



IN THE SUPREME COURT OF THE STATE OF DELAWARE

<p>REO TRUST 2017-RPL1,</p> <p>Plaintiff Below,</p> <p>Appellant,</p> <p>v.</p> <p>SHORT SALE, LLC,</p> <p>Defendant Below,</p> <p>FSC LENDING LLC</p> <p>Interested Party, Below</p> <p>Appellees and</p> <p>Cross Appellants</p>	<p>No. 306, 2023</p> <p>On Appeal from the Superior Court of the State of Delaware in C.A. No.: N20L-10-029 DJB</p>
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**CORRECTED APPELLANT'S REPLY BRIEF ON APPEAL AND
CROSS-APPELLEE'S ANSWERING BRIEF ON CROSS APPEAL**

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Dated: December 28, 2023

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NATURE OF PROCEEDINGS

This is Appellants reply brief in support of its appeal and its answering brief to Cross-Appellants opening brief.

SUMMARY OF ARGUMENTS ON CROSS APPEAL

1. Denied. The Superior Court correctly concluded that it had subject matter jurisdiction and the foreclosure action was valid.
2. Denied. The Superior Court did not abuse its discretion in holding that there was no prejudice suffered as a result of the omission of the Estate as a defendant in the foreclosure action.

REPLY ARGUMENT

I. THE SUPERIOR COURT INCORRECTLY HELD THAT SHORT SALE COULD ASSERT DEFENSES FOR THE FIRST TIME AFTER THE SALE

A. Question Presented

Did the Superior Court err in holding that Short Sale did not waive its right to assert defenses, when Short Sale did not enter its appearance, filed no answer to the foreclosure complaint or participate in the foreclosure process in any manner prior to the foreclosure sale? (A167-168)

B. Merits of Argument

Appellant’s question presented is set forth above. Appellees selectively narrowed the question presented to “The Superior Court correctly held that Short Sale did not waive its right to assert defenses when the asserted defenses raised a question as to the Superior Court’s subject matter jurisdiction over the action at bar.”¹

Appellees understandably seek to conflate two defenses they raised in the Court below for the first time in post-sale motions: Lack of subject matter jurisdiction and failure to name a necessary party. Lack of subject matter jurisdiction is a defense that cannot be waived, but the necessary party defense is a

¹ Answering brief page 3

defense that can be waived. They focus their argument on the defense of lack of jurisdiction which will be addressed below regarding the cross appeal.

At no time did Appellees address the independent issue of why their failure to file any pleading prior to the sale, was not a waiver of the necessary party defense.² The focus of their efforts was on the language of 10 Del. C. §5061 and the jurisdictional argument. Once the jurisdictional issue was decided in Appellant's favor by the Superior Court, the Rules of Civil Procedure would still govern. Neither the Court below, nor Appellees adequately explained why the necessary party defense was not waived, when the Superior Court correctly observed that ,standing alone, the necessary party defense was waived.

Indeed, the Superior Court stated that absent the jurisdictional challenge, the Court would have found that the Short Sale's defense was waived for its utter failure to participate in the litigation.³ Inexplicably, however, after rejecting Short Sale's defense and finding that the Superior Court had jurisdiction, the Court below ignored its conclusion that the necessary party defense was waived. The Court analyzed this issue and concluded that despite being waived, the Estate was a necessary party, albeit one that suffered no harm as a result of the foreclosure, so

² Opinion pp. 7-10

³ Opinion p. 6. "Had a jurisdictional challenge not been raised, this Court would have found that Movant's position this late in time was waived."

not indispensable. This conclusion was internally inconsistent, error and contrary to well established case law for the reasons sent forth in the Opening Brief. To allow waivable defenses to be asserted post sale will only encourage other defendants to engage in similar dilatory tactics.

REPLY ARGUMENT

II. THE SUPERIOR COURT INCORRECTLY HELD THAT THE FORELCOSURE WAS DEFICIENT FOR FAILURE TO INCLUDE THE ESTATE AS A NECESSARY PARTY

A. Question Presented

Did the Superior Court err in holding that the Estate was a necessary party to REO's foreclosure of the property when its interest was completely divested by the prior HOA judgment sale? (A108)

B Merits of Argument

The Estate was not a necessary party to the foreclosure action when it was a party to the proceeding brought by the HOA, where it could have participated, and its interest in the property was divested after the execution sale.

Superior Court Civil Rule 19 defines when a party is necessary:

Rule 19. Joinder of persons needed for just adjudication. (a) Persons to be joined if feasible. A person who is subject to service of process and whose joinder will not deprive the Court of jurisdiction over the subject matter of the action shall be joined as a party in the action if (1) in the person's absence complete relief cannot be accorded among those already parties, or (2) the person claims an interest relating to the subject of the action and is so situated that the disposition of the action in the person's absence may (i) as a practical matter impair or impede the person's ability to protect that interest or (ii) leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of the claimed interest. If the person has not been so joined, the Court shall order that the person be made a party. If the person should join as a plaintiff but refuses to do so, the person may be made a defendant, or, in a proper case, an involuntary plaintiff. If the joined party objects to venue and joinder of that party would render the venue of the action improper, that party

shall be dismissed from the action. (b) Determination by Court whenever joinder not feasible. If a person as described in subdivision (a)(1)(2) hereof cannot be made a party, the Court shall determine whether in equity and good conscience the action should proceed among the parties before it, or should be dismissed, the absent person being thus regarded as indispensable. The factors to be considered by the Court include: First, to what extent a judgment rendered in the person's absence might be prejudicial to the person or those already parties; second, the extent to which, by protective provisions in the judgment, by the shaping of relief, or other measures, the prejudice can be lessened or avoided; third, whether a judgment rendered in the person's absence will be adequate; fourth, whether the plaintiff will have an adequate remedy if the action is dismissed for nonjoinder.

Applying the criteria of Rule 19, the Estate was not a necessary party. First, complete relief could be granted to those already a party. The foreclosure sale divested the 100 percent of the ownership interest in the property and vested 100 percent ownership interest to the winning bidder.

Second, the Estate's interest in the property was divested as a matter of law in the HOA execution sale and it did not claim any remaining interest in the property. Finally, the foreclosure judgment did not impose or create any additional liability on the Estate, as this was an *in rem* proceeding.

This result is supported by *Wilmington Savings Fund Society v. Gillette*, 2017 Del Super. LEXIS 157 (Del. Super. 2017) , affirmed, *Gillette v. Wilmington Savings Fund Society*, 245 A. 3d 498 (Del. Supr. 2017). Appellee seeks to distinguish that case because in *Gillette*, Defendant was also a mortgagor. Following that logic, Appellees contend that the Court held that as long as one

mortgagor is named, the foreclosure is valid.⁴ That conclusion makes no sense. Either a part is necessary or its not. That fact is not dependent on whether another Defendant is similarly situated.

In fact, the Court in *Gillette* held that the deceased mortgagor's estate was not necessary because "[d]efendant was the sole owner of 18 Park Avenue. Therefore there is no need for Slinghuff's estate to be joined to this action ." *Id* at *4 and 5. There was no mention of Gillette's status as a co- mortgagor for its holding that the Estate was not a necessary party.

It is for the same reasons that heirs and other successors in interest to the deceased's interest in the property are to be named according to Section 5061. Because they have an interest in the property that is subject to divestiture.

The Court below correctly concluded that the Estate obviously had no interest in the property as it did not participate in either of the sale processes in any manner.

⁴ Answering brief p. 17

REPLY ARGUMENT

III. THE SUPERIOR COURT INCORRECTLY GRANTED FCS' MOTION FOR DISTRIBUTION OF PROCEEDS

A. Question Presented

Did The Superior Court err in holding that first mortgage holder FCS was entitled to distribution of sheriff sale proceeds after the foreclosure sale brought by the second mortgage holder REO, misapprehending established law and upending long standing practice? (A169-171)

B. Merits of Argument

Appellee questions why former counsel for Appellant wrote a letter stating that Appellee's mortgage would be paid first. ⁵ Appellee alleges that this is somehow an admission on the party of Appellant. This was an incorrect legal conclusion which could not be binding on Appellant nor the sheriff that distributes the proceeds. *Cox Communications, Inc. v. T-Mobile US, Inc.*, 273 A3d 752, 766 (Del Supr, 2022) *citing*, *Levinson v. Del. Comp Rating Bureau, Inc.*, 616 A2d 1182, 1186 (Del. 1992) (Admissions are limited to factual matters and not legal conclusion.)

Appellee argues that while 10 Del. C. §4985 controls how liens are discharged upon execution sale, 25 Del C. §2106 controls the order of distribution.

⁵ Answering brief p. 19

Section 2106 does no such thing.⁶ It does not address the order of distribution of sheriff sale proceeds at all. That statute only states that a mortgage shall be a lien from the time of recording. No one is arguing that Short Sale's mortgage was not a lien, not recorded first or does not have lien priority.

10 Del. C. § 4985 on the other hand, does address the distribution of proceeds when the lien is discharged as a result of an execution sale:

Discharge of liens upon execution sale; exceptions.

Real estate sold by virtue of execution process shall be discharged from all liens thereon against the defendant, or against one or more of the defendants, if there is more than one, whose property such real estate is, except such liens as have been created by mortgage or mortgages prior to any general liens; and with respect to such, the sale shall be a discharge to the extent to which the proceeds thereof may be legally applicable to a judgment or judgments obtained for the debt, to secure the payment of which the mortgage or mortgages respectively, if there is more than one, appear to have been given, and the real estate shall also be discharged from all right of dower and curtesy therein of any defendant in the execution. (emphasis added)

Section 4985 makes two things clear: First, mortgages that have priority over a judgment are not discharged by the execution process. Second, proceeds from the execution sale is only distributed if the mortgage was reduced to

⁶ § 2106. **Priority of mortgage from time of recording.**

A mortgage, or a conveyance in the nature of a mortgage, of lands or tenements shall have priority according to the time of recording it in the proper office, without respect to the time of its being sealed and delivered, and shall be a lien from the time of recording it and not before.

judgment. (“proceeds thereof may be legally applicable to a judgment or judgments obtained for the debt”) *Id.*

While Appellee relies on *Eastern Savings Bank v. CACH*, 55 A.3d 344, 350 (Del. Supr. 2012).and argues that *CACH* did not distinguish between mortgages and general liens, this Court had endorse Appellant’s interpretation of Section 4985 and *Cedar’s Inn, Inc. v. King’s Inn, Inc.* 269 A2d 781 (Del. Super. 1971), and noted that:

“we note that our statutory interpretation is consistent with *Cedar Inn v. King’s Inn, Inc.* Cedar Inn involved sheriff’s sale property with encumbrances in the following order of priority: (1) Delaware Trust Company mortgage, (2) Cedar Inn, Inc. mortgage, and (3) Delaware Trust Company judgment lien. Cedar Inn foreclosed on the property subject to the Delaware Trust Company mortgage, meaning that the Delaware Trust Company’s first mortgage remained on the property after the foreclosure sale. In setting the order of distribution for the remained two liens, the judge held that the sheriff sale proceeds be paid first to Cedar Inn’s mortgage, then to the Delaware Trust Company’s judgment lien”(emphasis added).*CACH* at 350 .

Woolley’s is even clearer, stating without reservation that a first lien created by a mortgage “does not share in the distribution of the proceeds” when a second priority general lien takes a property to sale. *Woolley’s Practice in Civil Actions*, Section 1140.

Appellee fails to explain why its first mortgage differs from the Delaware Trust first mortgage in *Cedar Inn* described above or this statement in *Woolley’s*. The only answer that makes sense in the scheme of all the laws cited, is that the

recording statute determines the priority of payment of all liens that are discharged by a sale. Since Appellee's first mortgage is not discharged by the foreclosure sale, it does not stand in line for proceeds.

This Court should decline to interpret the laws in a manner inconsistent with Delaware practice. This issue was well established law, as noted by the submission of the Sheriff of New Castle County, and evidenced by the dearth of any caselaw⁷, until now, over the distribution of proceeds in a plain vanilla second mortgage foreclosure sale. Where were the other first mortgage holders petitioning for proceeds? They do not exist, because it was not the law. Properties were sold subject to any first mortgages, (hence the "buyer beware" admonishment by the sheriffs). It was then up to the new owner to negotiate a release of that mortgage.

CACH had a unique fact pattern where the judgment was recorded first, which prompted litigation which had to go to appeal and cite scant legal authority to "well establish" the law, in Appellee's opinion.

⁷ Opinion p. 8 "This issue of first impression is ripe for interpretation".

CROSS APPEAL ARGUMENT

I. THE SUPERIOR COURT CORRECTLY RULED THAT THE MORTGAGE FORECLOSURE ACTION WAS NOT VOID *AB INITIO* BECAUSE THE SUPERIOR COURT HAD SUBJECT MATTER JURISDICTION

A. Question presented

Whether the Superior Court had subject matter jurisdiction over this foreclosure action.

B. Scope of Review

The interpretation of statutes is question of law that this Court reviews *de novo*. *Eastern Savings Bank v. CACH*, 55 A.3d 344, 347 (Del. Supr. 2012) *citing Le Van v. Independence Mall, Inc.*, 940 A2d 929, 932 (Del. Supr. 2007).

C. Merits of Argument

Appellees confusingly contend that the Court below never decided the subject matter jurisdiction issue and whether the action was void.⁸ To the contrary, the Superior Court held that it did have jurisdiction.⁹

Appellees argue that 10 Del. Code. Section 5061 must be strictly construed and a failure to comply with a strict interpretation of the statute deprives the Superior Court of jurisdiction.¹⁰ However the case cited to support this concept

⁸ Answering brief p.30

⁹ Opinion p. 7

¹⁰ Answering Brief at 13

Brooks v. BAC Home Loans Servicing, LP, 53 A. 3d 301 (Del. 2012)(Order), does not stand for this proposition. *Brooks* merely states that jurisdiction is conferred by Section 5061. It does not mandate a strict construction of the statute.

To the contrary, statutes conferring jurisdiction are to be liberally construed. e.g. *Health Trio, Inc. v. Margules*, 2007 Del. Super. LEXIS 34, p. 16 (Del. Super. 2007); *Wife S. v. Husband S.* 295 A2d 768, 771 (Del. Ch. 1972); *State v. Allen-Anderson*, 2017 Del. Super. LEXIS 232, *5 (Del Super. 2017). This was the standard properly applied by the Superior Court.¹¹

This argument focuses on Section 5061. Under a literal reading of Section 5061 the mortgagor must be named in a foreclosure. In this case, the mortgagor is deceased and cannot be named as a party. Section 5061 then goes on to add that an “heir, executor, administrator, or successor” may be summoned to appear. The question then becomes, who is a successor to the mortgagor who would be a proper defendant to a *sci fa. sur* mortgage action.

The terms ‘successor’ is quite broad. Since this is an *in rem* action against a parcel of real estate only, logically, it would be person or entity that succeeded in the ownership of the property. It should not be the Estate or the Heirs of the deceased, as their interests in the property were divested at the HOA Execution

¹¹ Opinion, p. 7

Sale. So to reach the only logical conclusion, a liberal reading of Section 5061 would include the current owner, Short Sale as a successor.

In the Court below, Appellant argued that the Appellee “stepped into the shoes” of the Estate. That phrase was intended to mean that the Appellee was the successor to the interest of the mortgagor in the property, which continues to be subject to the Appellant’s lien. At no time did Appellant argue that the Appellee was now personally liable for the underlying debt, merely that that the property Appellee owned continued to be saddled with that obligation.¹²

Section 5061 does not mandate that the person or entity that owes the money (borrower) be a party to the foreclosure. That would be the Estate. There are many circumstances when the borrower is not a named party. This is the case when an heir is a defendant, or only one co-owner signs the note, or the mortgagor has been discharged in bankruptcy. This is an *in rem* proceeding. The failure to name a defunct mortgagor, whose interest was legally terminated in a prior judicial proceeding does not deprive the Superior Court of jurisdiction and to adjudicate the rights of all interested parties.

¹² A199-201

CROSS APPEAL ARGUMENT

II. THE SUPERIOR COURT CORRECTLY HELD THAT THERE IS NO PREJUDICE AS A RESULT OF THE FAILURE TO NAME THE ESTATE AS A PARTY TO THE FORECLOSURE ACTION

A. Question Presented.

Whether the Superior Court erred in holding that there was not sufficient prejudice to vacate the mortgage foreclosure sale.

B. Scope of Review.

The Superior's Court's decision to not set aside a Sheriff's sale is reviewed by the Court for an abuse of discretion. *Burge v. Fidelity Bond & Mortgage Co.* 648 A2d, 414, 421 (Del. 1994)

C. Merits of Argument

Appellee struggles to find any party that has experienced real and concrete prejudice by this ruling. It resorts to an admirable effort to claim harm to the Estate. What was the prejudice to the Estate? None is presented. According to Appellees, it was denied the opportunity to participate in the foreclosure. The Estate did not lose any rights in this property as a result of this foreclosure. Its interest in the property was already gone. It has not incurred any liability for any debt as a result of this sale. This was an *in rem* action. Has the Estate been denied a benefit as a result? None was suggested. Neither the Court nor Appellant could

imagine any, nor apparently can Appellees as they speak in broad and sweeping terms, not concrete facts.

The Estate's interest in the property was cut off by the execution proceedings brought by HOA. Its interest was gone before the foreclosure proceedings commence. Short Sale was not concerned about this potential prejudice when it did not assert that it was a necessary party during the foreclosure process. Because there was no prejudice. What has changed? Nothing.

Appellees then resort to the argument that the "public" has been harmed by a violation of the process, but there is 'absolutely no way to know how badly'¹³ as there is a "direct and unknowable impact the amount that would be realized at the sale". Who is prejudiced if, as intimated, the sale proceeds are impacted? The mortgage company if the sale proceeds are insufficient to satisfy the mortgage? They are a party. Not the Estate, whose interest was already divested at the execution sale. It would not share in any excess proceeds (excess proceeds, if any, would go to the owner, Short Sale), and is not liable for any deficiency, as this was an *in rem* proceeding.

¹³ Answering brief p. 36

There were no facts presented to support Appellees' contention that the Superior Court abused its discretion in finding that there was no prejudice to justify setting aside the sale.

If there is the pervasive prejudice to the mortgage foreclosure process,¹⁴ Appellee's post sale motions' are the culprit, as the Superior Court's ruling has upended established Delaware practice. The only way to avoid this cloud of prejudice is to reverse the trial court.

¹⁴ Answering brief p. 37.

CONCLUSION

The proper result is that this sale was valid. FCS, as the winning bidder at the sheriff sale, must remit its bid amount to the sheriff, who then will distribute the net proceeds first to REO, the foreclosing lender, followed by any junior judgment liens which are otherwise discharged from the Property (of which there appear to be none). The first priority mortgage continues to attach to the property, is not extinguished and does not share in the proceeds. Proceeds go to the foreclosing lender, in this case, REO.

Dated: December 28, 2023

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