ARIZONA SUPREME COURT
ORAL ARGUMENT CASE SUMMARY

FIRST AMERICAN TITLE INSURANCE CO. v. ACTION ACQUISITIONS, LLC. and FREE FOR NOW, L.L.C.

CV-07-0412-PR
1 CA-CV 06-0782 (Opinion)

PARTIES AND COUNSEL:

Petitioner: Daniel Kloberdanz of Berens, Kozub & Kloberdanz for Action Acquisitions and Free for Now.

Respondent: Capitol Title, represented by Christine Farnsworth and Eric M. Jackson of Jackson White PC. Ari Ramras, Ramras Law Offices, PC will be arguing for First American Title Insurance Company.

FACTS:

This case addresses whether a standard term in a title insurance policy that excludes coverage when the insured fails to "pay value" for a title may bar coverage when a Sheriff's sale is set aside because the value the insured paid for title to a foreclosed home was so low that it shocked the conscience of the court.

The facts are relatively simple. At a sheriff's sale several properties were sold and the insureds, Action Acquisitions and Free for Now, made the prevailing bid for a home that had been foreclosed due to unpaid homeowners' association assessments. A.R.S. §33-1807(A) (B) (Provides that planned community associations have liens for assessments that may be foreclosed in the same manner as a real estate mortgage). At the time of the sheriff's sale here, the home was valued at between $300,000 and $400,000 and was subject to a $162,000 deed of trust. Accordingly, as the opinion notes, even viewing the situation conservatively, when one "does the math," the insureds' $3,500 bid - the only bid offered - constituted less than three percent of the home's fair market value.

After the six-month statutory redemption period expired, the insureds obtained a sheriff's deed and purchased a $400,000 owners' title insurance policy (ALTA Homeowner's Policy of Title Insurance (1998) issued by Capital Title and underwritten by First American ("insurers").

The previous homeowner filed a motion to set aside the Sheriff's sale on numerous grounds, including that the price the insureds paid at the Sheriff's sale shocked the court's conscience. *See Mason v. Wilson*, 116 Ariz. 255, 257, 568 P.2d 1153, 1155 (App. 1977). The superior court, J. Katz, permitted the insureds to intervene in that action. The court later granted the motion to set aside the sale because the purchase price was so grossly inadequate that it shocked the court's conscience.

Because the insureds assumed they had coverage under the title policy, they did not appeal the court's order setting aside the Sheriff's sale. They made a claim under the title policy seeking reimbursement for the policy limits of $400,000.

The insurers denied coverage and filed a declaratory action seeking a determination whether the insureds were entitled to coverage under the policy. The insureds counterclaimed for breach of contract in a third-party complaint against Capital Title, issuer of the policy.

The insurers moved for summary judgment arguing coverage for the loss was barred by two standard form policy exclusions: (1) Exclusion 4(a), providing that insureds were not insured against loss resulting from risks "created, allowed, or agreed to by" the insureds; and (2) Exclusion 5, providing that the policy excluded losses resulting from "failure to pay value for [the] Title."

The superior court: (1) granted the insurers summary judgment; (2) denied the insureds' cross motion, finding the insureds "knowingly incurred the risk that the sale could be set aside;" (3) found the insureds' claim barred by Exclusion 4(a); and (4) declined to address the insurers' argument that Exclusion 5 also barred coverage.

The insureds appealed. The opinion held that Exclusion 5, "the value clause," precluding coverage for losses resulting from an insured's failure to pay value, barred insureds from recovering after the Sheriff's sale was set aside. The court held: (1) that the purpose of the exclusion was to bar coverage when an insured lost title for failure to pay adequate consideration; and (2) the term "value" for purposes of the exclusion did not mean any consideration. The court noted that the insureds were in the business of buying homes being foreclosed due to unpaid homeowner's association assessments and they bid only the minimum required to cover the association liens. The court determined that permitting the insureds to recover the market value from the insurer under such circumstances would violate public policy. The court held that insured purchasers who acquired real property for a grossly inadequate price are not bona fide purchasers for value. Finally, the court held that the reasonable expectation concept, when interpreting a contract that is allegedly an adhesion contract, must be limited by something more than the fervent hope usually engendered by loss.

ISSUES:

> "1. Did the court of appeals misinterpret Exclusion 5 of the Policy which excludes coverage for any loss "resulting from . . . [f]ailure to pay value for [the] Title?
>
> 2. Did the court of appeals err in applying the correct insurance policy interpretation rules and in failing to consider the insureds' expectations as well as the relevance of the insureds' knowledge of the bid price which led to the sale being overturned?"

ADDITIONAL ISSUE NOT ADDRESSED BY THE COURT OF APPEALS

> "The court of appeals did not address the applicability of Exclusion 4(a), the sole basis for the trial court's granting summary judgment."

Definitions:

Adhesion contract: An adhesion contract is a nonnegotiable contract with standard terms that customers must agree to without modification.

Bona fide purchaser for value: Commonly called a "BFP" in legal and banking circles, this term refers to one who has purchased property in good faith for a stated value, innocent of any fact that would cast doubt on the right of the seller to have sold the property in good faith. This status is vital if the true owner shows up to claim title, since the BFP will be able to keep the asset, and the real owner will have to look to the fraudulent seller for recompense.