

Dated: June 20, 2012



Eileen W. Hollowell

Eileen W. Hollowell, Bankruptcy Judge

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9 **UNITED STATES BANKRUPTCY COURT**
 10 **FOR THE DISTRICT OF ARIZONA**

11 In Re:)
 12)
 13 INTERGALECTIC PROPERTIES, LLC,)
 14)
 15 Debtor.)
 16)
 17 PEERLESS INDEMNITY INSURANCE)
 18 COMPANY,)
 19 Plaintiff,)
 20 vs.)
 21)
 22 INTERGALECTIC ROPERTIES, LLC, an)
 23 Arizona limited liability company; ZIONS)
 24 FIRST NATIONAL BANK, a Utah)
 25 corporation; BUSINESS DEVELOPMENT)
 26 FINANCE CORP., an Arizona corporation;)
 the SMALL BUSINESS)
 ADMINISTRATION, a United States)
 governmental agency; BROWN &)
 O'HAVER, an Arizona limited liability)
 company; GAYLE ESKAY MILLS, Chapter 7)
 Trustee; INNOVATIVE DESIGN &)
 CONSTRUCTION, LLC, an Arizona limited)
 liability company; and Does 1 through 50,)
)
 Defendants.)

Chapter 7 Proceedings

Case No. 4:09-bk-33531-EWH

Adv. No. 4:11-ap-01312-EWH

SECOND AMENDED FINDINGS
OF FACTS
AND CONCLUSIONS OF LAW
AS TO MOTION FOR SUMMARY
JUDGMENT BY ZIONS FIRST
NATIONAL BANK

1 This matter comes before the Court on an Interpleader action initiated by Peerless
2 Indemnity Insurance Company (“Peerless”) and on the Motion for Summary Judgment filed by
3 Zions First National Bank (“Zions”) and Joinder to Zions’ Motion by Business Development
4 Finance Corporation/Small Business Administration (“BDFC/SBA”).

5 THE COURT has considered the following pleadings (the “Pleadings”):

- 6 1. Motion for Summary Judgment [Docket Entry (“DE”) 41], Statement of Facts in
7 Support of Motion for Summary Judgment [DE 42], and Affidavit of Kenneth Pugh
8 [DE 43], each filed by Zions First National Bank (“Zions”);
- 9 2. Joinder to Zions’ Motion for Summary Judgment [DE 44] filed by BDFC/SBA;
- 10 3. Trustee’s Response to Zions’ Motion for Summary Judgment [DE 53] and
11 Response to Zions’ Statement of Facts [DE 54] filed by Chapter 7 Trustee Gayle E.
12 Mills (“Trustee”);
- 13 4. Limited Joinder in Trustee’s Opposition to Zions’ Motion for Summary Judgment
14 [DE 59] and Statement of Facts related to Limited Joinder in Trustee’s Opposition
15 to Zions’ Motion for Summary Judgment [DE 60] filed by Rampal Yadav
16 (“Yadav”);
- 17 5. Opposition to Zions’ Motion for Summary Judgment filed by Innovative Design &
18 Construction, LLC (“Innovative”) [DE 64];
- 19 6. Limited Joinder in Trustee’s Opposition to Zions’ Motion for Summary Judgment
20 filed by Yadav [DE 66];
- 21 7. Brief in Opposition to Zions’ Motion for Summary Judgment [DE 70], Response to
22 Zions’ Motion for Summary Judgment [DE 71], and Controverting Statement of
23 Facts in Opposition to Zions’ Motion for Summary Judgment [DE 72], each filed
24 by Brown & O’Haver, L.L.C. (“Brown & O’Haver”);
- 25 8. Reply in Support of Motion for Summary Judgment filed by Zions [DE 73]; and
- 26 9. Reply in Support of Motion for Summary Judgment filed by BDFC/SBA [DE 74].

- 1 10. Motion for Summary Judgment filed by Innovative Design and Construction,
2 LLC (“Innovative”) [DE 45]. Statement of Facts filed by Innovative [DE 46].
3 11. Opposition to Innovative Motion for Summary Judgment filed by BDFC/SBA
4 [DE 51]. Counter Statement of Facts to Innovative Motion for Summary
5 Judgment filed by BDFC/SBA [DE 52]; Zions Joinder in Opposition [DE 63].
6 12. Trustee response to Motion for Summary Judgment filed by Innovative [DE 55].
7 Trustee response to Motion for Summary Judgment filed by Innovative
8 Statement of Facts [DE 56].
9 13. Limited Joinder in Trustee’s Opposition to Innovative’s Motion for Summary
10 Judgment filed by Rampal Yadav [DE 61]. Limited Statement of Facts for
11 Limited Joinder in Trustee’s Opposition to Innovative’s Statement of Facts filed
12 by Rampal Yadav [DE 62]. Amended Response to Limited Joinder in Trustee’s
13 Opposition to Innovative’s Motion for Summary Judgment filed by Rampal
14 Yadav [DE 68 and DE 67]. This Limited Joinder was untimely filed and is
15 therefore stricken.

16 The Court entertained argument on April 17, 2012 by Zions, BDFC/SBA, the Trustee,
17 Innovative, Brown & O’Haver and Yadav.

18 Now, being fully briefed on the issues set forth in the Pleadings and having fully
19 considered the same, this Court makes the following FINDINGS OF FACT:

20 1. Each of the Defendants to this Interpleader Action expressly submitted to the
21 jurisdiction of this Court.

22 2. On December 30, 2005, Debtor/Defendant Intergalectic Properties, LLC,
23 (“Debtor”) executed and delivered to Zions a Business Loan Agreement (the “Loan Agreement”)
24 and a Promissory Note (the “Note”) in the principal sum of \$1,774,000.00.

1 3. Pursuant to the terms of the Loan Agreement and Note, Zions loaned
2 \$1,774,000.00 to Debtor in exchange for Debtor's promise to repay the same, plus applicable
3 interest, fees, and costs.

4 4. The annual rate of interest under the Note was the prime rate of interest, as defined
5 in the Note ("Prime"), plus 1.25%. The Default Rate was Prime plus 4.25% per annum.

6 5. As security for the Note, Debtor executed and delivered to Zions a Deed of Trust
7 which was recorded in the Official Records of Pima County, Arizona on December 30, 2005, at
8 Sequence No. 20052521151, Docket 12711, Page 7794.

9 6. The Deed of Trust granted Zions a first position lien encumbering the real property
10 located at 333 West Drachman Street, Tucson, Arizona 85705, which is legally described in the
11 Deed of Trust (the "Real Property").

12 7. Zions was also assigned the present and future rents associated with the Real
13 Property through an Assignment of Rents which was recorded on December 30, 2005, with the
14 Pima County Recorder's Office at Sequence No. 20052521152, Docket 12711, Page 7810.

15 8. As additional security, Zions was granted a secured interest in personal property of
16 the Debtor pursuant to the Commercial Security Agreement dated December 30, 2005 (the
17 "Security Agreement").

18 9. The Security Agreement granted Zions a secured interest in all furniture, fixtures,
19 equipment, machinery, contracts, inventory, accounts relating to rents, general intangibles, and
20 rental income then owned and thereafter acquired, at the Real Property (collectively the "Personal
21 Property").

22 10. Zions perfected its secured interest in the Personal Property by filing a Uniform
23 Commercial Code Financing Statement on January 4, 2006 (the "UCC-1") with the Arizona
24 Secretary of State at File No. 2006-13974962.

25 11. On December 28, 2005 Debtor/Defendant Intergalectic Properties, LLC
26 ("Intergalectic") executed and delivered to BDFC/SBA a Note in a loan amount of \$1,093,000.00.

1 12. The annual rate of interest under the Note was 5.7%.

2 13. As security for the loan from Defendant BDFC/SBA to Debtor in the principal sum
3 of \$1,093,000.00, Debtor also granted to BDFC/SBA a security interest in the Real Property
4 pursuant to a Deed of Trust, Assignment of Leases and Rents, Security Agreement and Fixture
5 Financing Statement (the "BDFC/SBA Deed of Trust").

6 14. The BDFC/SBA Deed of Trust was recorded on December 30, 2005, with the Pima
7 County Recorder's Office at Sequence No. 20052521155, Docket 12711, Page 7848.

8 15. BDFC's interest in the BDFC/SBA Deed of Trust was subsequently assigned to
9 Defendant Small Business Administration ("SBA"), but SBA later re-assigned that interest to
10 BDFC.

11 16. The BDFC/SBA Deed of Trust was junior to Zions' Deed of Trust.

12 17. In January, 2007, Debtor sold the Real Property to Scan Seminole, LLC ("Scan"),
13 which assumed the loan from Zions and all the obligations associated therewith pursuant to a
14 Loan Assumption Agreement and Amendment of Deed of Trust and Fixture Filing and
15 Assignment of Rents, which was recorded with the Pima County Recorder's Office on January
16 19, 2007, at Sequence No. 20070131193, Docket 12974, Page 5356.

17 18. In addition to assuming the debt owed to Zions, Scan borrowed funds from Debtor
18 and granted to Debtor, as security for that loan, a deed of trust against the Real Property junior to
19 that of Zions and BDFC/SBA.

20 19. Scan defaulted on its obligations to Debtor and Debtor conducted a trustee's sale.

21 20. Debtor became title holder of the Real Property, subject to Zions' and
22 BDFC/SBA's security interests.

23 21. In June 2009, Scan defaulted on its loan obligations to Zions, and Zions initiated
24 foreclosure proceedings.

25 22. Zions' trustee's sale was scheduled for December 30, 2009.

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1 23. Debtor filed its bankruptcy case (Case No. 4:09-bk-33531-EWH) in the United
2 States Bankruptcy Court for the District of Arizona on December 29, 2009, effectively staying the
3 sale.

4 24. On September 23, 2010, a fire occurred at the Property.

5 25. On September 23, 2010 the amount owed to BDFC/SBA under its Note and Deed
6 of Trust was \$1,093,000.00 plus interest and fees.

7 26. On October 28, 2010, the Court signed an Order Granting Stay Relief to Zions (the
8 "Order").

9 27. Zions conducted a trustee's sale of the Property on November 29, 2010.

10 28. At the trustee's sale, Zions was the successful bidder with a credit bid of
11 \$1,655,200.00 (the "Purchase Price").

12 29. On the date of the sale, Zions was owed \$2,184,651.09.

13 30. The amount owed to Zions on the date of sale is itemized as follows:

Principal:	\$1,640,341.38
Interest:	\$ 274,025.48
Late Fees:	\$ 12,599.31
Taxes and Insurance	\$ 7,611.23
Prepayment Penalty	\$ 82,017.07
Fees and Costs	\$ 72,058.88
<u>Property Taxes</u>	<u>\$ 95,997.74</u>
TOTAL	\$2,184,651.09

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20 31. After crediting the debt with Zions' Purchase Price and an earnest money payment
21 of \$128,100.00 that Zions received from a prospective Note buyer who failed to close the Note
22 sale, the amount due and owing to Zions is \$401,351.09.

23 32. Zions later sold the property to Lalit Kamar Garg on March 21, 2011, for
24 \$1,000,000.00. Zions, as seller, paid the property taxes, which had accrued over 3 years, in the
25 amount of \$95,997.74.
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1 **The Insurance Policy**

2 33. Peerless issued insurance policy number CBP 1896478 to Executive Inn & Suites
3 of Tucson (the "Insurance Policy").

4 34. The Insurance Policy covered loss occurring in relation to the Property.

5 35. The Insurance Policy was effective from July 1, 2010 through July 1, 2011.

6 36. The Additional Interests Schedule of the Insurance Policy identifies Zions as the
7 first position Mortgage Holder and BDFC/SBA as the second position Mortgage Holder.

8 37. The Insurance Policy provides that Peerless will pay for covered loss to each
9 Mortgage Holder in their order of precedence.

10 38. In addition to the obligations undertaken by Peerless pursuant to the Insurance
11 Policy, Zions' Deed of Trust provides:

12 **Maintenance of Insurance.** Trustor shall procure and maintain policies of
13 fire insurance with standard extended coverage endorsements on a
14 replacement basis for the full insurable value covering all improvement on the
15 Real Property in an amount sufficient to avoid application of any coinsurance
16 clause, and with a standard mortgagee clause in favor of Lender.

17 ...

18 **Application of Proceeds.** Trustor shall promptly notify Lender of any loss or
19 damage to the Property. Lender may make proof of loss if Trustor fails to do
20 so within fifteen (15) days of the casualty. Whether or not Lender's security
21 is impaired, *Lender may, at Lender's election, receive and retain the proceeds*
22 *of any insurance and apply the proceeds to the reduction of the indebtedness,*
23 *payment of any lien affecting the Property, or the restoration and repair of the*
24 *Property. If Lender elects to apply the proceeds to restoration and repair,*
25 *Trustor shall repair or replace the damaged or destroyed improvements in a*
26 *manner satisfactory to Lender. Lender shall, upon satisfactory proof of such*
expenditure, pay or reimburse Trustor from the proceeds for the reasonable
cost of repair or restoration if Trustor is not in default under this Deed of
Trust. (emphasis added).

24 39. BDFC/SBA's Deed of Trust states in pertinent part as follows:

25 Grantor will continuously maintain hazard insurance of such type or types and in
26 such amounts as Beneficiary may from time to time require, on the
improvements now or hereafter on the Property, and will pay promptly when due

1 any premiums therefor. All insurance shall be carried in companies acceptable to
2 Beneficiary and the policies and renewals thereof shall be held by Beneficiary
3 and have attached thereto mortgagee or loss payable clauses in favor of and in
4 form acceptable to Beneficiary. In the event of loss, Grantor will give immediate
5 written notice to Beneficiary and Beneficiary may make proof of loss if not made
6 promptly by Grantor, and each company concerned is hereby authorized and
7 directed to make payment for such loss directly to Beneficiary instead of to
8 Grantor and beneficiary jointly, and the insurance proceeds, or any part thereof,
9 may be applied by Beneficiary at its option either to the reduction of the
10 indebtedness secured hereby or to the restoration or repair of the Property
11 damaged. In the event of a Trustee's sale or other transfer of title to the Property
12 in extinguishment of the indebtedness secured hereby, all right, title, and interest
13 of Grantor in and to any insurance policies then in force shall pass at the option
14 of Beneficiary to the purchaser or Beneficiary.

15 40. Peerless has already paid out insurance proceeds of \$243,304.00 on the fire damage
16 claim.

17 41. Peerless evaluated the claim and at the time of filing this Adversary Proceeding, is
18 prepared to issue \$505,148.76 under the Insurance Policy's real property coverage and
19 \$92,588.56 under the Insurance Policy's personal property coverage, along with \$9,411.50 for
20 business income loss.

21 42. The total amount Peerless interpleads in this action is \$607,148.82 (the "Insurance
22 Proceeds").

23 **The Competing Claims.**

24 43. Zions asserted a claim to the Insurance Proceeds pursuant to its designation as the
25 first position Mortgage Holder under the Insurance Policy.

26 44. In addition, Zions asserted a claim to the Insurance Proceeds pursuant to the
provisions of its Deed of Trust.

45. BDFC/SBA asserted a claim to the Insurance Proceeds pursuant to its designation
as the second position Mortgage Holder under the Insurance Policy.

46. In addition, BDFC/SBA asserted a claim to the Insurance Proceeds pursuant to
the provision of its Deed of Trust.

1 47. Further, Defendant Brown & O’Haver asserts a claim to a portion of the
2 Insurance Proceeds based on theories of equitable relief.

3 48. According to the Agreement and Assignment, Debtor agreed to pay Brown &
4 O’Haver a fee in exchange for Brown & O’Haver preparing and presenting Debtor’s insurance
5 claim to Peerless.

6 49. Defendant Innovative asserted a claim to the Insurance Proceeds in relation to
7 remedial and other related service provided to the Property, memorialized in a Mechanic’s
8 Lien.

9 50. Innovative’s work was performed in June, July and August of 2011, which was
10 after the sale by Zions on March 21, 2011 to Lalit Garg.

11 51. Gayle Eskay Mills, Trustee of Debtor’s Chapter 7 bankruptcy estate, asserted
12 that the Insurance Proceeds are property of the estate.

13 52. Rampal Yadav asserted a claim alleging the Insurance Policy was not property of
14 the bankruptcy estate.

15 53. Peerless Indemnity Insurance Company asserted a claim for a portion of the
16 proceeds, seeking payment of the attorneys’ fees it incurred in filing this Interpleader action.

17 **CONCLUSIONS OF LAW**

18 1. The Court finds *Granite State Ins. Co. v. Employers Mutual Ins. Co.*, 125 Ariz. 275,
19 609 P.2d 90 (App. 1980) dispositive of the issues before the Court.

20 2. The Granite Court follows what is known as the “New York Rule” relative to
21 payment of insurance proceeds in event of loss. *Id.* at 279, 609 P.2d at 94.

22 3. The New York Rule provides that “[t]he obligation of the insurer to its insured is
23 established at the time of the fire and the obligation is not diminished or affected by the eventual
24 compensation of its insured from another source.” *Id.*

25 4. Arizona has adopted the New York Rule. *Id.*

26

1 5. A mortgagee payee under an insurance policy differs from a basic loss payee in
2 that a loss payee is appointed by the insured to collect the proceeds to the extent the insured is
3 entitled to the proceeds whereas a mortgagee payee has an independent agreement with the
4 insurer as though the mortgagee applied for the insurance coverage independent of the insured.
5 *Id.* at 277-278, 609 P.2d at 92-93.

6 6. A mortgagee payee is entitled to insurance proceeds arising from loss which
7 occurred while the mortgagee payee was mortgagee even if the mortgagee forecloses the
8 insured property and takes title to said property before payment of the insurance proceeds. *See*
9 *Roosevelt Savings Bank of the City of New York v. State Farm Fire & Casualty Co.*, 27
10 *Ariz.App.* 522, 556 P.2d 823 (1976) (awarding mortgagee insurance proceeds from loss
11 occurring while mortgage was in effect even though mortgagee took title to the property before
12 proceeds were paid).

13 7. Zions and BDFC/SBA were the mortgagee payees under the Insurance Policy on
14 the date of the Loss.

15 8. Therefore, Zions' and BDFC/SBA's right to the Insurance Proceeds was
16 established on the date of the Loss.

17 9. Zions' subsequent sale of the Property does not interfere with its already-
18 established right to the Insurance Proceeds.

19 10. Zions was not required to seek a deficiency judgment under A.R.S. § 33-814 in
20 order to establish its right to the Insurance Proceeds, and its failure to do so is not fatal to its claim
21 for the Insurance Proceeds. Trustee's objection based on its argument that Zions' claim was fully
22 satisfied upon the foreclosure is overruled.

23 11. Zions and BDFC/SBA are entitled to the Insurance Proceeds based on their
24 positions as mortgagees/payees under the Insurance Policy.

25 12. Zions and BDFC/SBA are further entitled to the Insurance Proceeds based on the
26 plain language of their respective Deeds of Trust.

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13. Zions' interest in the Insurance Proceeds is senior to that of any other party asserting a claim to the Insurance Proceeds.

14. The Court concludes that Zions' Motion for Summary Judgment should be and is therefore granted.

15. The Court, having reviewed the relief requested, concludes that Zions is entitled to payment from the Insurance Proceeds in the amount requested of \$401,351.09, with the remaining proceeds to be paid to BDFC/SBA.

16. No funds shall be disbursed until the remaining factual issues are addressed by the Court and an Order is entered in that regard.

17. The Court concludes that Innovative's Motion for Summary Judgment should be and is therefore denied.

DATED _____

Hon. Eileen W. Hollowell
United States Bankruptcy Court Judge

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APPROVED:

ALTFELD & BATAILLE, P.C.

By 

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