

Recent Bankruptcy Developments, Vol. 8, No. 1
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SECURITY INTERESTS, INSURANCE PROCEEDS, TRANSFERRED COLLATERAL

Wells Fargo Bank v. Courson (In re Courson), 2009 WL 1871494 (Bankr.E.D.Wash., June 24, 2009, Adv. No. A04-00247)

This is a fight between Wells Fargo, which financed the debtor's purchase of a boat and trailer, and a subsequent owner, lender and insurance company. The parties were fighting over the proceeds of a policy covering destruction of the boat and trailer. The Debtor (Courson) purchased the boat and trailer with funds lent by Wells Fargo. He sold the boat to Buxton, who financed his purchase with money lent by Geso Credit Union (Geso). Buxton took out an insurance policy from Safeco and named Geso as an additional loss payee/mortgagor. Neither Buxton, nor Geso, nor Safeco were aware of Wells Fargo's interest in the property at the time of their transaction. Wells Fargo's security interest in the boat was perfected. Geso's was not, and even if it had been, it would have been junior to Well Fargo. When the boat was destroyed Safeco paid Geso the amount due under the policy. Wells Fargo sued everyone on numerous theories.

In a separate opinion, the Bankruptcy Court found Courson's debt to Wells Fargo non-dischargeable, presumably under 11 U.S.C. §523(a)(2) or (6). However, that was all Wells Fargo won. The Court held that under the applicable version of the Washington UCC, the insurance proceeds were not part of Wells Fargo's collateral because Wells Fargo was not named in the policy and the proceeds were paid directly to Geso. If Courson had properly insured the property as he was obligated to do, Wells Fargo would have been entitled to the proceeds of that policy. If the proceeds of the Safeco policy had been paid to Buxton instead of Geso, Wells Fargo would have prevailed because Buxton was Courson's successor in interest and therefore would have held the proceeds subject to Wells Fargo's lien, just as Buxton held the property subject to Wells Fargo's lien. Only in this strangest of circumstances was Wells Fargo deprived of both the value of its interest in the boat and trailer and the insurance proceeds that arose from their destruction.

Is this an unfair result? Although it seems unfair at first blush, perhaps it is not. If the property had never been transferred to Buxton and Courson had simply failed to insure it, Wells Fargo would have been no worse off. If Wells Fargo had been diligent in policing its collateral, it could have discovered the lack of insurance, if not the unauthorized transfer. Did Geso and Buxton receive a windfall? Yes, I think they did. At the time Buxton purchased the boat and trailer and Geso financed them, Buxton's interest in the property was subject to Wells Fargo's security interest. That is, Buxton's and Geso's equity (and the value of their insurable interest) in the property was limited to the difference between the value of the property and the amount owed to Wells Fargo. Safeco apparently allowed them to insure the property for a greater value and paid the higher amount when the property was destroyed. However, Buxton's and Geso's good fortune was not at the expense of Wells Fargo because Safeco had no obligation to pay Wells Fargo under any circumstance. As the Court saw it, as between several innocent parties, there was no reason to have the loss fall on anyone other than Wells Fargo.

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