relating to 267 W. Main. The Corporation Assignment Document, on its face, establishes that AMS received value from IMC for the Mortgage relating to 267 W. Main. Because AMS did not produce the bailee letter and/or proper accounting documents, AMS has no evidence to refute the Corporation Assignment Document or otherwise prove that IMC did not pay AMS for the Documents. AMS argues that this is an unusual situation,

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<sup>21</sup>AMS presented only Lambert's testimony regarding these title searches. AMS alleges that it had no knowledge of this particular Securitization even though it was aware generally of the concept of securitization and equally aware that the signed original Documents were negotiable.

yet it did nothing to preserve its rights - including preserving the documents it might need in the event of litigation, such as the bailee letter. AMS did not offer (and, in the absence of the bailee letter, could not offer) any evidence that IMC failed to pay for any of the collateral files in the bulk transfer. The Corporation Assignment Document states that IMC gave "value" to AMS for the Mortgage relating to 267 W. Main; there is no evidence (other than Lambert's testimony) that IMC paid for all collateral files in the bulk transfer except the Lonsway loans. The fact that AMS kept the Lonsway loans on the books as assets is some indication of non-payment, but that fact, alone, does not establish that IMC did not pay for the Note and Mortgage relating to 267 W. Main and cannot overcome the express acknowledgment by AMS that it received value for the Mortgage. Although possession of the original Documents does not, alone, establish ownership (Karen Kettle's testimony), given the standard practice in the industry that every "bailment" requires payment for or return of files, possession of the files is *prima facie* proof of ownership. In trying to contradict its own Corporation Assignment Document, AMS needed to show more than the fact that it continued to carry the Lonsway loans on its books. Under the totality of the circumstances, AMS failed to establish, by the preponderance of evidence, that IMC did not pay AMS for the Documents relating to 267 W. Main.

If IMC paid AMS for the Documents relating to 267 W. Main, then there is no question that the transfer to Chase is good and that Chase has good title. *Arguendo*, even if IMC did not pay for

these Documents, Chase would still prevail as a holder in due course. In light of the fact that AMS did not carry its burden of proof, this Court finds that Chase has the first and best lien on 267 W. Main by virtue of ownership of the 267 W. Main Mortgage and is entitled to receive the proceeds from the sale of 267 W. Main applicable to and based on such Mortgage.

An appropriate order will follow.

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**HONORABLE KAY WOODS**  
**UNITED STATES BANKRUPTCY JUDGE**

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF OHIO

IN RE: \*  
\*  
VEND INVESTMENT, INC., \*  
\* CASE NUMBER 02-41565  
\*  
Debtor. \*  
\*  
\*\*\*\*\*  
\*  
VEND INVESTMENT, INC., \*  
\* ADVERSARY NUMBER 04-4062  
\*  
Plaintiff, \*  
\*  
vs. \*  
\*  
MAHONING COUNTY TREASURER, \*  
et al., \* HONORABLE KAY WOODS  
\*  
Defendants. \*  
\*

\*\*\*\*\*  
O R D E R  
\*\*\*\*\*

For the reasons set forth in this Court's Memorandum Opinion entered this date, Chase is the legal owner of the AMS Mortgage in answer to Issue No. 1 in the June 23, 2004 Order. Issue No. 2 was resolved by Stipulation as Between Dean W. Fried and American Mortgage Solutions, Inc., which establishes that Dean W. Fried ("Fried") is the owner of the judgment lien, subject to an agreement for its collection between Fried and AMS. Chase has the first and best lien on 267 W. Main by virtue of ownership of the Mortgage and is entitled to receive the proceeds from the sale of 267 W. Main applicable to and based on such Mortgage. The Trustee

is directed to pay the proceeds of the sale to the lien holders in the order of their priority.

**IT IS SO ORDERED.**

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**HONORABLE KAY WOODS  
UNITED STATES BANKRUPTCY JUDGE**