IN THE SUPREME COURT

STATE OF ARIZONA

CENTERPOINT MECHANIC LIEN CLAIMS, LLC, Respondent/Cross-Petitioner, v. COMMONWEALTH LAND TITLE INSURANCE COMPANY, Petitioner/Cross-Respondent.	No. CV-23-0164-PR Arizona Court of Appeals No. 1 CA-CV 21-0039 Maricopa County Superior Court No. CV2011-008600

RESPONDENT AND CROSS-PETITIONER CENTERPOINT MECHANIC LIEN CLAIMS, LLC'S RESPONSE TO AMICUS BRIEF

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INTRODUCTION

American Land Title Association ("ALTA") is the self-proclaimed "premiere national trade association and voice" of title insurance companies, and the drafter of the lender's title policy forms at issue.[1] It is hardly surprising that ALTA has joined the fray in response to Commonwealth's[2] cry for aid; after all, one of its largest constituent members is desperately trying to escape liability under those title policies. But, ALTA's efforts are for naught.

The ALTA Brief conspicuously fails to rebut that Commonwealth's purported "coverage" defenses are precluded here under *Morris* and its progeny, and under the doctrine of issue preclusion.[3] Instead, it states dismissively (at 2) that the Court of Appeals' application of *Morris* and its progeny was "unnecessary," despite that *Morris* and its progeny are controlling. ALTA fails to mention, or to dispute in any way that Commonwealth's purported coverage defenses are independently foreclosed by the *Morris* Judgment.

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[1] Amicus Curiae Brief of American Land Title Association in Support of Commonwealth Land Title Insurance Company's Petition for Review ("ALTA Brief") at 1.

[2] Capitalized terms in this Response have the same meanings as in Respondent and Cross-Petitioner Centerpoint Mechanic Lien Claims, LLC's Supplemental Brief ("CMLC's Brief"), unless otherwise defined herein.

[3] CMLC's Brief at 4-9. ALTA also ignores that CMLC is entitled to judgment on coverage under several additional grounds. CMLC's Response to Petition for Review ("CMLC's Response") at 13-15.

Apart from that, and contrary to ALTA's argument, the Court of Appeals complied with and properly applied Arizona's rules for construing insurance policies. The Court of Appeals correctly concluded, pursuant to those rules, that Commonwealth's arguments under Conditions 8(a)(ii) and 10(b) of the title policies (Tr. Ex. 10, 22) relate solely to an insurer's indemnification liability for claims that are covered, rather than constituting any sort of coverage defense(s).

ALTA also echoes (at 11) Commonwealth's purported "no-loss" argument, which—in addition to being precluded—is contrary to Arizona law. Under controlling precedent, diminution in the value of the insured deed of trust is the measure of loss under a lender's title policy, calculated as of the policy issuance date.[4] Some non-Arizona cases may differ about ***when*** such a loss is to be measured, but there is no legitimate disagreement that diminution in value of the insured mortgage/deed of trust constitutes "loss or damage" under a lender's title policy.[5]

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[4] CMLC's Response at 8-11. The insureds here indisputably suffered diminution in value losses. Accordingly, and as shown below, ALTA's and Commonwealth's actual argument is that Commonwealth's express liability for such losses under Condition 8(a)(iii) of the title policies was ***extinguished*** by alleged subsequent payments to the insureds from sources other than the insured deeds of trust.

[5] Moreover, as shown below, this is one of several positions taken in the ALTA Brief that directly contradict positions ALTA has previously published in its "Title Insurance Law Newsletter," which it says is "The Authoritative Source of Land Title Industry Litigation News Since 1992" ("Newsletter").

In any event, this purported "no-loss" argument is also directly contrary to the express provisions of the title policies. The argument thus violates Arizona's rules for construing the provisions of insurance contracts because, as discussed below (at 10-15), it would render several of those provisions meaningless.

I. COMMONWEALTH'S PURPORTED COVERAGE DEFENSES ARE PRECLUDED HERE.

Each of the title policy provisions in question (Condition 8(a)(ii), Condition 10(b), and Exclusion 3(c)) relates to damages and/or liability, rather than coverage. Purported "coverage" defenses based on any such provision(s) are, accordingly, precluded here under *Morris* and its progeny.[6]

ALTA also disregards that Commonwealth actually litigated—and lost—these same "no-loss" and termination of liability arguments in the Reasonableness Action, and that the final *Morris* Judgment expressly binds Commonwealth to both the fact and amount of $5 million in damages under each title policy. In any event, ALTA does not dispute that Commonwealth's purported coverage defenses are also precluded here under the doctrine of issue preclusion.[7]

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[6] CMLC's Brief at 4-6.

[7] CMLC's Brief at 6-9. Any purported Condition 10(b) defense also fails as a matter of law—in addition to being precluded as set forth above—because the insureds suffered compensable diminution in value losses under the title policies before the alleged releases of their insured deeds of trust. *Fid. Nat'l Title Ins. Co. v. Osborn III Partners LLC*, 250 Ariz. 615, 624 ¶ 40 (App. 2021).

II. THE COURT OF APPEALS PROPERLY APPLIED ARIZONA'S RULES FOR CONSTRUING INSURANCE POLICIES.

ALTA contends erroneously (at 2) that the Court of Appeals found that Conditions 8(a)(ii) and 10(b) were defenses to liability, rather than coverage defenses, solely because the word "liability" appears in the headings of those Conditions. ALTA further contends (at 6), again erroneously, that the Court of Appeals thereby failed to follow Arizona's rules that "an insurance contract must be read as a whole and construed to give effect to all its provisions and to prevent any of the provisions from being rendered meaningless." ALTA is demonstrably wrong on both counts.

Initially, although ALTA complains that the Court of Appeals noticed (at ¶¶ 42, 43) that the relevant policy headings refer to Commonwealth's "liability," rather than to coverage, ALTA—the drafter of the title policies—does not explain why such headings were not intended to reflect the import of these Conditions. Regardless, the Court of Appeals' analysis went far beyond those headings. The Court of Appeals analyzed (at ¶¶ 45-47) dictionary definitions of "coverage" and "liability," in the context of *Morris* and its progeny. The Court of Appeals further analyzed (at ¶ 49) how those definitions applied in the context of the title policies' Covered Risks, Exclusions, and Exceptions. Additionally, the Court of Appeals examined (at ¶¶ 42, 43) the "terms and placement" of these Conditions. Ultimately—after considering all of the foregoing—the Court of Appeals rightly concluded (at ¶

50) that such Conditions “are unrelated to the question of what constitutes a covered event under the policies.”

The text of each Condition plainly refutes ALTA’s argument that it determines “coverage.” Condition 8 states in relevant part (emphasis added):

> **8. DETERMINATION AND EXTENT OF LIABILITY**
>
> This policy is a contract of indemnity against actual monetary loss or damage sustained or incurred by the Insured Claimant who has suffered loss or damage ***by reason of matters insured against by this policy***.
>
> (a) The ***extent of liability*** of the Company for loss or damage under this policy shall not exceed the least of (i) the Amount of Insurance, (ii) the Indebtedness, (iii) the difference between the value of the Title as insured and the value of the Title subject to the risk insured against by this policy . . . .

The first sentence unambiguously indemnifies the insured for loss or damage resulting from “matters insured against,” which plainly means ***covered*** under other policy provisions. Subsection (a) then expressly states the formula for calculating the “extent of liability of the Company” for such covered losses or damages. Condition 8(a) thus indisputably states how the insurer’s indemnification ***liability*** is calculated for losses and damages that are ***covered*** under other provisions of the title policy, and so has nothing to do with coverage.

ALTA is further mistaken when it claims (at 6) that there is no published opinion in Arizona supporting this characterization of Condition 8. In *Equity Income*

Partners, LP v. Chi. Title Ins. Co., 241 Ariz. 334 ¶ 1 (2017), this Court found that Condition 8 (numbered 7 in that case) "explains how the insurer's liability is calculated . . . ." ALTA actually agrees with that finding (when it is not being Commonwealth's advocate). In one of its Newsletter articles, ALTA criticized a published decision on the grounds that the court there ignored that Condition 8 is the "measure of loss" provision under the lender's title policy, with ALTA specifically confirming:

> Condition 8(a)(ii) is the measure of loss provision. It says that loss equals 'the difference between the value of the Title as insured and the value of the Title subject to the risk insured against by this policy.' Perhaps the court missed it because it is such a short statement about such an important and complicated subject.[8]

In its Claims Handbook (Tr. Ex. 32), Commonwealth acknowledges that Condition 8 is "the policy's formula for measurement of loss or damage under the loan policy."[9]

The Court of Appeals' characterization of Condition 10(b) is also unassailable. Condition 10(b) states (emphasis added):

> **10. REDUCTION OF INSURANCE; REDUCTION OR TERMINATION OF LIABILITY**
>
> (b) The voluntary satisfaction or release of the Insured Mortgage shall ***terminate all liability of the Company*** except as provided in Section 2 of these Conditions.

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[8] Respondent's Appendix attached hereto ("APP") at APP004.

[9] APP078.

Again, since the insurer's ***liability*** is limited to losses or damages resulting from "matters insured against [i.e. covered] by this policy" (pursuant to Condition 8), there could be no termination of liability under Condition 10(b) unless and until such covered losses existed. Condition 10(b) itself thus has no relevance to coverage.[10]

ALTA's argument that the Court of Appeals misconstrued Conditions 8 and 10 boils down to its unsupportable contention (at 8) that such Conditions "were intended by the parties to be conditions or prerequisites to coverage," which is predicated on ALTA's erroneous assertion (*id.*) that the preamble of the Covered Risks section supposedly says that "coverage was subject to the Exclusions and Conditions." In truth, what that preamble actually says is that the insurer's indemnification ***liability*** for losses or damages "sustained or incurred by reason of [Covered Risks]" is subject to the Exclusions, Exceptions, and Conditions. Consistent with this, Commonwealth explains in its Claims Handbook: "In other words, coverage under the policy exists only to the extent set forth in the insuring clauses. And the ***protection afforded thereby*** is limited by the exclusions, exceptions and other terms and conditions of the policy."[11]

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[10] Inexplicably, ALTA contends (at 11) that Condition 10(b) states: "repayment of the loan shall terminate all liability of the Company," when that is not the case. Any arguments by ALTA based on that misstatement must therefore be rejected.

[11] APP077 (emphasis added).

III. THE INSUREDS SUFFERED COVERED LOSSES AND DAMAGES.

ALTA's purported "no-loss" argument is precluded as a matter of law, as set forth above. Regardless, the insureds here unquestionably suffered covered diminution in value damages of $19.5 million resulting from the mechanics' liens.[12] ALTA knows (but nevertheless disregards) that diminution in the value of an insured deed of trust is the measure of loss under a lender's title policy. Indeed, ALTA itself instructs that a loss under a lender's title policy "equals the difference between" two values: "one being the value of the property subject to the matter for which there is coverage and the other being the value of the property with its title as insured."[13]

Under Arizona law, these lender's title policies are ambiguous because they do not contain a definition of loss or damage, and so are construed against the insurer on that point. *Swanson v. Safeco Title Ins. Co.*, 186 Ariz. 637, 640-41 (App. 1995). Lender's title policies are also ambiguous under Arizona law because they do not

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[12] CMLC's Response at 8-11.

[13] APP029. In a different Newsletter article criticizing a published decision, ALTA complained:

> This decision is a vivid illustration of the fact that the ALTA loan policy still contains the same value loss formula found in the ALTA owner's policy, despite the fact that courts have been applying the diminution in security formula for loan policy losses for more than 40 years.

APP022.

identify the date for calculating loss or damage, and so are construed against the insurer on that point as well. *First Am. Title Ins. Co. v. Johnson Bank*, 239 Ariz. 348, 353 (2016). Applying those principles, this Court held in *Johnson Bank* that "the lender's diminution-in-value loss should be calculated as of the date the title policy was issued rather than as of the date of foreclosure."[14]

ALTA is quite familiar with (but nevertheless disregards) this controlling precedent. Indeed, in one of its Newsletters ALTA was sharply critical of this Court's reasoning and decision in *Johnson Bank*, yet acknowledged the ambiguity of its lender's title policies on this critical issue, concluding that: "The most rational statement by the majority [in *Johnson Bank*] was that a title insurer could avoid this lunacy [of the Court's decision] by inserting a loss date in the policy."[15]

In any event, this purported "no-loss" argument—in addition to being precluded—would render various provisions of the title policies meaningless, and thus would violate the very canons of Arizona law for construing insurance contracts that ALTA has invoked so vehemently in support of its baseless attack on the Court

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[14] *Id.* at 348 ¶ 1. *See also*, *Equity Income*, 241 Ariz. at 336 ¶ 8 (diminution in value loss under lender's title policy calculated as of policy issuance date). *Johnson Bank* clearly applies here. The mechanic's liens resulted in the "total failure of title" that this Court found in *Johnson Bank* (at ¶ 36) supports using the policy issuance date, because the liens prevented the "known, intended use of the property [sale of Centerpoint to pay the insureds], and caused the borrower to default on the loan [by failing to pay the insureds pursuant to their insured deeds of trust]." *Id.* at 348 ¶ 1.

[15] APP044.

of Appeals' ruling. To begin with, Condition 8(a)(iii) of the title policies expressly indemnifies the insured for losses or damages equal to "the difference between the value of the Title as insured and the value of the Title subject to the risk insured against by this policy." The word "Title" is defined in Condition 1(l) as: "The estate or interest described in Schedule A," which, under the title policies at issue, are the insureds' respective deeds of trust against Centerpoint. Accordingly, pursuant to Condition 8(a)(iii) Commonwealth expressly indemnified the insureds here for the diminution in value of their insured deeds of trust against Centerpoint resulting from mechanic's liens.[16] Condition 8(a)(ii), however, caps the amount of the insurer's liability for such loss at the amount of the "Indebtedness," if that amount is less than the diminution in value of the insured deed of trust under Condition 8(a)(iii).

The "Indebtedness" is an indispensable component for calculating insured losses, as of a particular date, for diminution in value under Condition 8(a)(iii), i.e., the difference between "the value of the [deed of trust] as insured" and "the value of the [deed of trust] subject to the risk insured against by this policy." Those comparative values are determined—as of that date—by: (1) the fair market value of the underlying property; (2) the priority of the insured deed of trust; and (3) the

[16] Any separate deeds of trust against other properties, which are not insured under the title policies (such as Universal had here), are thus entirely irrelevant to Commonwealth's express indemnification obligation under Condition 8(a)(iii).

amount of the "Indebtedness." ALTA's argument, however, would require Condition 8(a) to be construed so that the amount of the "Indebtedness" for purposes of Condition 8(a)(ii) is measured as of some different, unspecified future date that is different from the date for measuring "Indebtedness" for purposes of Condition 8(a)(iii). "Indebtedness" cannot, under any applicable canons of construction, secretly mean something under Condition 8(a)(ii) that is entirely different than its meaning under Condition 8(a)(iii).[17] In any event, Condition 8(a) would make no sense and have no meaning unless each of the alternative limits on the insurer's liability under subparts (a)(i) through (iii) is calculated as of the same date.

ALTA's argument that "Indebtedness" under Condition 8(a)(ii) means something different than "Indebtedness" for purposes of Condition 8(a)(iii) would render the insurer's indemnification liability for diminution in value losses under Condition 8(a)(iii) meaningless. Indeed, under the purported "no-loss" argument, whenever a title insurer could claim that the insured ***might*** at some future point collect something on the "Indebtedness" from a source other than its insured deed of trust—even after the diminution in value of its insured deed of trust has been irrevocably fixed—such diminution in value would be irrelevant and the title

[17] Like Humpty Dumpty in Lewis Carroll's Through the Looking-Glass, ALTA essentially claims that: "When I use a word, it means just what I choose it to mean—neither more nor less."

insurer's indemnification liability for such loss would disappear.[18] Moreover, such a result would clearly nullify the purpose of the title policy to insure the validity and priority of the insured deed of trust.[19]

This purported "no-loss" argument would also render Condition 8(b)(ii) of the title policies meaningless. According to the express terms of Condition 8(b)(ii), since Commonwealth elected to litigate against the mechanic's liens but was "unsuccessful in establishing the Title or the lien of the Insured Mortgage as insured," the result is that "the Insured Claimant [has] the right to have the loss or damage [for which Commonwealth is liable] determined as of the date the claim was made by the Insured Claimant or as of the date it is settled and paid." The insureds thus have the express right here to have their losses and damages determined on the date when they made their claims in 2010, when both the "Indebtedness" under

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[18] ALTA is impermissibly reading into its title policy a non-existent "excess clause" under which the insurer is liable only after all other conceivable means of recovery on the "Indebtedness" have been exhausted. *See, Am. Family Mut. Ins. Co. v. Continental Cas. Co.*, 200 Ariz. 119, 121(App. 2001). ALTA could certainly have included such a clause, but did not do so. As explained in *Citicorp Savings of Ill. v. Stewart Title Guar. Co.*, 840 F.2d 526, 529, 531 (7th Cir 1988): "[ALTA] clearly did not [include such a provision] and ought not to gain through strained 'interpretation' what it failed to earn in the drafting."

[19] This argument also contravenes public policy because it would "provide the insurer with an opportunity to shield its eyes from the insured's actual, economic, and consequential losses." *Johnson Bank*, 239 Ariz. at ¶ 26 (citation omitted).

Condition 8(a)(ii), and diminution in value under Condition 8(a)(iii), were approximately $19.5 million.

The purported "no-loss" argument would also render Condition 11 of the title policies meaningless. According to Condition 11:

> **11. PAYMENT OF LOSS**
>
> When liability and the extent of loss or damage have been definitely fixed in accordance with these Conditions, the payment shall be made within 30 days.[20]

The "no-loss" argument would simply read this Condition out of existence—even when the amount of the insured's diminution in value damages is definitely and irrevocably fixed—whenever the insurer could claim that there is some chance (however remote) that the "Indebtedness" might be reduced in the future from some source other than the insured deed of trust.

ALTA's contention (at 2) that "the applicable language of the Policies and Arizona case law require proof of actual damages or loss as a prerequisite to coverage" is also incorrect. Notably, nothing in the title policies requires proof of loss or damage, let alone as such a prerequisite to coverage.[21] To the contrary,

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[20] The latest deadline for such payment, under any of the alternative deadlines from non-Arizona jurisdictions for measuring loss, would thus have been 30 days after Centerpoint was sold. Pursuant to *Johnson Bank*, however, under Arizona law the deadline for payment here was 30 days after policy issuance.

[21] ALTA itself declared in a Newsletter that a published decision was wrongly decided because in analyzing the applicability of Exclusion 3(c), the court was "ignoring the fact that proof of loss is not a coverage issue." APP054.

according to Condition 4 of the title policy the insurer may request a signed proof of loss from the insured, but only when "the Company is unable to determine the amount of loss or damage" itself. Here, the amount of loss or damage was readily apparent to Commonwealth, because the value of the insured deeds of trusts was $19.5 million "as insured," but $0.00 because of the $38 million in mechanic's liens that Commonwealth knowingly insured against. This was true from the moment the title policies were issued through the time when Centerpoint was sold.

Exclusion 3(c) of the title policies was waived because it was never disclosed or raised as a coverage defense by Commonwealth in the trial court, and cannot be resurrected by an amicus brief such as ALTA's. In any event, Exclusion 3(c) states that coverage for Covered Risks is excluded when the insured suffers no loss or damage. This is noteworthy in two respects. First, the fact that coverage is ***excluded*** when there is no loss or damage means that proof of loss or damage is not a "prerequisite to coverage." Coverage could not be excluded unless it already existed. Second, Commonwealth has the burden of proving that there was no loss or damage under Exclusion 3(c). *See Hudnell v. Allstate Ins. Co.,* 190 Ariz. 52, 54 (App. 1997) ("[T]he insurer has the burden of proving that a policy exclusion is applicable."). Nothing in the title policy requires the insured to prove to the contrary as a prerequisite to coverage.

ALTA blithely asserts (at 10) that "because the insurer in a lender's policy is insuring the amount of the loan only, the coverage automatically reduces over time as the loan is paid," supposedly forever (at least in ALTA's and Commonwealth's view). This assertion is misleading because the lender's title policy does not insure the loan; it insures the validity and priority of the insured deed of trust. "Coverage" is thus not reduced over time by payments on the loan. The amount of the outstanding "Indebtedness" on the subject loan is only relevant to computing the amount of the insurer's indemnification ***liability*** under Condition 8(a) of the title policies, as of the date upon which such liability is to be calculated pursuant to controlling law, i.e., the policy issuance date in this case.

CONCLUSION

The ALTA Brief magnifies the fatal flaws in Commonwealth's arguments. Sadly, but perhaps not surprisingly, the ALTA Brief also demonstrates that ALTA prefers to make duplicitous arguments about the meaning of its title policies on behalf of one of its members—even one acting in bad faith—rather than amending the language of its lender's title policy in a way that could support any of its current arguments. All relief requested in the ALTA Brief should be denied.

September 11, 2024

Respectfully submitted,

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The TITLE INSURANCE LAW NEWSLETTER

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Title Insurance

Use Restriction Does Not Make Title Unmarketable, But Might Be an Encumbrance

Chesapeake Land Development Company LLC v. Chicago Title Ins. Co., ___ F.Supp.3d ___, 2017 WL 5930295 (W.D.Okla. 2017) (permanent citation not yet available).

An Oklahoma court has said that, in that state, a use restriction does not make title unmarketable, but might be an encumbrance on title, and thus refused to dismiss a policy coverage lawsuit. The court declined to decide at this time if the restriction is outlawed under the marketable record title act; if it is, it is no longer an encumbrance.

Chesapeake Land Development Company bought two adjoining lots in Nichols Hills, Oklahoma in 2007. Both lots were made subject to use restrictions, one lot for park purposes and the other for use as a church. The use restrictions were contained in two successive pairs of deeds, recorded in 1954 and 1956.

Capitol Abstract issued a Chicago Title commitment to Chesapeake, excepting the 1956 pair of restrictions but not the 1954 set. Capitol's examiner allegedly told Chesapeake it would remove the exceptions if the restrictions were released by the seller, the First Church of Christ, Scientist. The church released the restrictions and Chesapeake bought the parcels for $10 million. The policy was issued without exceptions for either set of restrictions.

Chesapeake now claims that it did not know about the restrictions that allegedly benefit members of the Nichols family, reserved in the 1954 deeds. Chesapeake says it first learned of the Nichols restrictions when it was negotiating to sell the property in 2014.

Chesapeake submitted a policy claim. Chicago Title accepted the claim and elected to clear title under a reservation of rights, hiring a local attorney to seek to resolve the restriction issue. The sale allegedly died. Then Chesapeake sued Chicago Title for breach of contract and bad faith. The case is pending in Oklahoma federal court.

Chicago Title moved to dismiss, based on three grounds. First, the insurer said, the use restrictions did not make title unmarketable. It founded its argument mainly on the line of cases that have distinguished between matters affecting the use of property versus those that encumber title, including the recent Oklahoma decision of *Choate v. Lawyers Title Ins. Corp.*, 385 P.3d 670 (Okla. App. 2016). It also cited decisions holding that at least some recorded restrictions do not make title unmarketable. *Pavilion Park, LLC v. First Am. Title Ins. Co.*, 2011 WL 43222 (W.D. Ky. 2011); *McGonagle v. Stewart Title Guar. Co.*, 432 S.W.3d 535 (Tex.

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App. 2014); and *Camp v. Commonwealth Land Title Ins. Co.*, 787 F.2d 1258, 1261 (8th Cir. 1986).

The court agreed that the mere existence of the restrictions did not make title unmarketable. It said:

> *As noted, the facts of this case are dissimilar from those cited by defendant in that the restrictive covenants limit the actual use to which the property can be put rather than what could be built on it. They also do not affect access to the Property or relate to defects in physical conditions on it. However, the conclusion reached in those cases—that the phrase "unmarketability of the title" in title insurance policies relates to defects which adversely affect ownership rights, not defects which merely diminish the property's market value—applies here. "An individual [or entity] can hold clear title to a parcel of land, although the same parcel is valueless or considered economically unmarketable because of some restriction or regulation on its use." Bear Fritz Land Co., 920 P.2d at 762-63. The two restrictive covenants at issue may affect the manner in which the parcels can be used and their economic marketability, but they do not necessarily impact title to the property. See Woody Creek Ventures, 830 F.3d at 1217-18 (collecting cases). The court concludes the amended complaint does not state a basis for a claim based on the "unmarketability of the title" clause of the insurance policy.*

The court said, however, that that did not end the coverage issue. Chesapeake's complaint also alleged that there were "encumbrances" on its title. The court noted that the ALTA policy does not define the term encumbrance. Thus, it was forced to look to Oklahoma law, which says that a restrictive covenant creates an interest in real property in the nature of an easement. The court concluded that "the restrictive covenants alleged here are encumbrances within the meaning of the policy."

The court said it was not prepared on a motion to dismiss to rule on Chicago Title's second argument, that the 1954 restrictions were outlawed under the Oklahoma Marketable Record Title Act. Such a motion tests the facial sufficiency of the allegations by the plaintiff. The effect of MRTA would go below that surface.

In addition, the court dismissed Chesapeake's claim for a supposed second title issue, the possible claim by the City of Nichol's Hills to an implied easement for a jogging path around the property. This easement is not a recorded grant. The city has not formally asserted that it holds such an easement. The sale that Chesapeake claims to have lost was not due to the possible implied jogging easement. The court said the result was that Chesapeake simply had not alleged that it had suffered a loss due to the implied easement. Absent that allegation, the court said the easement claim was deficient, and dismissed it.

Finally, the court refused to dismiss Chesapeake's bad faith claim based on Chicago Title's argument that the Oklahoma Supreme Court has not and would not extend the tort of first party bad faith to a title insurance policy issued to a business. The insurer based its argument on the statement in the recent Choate appeals court decision that the "Oklahoma Supreme Court has not expressly held this duty is owed by title insurers to its insureds," although it does apply to most insurance policies. The federal court judge predicted that "the Oklahoma Supreme Court, if squarely presented with the question, would likely apply the implied duty of good faith to title insurers, just as it does with other types of insurers."

Title Insurance

Borrower Not a Beneficiary of a Loan Policy

Taylor v. JP Morgan Chase Bank, N.A., ___ F.Supp.3d ___, 2017 WL 5969818 (N.D.Ala. 2017) (permanent citation not yet available).

An Alabama court has ruled that a borrower is not entitled to receive anything from the insurer that issued a policy to his lender, and therefore the borrower cannot sue the insurer for unjust enrichment.

Gary Taylor got a loan and granted a mortgage on his house as collateral. Nine years later, in 2011, Taylor discussed the idea of a loan modification with the lender, Homecomings. In that conversation, Taylor raised an alleged problem with the legal description in the mortgage he had granted. Homecomings allegedly made a claim on the Fidelity policy. Taylor now asserts either that Fidelity did not pay the claim, or that it did but that Homecomings "did not record payment on the mortgage." The latter statement might be interpreted as alleging that Homecomings did not apply the claim payment to reduce the debt on the note. In any event, Homecomings sued Tayler several years later under the promissory note and got a money judgment in the amount of the debt.

Taylor then filed a second lawsuit, in which he named various parties including Fidelity. The court had previously dismissed most of the claims against Fidelity. In this decision, it dismissed the claim for unjust enrichment. The court noted that unjust enrichment requires proof that the defendant holds money that either belongs to the plaintiff or that the defendant induced the plaintiff to pay due to mistake or fraud. The court said that Fidelity did not have any of Taylor's money. Taylor had not alleged that he was entitled to be paid under the policy issued to his lender. The only money paid by Taylor to Fidelity was the $235 premium for the loan policy. The court said that fact led nowhere:

> *The existence of a title insurance policy in favor of the mortgage holder does not create any legal entitlement to Plaintiff. BARLOW BURKE, LAW OF TITLE INSURANCE § 2.01 TITLE INSURANCE DEFINED (3rd ed. Aspen Publishers ed., 3rd ed. 2017) ("As a general rule, an owner-mortgagor gains no rights as an insured when his or her mortgagee takes out a title insurance policy."). Plaintiff has not stated a claim for unjust enrichment.*

Title Insurance

Utah Court Addresses Date and Measure of Loss and Timeliness of Claim Payment

Marcantel v. Stewart Title Guar. Co., ___ F.Supp.3d ___, 2017 WL 5991734 (D. Utah 2017) (permanent citation not yet available).

A federal court in Utah has offered a number of interpretations of the policy's loss provisions.

Curt A. Marcantel bought property in Park City, Utah, in March 2015 for $1,775,000. He got a policy from Stewart Title. In September 2015, someone offered Marcantel $1.9 million for the property. The buyer then allegedly discovered that the property was subject to a sewer easement not excepted in the policy, and reduced his offer price to $1,250,000. A few days later, the buyer increased his offer to $1,400,000. Marcantel did not close with that would-be buyer.

Marcantel did not submit a claim immediately. In March 2016, he demanded that Stewart Title pay him $745,000 within 10 days. About two weeks later, Stewart Title acknowledged receipt of the claim. Less than a week later, on March 29, Marcantel sued Stewart Title for breach of contract and bad faith.

On April 26, Stewart Title accepted the claim and informed Marcantel that the insurer intended to get an appraisal to measure the diminution in value caused by the sewer easement. In June, Stewart Title sent Marcantel the appraisal, showing a difference value of $68,000, along with its check in that amount. The insurer said that Marcantel's acceptance of the check was conditioned on his signing of a release and assignment of subrogation claims.

Marcantel rejected the payment. Stewart Title moved for summary judgment in the policy lawsuit. The court granted part of the motion.

Stewart said it was entitled to judgment because it had paid the loss. Marcantel's first argument in response was that the insurer breached the policy because it did not pay him within 30 days of its acceptance of his claim. Marcantel relied on Condition 12 of the 2006 ALTA policy, which says that, "[w]hen liability and the extent of loss or damage have been definitely fixed in accordance with these Conditions, the payment shall be made within 30 days."

The court agreed with Stewart that something more than acceptance of the claim had to occur before the 30-day clock began running. It noted that Condition 12 says that loss is owed when the "extent of loss" is "definitely fixed." It said that this phrase made it clear "that liability and the amount of loss or damage must be clearly determined before the thirty-day period begins." However, the court went on to say that:

> *To find the method of definitely fixing liability and loss or damage, the court first looks to the policy conditions. Unfortunately, the conditions do not specify a particular method for fixing liability and loss or damage. Yet several conditions suggest how this might be accomplished. First, the policy expressly provides that Stewart Title may settle with Marcantel: "the Company shall have the following additional options ... to pay or otherwise settle with the Insured Claimant the loss or damage provided for under this policy... ." ... Once the parties agree on a settlement, the policy appears to require Stewart Title to make payment within thirty days because "the extent of loss or damage [would be] definitely fixed in accordance with these Conditions."... Next, in circumstances that differ from the present case, it appears that liability and loss or damage might be fixed by arbitration or litigation.*

Further, the court said, the final determination clause provides yet another trigger for the starting of the 30-day time limit.

In this case, Stewart Title had decided to resolve the claim by making a payment to the insured. Thus, the 30 days would begin running when the amount of the loss was "definitely fixed." Stewart Title asserted that the loss became fixed when it received its appraisal report. Marcantel provided no interpretation of the "definitely fixed" phrase in response, other than that his loss became payable when the insurer accepted the claim. The court said that "argument is unsupported by the language of the policy and lacks logical appeal." It said that Marcantel's position was wrong because "the policy does not allow the insured to unilaterally fix the amount of loss or damage by submitting a claim or having it accepted." Further, Marcantel's theory is contrary to the final determination clause, which plainly states that a loss is not payable immediately after the insurer accepts the claim if it elects to clear title.

The court said that the amount of the loss still had not become fixed, because "the parties do not appear to have ever ascertained the amount of loss or damage under the policy conditions." Further,

> *Marcantel's demand not only differs from the appraisal Stewart Title obtained, but it also differs from his later demands and his expert report. ... Under these circumstances, it would be absurd to treat Marcantel's loss or damage as fixed at the time he made his initial demand or even when Stewart Title accepted his claim. Thus, Marcantel's position is without support in the contract language and, if adopted, would deprive Stewart Title of the ability to exercise its express options under the contract.*

Stewart Title also asked the court to rule that the date of loss was the policy date, which was the date on which its appraiser had valued the property. The court correctly noted that the policy does not set a loss date, other than the two dates that apply if the insurer seeks to clear title but fails. The court said that those dates did not apply to this claim.

Stewart said that policy date as loss date was supported by the Utah decision of *Breuer–Harrison, Inc. v. Combe*, 799 P.2d 716 (Utah App. 1990). The court agreed with Marcantel, who contended that Breuer-Harrison said only that the policy protects against matters that affected title as of the policy date. The court also rejected Stewart Title's reference to the preamble to

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the covered risks page, which similarly says only that the policy protects against title defects that exist on the date of policy.

The court also ruled that there was a question of fact about the amount of loss. It said that the title insurer had not cited any "policy provision that fixes any specific formula or process for determining the amount of loss or damage Stewart Title must pay." Thus, although Stewart Title argued that Marcantel's theory about how loss is measured was incorrect, the court said it had no policy provision by which to interpret his theory.

The court's statement that the policy does not contain a provision setting the measure of loss is all the more remarkable because it then went on to rely on that provision, Condition 8, in holding that Marcantel was not entitled to be paid attorney's fees he had incurred in making his policy demand. The court ruled correctly that Stewart Title owed no attorneys' fees because such fees are payable only when the insurer accepts the insured's defense in litigation or when, under Condition 5(b), it agrees to pay fees to clear title. Marcantel claimed he could collect fees under Condition 8, which says that the insurer will "pay those costs, attorneys' fees, and expenses incurred in accordance with Sections 5 and 7 of these Conditions." The court said neither provision had been triggered:

> *... [T]he court finds Stewart Title did not bring or defend any suit to establish Marcantel's title in the subject property and did not authorize Marcantel to incur costs or attorney fees. Thus, the court finds Marcantel is not entitled to attorney fees under Section 8 of the policy conditions.*

Condition 8(a)(ii) is the measure of loss provision. It says that loss equals "the difference between the value of the Title as insured and the value of the Title subject to the risk insured against by this policy." Perhaps the court missed it because it is such a short statement about such an important and complicated subject.

The court reiterated the purported lack of a loss provision, or one about claim investigation, in discussing Stewart Title's request to dismiss Marcantel's bad faith claim. The court said the lack of any policy provision on those subjects created a question of fact about whether or not the insurer had conducted an adequate and timely investigation and had paid the full loss owed:

> *Stewart Title is not entitled to summary judgment on Marcantel's claim for breach of the implied covenant of good faith and fair dealing because there are questions of fact about whether Stewart Title reasonably and diligently in investigated and paid Marcantel's claim. "[T]he degree to which a party to a contract may invoke the protections of the covenant turns on the extent to which the contracting parties have defined their expectations and imposed limitations on the exercise of discretion through express contract terms." Smith v. Grand Canyon Expeditions Co., 84 P.3d 1154, 1159 (Utah 2003). Here, Stewart Title does not point to any policy provision that sets forth the method for calculating loss or damage under the policy. Nor does it cite to any provision setting a timeframe for its investigation. Instead, the policy appears to leave significant leeway for Stewart Title to evaluate and pay claims. The implied covenant of good faith and fair dealing requires Stewart Title to reasonably, and in good faith, evaluate and pay claims.*
>
> *As Marcantel points out, this is a highly fact-intensive inquiry. ... Here, Marcantel claims the actual amount a buyer offered before and after learning of the easement provides a proper calculation of damages. Stewart Title contends that its appraisal provides a proper basis for valuation. Stewart Title believes it was free to ignore Marcantel's evidence and pay only the amount of loss found in the appraisal. The court cannot find for Stewart Title on the current record. The policy does not specify any explicit method for calculating loss or damage. A jury will ultimately have to decide whether Stewart Title engaged in reasonable good faith efforts to value the property. Based on the foregoing, Stewart Title is not entitled to summary judgment on Marcantel's claim for breach of the implied covenant of good faith and fair dealing. No express contract term governed the calculation of loss or damage under the contract and the parties submit competing evidence about the proper valuation.*

This is one of the few decisions to hold that the lack of detailed policy terms concerning how a claim is processed, investigated, measured and paid leaves the insurer open to a bad faith claim, by failing to set objective and contractual standards and procedures. The title insurance business has had every encouragement to flesh out claim handling procedures in the policy but has yet to grips with the issue. The Texas-promulgated T-1 owner's policy does contain a claim investigation provision.

Title Insurance

Insurer in Transaction Gets First Dibs on Forfeited Money

United States v. Gettel, ___ F.Supp.3d ___, 2017 WL 3966635 (S.D.Cal. 2017) (permanent citation not yet available).

In a federal forfeiture, a title insurer that held a constructive trust on a certain parcel was entitled to the money from the sale of that property, in priority over other creditors whose losses could not be traced to that real estate.

Courtland Gettel was charged by the feds with conspiracy to commit wire fraud and criminal forfeiture, based on a fraud scheme in which Gettel bought distressed luxury homes in La Jolla and Del Mar, California and re-sold them for a profit. The fraud was in Gettel inflating the homes' value to lenders, concealing the actual purchase prices and other falsehoods.

Gettel scammed the lenders for about $33 million. Gettel entered into a plea agreement that admitted the facts about certain loans and purchases. When the feds shut him down, Gettel and his ex-wife were in escrow to sell a house in Coronado. The proceeds went into a bank account controlled by the United States Marshall Service, which held the money subject to the pending forfeiture action. In June of 2016, the court issued a forfeiture order and the government published notice that it was holding the sale proceeds under that order and inviting victims to step forward to claim the money. Eight parties, including several owners, lenders and one title insurer, claimed the money.

The court awarded the money to Stewart Title Guaranty. It had paid claims to three lenders swindled by Gettel. One insured, Partner's Capital, had lent money for the purchase of property in Del Mar. Stewart paid a loss because Gettel had concealed two prior deeds of trust on the Del Mar property from Partner's Capital. The court ruled that Stewart had an interest in the Coronado house because, on top of the other chicanery, Gettel had diverted the Partner's money to be used to buy the Coronado house.

The court held that Stewart Title was entitled to a constructive trust on the Coronado house because the Partner's money was used to buy it, and Partner's had not received a valid collateral interest in the Del Mar as promised.

The court rejected the other victims' argument that the money should be distributed to all of them pro rata. Under Title 21, United States Code § 853(n)(6), a person having a superior right, title or interest in the property is entitled to the proceeds of sale.

As a holder of a constructive trust on the house, Stewart Title had title to the Coronado house that was superior even to Gettel's title. Stewart Title's claim to the proceeds was better than that of the other creditors because they could not claim an interest in the house.

Title Insurance

Insurer-Subrogee Barred from Fixing Title After Insured Failed

Bank of New York Mellon v. Georg, ___ A.3d ___, 2017 WL 6421279 (Md.App. 2017) (permanent citation not yet available).

When the insured lender had already attempted to reform a mortgage to undo a tenancy that made the lien unenforceable, the title insurer that bought the loan was not entitled to bring a second action seeking the same remedy.

Heinz Otto Georg and his wife Susan M. Georg bought land in Cockeysville, Maryland and then borrowed about $800,000 as a construction loan and another $100,000 as a home equity loan. They both signed those mortgages.

In 2006, First Horizon agreed to make a refinance loan to be used to pay off both of the earlier loans. Only Heinz signed the new note and mortgage. However, both Heinz and Susan signed affidavits swearing to the unpaid balances on the loans that First Horizon would pay off. The loans were paid off and the new mortgage recorded. Old Republic issued a policy to First Horizon. Heinz and Susan made payments on the First Horizon loan for years. However, when they stopped paying and the servicer started foreclosure in 2009, the Georgs asserted that the mortgage was void because they held title as tenants by the entireties and Susan had not signed the mortgage.

The lender submitted a claim to Old Republic, which hired an attorney to seek to reform the mortgage and to claim a valid first lien by equitable subrogation. On the eve of trial, the lawyer asked the court to substitute the holder of the loan for the loan servicer as plaintiff. The Georgs' counsel lept on this opportunity, and asked the court to dismiss the case because the servicer had no standing to prosecute the trial. The court ruled that Susan Georg did not "know" enough about the loan to show her intent to be bound by the mortgage, so it refused to reform the instrument. The court also said this ruling was effectively contingent on whether or not the servicer had the right to serve as plaintiff.

Old Republic bought the loan. Then it filed a second action asking the court to rule that the mortgage was valid. In this 45-page decision, the court never even got close to deciding the merits of that rather simple issue. It stayed on the fringes, finding only that Old Republic was "in privity" with the insured, and therefore was judicially estopped from "relitigating" the issue of whether or not the mortgage was binding.

This is an ugly and frustrating decision. It transparently stitches together a series of errors and mishaps to deliver the borrowers the magical gift of a lien-free million-dollar house. The doctrine of tenancy by the entireties was not invented to deliver a lien-free house to spouses who shared equally in the benefit of the loan.

This decision also starkly illustrates the fact that a title insurer rarely is permitted to seek to clear title as subrogee, after the insured has already tried to do so.

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Agent Focus

Agent's Closing of His Own Loan Ends Badly

First American Title Ins. Co. v. Sadek, ___ F.Supp.3d ___, 2017 WL 6663899 (D.N.J. 2017) (permanent citation not yet available).

A person who owned both a mortgage banker and a title agency, and who closed a refinance loan to himself but failed to pay off the old loans or record the new mortgage, now owes the title insurer for conversion. The court will conduct a trial on the insurer's fraud claim and its request to make the debt exempt from bankruptcy discharge.

David Sadek owned and was president of First Financial Equities, a mortgage banker in Englewood, New Jersey. He, his wife Etty and his mother all were officers of and received salaries from Winthrop Abstract LLC in New York and Winthrop Abstract of New Jersey LLC. Those companies did all or most of the title work for Sadek's loan business.

The Sadeks also got loans through First Financial, which were then sold to investors. In 2005, the Sadek home in Teaneck, New Jersey had two mortgages on it. The Sadek "applied" with their own company for a refinance loan of $792,000. Winthrop Abstract did the title search and closed the loan. However, the title company did not pay off the two existing loans or record the new mortgage. Sadek sold the loan to National City Bank. Winthrop issued a First American title insurance policy to the lender although the mortgage had not been recorded.

Four months later, the Sadeks sold the house to Daniel and Tsipora Gurell. They issued a First American title commitment and policy to the Gurells that did not except any of the mortgages, recorded or unrecorded. The Sadek title agency handed over the net proceeds of almost $600,000 to the Sadeks. David Sadek kept making payments on the existing loans after the sale.

Eventually, the wheels fell off this scheme, and First American stepped in to protect its insureds. It sued the Sadeks for fraud, conversion and as assignee of the refinance loan. The Sadeks had taken refuge in bankruptcy court, so First American also asked the court to declare the debt to be non-dischargeable. The insurer moved for summary judgment.

The court granted the insurer a judgment based on conversion. It found that the insurer had proven the elements of that claim under New Jersey law, which is the taking of someone else's property without permission. Although the plaintiff must show intentional taking of property to establish conversion, it need not show fraudulent intent.

The court refused to grant First American summary judgment on its fraud claim, however. Sadek combatted the insurer's claim that he intended to deceive and bamboozle the lender and buyers with the assertion that he "was a busy businessman." This was his entire explanation for the fact that his title company breached its closing instructions by failing to pay off the existing loans and by not recording the new mortgage on the loan that Sadek then sold to a bank, and as to why Sadek had continued to send monthly payments for the next two and a half years on the loans that were not paid off.

The court admitted that the insurer "has put forward circumstantial evidence that Mr. Sadek committed common law fraud." However, because Sadek had made his "I'm so busy" statement under oath, the court said he was entitled to a trial on the fraud claim. It said it would rule on the discharge issue after trial. Of course, title people have seen people convicted and sentenced to long prison terms based on considerably less evidence.

This case is another example of the danger that a title insurer assumes in appointing as a title agent a person who owns a business that could profit from the ability to manipulate the representation of the state of title and the handling of closing money. If title insurers really want to put customers in the title business, they should spend the money to set up the systems required to keep their transactions honest. This would just require that company offices and employees collect premiums, issue policies and disburse closing funds. The bad people of this world would no longer be in a position put innocent buyers like Daniel and Tsipora Gurell at risk. The expense of such company operations would be less than the cost to repair the damage caused by fraudsters, not the least of which is the damage to the industry's reputation.

Other lines of insurance also sell through independent agents. However, in no other line of insurance does that independent sales agent issue the policy. Further, no other type of insurance agent handles the money for the closing of real estate sales, including people's homes. Title insurers care about protecting those precious assets. They must finally take the action needed to protect homeowners from the risks the title industry has itself created and fostered.

Agent Focus

Agent Not Entitled to See Privileged Documents in Loss Recovery Suit

First American Title Ins. Co. v. Bowles Rice, LLP, ___ F.Supp.3d ___, 2017 WL 6329953 (N.D.W.Va. 2017) (permanent citation not yet available).

A title agent was not entitled to see the insurer's claim documents and attorney communications in the insurer's suit against the agent to recover claim losses paid on risks assumed by the agent.

Longview Power decided to build a $2 billion coal-fired power plant in Maidsville, W. Va., with a $1.1 billion construction loan made by Union Bank of California. First American issued a $775 million loan policy to Union Bank that gave mechanic's lien coverage. The Bowles Rice law firm wrote the policy as First American's agent.

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Old Republic and Stewart Title entered into reinsurance contracts with First American.

Longview and the project had problems. Mechanic's liens of more than $335 million were filed in 2012. Union Bank made a policy claim in April of 2013. Longview filed for bankruptcy protection in August of 2013. Longview and First American had several lawsuits over policy coverage. First American also paid to dispute the priority of the deed of trust versus the mechanic liens.

In 2014, First American settled the lien and policy claims by paying $41 million "as part of a global settlement in the Delaware bankruptcy court," as this court explained. First American recovered a portion of its loss through its reinsurance contracts, but only after Old Republic and Stewart contested liability and forced First American to litigate the claims.

In turn, First American filed this lawsuit for breach of contract against Bowles Rice in 2016. It alleged that Bowles Rice knew that construction had started on the power plant before the deed of trust was recorded, which created the mechanic lien risk and was the basis for the reinsurers' claims that the underwriting risk had been concealed from them.

This decision does not go to the heart of the claims. Bowles Rice wants to know everything about the settlements made by First American with the lien claimants, lender and reinsurers. It asked for the entire claim file, including reserves information and all communication between the insurer and its counsel. First American objected that the information was not relevant, and was protected by the attorney client privilege and attorney work product doctrine.

Bowles Rice responded that it was entitled to this information to determine if the settlements were in good faith, and that First American had impliedly waived the privilege by putting the subject of the settlements at issue in this action. First American replied that it was only required to prove the "objective reasonableness" of its settlements, which did not require use of privileged documents.

The magistrate judge ruled in favor of First American. Bowles Rice filed objections with the district court, which rejected them.

The district court began with West Virginia law, that an indemnitee seeking repayment for the settlement of a claim covered by the indemnity must prove that the amount of the settlement was reasonable. The reasonableness standard is objective, not subjective. The court considers "the amount paid in settlement of the claim in light of the risk of exposure."

Bowles Rice argued that First American was required to show that it acted in "good faith" in order to recover, based on a reference to that term in one decision of the state supreme court. This court said that, actually, the high court does not require proof of subjective good faith, but rather "it appears to treat acts that are 'reasonable and undertaken in good faith' as one and the same."

Bowles Rice was particularly interested in seeing the First American reserves history. It speculated that, if the insurer quickly increased its reserves at time of settlement, this might indicate that the settlement was for an unreasonably high amount. The court turned to West Virginia decisions that have held that insurance reserves can be very relevant in certain cases but not at all in others, depending on the facts and issues. In this case, the court said, the reserves were not relevant, because the settlement amount was weighed against the insurer's exposure, not its prior claim expense estimates.

The district court also held that First American did not impliedly waive the attorney-client privilege by asserting claims or defenses that put the attorney's advice at issue in the case. The court noted West Virginia law holding that an attorney's advice does not become an issue in the case merely because what the lawyer advised might be relevant. The court relied on cases holding that an indemnitee does not waive the attorney-client privilege merely by seeking indemnity, in the course of which it will be required to prove the reasonableness of the settlement terms.

The court concluded that First American had not put its lawyers' advice at issue because it would not rely on that advice to prove the reasonableness of the settlement amount. It observed that it was Bowles Rice, not First American, that wanted to use the lawyers' advice, to attack the settlement rather than defend it.

Agent Focus

Insurer Must Prove Reasonableness of Claim Settlement to Recover From Agent

Colonial Title Company, LLC v. Commonwealth Land Title Ins. Co., 2017 WL 4675535 (Tex.App.-Tyler) (unpublished).

Texas law requires a title insurer to prove that it settled a policy claim prudently and in good faith as a predicate to recovering the settlement amount from the agent that caused the loss.

In 2001, Colonial Title Company LLC closed a refinance loan from Countrywide to William Henson that was supposed to have been secured by Henson's manufactured housing unit. The deed of trust identified the land but not the housing unit as the encumbered property. Colonial Title issued a Commonwealth policy to Countrywide.

Henson defaulted. Countrywide tried to foreclose. Henson filed an action claiming that the deed of trust was void under the Texas Constitution. At the time the loan was made, the Texas Constitution did not allow a lender to take a lien on homestead property for the refinance of the purchase price of a manufactured home. Countrywide made a policy claim to Commonwealth, whose claims counsel determined that the lien was void and that the error was the fault of Colonial Title.

Commonwealth gave two notices to Colonial Title about the claim. The agent did not respond or say that it disagreed with Commonwealth's analysis. The insurer then settled with the lender's assignee for policy limits of $46,510 plus

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attorney's fees and expenses of about another $25,000. Commonwealth then asked Colonial to reimburse it for the loss paid. When it refused, Commonwealth sued Colonial.

Both sides moved for summary judgment. The trial court granted Commonwealth's motion and entered judgment for roughly $71,000. Colonial appealed, and the court sent the case back with the instruction to the trial court to determine if the settlement was prudent and in good faith.

The appeals court imposed the good faith standard based on general Texas law of indemnity contracts. The rules on which the court relied are these:

> *Parties may include in [an] indemnification agreement the unconditional right of the indemnitee to settle a claim before the indemnitee's liability to the injured party has been judicially determined, thus immediately binding the indemnitor to reimburse the indemnitee for the sums paid out. ... Where an indemnitee voluntarily settles a claim of its indemnitor, absent an unconditional contractual right to settle, without obtaining a judicial determination of its liability, it assumes the burden in its action for reimbursement of proving that it was potentially liable to the claimant, the settlement was prudent and made in good faith, and the amount was reasonable.*

Colonial Title argued that Commonwealth did not prove the reasonableness of its settlement. The agent went further, arguing that the terms were *not* reasonable.

Commonwealth argued that it did not make a settlement, but rather paid what it was contractually obligated to pay the lender. Based on the rules stated above, the appeals court said that this was a settlement, because it *was not* the payment of a court order or judgment. However, the court noted that the policy says that loss is the lesser of three numbers, one of which is policy limits. The fact that Commonwealth "settled" with the insured for the amount dictated by the policy's terms was evidence that the settlement was reasonable. The court also said that the fact that the deed of trust was unconstitutional and void, which Colonial Title was given the right to dispute but did not, was further evidence that Commonwealth's decision to settle was reasonable.

However, the court said that, without evidence as to why Commonwealth paid policy limits versus the value of the land and house, the court said that fair minded jurors might disagree about the reasonableness of the settlement amount, precluding summary judgment in the insurer's favor.

The court did not address the statement from the Texas decisions that said that the indemnitor may dispute the reasonableness of the settlement when the indemnity does not contain a provision giving the indemnitee "an unconditional contractual right to settle." It is the editor's opinion, after having reviewed scores of agency contracts, that all or most such agreements do give the insurer the unfettered right to settle a policy claim without the consent of the agent. Such an unconditional right to resolve a policy claim is necessary for the insurer to know that it has the power to resolve the claim in good faith *toward the insured.* The title agent should not have the right to insert itself in the claim, because it has the self-interest of trying to limit the amount paid to the insured. See J. Bushnell Nielsen, *Title and Escrow Claims Guide,* 2017 Edition, American Land Title Association, 17.8.2, *Title Losses Payable By Agent*.

Escrow Matters

When Neither Party Prepared to Close, Neither Can Sue for Breach of Purchase Contract

Orlando Int'l Hotels, LLC v. Robert J. Guidry Investments, LLC (In re First Farmers Financial Litigation), ___ F.Supp.3d ___, 2017 WL 6026652 (N.D.Ill. 2017) (permanent citation not yet available).

When a purchase contract requires concurrent performance by buyer and seller as conditions to closing, but neither performs those duties, neither is entitled to sue the other for breach of contract. Instead, the contract is simply void and unenforceable by either side.

Orlando International Hotels LLC and Robert J. Guidry Investments LLC contracted to buy a Doubletree by Hilton Hotel in Orlando, Fla., after they submitted the winning bid of about $30 million in an online auction. The sellers were two receivers who had been appointed to get rid of the assets of Nikesh Patel and his company, First Farmers Financial LLC. Patel made millions by selling fake loans that were purportedly guaranteed by the federal government.

The buyers deposited about $1.5 million into escrow as a down payment. The escrow did not close on or before the contractual closing date.

The purchase contract said that the seller would deliver the deed to the buyer "concurrent with the delivery of the Cash to Close to the Seller," and set a date and time for closing. The seller was required to deliver title subject only to the permitted title exceptions.

The sellers sent a Fidelity title commitment that contained an exception for any appeal from the court order approving the sale by the receivers. The appeal exception was not a permitted exception. The buyers wanted the exception removed, which the sellers were unable to do by the closing date. Neither buyer nor seller showed up for closing or delivered the required deposits into escrow.

The day after the scheduled closing, the buyers sent a letter to the receivers saying that they were terminating the contract because of the sellers' breach of the title insurance closing condition and wanted their deposit back. About ten days later, the receivers wrote to say that they objected to the return of the deposit, and proposing a new closing date two weeks hence. Then, when the 30-day appeal period had expired, the sellers had Fidelity issue an amended commitment that dropped the appeal exception.

However, the closing still

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did not occur. Several months later, the court approved the sale of the hotel to another buyer for about $5 million less.

The buyers sued the receivers for the return of their earnest money deposit. Both sides moved for summary judgment, with each claiming that the other had breached the contract. The buyers and sellers agreed that the purchase contract created sequential duties leading to closing. However, they each claimed that the contract required a different sequence of events. The buyers said that delivery of a clean title commitment was a condition precedent to the buyers' delivery of the purchase money, and that the buyers were thus excused from performing. The sellers argued that they were not required to deliver clean title until the buyers delivered the money, and that the buyers suggested the appeal exception to Fidelity to disguise their own inability to come up with the purchase money.

Applying Florida law, the court held that the contract required both parties to perform simultaneously and that neither side had met its closing obligations. Thus, both breached the contract and had lost the right to enforce it. The court reviewed several decisions from Florida and other states that have adopted the principle that both parties must perform concurrently under real estate purchase contracts that contain time-of-the-essence provisions and where the buyer refused to deliver money because of a title issue that the seller could have solved with the purchase money. The court noted the California decision of *Pittman v. Canham,* 3 Cal.Rptr. 2d 340 (Cal. App. 1992), in which the court explained that, while the buyer may have been reluctant to make the deposit into escrow, "in a contract with concurrent conditions, the buyer and seller cannot keep saying to one another, 'No, you first.'" The *Pittman* court held that the "failure of both parties to perform concurrent conditions during the time for performance results in a discharge of both parties' duty to perform."

This decision provides a very scholarly analysis of this thorny issue, which can also be a malpractice trap for the unwary lawyer.

Conveyance News

Borrower Cannot Worm Out of Mortgage Based on Acknowledgment Omission

Central Mortgage Co. v. Seye, ___ N.E.3d ___, 2017 -Ohio- 8713, 2017 WL 5713411 (Ohio App. 10 Dist. 2017) (permanent citation not yet available).

An Ohio court has wisely ruled that a borrower may not have his own mortgage declared void due to an inadvertent blank space in the acknowledgment, since the sole purpose of the acknowledgment is to provide a safeguard against forgery and a mortgage is enforceable against the borrower even without notarization.

Mamadou Seye and Mohamad Kebe got a loan secured by their house in Ohio. They defaulted. The holder of the loan, Central Mortgage, filed a foreclosure action. Seye and Kebe filed counterclaims and third party claims against the lender, closing company and title insurer. Their one claim relevant to this article was that their names had not been typed into the acknowledgment block on the mortgage.

After dismissing the borrowers' claims, the court entered a judgment reforming the mortgage to include the borrowers' names in the acknowledgment based on mutual mistake. Seye and Kebe appealed, and the court affirmed.

The court began by noting the applicable statutes. Ohio's R.C. 5301.01(A) says that a deed, mortgage, land contract or lease shall be acknowledged before a notary public, who shall certify and sign the certificate of acknowledgement. R.C. 2719.01 says that a written instrument containing an omission or error is still to be construed to give effect to the parties' intent.

Then the court the addressed the reason why the statutes require an acknowledgment, which is to protect against forgery:

> *The Supreme Court of Ohio has noted that the acknowledgement required by R.C. 5301.01 "is for the purpose of affording proof of the due execution of the deed by the grantor, sufficient to authorize the register of deeds to record it." Basil v. Vincello, 50 Ohio St.3d 185, 188 (1990). Further, "'a defectively executed conveyance of an interest in land is valid as between the parties thereto, in the absence of fraud.'" Id. at 188-89, quoting Citizens Natl. Bank v. Denison, 165 Ohio St. 89, 95 (1956). It has been noted that "[t]he reasoning behind such a rule is to bind the parties to that which they intended." Seabrooke at 169. Thus, while "[t]he purpose of the acknowledgement statute (R.C. 5301.01) is to provide evidence of execution and authority for recordation," it is not intended "to provide a way of escape for a party who later wishes to renege on his agreement." Id.*
>
> *Accordingly, in the absence of fraud, a defect resulting from the failure to include a notarized acknowledgment of a signature "does not render the terms of the mortgage unenforceable as between the parties." Everbank v. Fleming, 2d Dist. No. 2012-CA-10, 2013-Ohio-3030, ¶ 5. Ohio courts have therefore upheld the validity of a mortgage despite a defect in the acknowledgement clause.*

This is a refreshing and excellent decision, particularly because it elevates substance over form using the correct legal analysis. The lender was ably represented by Adam J. Turer of Lerner, Sampson & Rothfuss and Michael J. Sikora, III, Richard T. Craven and C. Richley Raley, Jr. of Sikora Law LLC.

This decision contrasts with many others, which are appalling in their perversity. Many courts, particularly bankruptcy judges, regularly declare mortgages to be void or unenforceable solely because

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of some small inadequacy in the acknowledgment. Those courts forget, or do not care, that legislatures required acknowledgments to be affixed to recorded instruments only as a protection against forgery. Further, although the office of notary has existed since Roman times, the recent advent of electronic signatures and the idea of virtual closings has so compromised the notarial act that state legislators should be considering whether to repeal these recording laws. Your editor finds amusing the notion that a digital signature can truly be acknowledged, given that no physical signature is affixed and there is no paper document being signed.

Conveyance News

Lender Does Not Get First Lien Without First Proving That Its Mortgage Is on Correct Lot

West RADC Venture 2010-2, LLC v. Indymac Venture, LLC, 2017 WL 6273838 (Cal.App. 4 Dist.) (unpublished).

A lender that apparently took a deed of trust on the wrong lot, by mistake, cannot establish its "priority" over another deed of trust on the same lot without first proving that its security instrument was recorded against the correct parcel.

In 2004, Frank Eder owned two adjacent vacant lots in Rancho Mirage, California that are legally described as Lots 16 and 17 in a certain tract. Their street addresses are 68 and 70 Royal Saint Georges street.

Eder got two loans on the same day, each secured by one of the lots. One deed of trust referred to the property as Lot 16, having a street address of 70 Royal Saint Georges. The other deed of trust described the property as Lot 15, with a street address of 68 Royal Saint Georges. Title people know the punch line: the descriptions and addresses were flipped. The question is which identifier is correct for each loan.

Eder later said that the street addresses were correct when he signed the deeds of trust. A "loan processor" later attached the legal description pages, and stapled them to the wrong instruments. Both loans were sold to what became AmTrust Bank.

In 2007, Eder borrowed about $3 million from Indymac Venture and built a house at 68 Royal Saint Georges. That deed of trust used that street address and its correct corresponding parcel number, Lot 16. Indymac demanded a first lien. AmTrust issued a payoff letter that identified the loan only by loan number and the street address of 68 Royal Saint Georges. After making the payoff, Stewart Title recorded a release of the deed of trust that had referred to Lot 16.

In 2008, Eder and AmTrust signed a loan modification for its remaining loan, which should have been secured by Lot 15. They recorded two documents evidencing the loan mod. Both described the property as Lot 16. Eder noticed the problem and told AmTrust, but the lender did not straighten the issue out. AmTrust failed, and the FDIC sold the loan to West RADC Venture 2010-2.

Eder also borrowed more money from another lender, secured by a deed of trust against Lot 15 (likely because that lot appeared to be free and clear). Then Eder defaulted on all three loans. The other lender foreclosed on Lot 15 in 2010, preventing West RADC from imposing its security interest on what appears to be the intended lot.

Therefore, West RADC brought an action seeking a judgment declaring that it had the first lien on Lot 16, and thus had priority over the $3 million deed of trust held by Indymac Venture. The trial court granted summary judgment to West RADC, viewing the issue as a simple question of lien priority. The court granted West RADC a priority interest on Lot 16, including the valuable house built with Indymac's money.

Indymac appealed. In a lengthy and astute opinion, the appeals court held that this was not simply a question of priority:

> *Indymac is correct—priority and property rights are distinct issues. The recording laws generally do not govern the creation of interests in real property. Rather, they affect the priority of interests by defining when a person is deemed to have constructive notice of another interest in the property. (4 Miller & Starr, Cal. Real Estate (4th ed. 2016) § 10.1, pp. 10–11 to 10–12... .*
>
> *"Recording itself does not grant an interest in property...." ... Accordingly, before determining the priority of competing trust deeds, the court must first determine whether the party claiming lien priority has a security interest in the subject property. ...*
>
> *West RADC may be correct that recording and indexing its trust deed in the lot 16 chain of title provides constructive notice of the content of that trust deed. ... However, in this case, where the trust deed contains inconsistent descriptions of the encumbered property, the question remains—on what property does West RADC have a security interest? Recording and indexing West RADC's trust deed in the lot 16 chain of title does not answer that question. The threshold issue in this case is a contract interpretation question, not a priority question. And the contract interpretation issue is determined, not by the act of recording or indexing the trust deed, but by its terms and properly admissible extrinsic evidence of the parties' intent. ...*
>
> *Thus, while it may be true, as West RADC asserts, that Indymac took its interest " 'subject to' the interest of the West RADC [d]eed of [t] rust," the starting point is: Exactly what is the property interest created in the West RADC deed of trust? Is it an encumbrance on lot 15? Or is it on lot 16? Unless and until that question is answered, a discussion of priority is premature.*

The court held further that the West RADC deed of trust was ambiguous because it contained inconsistent descriptions of the property it

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encumbered. This fact further supported the conclusion that the deed of trust did not give unequivocal notice that it affected Lot 16. The court also buttressed its rulings with the testimony of Mr. Eder about his intent and the initial mistake, as compounded by AmTrust's later actions.

This is a thoughtful decision on a subtle issue that recurs in title claims but is rarely addressed by the courts.

Indymac was very capably represented by Lori C. Hershorin of Hershorin & Henry.

Conveyance News

Inflated HOA Lien Boomerangs on Filers

402 Lone Star Property, L.L.C. v. Bradford, 2017 WL 5759379 (Tex.App.-San Antonio) (unpublished).

The high bidder at a homeowners' association lien foreclosure sale, by demanding an inflated price to redeem, was found to have recorded a fraudulent lien. This subjected the bidder to statutory penalties and punitive damages of many times the lien amount.

Barry Bradford owned a home in San Antonio. He did not pay his homeowners' association fees. The association filed a lien and conducted a foreclosure sale. 402 Lone Star Property LLC, whose sole member is Craig Otto, bought at the sale.

Two days after the sale, Otto posted a notice on Bradford's door, telling him that, if he did not clear out quickly, Otto would file a forcible detainer action and have him thrown out. Bradford called a lawyer, who told him that Texas allows a home owner to redeem after such a sale. The lawyer sent a letter to Otto telling him that Bradford intended to redeem under section 209.011 of the Texas Property Code and asking for a statement of the redemption amount.

Instead, Otto posted another notice to vacate on Bradford's door, giving him three days to move out. A few days later, Otto filed a forcible entry and detainer action in justice court and posted a copy of the petition on Bradford's door. Several days after that, Otto sent the lawyer a Redemption Payoff Statement saying that Bradford could redeem for about $6,000. The lawyer sent Otto a check in the demanded amount. Otto dismissed the case and recorded a deed conveying the house back to Bradford. Then the worm turned.

Bradford sued Otto and his company for having inflated the redemption price, claiming common law fraud and the filing of a fraudulent lien. The case went to a jury trial. The jury awarded about $2,000 in actual damages for fraud, $20,000 in statutory penalties and $25,000 in exemplary damages for the fraudulent lien claim, $15,000 in attorney's fees and court costs.

Otto appealed. The appeals court struck some of the judgment as being double recovery for the same damages. It otherwise affirmed the judgment, however, including the finding that the inflated redemption demand was a fraudulent lien. The court said that Bradford was entitled to keep the larger of the two awards.

Otto argued that he did not understand the law that limited what he could demand as a redemption amount, and therefore he did not intentionally seek more than the law allowed. The appeals court said there was sufficient evidence to suggest to the jury that Otto knew he was overcharging for items such as the recording fee, so it upheld the finding that Otto had overcharged on purpose.

Otto also argued that the redemption statement was not filed or recorded, and thus was not a fraudulent lien under the Texas statute. The appeals court sidestepped the issue, saying only that the jury "could also infer that the Company and Otto intended for the Redemption Statement to be given the same legal effect as a court record or document by" mailing the statement after posting the notice to vacate on Bradford's door.

Otto also disputed the $20,000 penalty awarded by the jury for the statutory fraudulent lien claim. The law sets the penalty at the greater of $10,000 or the actual damages incurred by the lien recording. The jury reached the $20,000 award by penalizing both Otto and his company. Bradford countered that the law says that each "person" who files a fraudulent lien is liable in the statutoryno amount. Based on a 2012 decision, the court said that the jury could impose separate penalties against Otto and his company.

Finally, Otto said that the $25,000 award of exemplary damages was grossly excessive and unconstitutional. The key was the ratio. Otto compared the $20,000 statutory penalty plus the $25,000 exemplary damage award to the actual damages of $1,359.22 to conclude that a 33 to one ratio exceeded the constitutionally acceptable limit for exemplary damages. The appeals court disagreed, because the $20,000 award was a penalty, not exemplary damages. It said that it did not need to consider the issue further because Otto had not argued that a $25,000 exemplary damage award would be unconstitutional.

Given the current flurry of lawsuits around the country concerning homeowners' association liens, which has led scavengers to bid at those sales, this decision provides some valuable insights for both bidders and home owners.

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THE TITLE INSURANCE LAW JOURNAL

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Latest Developments in Nevada HOA Lien Coverage Actions

Wells Fargo Bank, N.A. v. Fidelity Nat'l Title Ins. Co., Case 3:19-cv-00241-MMD-CSD, order issued on September 20, 2022; TRP Fund VIII, LLC v. Bank of America, N.A., 2022 WL 17829029 (Nev.) (unpublished)*; PennyMac Corp. v. Westcor Land Title Ins. Co.,* (Eighth Judicial District Case No. A-18-781257-C, 2021 WL 5492852*; U.S. Bank, N.A., as Trustee v. Stewart Information Systems Corp.,* ___ F.Supp.3d ___, 2022 WL 17253787 (D.Nev.) (permanent citation not yet available).

This article will address numerous recent developments in the pending actions in Nevada concerning the coverage allegedly afforded by various endorsements for post-policy super-priority assessment liens.

These coverage issues stem in part from the 2014 decision by the Nevada Supreme Court, *SFR Investments Pool 1 v. U.S. Bank, N.A.*, 334 P.3d 408 (Nev. 2014). In SFR, the court construed the special version of the Uniform Common Interest Ownership Act adopted in Nevada. The uniform act promulgated by NCCUSL grants automatic priority to a first deed of trust or mortgage over all assessments levied after the security instrument is recorded. The *SFR* court held that the Nevada legislature had tinkered with that formula, by giving up to nine months of HOA assessments priority over a first deed of trust. Further, the court held that the effect of the super-priority assessment lien provision was not just to prevent the lender from foreclosing out those liens, but that the association could conduct a sale of its super-priority lien and extinguish the first position deed of trust. In addition, the Nevada high court held that provisions in recorded declarations subordinating the assessment liens to first position deeds of trust were for some reason unenforceable.

As this newsletter has described in past articles, the *SFR* decision has led to two large waves of lawsuits. The first was litigation over the effect of trustee sales conducted by associations on first deeds of trust. Those lawsuits produced several important rulings, including the Nevada Supreme Court's 2018 holding that the

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J. Bushnell Nielsen serves as editor. Please submit news and guest columns to **bnielsen@reinhartlaw.com**.

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lender can protect against foreclosure by tendering the amount of the super-priority assessments to the association before the association sale is conducted. See *Bank of Am., N.A. v. SFR Invs. Pool 1, LLC*, 134 Nev. 604, 612, 427 P.3d 113, 121 (2018), often called *SFR II*. Lenders continue to prevail over HOA sales based on the tender doctrine. See *TRP Fund VIII, LLC v. Bank of America, N.A.*, 2022 WL 17829029 (Nev.) (unpublished), issued on Dec. 15, 2022.

The second wave of litigation concerned lenders' title insurance policy coverage. Many of the earliest coverage actions were filed in or removed to federal court. A number of the cases were assigned to Chief Judge Miranda Du. On October 29, 2019, Judge Du issued a decision in *Wells Fargo Bank, N.A. v. Fidelity Nat'l Title Ins. Co.*, Case 3:19-cv-00241-MMD-CSD. In that decision, reported at 2019 WL 5578487, Judge Du held that neither the CLTA 110 endorsement nor the CLTA 115.2 endorsement assured the priority of the insured deed of trust over assessments levied after date of policy and foreclosed by the association. Judge Du also rejected the lender's argument that the Nevada law should be interpreted as declaring that all HOA assessment liens take their priority from the date of recording of the declaration that creates the association.

Judge Du then issued a series of decisions in which she summarily dismissed coverage actions brought by other lenders, based on the rulings in the *Wells Fargo* decision. Wells Fargo appealed to the Ninth Circuit. After that appeal was filed, many coverage actions were stayed pending the outcome of the *Wells Fargo* appeal, which the courts and the parties believed would be the pivotal coverage decision.

Judge Du also broadened here original ruling to fold in other endorsements. In *HSBC Bank USA, N.A. v. Fidelity Nat'l Title Ins. Co.*, 2020 WL 886940 (D.Nev. 2020), she ruled that there also was no coverage for post-policy assessment lien priority under the CLTA 100.13 endorsement. That endorsement provides the following coverage:

> The Company hereby insures the owner of the indebtedness secured by the insured mortgage against loss or damage which the insured shall sustain by reason of the lack of priority of the lien of the insured mortgage over the lien of any assessment which may be fixed or levied prior to acquisition of title by the insured… .

The 100.13 endorsement is designed to provide an assurance as to assessments levied under an instrument excepted in Schedule B. In the policy at issue in *HSBC*, the endorsement referenced not the declaration creating the homeowner association, but Exception 11, which was for an avigation easement in favor of the operators of a nearby private airport. Judge Du concluded that "Endorsement 100.13 is irrelevant here because it provides coverage for damages specifically sustained from a specific kind of aircraft-easement lien."

After many pending federal court cases were stayed, lenders began filing actions in state court instead. The lenders also took up the practice of suing both the title insurer and the local title agency that issued the policy, at least when that company was a Nevada-domiciled company. The astute counsel for the title insurers moved for so-called snap removal to federal court in a number of those actions. As several prior articles in this newsletter reported, those cases forced the Nevada federal judges to adopt a position for the first time on the doctrine of snap removal. All or most of the judges ruled that snap removal is not permitted, and that the local title agents had not been joined fraudulently in order to frustrate federal diversity jurisdiction. Those cases were remanded to state court.

While the *Wells Fargo* appeal was pending, lender's counsel was seeking ammunition to undermine Judge Du's reasoning concerning the coverage of the endorsements. Those lawyers used discovery in other cases to compile a hodge podge of bulletins and memos issued by title insurers, that instructed offices and agents the circumstances under which they could be issued.

In April 2021, HSBC Bank submitted those bulletins to Judge Du in support of its motion for reconsideration of her dismissal of its action based on the reasoning in *Wells Fargo*. In her decision on that motion, *HSBC Bank USA, N.A. v. Fidelity Nat'l Title Group*, 2021 WL 1579896 (D. Nev. Apr. 22, 2021), Judge Du announced that she would consider this evidence if the *HSBC* case was remanded to her. She referred to the bulletins as "claims manuals." Judge Du said:

> Although it is a close call, the Court will consider the evidence newly discovered and that it could potentially

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> change the outcome of the dismissal order as to the bad faith claims.

On Nov. 5, 2021, the Ninth Circuit finally issued its decision in the *Wells Fargo* appeal. *Wells Fargo Bank, N.A., as Trustee v. Fidelity Nat'l Title Ins. Co.*, 2021 WL 5150044 (9th Cir. (Nev.)) (unpublished). The decision was short and simple. The court remanded the case to Judge Du. The Ninth Circuit had, on appeal, supplemented the record by taking judicial notice of the same bulletins submitted to Judge Du in the *HSBC* reconsideration motion. The court quoted liberally from her April 22 *HSBC* ruling, which the appellate justices interpreted as suggesting that Judge Du might alter or reverse her rulings that were the subject of the appeal. The Ninth Circuit made this further comment about the bulletins:

> Moreover, Fidelity's claims manuals are clearly relevant to Wells Fargo's claims in this case. In a related case with identical claims against Fidelity, we held that the Fidelity insurance claims manual is "probative of a variety of insurance products Fidelity offered that provide title insurance for property located within a homeowners' association." *Deutsche Bank Nat'l Tr. Co. v. Fid. Nat'l Title Ins. Co.*, No. 20-15849, 2021 WL 5002215, at *1 (9th Cir. Oct. 28, 2021). Thus, the manual is clearly probative to the same claims that Wells Fargo raises here. For instance, the manual could be read to support the amendment of Wells Fargo's statutory claim for unfair claims settlement practices and misrepresentation under NRS § 686A.310. Similarly, since Nevada law permits courts to consider the custom and practices of the trade even when construing a contract that is unambiguous in its terms, see *Galardi v. Naples Polaris, LLC,* 301 P.3d 364, 367 (Nev. 2013), the manual might be relevant to the breach of contract claim as well.

During the two-year *Wells Fargo* appeal period, the cases filed in state courts moved along, and resulted in at least several trial court decisions construing the coverage of various endorsements. Perhaps the leading such decision was issued on October 22, 2021 by Clark County District Judge Adriana Escobar, in *PennyMac Corp. v. Westcor Land Title Ins. Co.*, (Eighth Judicial District Case No. A-18-781257-C, 2021 WL 5492852. Judge Escobar ruled that there was no coverage for post-policy assessments liens under the CLTA 100 and CLTA 115.2 endorsements. That case was appealed to the Nevada Supreme Court as Case No. 83737.

After the *PennyMac* appeal was taken, a number of cases in both state and federal court were stayed pending the Nevada Supreme Court ruling in that case. See, for example, *U.S. Bank, N.A., as Trustee v. Fidelity Nat'l Title Ins. Co.*, 2022 WL 3346959 (D.Nev.) (Judge Gloria M. Navarro, issued August 11, 2022); *U.S. Bank, N.A., as Trustee v. Fidelity Nat'l Title Group, Inc.*, 2022 WL 17093198 (D.Nev.) (Judge Cristina D. Silva, issued November 21, 2022); and *Deutsche Bank Nat'l Trust Co. Americas, as Trustee v. Fidelity Nat'l Title Group, Inc.*, 2022 WL 3229180 (D.Nev.) (Judge Gloria M. Navarro, issued August 10, 2022).

On Sept. 20, 2022, Judge Du issued an order in the remanded *Wells Fargo* case, following a renewed motion to dismiss the case. The order is not available on Westlaw, although numerous decisions that are on Westlaw have since been issued, referring to the order. The order is Document 52 in the Pacer docket for the case, which is Case 3:19-cv-00241-MMD-CSD in the United States District Court for the District of Nevada.

Judge Du's decision was based primarily on the industry writings submitted by Wells Fargo's counsel. Whereas Judge Du and the Ninth Circuit had previously referred to a "fidelity claims manual," the judge now listed those materials as being 2013 endorsement manuals issued by Chicago Title and Fidelity; a 2009 Fidelity endorsement guide; an article by James Gosdin entitled *The 2006 ALTA Forms*; Stewart Title bulletins issued in 1991, 1993 and 2014; and a LandAmerica underwriting manual. The judge described the manuals and bulletins as being "guidelines for underwriters to understand the scope and effect of the endorsements."

The Wells Fargo policy contained five endorsements. The judge said that two were "relevant," being the CLTA 100 and the CLTA 115.2 (which she now described as being an ALTA 5 endorsement). The judge changed her mind only as to one clause, finding that there was coverage for the assessment liens under paragraph 1(a) of the CLTA 100 endorsement. She found no coverage under paragraph 2(a) of the CLTA 100, or the ALTA 5.

The judge began by noting that, in 2019, she had ruled that the lender's loss was caused by the change in the law wrought by the 2014 *SFR* decision, not by the declaration that created the homeowner association. She noted that she and other judges had used the same reasoning in other cases, such as *Wells Fargo, N.A. as trustee for Option One Mortgage Loan Trust 2007-5 Asset-Backed Certificates Series 2007-5 v. Fidelity Nat'l Title Ins. Co.*, Case No. 3:19-cv-00241-MMD-WGC, 2019 WL 5578487; and *Wells Fargo Bank, N.A. v. Commonwealth Land Title Ins. Co.*, Case No. 2:18-cv-00494-APG-BNW, 2019 WL 2062947 (D. Nev. May 9, 2019). However, she said,

> But when those cases were decided, neither this Court nor the other in this District considered the trade usage evidence Plaintiff now provides. Moreover, the Court takes this opportunity to reconsider whether the endorsements, as construed under Nevada's principles of contract interpretation, provide coverage for losses sustained by a joint working of CC&Rs and NRS § 116.3116.

Now, she said, she had concluded that the lender's loss was caused by the declaration and the statute "operating together."

This seeming innocuous statement was the necessary springboard for the court to reach its misguided conclusion that paragraph 1(a) of the CLTA 100 endorsement gives post-policy lien priority coverage. Paragraph 1(a) indemnifies the insured lender

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against loss caused by:

> The existence of any of the following: (a) Covenants, conditions or restrictions under which the lien of the mortgage referred to in Schedule A can be cut off, subordinated, or otherwise impaired… .

This protection is against a covenant or restriction that can "cut off" the insured mortgage. Title insurance people have always recognized that this coverage protects against a violation of a use restriction that causes the borrower's title to revert, which also voids the lien of a mortgage granted by the borrower, cutting off that lien. The use of the phrase "existence of" implies that the coverage goes beyond a pre-policy violation of the restriction, and instead indemnifies the lender against the *existence* of such a restriction on the Date of Policy. The terms assessment lien and association do not appear in this coverage; nor does the paragraph provide any coverage for priority of one lien versus another lien.

However, the court said that Fidelity asserted that paragraph 1(a) did not apply because the Nevada statute created the association super-priority assessment liens, not the declaration, while the lender predictably argued that it was the declaration that "was operative in creating the lien that the HOA later foreclosed upon." The court used that oblique reasoning to reach this conclusion:

> Because the CC&Rs authorized the creation of the lien that NRS § 116.3116 permitted to take superiority status over and eventually extinguish the deed of trust, the Court agrees with Plaintiff.

Judge Du acknowledged that she had simply revised her view about how the statute related to the terms of the declaration in imposing the super-priority assessment liens, saying:

> The Court takes this opportunity on remand to revise its reasoning and finds Plaintiff's argument that the CC&Rs and NRS § 116.3116 are symbiotic is persuasive.
>
> The CC&Rs clearly state that an HOA lien may be levied and enforced against a property for the payment of delinquent assessments. … Article IV Section 11 subsection g further states that once an assessment is deemed in default, "any officer of the [HOA] shall be permitted to authorize foreclosure proceedings for the purpose of collection of said delinquency." … Absent the CC&Rs, the HOA could not have levied the assessments that later formed the lien. But absent the statute, the superpriority portion of the HOA lien authorized by the CC&Rs would not have taken priority over the prior recorded first deed of trust. The CC&Rs and the statute therefore operated together to create the conditions which caused Plaintiff's loss.

The court then announced that the endorsement somehow gave coverage against post-policy liens because it protected against an aspect of the declaration:

> The phrasing of the endorsement further suggests that it is intended to cover situations where something—like the statute—works together with the CC&Rs to cut off or subordinate Plaintiff's interest some time after the Date of Policy. … This is because the endorsement uses the phrasing "can be cut off…" (Id.) This unequivocally describes something that may—but is not certain—to happen in the future. It accordingly logically describes what actually happened here: the CC&Rs and the statute effectively worked together to cut off Plaintiff's predecessor-in-interest's deed of trust.

The court further proclaimed that Fidelity's endorsement manual buttressed its position:

> And Plaintiff's proffered trade usage evidence also supports this result. Indeed, Fidelity National Title's Endorsement Guide states the CLTA 100 "[p]rovides comprehensive coverage for insured ALTA lender against loss by reason of present or future CC&Rs violations[.]" … The endorsement ensures "[t]here are no CC&Rs under which the lien of the insured mortgage can be cut off, subordinated or impaired." (Id.) This further suggests the CLTA 100(1)(a) endorsement covers Plaintiff's loss.

The fascinating aspect of the last ruling is that the statement quoted from the manual does not support the court's interpretation of the coverage in any way. The court closed its analysis with this seeming tautology:

> If the CC&Rs did not exist, no assessments would have been levied. The delinquent assessments provided grounds for establishing the HOA lien, the foreclosure of which would necessarily subordinate the first deed of trust, per NRS § 116.3116(2). Defendant therefore has not shown that CLTA 100(1)(a) does not provide coverage for Plaintiff's loss as a matter of law. Indeed, the Court rules to the contrary—CLTA 100(1)(a) covers Plaintiff's loss.

Judge Du found no coverage for the assessment liens under paragraph 2(a) of the CLTA 100 or the CLTA 115.2 endorsement, however. Paragraph 2(a) of the CLTA 100 indemnifies the insured lender against:

> Any future violations on the land of any covenants, conditions or restrictions occurring prior to an acquisition of title to the estate or interest referred to in Schedule A by the insured, provided such violations result in impairment or loss of the lien of the mortgage referred to in Schedule A, or result in impairment or loss of the title to the estate or interest referred to in Schedule A if the insured shall acquire such title in satisfaction of the indebtedness secured by the insured mortgage[.]

Fidelity argued that this

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coverage was not invoked because Wells Fargo did not come into title to the property on foreclosure, and because coverage is limited to "future violations *on the land*."

The court did not agree that the lender's taking of title was a condition to coverage. It said instead that the phrase was "a temporal modifier of when coverage may apply." That would appear to be a distinction without a difference. However, the court did agree that "an HOA lien is not a violation 'on the land.'" The court explained its reasoning as follows:

> To elaborate, the Court is persuaded by Defendant's argument that CLTA 100(2)(a) must be describing some sort of future, physical violation, such as building a shed that violates the CC&Rs. … This endorsement would provide coverage in that event. But mere nonpayment of HOA dues, such as those that eventually led to this dispute, is not covered by this endorsement because nonpayment of dues is not any sort of physical violation that could reasonably qualify as a violation "on the land." Indeed, the sort of violation that led to this dispute is covered by another provision of this same endorsement—as explained above—instead of this one. And 'on the land' suggests a physical violation from its plain meaning as well. After all, land is physical.

The court also agreed with Fidelity's argument that "[a] ll provisions of CC&Rs are covenants running with the land so the inclusion of the phrase 'on the land' must have been done with a specific purpose."

Judge Du also held that the CLTA 115.2 endorsement (which she labeled as the ALTA 5) provided no post-policy assessment priority coverage. Wells Fargo argued that this coverage was given in paragraph 2 of the endorsement, which indemnifies the insured against loss caused by:

> The priority of any lien for charges and assessments at Date of Policy in favor of any association of homeowners which are provided for in any document referred to in Schedule B over the lien of any insured mortgage identified in Schedule A.

Wells Fargo asserted that this coverage, which at least used the terms lien, charge and assessment, gave blanket post-policy priority coverage. Fidelity argued that the coverage was limited to assessments that were delinquent on the Date of Policy, because of its use of the phrase "at Date of Policy." The court agreed with Fidelity, saying:

> The Court does not find this endorsement ambiguous. It provides coverage when any charges or assessments are due and owing at Date of Policy, when those dues become a superpriority lien after Date of Policy. … For example, this endorsement would provide coverage if a borrower started missing payments for HOA dues three months before date of policy, if the borrower continued to fail to make payments and accordingly those missed payments became a superpriority lien six months after date of policy (thus totaling nine months of missed assessments). As Defendant argues, that is not what happened here. … Here, the borrower did not stop making payments of her HOA dues until 2014—years after Date of Policy. … Thus, the ALTA 5 endorsement does not apply to the facts of this case.
>
> Plaintiff's contrary argument that Date of Policy is not the focal point of the coverage inquiry under ALTA 5 is unpersuasive. (ECF No. 29 at 20.) Indeed, it is based on an inapplicable premise—that ambiguities or uncertainties in insurance policies should be construed in favor of the insured. (Id.) But there is no ambiguity or uncertainty here. The charges or assessments that could create coverage under this policy must be "at Date of Policy[.]" … Thus, there is no need to consult trade usage evidence, though the Court could. Said otherwise, though the Court could consult trade usage to "ascertain" or "illuminate" the meaning of "Date of Policy," there is no need because it is clear what Date of Policy means. … Plaintiff's attempt to read out or otherwise diminish the importance of Date of Policy is unpersuasive.

The court also found that the "trade usage evidence" does "not exactly support" Wells Fargo's argument. The court noted that Mr. Gosdin's article *did not* say that there was post-policy assessment coverage under the ALTA 5 endorsement. On that point, it appears that Wells Fargo offered commentary about other endorsements, which contain similar but different coverage.

Judge Du issued several more decisions in which she adopted the same analysis of endorsement coverage. See, for example, *Deutsche Bank Nat'l Trust Co., as Trustee v. Fidelity Nat'l Title Ins. Co.*, 2022 WL 4379194 (D.Nev.) (Case No. 3:19-cv-00468-MMD-CSD, issued on September 22, 2022).

However, the Nevada federal judges do not all agree with Judge Du's interpretation of these endorsements. For example, in *U.S. Bank, N.A., as trustee v. Stewart Information Systems Corp.*, ___ F.Supp.3d ___, 2022 WL 17253787 (D.Nev.) (permanent citation not yet available), Judge James C. Mahan refused to hold that the CLTA 100 endorsement granted coverage. Judge Mahan dismissed the case on August 22, 2022, about one month before the *Wells Fargo* decision was issued. U.S. Bank moved to reconsider, likely based on *Wells Fargo*. Judge Mahan issued his decision on that motion on November 28, 2022, about two months after Judge Du's *Wells Fargo* decision. He took a very different stance on coverage, saying this:

> The bank does not provide a single controlling authority to support its position that the court committed clear error in its dismissal. It provides a litany of treatises that purport to support its position and argues that an endorsement serves as the ultimate authority in an insurance contract

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superseding all other provisions, no matter how clear and unambiguous they may be. … It seeks a second bite at the apple on arguments that this court has summarily denied, and it does so through a highly disfavored procedural vehicle.

The bank inartfully argues in summary that application of exclusion 3(d) "was clear legal error because endorsements [sic] cannot be applied [sic] endorsements. The law is well-established on this point. The basic insurging [sic] provision broadly insurer [sic] the priority of the insured mortgage," and endorsements alter the scope of coverage under the policy by "mooting" specific policy language … As the court reads this thoroughly unproofread passage, the bank essentially invokes the same argument it raised in its response to the motion to dismiss. …

An insurance policy is a contract. *Pioneer Title Ins. v. Cantrell*, 286 P.2d 261, 263 (Nev. 1955). It must be read as a whole. *Am. Excess Ins. Co. v. MGM*, 729 P.2d 1352, 1354 (Nev. 1986). Exclusion 3(d) excludes coverage for claims arising from liens "attaching or creating subsequent to the Date of Policy." … This is fatal to the bank's claim. The policy clearly states that any lien arising after the issuing date is not covered.

Even revisiting the bank's argument that the endorsement supersedes this clear language does not change this court's analysis. Endorsements can add additional coverages in insurance policies. … Endorsement 100, the provision at issue here, states it "does not modify any of the terms and provisions" of the policy, including the date of policy. …

This language is, again, clear and unambiguous. Exclusion 3(d) specifically exempts after-arising liens from coverage. Endorsement 100 then goes on to explicitly state that it does not modify any terms of the original policy—where exclusion 3(d) is located. Thus, there is no conflict in the terms such that the bank's non-binding authority would necessitate reconsideration of this court's order. If STGC had meant for Endorsement 100 to supersede the policy, there would not be language in the Endorsement specifically disclaiming modification of the policy.

Title insurance is necessarily a retrospective device. It cannot function prospectively or else it would subvert the title system entirely. Title insurance is premised on protecting against risks that are "already in existence on the date the policy is issued." *Philadelphia Indem. Ins. Co. v. Chicago Title Ins. Co.*, 771 F.3d 391, 400 (7th Cir. 2014) (quoting *GMAC Mortg., LLC v. First Am. Title Ins. Co.*, 985 N.E.2d 823, 828 (Mass. 2013)). To force a title insurer to protect against title defects that do not—and in this case, could not—exist on the date the policy was issued would wholly undermine the business model of title insurance. It would allow the insured to pay a one-time fee that guaranteed defense of any future title dispute, effectively outsourcing all legal claims at a flat rate upon issuance of the policy.

Finally, STGC did not waive its exclusion 3(d) position and it is not estopped from relying on that position. The doctrines of waiver and estoppel cannot extend the scope of coverage of an insurance policy, and title insurance provides no coverage for future title defects. See *Sewell v. Capital One Fin. Corp.*, 401 F.Supp.3d 1159, 1175 (D. Nev. 2019) (citing *Walker v. Am. Ins. Co.*, 254 F.Supp. 736, 741 (D.D.C. 1966)).

Thus, Judge Mahan's central finding is that title insurance is built and priced based on the fundamental premise that all coverage is retrospective. In evaluating the CLTA endorsement, Judge Du did not even take that fact into account. The reader should also note that, whereas Judge Du referred to the bulletins as "evidence of trade usage," Judge Mahan referred to them as "a litany of treatises" not worthy of further mention.

The Nevada homeowner assessment decisions are the first and only situation in which there has been a multitude of rulings about the nature and contours of endorsement coverages in relation to one particular type of risk. These decisions are worthy of careful study by underwriters, managers and claims people, for the numerous lessons they teach about careful and consistent drafting of endorsement coverages. On balance, the decisions do not suggest any fatal flaw or ambiguity in the drafting of the CLTA 100, CLTA 115.2, ALTA 9, ALTA 5 or other endorsements that the Nevada courts have considered. Still, that does not mean that the language in those endorsements could not be reinforced.

The other aspect of the recent Nevada decisions is the use of underwriting bulletins as "evidence of trade usage." Judge Du's analysis of this question is flawed in at least one regard, likely due to ignorance about how such bulletins are used and why they are drafted. Trade usage is normally offered to define or describe a term of art or a practice within an industry. The underwriting bulletins and other material supplied to Judge Du did not define a term of art or describe an industry practice. Further, an underwriting bulletin is not a word-by-word exegesis of the terms of an endorsement or the coverage afforded by it. An underwriting bulletin is written by an underwriting lawyer to agents and title officers, explaining the circumstances under which the endorsement may be issued without approval by underwriting counsel. The bulletin describes what the title officer must do to issue the endorsement, not what the coverage means. Any description of the endorsement's coverages is merely to remind the reader why the customer is asking for the endorsement.

If there were an article picking apart the terms of a particular endorsement, word for word, and stating the event or condition that would trigger coverage, that article

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might be termed a scholarly work that illuminates the industry position concerning the scope of the endorsement's coverage. Such an article would still need to pass muster as true scholarship, based on the author's qualifications and personal knowledge of the drafters' intent. In the unfortunate decision of *Nationwide Life Ins. Co. v. Commonwealth Land Title Ins. Co.*, 687 F.3d 620 (3rd Cir. (Pa.) 2012), the Third Circuit based its interpretation of the ALTA 9 endorsement in part on an internet-based summary of the endorsement prepared by a title agent, not Commonwealth Land Title. The court made no critical analysis of the author's personal knowledge or scholarly qualification.

Finally, a court will sometimes agree to consider an insurer's own marketing materials as evidence of its good or bad faith in denying a claim that the publicity brochure suggests should be covered. Judge Du suggested that she might consider the underwriting bulletins in relation to the claim of bad faith conduct. However, to support a claim that an insurer failed to honor its own representation about the coverage of an endorsement, that statement must have been delivered to customers and relied on by them. An underwriting bulletin is an internal communication and is not delivered to customers. Further, marketing materials prepared by one insurer should never be admitted as evidence of bad faith conduct by a different insurer. The three bulletins presented by Wells Fargo were prepared by Stewart Title, and should not be considered as evidence of bad faith conduct by Fidelity, which did not publish the bulletins.

Title Insurance

Loan Policy Loss Measured as Market Value of Lost Parcel, Not Lender's Diminution in Security

Wells Fargo Bank, N.A. v. Stewart Title Guar. Co., ___ F.4th ___, 2022 WL 17574341 (10th Cir. (Utah) 2022) (permanent citation not yet available).

The Tenth Circuit has affirmed a judgment measuring loss under a loan policy as the market value of a parcel the borrower did not own, despite the apparent acknowledgment by the trial court that the lender was fully secured by valid liens on other real estate that was also included in the policy. The appeals court went further, granting the lender interest on the loss amount because that amount was supposedly definite and fixed.

Wells Fargo Bank made a loan to Talisker Finance Inc. The loan was secured by deeds of trust on three large parcels owned by Talisker's affiliates. Wells Fargo got one title insurance policy from Stewart Title Guaranty that insured the deed of trust encumbering all three parcels.

Talisker defaulted. It "couldn't deliver good title to part of the land promised as collateral," the appeals court reported. The entire decision is made up of similarly imprecise statements that leave the reader in doubt about the facts.

The land insured by the policy was denominated as Parcels A, B and C. The land not owned by the borrower was about 127 acres that made up part of Parcel B. The portion of Parcel B that the borrower did own was known as Bonanza Flats.

Wells Fargo made a claim on the policy. Stewart Title appears to have acknowledged that there was coverage, but the lender and insurer disagreed on the loss payable to Wells Fargo. The lender filed suit. The case went to trial. Both parties put on appraiser testimony at trial. The appraisers used different methods for measuring the loss. The trial court ruled that loss equaled the market value of the parcel not owned by the borrower's affiliate, including the value of the improvements on that land. The property was a ski slope. The improvements were two chairlifts, a telecommunication facility and a ski patrol building. The district court included the value of these improvements when determining the value of the lost parcel. The district court awarded Wells Fargo $3,210,200 as the value of the land and improvements.

The appeals court affirmed the verdict and judgment.

The appeals court correctly recited some of the principles about how loss is valued under a title insurance policy. For example, it stated that, when the policy insures more than one parcel, loss can equal the value of the parcel with bad title plus the effect of the loss of that land on another insured parcel. In this case, the district court did not consider any effect on Parcels A or C due to the loss of the 127 acres, because those parcels were not contiguous to the lost parcel.

In describing the measure of loss under a loan policy, the court began correctly enough. It stated that the trial court had "… explained that the policy had protected against a diminution in value of the collateral." The trial court had also said that "the parties should have started with the combined values of Parcels A, B, and C."

The trial court appears to have been headed in the right direction. It is true that loan policy loss is equal to the amount by which the defect in title reduces the lender's collateral, if the total collateral value is reduced to less than the loan amount. However, the lender suffers no loss due to a title defect if it retains a valid lien on collateral that is worth the amount of the loan or more than that number. In order to determine if any loss has been suffered by the lender, the court must consider the value of all remaining valid loan collateral. See *Blackhawk Production Credit Ass'n v. Chicago Title Ins. Co.*, 144 Wis.2d 68, 423 N.W.2d 521 (1988), in which the court stated:

> If the interest held by [the lender] was valueless without the superior lien, it cannot claim any lost value because the lien existed. Conversely, if the security interest held by [the lender] had established value, the greatest amount it can recover as a mortgagee for the title defect under its policy of title insurance is the value of the interest held in the land up to the stated policy limits of the insurance.

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Similarly, in *Green v. Evesham Corp.*, 430 A.2d 944 (N.J. Super. Ct. A.D. 1981), a $60,000 prior mortgage was not excepted in a policy insuring a $15 million mortgage. The lender purchased the property and bought out all other lien interests. It resold the property at a profit. Then it demanded from the insurer the amount paid to the prior missed mortgagee. The court found no loss because, once it owned the entire property, the lender held collateral of $4 million more than its debt. In *Chicago Title Ins. Co. v. The Huntington National Bank*, 1998 WL 548959 (Ohio App. 5 Dist.) (unpublished), modified by 719 N.E.2d 955, 87 Ohio St.3d 270 (1999), the insured lender obtained mortgages on two houses owned by the borrower. A prior mortgage on one parcel was not excepted in the policy. The measure of loss was the extent to which the lender's combined security in the two mortgaged properties was reduced by the prior mortgage.

The appeals court proceeded down the wrong path. It misconstrued the loan policy measure of loss by assuming that loss is measured the same way under both an owner's and a loan policy, saying:

> The policy measured the diminution in value based on a standard formula:
>
> Value of the insured estate – collateral that was received = Loss.
>
> This formula started with "the value of the insured estate." … Here the "insured estate" consisted of the combination of Parcels A, B, and C. So the starting point of the calculation was the combined value of these parcels. The policy then required subtraction of the value of the collateral "subject to the [title] defect." … This amount equaled the value of the collateral that Wells Fargo had actually received (the value of Parcels A and C and the part of Parcel B that Talisker was able to deliver). Wells Fargo was entitled to the difference between these amounts.

Therefore, the court said that loss equaled the value of the 127 acres.

Stewart Title asserted that this "formula" was wrong, and that "the loss of the collateral didn't diminish the value of the collateral as a whole." Stewart Title pointed out that the trial court should not have awarded Wells Fargo any policy loss, because the lower court had made the following two statements that supported Stewart's position:

> [I]t does not matter that [Stewart's expert witness] calculated the [diminution in value] in relation to [the other part of Parcel B] when he should have used the entire collateral estate. Either way, there is no diminution in value.

> The court concludes that there is no diminution in value to the collateral estate based on the loss of the Claim Property.

The appeals court did not seem to grasp Stewart's argument. Its only response was to say:

> Stewart's focus disregards the context of both excerpts. They discuss the effect of the lost parcel on the value of the rest of the collateral—not the separate value of the lost parcel.

The court also rejected Stewart Title's argument that the ski slope should have been valued as land only, not including the chair lifts, communication building and ski patrol building, because Wells Fargo had not intended to include the buildings in its loan collateral. Stewart pointed out that, in making the loan, Wells Fargo had not even appraised the value of the improvements. Also, Wells Fargo never asked Stewart Title to pay the value of those improvements in its two proofs of loss.

The court responded with the simplistic conclusion that the value of the structures should be included because they were fixtures that are included in the policy definition of Land. The court also noted that Utah follows the standard definition of improvements as being buildings and structures affixed to the land. Based on those rules, the court said there was no obvious error in including the value of the improvements as a loss payable by Stewart Title.

The court also rejected Stewart Title's final argument, that the amount awarded by the trial court of $3,210,200 was not a number proposed by any witness at trial. The appeals court said this fact "proves little." It explained that the trial court combined the $330,200 value of the land as set by Stewart's expert witness appraiser with the $2,860,000 that Wells Fargo's appraiser ascribed to the chair lifts and buildings.

The fact that the trial judge plucked numbers from several sources should have given the appeals court pause in its final ruling, in which it said that the district court should have awarded prejudgment interest to Wells Fargo. In Utah, prejudgment interest is available if damages "are complete" and are measurable by "fixed rules of evidence and known standards of value." Smith v. Fairfax Realty, Inc., 82 P.3d 1064, 1068 (Utah 2003). Stated differently, the amount of the loss should be so concrete that any person could calculate the amount "with mathematical accuracy in accordance with well-established rules of damages." *AE, Inc. v. Goodyear Tire & Rubber Co.*, 576 F.3d 1050, 1055 (10th Cir. 2009).

The district court did not conclude that the loss was fixed. District Court Judge Tena Campbell said the opposite, that "too many uncertainties existed for this calculation." Perhaps that was because the judge needed to hear hours of expert testimony, and then set the loss in an amount that was different from the figures offered by any of the appraiser experts. Also, the judge had reviewed several proofs of loss, none of which claimed loss in the amount set by the court. However, the appeals court waded in. It said "[t]he calculation was possible from the appraisals of the lost parcel and the improvements." Interestingly, it based its conclusion on *Smith v. Fairfax Realty, Inc.*, 82 P.3d 1064 (Utah 2003), in which a jury set damages based on the opinion of an appraiser. The appeals court said:

> Here too the factfinder relied on the appraisers' use of accepted principles. For the land itself, the district court relied on Stewart's appraiser, who had relied on the comparable sales approach. For the high-speed chairlifts, the district court relied on

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Wells Fargo's appraiser, who had relied on the cost approach. For the telecommunication facility, the court relied on the same appraiser, who had relied on the cost approach and income capitalization approach. For the ski patrol building, the court relied on both parties' appraisers, who had agreed on the value based on the cost approach. All of these approaches are generally accepted methods of appraising property. See Appraisal Institute, The Appraisal of Real Estate 36 (14th ed. 2013) (stating that three approaches for appraising a property's value are the "cost approach," the "sales comparison approach," and the "income capitalization approach").

The court thus awarded Wells Fargo prejudgment interest on the loss amount.

This decision is a vivid illustration of the fact that the ALTA loan policy still contains the same value loss formula found in the ALTA owner's policy, despite the fact that courts have been applying the diminution in security formula for loan policy losses for more than 40 years. It seems likely that a loan policy loss provision modeled after *Blackhawk* or *Green v. Evesham* would have avoided this unfortunate decision. Now that the decision has been issued, the need to adopt such a provision is all the greater.

Title Insurance

Virginia Rejects Search Negligence Claim Based on Title Insurance Policy

Landfall Trust LLC v. Fidelity Nat'l Title Ins. Co., ___ F.Supp.3d ___, 2022 WL 17834051 (E.D.Va. 2022) (permanent citation not yet available).

A Virginia federal court has dismissed an insured's claim that a title insurance policy creates an implied search duty, based on the economic loss doctrine and the source-of-duty rule.

In 2002, a developer platted property in Lancaster County, Virginia as Henry's Island. The developer recorded a declaration of covenants, conditions and restrictions for Henry's Island that created a homeowner's association. The plat included ten residential lots and two common areas labeled as the primary and reserve drain fields. The declaration recited easement rights in the drain fields and allocated the responsibility for their maintenance.

In 2018, Landfall Trust LLC bought Lots 9 and 10 of Henry's Island. Fidelity National Title issued a policy to Landfall Trust. Schedule A of the policy insured ownership of Lots 9 and 10, together with several access easements. Schedule B contained an exception for the terms of the declaration.

In November 2021, Landfall Trust contracted to sell Lots 9 and 10 to Jesse Crotty for $1,381,050. Crotty received a title insurance commitment from Fidelity. The first version of the commitment proposed to insure title to Lots 9 and 10 only. That commitment was replaced by a version that stated that Landfall Trust owned Lots 9 and 10, and that the homeowner's association owned a "drainfield easement appurtenant to" Lot 9. The Schedule A legal was modified to add an easement for "a perpetual appurtenant easement for a septic force main" running on a path along the primary drain field area.

Landfall Trust has now sued Fidelity. It alleges that the "issuance of the second binder meant [Landfall Trust] was unable to convey to Crotty all of the property [Landfall Trust] was obligated to convey under the terms of the Crotty Contract." Landfall also alleges that Crotty demanded that it be released from its contract, and that Landfall asked Fidelity "to provide coverage or to provide an accurate description of what Plaintiff owned, per the terms of the Insurance Policy." Landfall also alleges that Fidelity responded to this request as a claim notice, and that it accepted coverage in part. Landfall also alleges that there was a mediation with Crotty that caused Landfall "to concede that Crotty had identified title problems," and release Crotty from the contract.

Landfall then sued Fidelity, claiming that some coverage of the policy was invoked by the Crotty dispute. Landfall's complaint contained two claims, for breach of contract and title search negligence. Fidelity filed a motion to dismiss.

The court elected not to dismiss the breach of contract claim. It said that Landfall had alleged, "albeit convolutedly," that Fidelity had a duty to pay a loss or cure the alleged title problem. Fidelity argued that there was no coverage, because the policy did not insure Landfall that it owned the drain field, and excepted the declaration that defined the lot owners' rights in that area. Landfall argued that the exception did not negate the claimed coverage because its "loss does not 'arise by reason of' the existence of the drainage field rights." Rather, it said, the "problem here is that Fidelity did not draft the legal description in Schedule A so as to unambiguously convey to [Landfall] all of its rights under" the declaration. Landfall also argued that, because Fidelity "has issued conflicting descriptions of the property in the First and Second Binders, the Defendant must bear the risk of any erroneous property descriptions." The court said it would not delve into the merits of the coverage issue on a motion to dismiss.

The court did, however, dismiss Landfall's negligence claim. Landfall claimed two kinds of negligence: title search error, and negligence in the production of legal descriptions for the property. Fidelity countered that both claims were barred by Virginia's source-of-duty rule and the economic loss doctrine. The court agreed.

The source-of-duty rule marks off "the boundaries of civil liability" by precluding a party from recovering in tort from a defendant's breach of a contractual duty. *Tingler v. Graystone Homes, Inc.*, 834 S.E.2d 244, 255–56 (Va.

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2019). Thus, "tort liability cannot be imposed upon a contracting party for failing to do a contractual task when no common-law tort duty would have required [the contracting party] to do it anyway." *Id*. at 255. In other words, claims that merely involve "allegations of negligent performance of contractual duties" are "not actionable in tort." *Richmond Metro. Auth. v. McDevitt St. Bovis, Inc.*, 507 S.E.2d 344, 347 (Va. 1998). "A tort action cannot be based solely on a negligent breach of contract." *Id*.

Similarly, Virginia's formulation of the economic loss rule is that, "when a plaintiff alleges and proves nothing more than disappointed economic expectations assumed only by agreement, the law of contracts, not the law of torts, provides the remedy for such economic losses." *Filak v. George*, 594 S.E.2d 610, 613 (Va. 2004). Thus, "recovery in tort is available only when there is a breach of a duty 'to take care for the *safety* of the person or property of another.' " *Sensenbrenner v. Rust, Orling & Neale, Architects, Inc.*, 374 S.E.2d 55, 58 (Va. 1988) (quoting *Blake Const. Co. v. Alley*, 353 S.E.2d 724, 726 (Va. 1987)).

The source-of-duty and economic loss rules have been applied to bar tort claims based on insurance policies, in *Selective Ins. Co. of the Southeast v. Williamsburg Christian Academy*, 458 F. Supp. 3d 409 (E.D. Va. 2020) and *Metro Life Ins. v. Forman-Hubka*, No. 1:15CV12, 2016 WL 10489865, at *3 (E.D. Va. Mar. 28, 2016)).

This court held that the negligence claim was barred because Fidelity's alleged duty to search title and produce legal descriptions "arose solely out of the Insurance Policy." The court said that Landfall's negligence claim was limited to "allegations of negligent performance" of policy obligations. Landfall's claimed damages also invoked the economic loss rule, because the claimed damages "merely represent Plaintiff's economic loss from Defendant's alleged misconduct."

Landfall argued that the search duty did not emanate from the policy but from "another source of duty" that "allows the negligence claim to exist independently of the breach of contract claim." The court said that Landfall gave no authority in support of that argument, however. It merely cited cases from other states that do not follow the economic loss rule. The court said it was bound to apply Virginia law, because Landfall had brought this action "in a Virginia federal court for events occurring exclusively in Virginia."

This decision is in line with *Layman v. Friedlander*, 2003 WL 1958692 (Va.Cir.Ct.) (unpublished), which also rejected a title search claim against a title insurer and its agent based on the economic loss doctrine.

Title Insurance

Owner's Policy Terminates on Voluntary Conveyance, With a Wrinkle Added by Adverse Possession

Shah v. Fidelity Nat'l Title Ins. Co., 2022 WL 17333295 (Cal.App. 5 Dist.) (unpublished).

A voluntary conveyance by the insured terminated a CLTA owner's policy. An otherwise simple holding was complicated by the fact that the insured's title interest was extinguished before the deed, but he later regained title by adverse possession.

In 1995, Jay C. Shah purchased agricultural land in San Jose from Mary Silva for $350,000. Shah took title as trustee under a 1993 living trust. Fidelity National Title issued a California Land Title Association 1990 form standard owner's policy to Shah, as trustee. The policy insured Shah as being vested with fee simple title.

Mary Silva, however, did not have fee simple to convey. In 1959, she was granted a life estate, and her heirs held the remainder interest.

Silva died on May 4, 2002. On that day, title to the land passed to her heirs by operation of law. About six weeks later, Shah recorded a deed conveying the land to his parents, as trustees of their revocable trust. Shah later claimed that the deed represented a mortgage rather than a sale or gift. In any event, there were nine more recorded transfers of the land from 2005 to 2010, between Shah, his parents, and their respective trusts.

In 2007, Shah borrowed $350,000 from a private lender, Conquest, secured by a deed of trust against the land. Shah defaulted on the loan. Conquest recorded a notice of default and set the trustee's sale for February of 2009. Shah tried to refinance to avoid foreclosure. A preliminary title report issued for the refinance lender disclosed that Silva had only a life estate, that her 1995 deed transferred a life estate measured by her life (a life estate *per autre vie*), and that estate was extinguished on her death in 2002.

This news put the refinance on hold. However, Conquest held a trustee's sale in February of 2009, and the high bidders were Bob and Judy Schwartz.

In March 2009, Shah sued Silva's heirs, the Schwartzes and Conquest to quiet title. He alleged title by adverse possession. On the same day the suit was filed, Shah submitted a claim notice to Fidelity, demanding indemnity and payment of the attorneys' fees he was about to incur in the suit he had just filed.

Fidelity denied Shah's claim based on Condition 2(b) of the policy, which in the CLTA form policy is labeled After Conveyance of Title by an Insured. Fidelity said that the 2002 deed from Shah to his parents had terminated the policy, because it was a voluntary conveyance. Condition 2(b) says:

> The coverage of this policy shall continue in force as of Date of Policy in favor of an insured only so long as the insured retains an estate or interest in the land, or holds an indebtedness secured by a purchase money mortgage given by a purchaser from the insured, or only so long as the insured shall have liability by reason of covenants of warranty made by the insured in any transfer or conveyance of the estate

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> or interest. This policy shall not continue in force in favor of any purchaser from an insured of either (i) an estate or interest in the land, or (ii) an indebtedness secured by a purchase money mortgage given to an insured.

Shah settled with the Silva heirs, Conquest, and the Schwartzes. His quiet title action was dismissed. Shah incurred $135,000 in attorney fees, costs and expenses in the quiet title action.

Shah sued Fidelity in 2011, for breach of contract and alleged bad faith conduct. The trial court granted Fidelity's demurrer. Shah appealed, and that court reversed, in 2016. After discovery, both sides moved for summary judgment. The trial court granted Fidelity's motion, holding that the policy terminated on Shah's voluntary conveyance in 2002. The court further held that Shah conveyed fee simple title, based on his adverse possession that ripened in 2007.

Shah appealed to the Sixth District Court of Appeal. The appeal was transferred to the Fifth District. The court affirmed. The court rejected all three of Shah's highly inventive arguments as to why the policy did not terminate.

First, Shah contended that his 2002 deed did not transfer any interest, and certainly not the fee simple estate insured in the policy, and therefore the deed did not terminate the policy. The appeals court said that the parties agreed that the June, 2002 deed was given after Shah's life estate *per autre vie* terminated on Silva's death. The court observed that Shah's title insurance coverage did not end "simply because his life estate *per autre vie* terminated and he no longer held title to the property when Silva died." The court said that such an interpretation "would only serve to invalidate the most serious of title claims—those involving a total loss of title—and defeat the purpose of title insurance."

Fidelity contended essentially the opposite, that Shah had no title to convey in 2002, but that he obtained title by adverse possession and that estate ripened in 2007. Fidelity based its argument largely on what Shah had alleged in his quiet title action. Fidelity further asserted that, when Shah obtained fee title by adverse possession in 2007, the 2002 conveyance became effective by operation of law under the after-acquired title doctrine. Thus, his title insurance coverage terminated in May 2007.

The appeals court adopted Fidelity's reasoning. The court said that the after-acquired title doctrine is well-established in California, and applies whenever a person purports to grant a fee simple estate. Any claim of title the grantor later acquires passes by operation of law to the grantee, or his successors, according to Civil Code, § 1106. The court also cited *Noronha v. Stewart* (1988) 199 Cal.App.3d 485, and 3 Miller & Starr, Cal. Real Estate (4th ed. 2022) After-acquired Title, §8:74, in support of California's application of the doctrine.

The court said that Fidelity had presented evidence that Shah acquired title to the property by adverse possession on May 4, 2007. Fidelity relied on Shah's own allegations in his verified complaint in the quiet title action, plus deposition testimony that Shah was in sole possession of the land and proof that he had paid all real property taxes on the property during the adverse possession period.

Once the court had worked out how Shah had conveyed title to his parents' trust, it was able to fit the facts of this case squarely within the holding of the leading California decision on policy termination, *Kwok v. Transnation Title Ins. Co.* (2009) 170 Cal.App.4th 1562. In *Kwok*, a husband and wife formed a limited liability company and were its only members. The LLC bought property and got a CTLA standard form title insurance policy. The LLC later transferred the property via grant deed to the Kwoks, as trustees of their revocable family trust, and dissolved the LLC. Still later, the Kwoks made a claim on the policy concerning an easement dispute. The appeals court held that the policy terminated on the deed to the trustees. The appeals court held that the *Kwok* analysis applied.

This shifted the burden to Shah to prove that there was an issue of fact about whether or not the policy remained in effect. Shah did not even address the after-acquired title doctrine. On appeal, he said Fidelity could not rely on his quiet title allegations as establishing that he had obtained title by adverse possession in 2007, because the case did not result in a final judgment. The court disagreed. First, it observed that a judgment is not required for vesting of title by adverse possession. It cited California cases holding that fee simple title vests in the adverse possessor by operation of law at the moment the requisite conditions for adverse possession have been established for the statutory period, and that the possessor is not required to take further steps to acquire title after those conditions have been met. *Marriage v. Keener* (1994) 26 Cal.App.4th 186; *People ex rel. Harris v. Aguayo* (2017) 11 Cal.App.5th 1150. The court also noted that a person's allegations from a prior pleading can be used as evidence to meet a moving party's burden to demonstrate the absence of a fact issue. *Magnolia Square Homeowners Assn. v. Safeco Ins. Co.* (1990) 221 Cal.App.3d 1049. Therefore, the court held that Shah had failed to demonstrate the existence of a triable issue about whether or not he later acquired fee simple title, or whether his 2002 deed conveyed that title.

Shah's second argument was that the 2002 deed was really a mortgage, not a conveyance. Fidelity cited Civil Code, § 1105 in response. That statute says that "[a] fee simple title is presumed to be intended to pass by a grant of real property, unless it appears from the grant that a lesser estate was intended." It also cited *Schwen v. Kaye* (1984) 155 Cal.App.3d 949, which held that a seller who gave a grant deed was estopped to deny that the deed conveyed title she later obtained under the after-acquired title doctrine, because the deed expressed no intent to reserve any estate to the grantor. The court again held that Fidelity had met its initial burden of proof.

Shah's only rebuttal evidence was self-serving declarations signed by his parents and himself. Shah's affidavit asserted that his parents lent him money and the grant deed "was merely security for the loan." Worse, Shah's parents did not even say that much. Their affidavits merely stated that they did not pay cash for the land, open an escrow or buy title insurance. The court said that the "vague statement appearing *only in Shah's declaration* as to a verbal agreement with his parents

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that the deed was subject to being reversed on certain conditions of his performance" and that he treated the deed as a mortgage "falls far short of those requirements necessary to justify the overthrow of a deed absolute on its face." It said:

> It must appear to the court beyond all reasonable controversy that it was the intention of not only one but all of the parties that the deed should be a mortgage. "A mere secret intention on the part of one of the parties, not disclosed or communicated to the other, will not have the effect of changing the character of the transaction." *Wehle v. Price, supra*, 202 Cal. at pp. 396–397… .

Moreover, the court said, not even Shah had established that a debt existed on the day the deed was delivered, because his affidavit said his parents lent him money six months *after* the deed was given. Thus, Shah could not prove that a deed absolute on its face should be construed as a mortgage.

Shah's third argument was that the policy never terminated, because he has remained in possession continuously, and thus has retained the necessary "estate or interest" for continuance of coverage under Condition 2(b). Shah described his interest as a "possessory estate," using the definition found in Black's Law Dictionary. Shah said the evidence of this continuing estate was the fact that he had continued to collect rent from a local rancher under a cattle grazing lease.

The court said that Shah's argument failed because the policy insures a title interest, not a possessory interest. It said:

> Section 2(b) of the title policy states that coverage continues in favor of an insured "only so long as the Insured retains an estate or interest in the land …." When construing the policy as a whole, this language is not ambiguous. Among other things, the policy insured "against loss or damage ... sustained or incurred by the insured by reason of: [¶] 1. Title to the estate or interest described in Schedule A being vested other than as stated therein." Schedule A of the policy uses the same language to state: "The estate or interest in the land described herein and which is covered by this policy is: A Fee." Thus, the express language of the policy indicates the coverage provided is title protection, not occupancy or a right to collect rents or profits. This language is consistent with the purpose of title insurance. (See *Siegel v. Fidelity Nat. Title Ins. Co.*, (1996) 46 Cal.App.4th 1181, 1191 [" 'A title policy is "... a contract to indemnify against loss caused by defects in the title or encumbrances on the title" ' "].)
>
> … Under the express terms of the policy, coverage terminated when Shah voluntarily conveyed the property and thereafter acquired fee title by operation of law. (See *Londen Land Co., LLC v. Title Resources Guar. Co.* (9th Cir. 2012) 467 Fed. Appx. 708, 709–710 [insured did not "retain an estate or interest in the land" within meaning of continuation of coverage provision when it conveyed land to LLC in fee simple because it "conveyed the entirety of its estate or interest"].) Accordingly, Shah cannot demonstrate the existence of a triable issue of fact regarding continuation of coverage based on his possession and occupancy of the property or his collection of rents.

The court thus affirmed the dismissal of the case, because the policy had terminated.

In a footnote, the court dealt with Shah's further alternate argument that, even if the policy was terminated by his 2002 deed, it was revived when his parents later conveyed the land back to Shah. The court said this:

> We likewise reject Shah's argument that coverage did not terminate under the after-acquired title doctrine with the 2002 grant deed because his parents thereafter transferred title back to him and thus he succeeded his parents in obtaining fee title to the property. The case Shah cites, *Noronha v. Stewart, supra*, 199 Cal.App.3d at page 489, does not discuss such a rule. In any event, the question under section 2(b) of the title policy is whether Shah voluntarily conveyed his interest so as to terminate coverage, not who ended up with title after multiple voluntary conveyances.

In reaching this conclusion, the court was entirely in line with the holdings of two prior California decisions. In *Fidelity Nat'l Title Ins. Co. v. Butler*, 2017 WL 2774337 (Cal.App. 3 Dist.) (unpublished), the court held that a policy terminated on the insureds' voluntary conveyance to a third party, and was not revived based on the affidavit testimony of the grantee saying that he had reconveyed the property to the insureds by an unrecorded deed. Similarly, in *Pak v. First American Title Ins. Co.*, 2020 WL 6886551 (Cal. App. 2 Dist.) (unpublished), the insureds first conveyed the property to their LLC, then signed a "rescission agreement." The court held the rescission agreement did not revive the policy. It said "The rescission of the quitclaim deed merely restored the status quo ante as between the Paks and their LLC. It does not mean the Paks rewound the passage of time and undid the attendant consequences of their original decision."

The court ended by devoting several pages admonishing Shah's counsel, Craig J. Bassett, for "making repeated, unfounded personal attacks on the trial court and opposing counsel in his appellate papers, apparently because he disagreed with the trial court's decision." It ended that critique with the warning that "such conduct in a future case may subject him to sanctions much harsher than this warning."

To your editor's knowledge, this is the first decision to interpret the policy termination provision in relation to a conveyance made after the insured lost the estate conveyed by his recorded deed, and also the first to address the issue of whether a possessory interest is an estate retained by the insured that causes the policy to continue.

Fidelity National Title was very ably represented by Ryan Christopher Squire and Zi Chao Lin of Garrett & Tully, Pasadena.

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Agent Focus

Title Agent May Seek Declaration That Its Insured Has Good Title

Richardson v. Republic Title of Texas, Inc., 2022 WL 17843594 (Tex.App.-Dallas) (unpublished).

After a former property owner sent a notice to all title companies claiming that a later transfer of the property was void, the title agent that insured one of those grantees had the capacity to sue to quash the former owner's claim of title. The court also confirmed that the former owner's claim was baseless, quieting title in the later owner.

Derrick Richardson was a home builder who wanted to get work from the military. In 2008, he formed FortCon, Incorporated with his then-girlfriend Tracey Hickman-Thomas. FortCon's certificate of formation named Hickman-Thomas as its sole director and shareholder, so that FortCon could claim on federal contracts that it was a woman-owned business.

In 2009, Richardson conveyed six residential lots in Hutchins, Texas to FortCon. In May of 2020, Hickman-Thomas sold five of the six lots to Shepard Place Homes Inc. In July, Shepard Place deeded the lots to Camden Homes LLC. Republic Title issued a policy to Camden Homes.

Richardson discovered what Hickman-Thomas had done. In October 2020, he sent a letter addressed to local title companies, Camden Homes, Shepard Place Homes, the City of Hutchins Police Department, members of the Hutchins City Council, the Dallas District Attorney's Office and several banks. He said the deed from FortCon to Shepard Place Homes was fraudulent. He claimed to be the true owner of the lots, and that Hickman-Thomas lacked authority to sell them. He told the title companies to "pause or cease any conveyance of title regarding these lots … and advise [others] that these lots were illegally conveyed and shall be void."

Several months later, Republic Title conducted Rule 202 depositions of Richardson and Hickman-Thomas to figure out what had happened. Then it filed a petition for declaratory judgment against Richardson, seeking an order declaring that Hickman-Thomas had authority to sign the deed from FortCon. Richardson's lawyer withdrew. Republic Title moved for summary judgment. Richardson filed a *pro se* response. The trial court granted Republic Title's motion for summary judgment. Richardson appealed.

Richardson's first argument on appeal was that Republic Title did not have standing to bring the action, because its injury was hypothetical and speculative and its claim was not ripe. Richardson's contention was that Republic Title had no injury of its own, and was a mere agent of Camden Homes in bringing the action.

The court reviewed the issue of standing *de novo* because standing is a component of subject matter jurisdiction and a threshold requirement for maintaining an action. To establish standing, a plaintiff must allege "a concrete injury … and a real controversy between the parties that will be resolved by the court." *Farmers Tex. Cnty. Mut. Ins. Co. v. Beasley*, 598 S.W.3d 237, 241 (Tex. 2020). The injury alleged must be threatened or actual, not hypothetical.

The appeals court said that the question about Republic Title's rights was not one of standing but of capacity. It cited *King-Mays v. Nationwide Mut. Ins. Co.*, 194 S.W.3d 143, 145 (Tex. App.—Dallas 2006, pet. denied) in which a party questioned an insurer's capacity to sue because it had not proven that it brought the action as subrogee for its insured. A plaintiff has standing when it is personally aggrieved, whether or not it acts with legal authority; a party has capacity when it has the legal authority to act, whether or not it has a justiciable interest in the controversy. The important difference is that a lack of standing can be raised at any time, but a challenge to a party's capacity must be raised by a verified pleading in the trial court. Richardson had not raised the issue of capacity before the trial court, and thus had failed to preserve the issue on appeal.

The court then addressed Richardson's argument that Republic Title had not suffered an injury, so its claim was not ripe. The court noted that an issue is ripe when "an injury has occurred or is likely to occur." The "situation must manifest the ripening seeds of a controversy, which appear where the claims of several parties are present and indicative of threatened litigation" that is imminent and seemingly unavoidable.

The court said that Richardson had made the claim ripe by sending his letter. Republic Title had attached a copy of that letter as an exhibit to its motion for summary judgment. In that letter, Richardson claimed to have filed a police report with the City of Hutchins Police Department for theft of property. He specifically said:

> Title Companies: Please pause or cease any conveyance of title regarding these lots. Also, please … advise that these lots were illegally conveyed and shall be void.

The court said there was thus a credible threat of imminent litigation threatening ownership of the lots, which would invoke Republic Title's duties under the Camden Homes policy, making the matter ripe.

Richardson next claimed that the trial court should have granted his motion for a new trial and to suspend its decision on Republic Title's summary judgment motion, because he needed more time to prepare his case. A large factor raised by Richardson was that his first lawyer resigned without having answered Republic Title's written discovery, and his new lawyer needed time to get up to speed. The court affirmed the denial of that motion.

Finally, the court addressed the merits of Richardson's claim that Hickman-Thomas lacked authority to convey the lots. Richardson had produced off-record documents indicating that he had removed Hickman-Thomas as president and director of FortCon in 2015. He said that Hickman-Thomas lied when she testified that she was the president, director and sole shareholder of FortCon from 2009 through the time of her deposition in January of 2021. Richardson also claimed that "publicly available documents" identified him as president of FortCon in 2020, so that Republic Title "had

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constructive notice of same."

Republic Title presented the evidence that it had relied on in insuring the deed signed by Hickman-Thomas that ran to Shepard Place Homes. Those documents included the 2008 Certificate of Formation for FortCon, which identified Hickman-Thomas as the sole director, the 2009 general warranty deed to FortCon, a 2015 application for reinstatement of FortCon's charter signed by Hickman-Thomas, and a certificate of consent to action without meeting of the sole director signed by Hickman-Thomas as president. Republic Title also produced an affidavit from Hickman-Thomas swearing that, from 2009 to the date of the affidavit, she was the president, sole shareholder and director of FortCon, and a December 20, 2019 tax citation from Dallas County identifying Hickman-Thomas as director of FortCon. Hickman-Thomas admitted in her deposition that she had asked to be removed from FortCon, but she never received any documentation removing her and she took no further action after that email exchange with Richardson.

The court said that Richardson's claimed evidence, which was primarily his own testimony, was "no more than a mere scintilla." The court said that the public documents also did not establish that Richardson was president of FortCon. Those documents were a franchise tax report signed by Richardson and a change of registered agent from Hickman-Thomas to Richardson. The court noted that Hickman-Thomas might well have remained president and sole director after the change in registered agent. Thus, there was no evidence that Hickman-Thomas lacked authority to transfer the lots, and the deed was not invalid.

This may be the first decision to affirm a title insurer's right to sue to defend ownership of property that has been attacked in a letter written to title companies seeking to chill any future sale of the property. The letter campaign is a common and effective technique in preventing the resale of property. Title companies who receive such a letter sometimes have two capacities—as representatives of any prospective purchaser, and as insurer to the present record owner.

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Title Insurance

The Rationale Behind the Date of Loss Under Owner's and Loan Title Insurance Policies

J. Bushnell Nielsen, Editor

The ALTA Forms Committee appears to be poised to incorporate a date of loss in its standard form title insurance policies for the first time. The proposed dates of loss are very different from the dates that courts have adopted. Further, the proposed dates of loss are the same for both owner's and loan policies, whereas the courts have recognized that different dates should apply to the two policy types. This article reviews the rationale behind the court-established dates of loss and the issues that would be created in adopting new and very different dates of loss.

In the draft owner's and loan policies issued on Jan. 15, 2019, the ALTA Forms Committee include new Conditions 8(b) and 8(c), which say:

> b. The Insured Claimant has the right to have the amount of the loss or damage payable under this policy determined as of:
>
> i. the date the notice of claim required by Condition 3 is received by the Company; or
>
> ii. the date the liability of the Company for loss or damage under this policy is finally established by a court or arbitrator of competent jurisdiction.
>
> c. If the Company pursues its rights under Condition 5.b. and is unsuccessful in establishing the Title or the lien of the Insured Mortgage, as insured:
>
> i. the Amount of Insurance will be increased by 10%; and
>
> ii. the Insured Claimant may choose, as an alternative to the dates set forth in Condition 8.b., to have the amount of the loss or damage payable under this policy determined as of the date the settlement action, proceeding, or other act described in Condition 5.b. is concluded.

These provisions borrow from the loss date provision found in Condition 8(b)(ii) of the 2006 policies, which says that if the insurer is unsuccessful in its action to clear title, "the Insured Claimant shall have the right to have the loss or damage determined either as of the date the claim was made by the Insured Claimant or as of the date it is settled and paid."

The first change of note in the draft language is the new loss date, which is the date on which "the liability of the Company for loss or damage under this policy is finally established by a court or arbitrator of competent jurisdiction."

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The Title Insurance Law Newsletter, which is distributed electronicly each month by the American Land Title Association (ALTA), reports on cases addressing title insurance coverage, class actions and regulatory enforcement, escrow and closing duties, agent/underwriter disputes, conveyancing law, and RESPA and TILA compliance and violations.

This publication provides helpful information for title agents, approved attorneys, underwriters, claim administrators and attorneys who practice in title insurance defense work or conveyancing disputes.

J. Bushnell Nielsen serves as editor. Please submit news and guest columns to ***bnielsen@reinhartlaw.com***.

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All modern ALTA policies have contained a provision stating that, when the insurer elects to clear title, loss is not payable until there has been a "final determination" by a court that is adverse to the title as insured. This is found in Condition 9(b) of the 2006 policies. The final determination provision makes it clear that, when the insurer has made the election to clear title by litigation, no loss is payable until that action has been fully decided, and then only if the title is not cleared. Once that final determination has been entered, loss is payable within 30 days, as stated in Condition 12.

The proposed "finally established" clause in Condition 8(b)(ii) is not the final determination provision, although the use of two very similar phrases would likely cause confusion. The draft policies would heighten that confusion, by replacing the long-established term "final determination" with the phrase "final, non appealable determination." The proposed "finally established" clause refers to the date on which the insurer's liability under the policy has been established by a court or arbitrator, not the date title is fixed.

This proposed date is surprising for several reasons. First, most losses are paid with no litigation between the insured and insurer, and none of the loss provisions contemplate that such litigation will be necessary. Thus, for all claims in which there is no litigation between the insurer and insured, this date of loss would not apply.

Second, the "finally established" term does not mesh with Condition 12, which says that, "[w]hen liability and the extent of loss or damage have been definitely fixed in accordance with these Conditions, the payment shall be made within 30 days." It is rare indeed for an insurer to be able to accurately determine the amount of loss and to pay that loss, all within 30 days after the event that fixes the date of loss. The 2019 draft would also inexplicably replace the important term "definitely fixed" with the phrase "determined in accordance with the Conditions." That change appears to erase the policy term stating that loss must be fixed by some method before it can be paid. Further, the replacement phrase is inscrutable, since the policy's own terms do not fix or establish the loss amount payable to an insured.

Third, in the rare instance in which there is litigation between the insurer and insured, the issue is very often the amount of loss payable to the insured. In many cases, the insured makes a claim, the insurer admits there is coverage, and the insurer pays a loss to the insured. The insured sues the insurer because it believes that the loss paid is less than what is owed. The court then decides the amount of loss payable, most often based on the testimony of dueling appraisers retained by insurer and insured. Those appraisers each render two value opinions—one being the value of the property subject to the matter for which there is coverage and the other being the value of the property with its title as insured. Loss equals the difference between those two values. In order to render those value opinions, the appraisers must use a valuation date. At present, in 48 states, appraisers value the property as of the date the insured discovered the title issue, when the claim is made under an owner's policy. Only Georgia and Virginia use a different date of loss, which is the policy date. *Beaullieu v. Atlanta Title & Trust Co.*, 60 Ga.App. 400, 4 S.E.2d 78 (1939); *The Title Ins. Co. of Richmond, Inc. v. Industrial Bank of Richmond, Inc.*, 156 Va. 322, 157 S.E. 710 (1931). Policy date is also workable for an appraisal report.

The "finally established" provision would create a circularity problem in every such dispute. How can appraisers opine at trial about the "difference value" caused by the covered matter when the date on which the property is to be valued is in the future, on the date on which the court renders its final ruling in that insurance coverage case? Appraisers are barred by appraisal standards from rendering an opinion about a future value, because such an opinion would be pure speculation. A court could never "finally establish" the insurer's liability if it could not hear testimony about the amount of loss. The result would necessarily be that the "finally established" date of loss could never be used. This would belie the notion that the insured is being offered the right to select one of two dates of loss.

Fourth, and perhaps most importantly, there simply is no logical rationale as to why the date of loss should be ascribed as being either the date on which a court determines that the insurer must pay a loss or the date on which the insured makes a claim. A loss date without a solid underlying rationale would be unworkable in practice and a source of frustration to insureds and insurers alike.

Nearly 70 years ago, a California court enunciated a date of loss with a rationale that has been approved by nearly every state that has

considered the issue since that time. In *Overholtzer v. Northern Counties Title Ins.* Co., 116 Cal.App.2d 113, 253 P.2d 116 (Cal.App. 1 Dist. 1953), the court said that loss is measured as of the date on which the insured owner discovered that his or her title was subject to the covered title issue. This gives the insured the benefit of both any increase in value from the policy date to the date of discovery, and the value of improvements the insured has made to the property in the intervening time, in reliance on title being as stated in the policy. However, once the insured is aware of the title issue, he or she can no longer rely on title as being as insured, and the loss payable by the insurer cannot be increased based on improvements or changes made by the insured after the date of discovery. Also, the insured is encouraged to make a notice of claim promptly on discovery of the title issue, because the insurer will not pay as loss any change in property value between discovery and the claim notice date.

The only reason there is any continued wrangling over the date of loss is that an insured sometimes seeks a loss payment that includes a change in the market value of the property in addition to the loss in value caused by the title defect. Title insurers do not pay the amount by which market value changes as if that were loss payable under the policy. Over forty years ago, *McLaughlin v. Attorneys' Title Guaranty Fund Inc.*, 61 Ill. App.3d 911, 378 N.E.2d 355 (1978) stated:

> *A title insurance policy does not insure the value of any particular property. In fact, it does not insure the property at all. If the value of the property appreciates or depreciates, the title policy is not affected.*

All such attempts to make title insurers pay for changes in market value would end if the owner's policy incorporated a date of loss modeled after *Overholtzer*.

The lack of a valid rationale behind the two loss dates found in the draft ALTA policy becomes obvious by comparison to *Overholtzer.* A claim notice loss date would encourage an insured to delay making a claim when the market value of the property is increasing. That date would cause a title insurer to pay for that increase in market value between the date of discovery and the date the claim was made. There is no valid rationale for the insurer to pay the insured for such an increase after the insured learned of the title issue.

The "finally established" loss date would in some cases extend the loss date for several years past the date of discovery. If the property decreased in value while the insurer and insured litigated the coverage issue, the insured would pay a double penalty—having to sue the insurer in order to be paid, and then receiving a lesser payment because of the market value decline. An insured could become rightly suspicious that an insurer would have an incentive to drag out coverage litigation in a declining market. This could create an unnecessary stain on the title industry's reputation.

There also is no reason for the title insurance policy to include two alternate dates of loss. The loss date should be supported by a valid rationale. There should not be a favorable or unfavorable loss date, seen from the perspective of either the insured or the insurer. Again, the insured would be even less satisfied if, in reality, there was no viable election to be made, because only one date was workable.

The loss dates in the draft policies are the same in both the owner's and loan policy forms. The proposed loss dates are even less viable for use in a loan policy (which does not insure a loan, and would be better titled as a lender or mortgagee policy).

Courts have established different loss dates for the loan policy than for the owner's policy, because there is a different rationale as to when a lender suffers a loss due to a title issue. One early case measured loss under a loan policy as of the date on which the insured lender discovered the title defect, treating a loan policy as operating under the same principles that apply to an owner's policy. *Narbeth Building & Loan Ass'n v. Bryn Mawr Trust Co.*, 126 Pa.Super. 74, 190 A. 149 (1937). Since then, as a number of courts have stated, an owner suffers an "immediate" loss when the insured discovers a defect in title, whereas a lender does not suffer a loss due to a title defect until it loses its loan collateral or becomes the owner of the property.

Because of this difference in the nature of the two forms of policy, modern decisions acknowledge that the date of loss is different under the two forms of policies, and that the date of discovery is not appropriate for a loan policy because the lender does not suffer a loss on that date. Thus, when the insured forecloses the insured mortgage and takes title, the loss payable to the insured is measured based on the covered matter's effect on the value of the property as of that date. The seminal modern decision establishing that loss date is *Karl v. Commonwealth Land Title Ins. Co.*, 20 Cal.App. 4th 972, 24 Cal.Rptr.2d 912 (Cal.App. 4 Dist. 1993), which explained why that date should be used:

> *At [foreclosure sale], the lender's note is extinguished and replaced by assets recovered on foreclosure: either cash as paid by a third party bidder or the realty as bought in by the foreclosing lender. It is now possible to measure the value of the recovery by the lender, and we believe the loss which is insured by the title policy should be recognized as of that time.*
>
> *… The "fair market value as of foreclosure" approach also eliminates other concerns raised by the plaintiffs which otherwise are inherent in a delayed determination of loss. For example, following foreclosure lenders may invest cash or their own time and effort in renovation of the property. An increase in market value as a result of such contribution should not redound to the benefit of the insurer. Similarly, a lender's expertise in marketing which results in a sale at higher than market value should not profit the insurer. … Finally, it seems unfair to measure damage by a market sale which may occur at a time distant from the date of foreclosure, during which period inflation or deflation may have altered the value of the property.*

Similarly, if the insured lender takes a deed in lieu of foreclosure, the property is valued as of the date of the delivery of that deed. *Goode v. Federal Title Ins. Co.*, 162 So.2d 269 (Fla.App. 1964). If,

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however, the insured mortgage is extinguished by foreclosure of a lien for which there is policy coverage, the date of loss is the day on which the insured mortgage is extinguished. The leading decision on that point is *Chrysler Financial Services Corp. of America v. Chicago Title Ins. Co.*, 641 N.Y.S.2d 13, 14 (N.Y.A.D. 1 Dept. 1996).

Courts have correctly refused to apply the same loss dates to both forms of policies. In *First Internet Bank of Indiana v. Lawyers Title Ins. Corp.*, 2009 WL 2092782 (S.D.Ind.) (unpublished), the insured lender argued, based on *Overholtzer*, that loss should be measured on date of discovery for both owner's and loan policies. The court relied on *Karl* to find that loss under a loan policy is measured on the date on which the insured loses its security. In *First American Bank v. First American Transp. Title Ins. Co.*, 759 F.3d 427 (5th Cir. (La.) 2014), the court explained that measuring loss on the date of the foreclosure of a senior lien that extinguishes the insured lien "is appropriate because the foreclosure is when the insured actually incurs a covered loss." In *Old Republic Nat'l Title Ins. Co. v. RM Kids, LLC*, 337 Ga.App. 638, 788 S.E.2d 542 (Ga.App. 2016), the court acknowledged that Georgia uses the policy date as the loss date for owner's policies, but it identified the loss date for a loan policy as being the date on which the lender takes title. See also *Associated Bank, N.A. v. Stewart Title Guar. Co.*, 881 F.Supp.2d 1058 (D.Minn. 2012), which stated that "the majority of courts considering the issue have held that such loss cannot be measured until the note has not been repaid and the security for the mortgage is shown to be inadequate," and which cited *Falmouth Nat'l Bank v. Ticor Title Ins. Co.*, 920 F.2d 1058 (1st Cir. 1990), which collected decisions on the issue from numerous jurisdictions. Even Arizona, which recently announced that the date of policy is sometimes the date of loss under a loan policy, has admitted that the date of discovery is the proper loss date under an owner's policy, because insureds under the two types of policies incur losses at different times. See *Equity Income Partners LP v. Chicago Title Ins. Co.*, 2012 WL 3871505 (D.Ariz.) (unpublished).

Thus, there is a very strong consensus amongst the modern decisions that the date of loss under a loan policy is one of two dates: when the lender takes title to the property, or when the insured mortgage is extinguished by a covered event, such as the foreclosure of a superior lien for which there is policy coverage. These dates are backed by strong reasoning that has been developed over many decades.

The proposed dates of loss in the draft ALTA loan policy are completely at odds with the court-established loss dates. The claim-date loss date would likely cause lender insureds to open a new debate about the subtle principle that no loss is immediately payable to a lender that has not yet taken title to the property. It would be a good idea to add a loss date to the loan policy. However, the best loss dates would be those that have already been adopted by the courts, because of the sound reasoning behind those dates.

The opinions expressed in this article are those of the author only, and may not represent the views of American Land Title Association or any of its members.

Title Insurance

Seller Church May Owe Insurer for Taxes Imposed After Property Placed Back on Tax Roll

Title Resources Guar. Co. v. The Lighthouse Church & Ministries, ___ S.W.3d ___, 2019 WL 3293692 (Tex.App.-Houston 2019) (not yet released for publication).

Lighthouse Church bought vacant land in Harris County in 2011. Thereafter, the land was exempt from real estate taxes under Tax Code Section 11.20(a)(6), which applies to land owned by a religious organization intended to house a place of worship. Lighthouse Church did not build a church on the property.

In 2014, the church contracted to sell the land to SLS Properties, under an unimproved property contract based on a form promulgated by the Texas Real Estate Commission. Paragraphs 13(A) and (B) of the contract addressed "prorations" and "rollback taxes," respectively. At closing, the church and SLS signed an Escrow Withhold Agreement, under which the escrow agent, Texas American Title Company, held some of the sale proceeds for possible tax rollbacks. If the assessor levied rollback taxes, the escrowee was to use the money to pay the taxes. However, if the escrowee "receive[d] proof of ... no additional taxes due from [the] Harris County Tax Assessor," it was to deliver the money to the church.

Texas American Title issued a Title Resources Guaranty policy to SLS that did not contain an exception for taxes that might be levied or billed in the future for the prior tax years.

Six months after closing, the Harris County Appraisal District sent a letter to the church and SLS, to say that it had canceled the exemption on the land because of the sale. Texas Tax Code section 11.201(a) says that, if the religious organization sells exempt land, "an additional tax is imposed on the land equal to the tax that would have been imposed on the land had the land been taxed for each of the five years preceding the year in which the sale or transfer occurs in which the land received an exemption... ."

Three taxing entities then demanded tax money from SLS for tax years 2012, 2013 and 2014. SLS paid the 2014 taxes that accrued after the closing date, and the escrowed money was used to pay the pre-closing 2014 taxes. The escrow, however, did not include enough money to pay the 2012 and 2013 taxes that the agencies claimed were due. TRG, on SLS's behalf, demanded that the church pay those taxes under the sale contract. The church refused. TRG paid the 2012 and 2013 taxes, totaling over $111,000.

Title Resources sued the church for breach of contract and quantum meruit,

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as subrogee of SLS. The primary dispute was about the correct reading of the purchase contract. The trial court ruled in the church's favor on summary judgment, holding that the contract required SLS to pay any taxes imposed for 2012 and 2013 due to the cancellation of the tax exemption. Title Resources appealed, and the court reversed, holding that the contract was ambiguous and that there were questions of fact that would have to be decided at a trial.

The purchase contract contained a provision 13(B) entitled Rollback Taxes. That boilerplate provision said that, if "this sale" or the buyer's later use of the property resulted in "the assessment of additional taxes," the buyer was required to pay those taxes. If, however, additional taxes were later imposed due to "Seller's change in use of the Property prior to closing or denial of a special use valuation on the Property claimed by Seller," the seller was required to pay the tax. The court concluded that there was no special use valuation on the property (which allows the owner to receive lower taxes because the assessed value is based on a less valuable use). It concluded that, if provision 13(B) alone controlled, the taxes were imposed because of the sale, and thus the taxes would be paid by the buyer, not the church.

However, the court said the sale contract and the escrow agreement had to be read together, because they were two contracts about the same sale transaction. It held that the church was unambiguously liable for paying all of the additional taxes under the terms of the escrow agreement. The escrow agreement said that, "if there are additional amounts due beyond the amount withheld, the seller will pay the additional monies to satisfy the amount due to the Tax assessor/collector."

Title Resources argued that the escrow agreement was the more specific provision on the subject, and therefore must control. The court refused to apply that rule, positing that Title Resources had not established that the escrow was "more specific" than 13(B) (even though it would appear that 13(B) did not apply at all). The court also cited a case holding that, when two contracts conflict, a later contract is presumed to supersede the prior one. However, the court did not apply that rule either. The court also rejected Title Resources' argument that a change in a form contract must be accorded special weight. The court said that rule is limited to the lining out of a specific paragraph in a form contract, not the adoption of a second contract. It noted that provision 13(B) could have been crossed off or marked up, but was not.

Having stretched in order not to find a rule that would harmonize the two provisions or allow the escrow to control despite its plain language, the court concluded that the two inconsistent provisions rendered the contract(s) ambiguous, and created issues of fact that the trial court would have to decide.

This decision suggests the double standard that is often applied when a title insurer seeks recovery in subrogation against a seller. In this case, the seller church may have received special consideration.

The decision also highlights some practical pointers about drafting of escrow instructions. Post-closing escrows do not stand alone; they become part of the purchase contract. Any term of the purchase contract that is modified by the escrow should be altered to reference the escrow and to mirror the escrow's terms. In this case, the court noted that provision 13(B) referred to Rollback Taxes and the escrow agreement referred to Tax Rollbacks and TLX Exemptions, which looked like the same subject even if they were not. Further, the court observed, neither of the terms used in the escrow were defined, although they were capitalized.

Title Resources was ably and doggedly represented by Debra Donaldson and Bradford W. Irelan of Irelan McDaniel PLLC in Houston.

Title Insurance

Law of Property Situs Controls Right to Sue for Bad Faith

Buhl Building, L.L.C. v. Commonwealth Land Title Ins. Co., 2019 WL 3916615 (Del.Super.) (unpublished).

Construing an ALTA policy that did not contain a choice of law provision, a Delaware court has ruled that the law that controls a claim of bad faith conduct is that of the state in which the insured property is located.

In 1998, Commonwealth Land Title issued a $34,450,000 owner's policy insuring the title to the Buhl Building, a landmark skyscraper office building in Detroit. In 2016, almost 20 years later, insured Buhl Building LLC signed a contract to sell the building to Weslan Properties Inc. for $43 million. Weslan got a First American title insurance commitment that contained an exception for any problem caused by a difference between the legal description as stated in the last deed and policy versus the property description recited in the Wayne County tax records.

Commonwealth "tried to resolve the Discrepancy with First American, but First American would not insure the Property with the Discrepancy." Weslan refused to buy the building. In 2017, Commonwealth offered to issue a policy to a purchaser that did not contain the same exception. Buhl may have made a claim for indemnity after the sale fell through. It appears from the court decision that Commonwealth did not offer to pay a loss.

Buhl Building sued Commonwealth and Fidelity National Financial Inc. Buhl alleged that Commonwealth and FNF "functioned as a single entity," the evidence of which was that they have offices in the same building in Jacksonville and that the claim acknowledgment letter was allegedly on FNF letterhead.

Buhl sued the two companies for breach of contract and bad faith. It claimed that Commonwealth did not promptly "clear" the title. It claimed a loss measured as the "decrease in the value of the Property after Weslan refused to purchase the Property" and its "costs in finding another buyer and trying to resolve the Discrepancy." However, Buhl admitted in later briefing that those damage claims are moot because it has since found another buyer for the property, presumably at a comparable or

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higher price.

Count III of the complaint alleged first party bad faith conduct, for Commonwealth's alleged refusal to indemnify Buhl "without a reasonable justification" and delay in addressing the First American exception issue. Buhl sought an award of punitive damages for its bad faith claim.

Buhl sued in Delaware Superior Court. Buhl is a Delaware limited liability company. Fidelity National Financial is a Delaware corporation with its principal place of business in Jacksonville, Fla. When Commonwealth issued the policy, it was domiciled in Pennsylvania. It is now domiciled in Nebraska. Its principal place of business is Jacksonville. The property is in Michigan, and the policy was issued in that state.

The choice of law matters in this dispute. Both Delaware and Pennsylvania recognize causes of action for first party insurer bad faith, and permit punitive damages awards. Michigan does not recognize a cause of action for first party insurer bad faith, or allow an insured to obtain an award of punitive damages against its insurer. The court cited *Casey v. Auto Owners Ins. Co.*, 729 N.W.2d 277, 286 (Mich.App. 2006), for those principles. *Casey* was based on *Roberts v. Auto-Owners Ins. Co.*, 422 Mich. 594, 604, 374 N.W.2d 905 (1985), and *Kewin v. Massachusetts Mut. Life Ins. Co.*, 409 Mich. 401, 423, 295 N.W.2d 50 (1980).

In this decision, the court granted the motions filed by Commonwealth and FNF to strike the bad faith claim because Michigan law controls the insurance contract, and to dismiss FNF as a party.

The court began with the fact that the form of the ALTA policy at issue (likely a 1992 version) did not contain a choice-of-law provision. That fact left the question open for debate. Buhl argued that Michigan law should not apply because Michigan did not have the most significant relationship to the policy.

The court began with the question of which state's law applied to decide the issue of which state's law governed the contract. It applied Delaware law for that question, because of the general rule that a court applies the law of the forum for procedural matters in the case, citing *Tumlinson v. Advanced Micro Devices, Inc.*, 106 A.3d 983, 987 (Del. 2013).

Delaware courts use a two-step analysis to determine which state's law applies to the substance of the case. The first question is whether there is a difference in the laws of the possible states. If so, the court decides which state has the most significant relationship to the case. The "most significant relationship" test as codified in the Restatement (Second) of Conflict of Laws is used in Delaware for contract claims.

The court said that the possible applicable state laws would be those of Delaware, Pennsylvania or Michigan. The court found that the law of insurance contracts in the three states is effectively the same. However, because of Michigan's stance on bad faith and punitive damages, the court said the state laws conflict on those claims. This raised the question of whether the court could or should apply the law of two different states as to the contract and bad faith claims.

The court looked to its own prior decision of *AT&T Wireless Servs., Inc. v. Fed. Ins. Co.*, 2007 WL 1849056 (Del. Super. June 25, 2007) for guidance. In that case, this court said that claims of breach of an insurance contract and insurer bad faith both arose from the same contract, so applying the same law to both claims promoted certainty in contractual relationships. In AT&T, the court also relied on other decisions holding that "no rational businessperson was likely to have intended the laws of multiple jurisdictions to apply in controversies arising from a single contract." This court concluded that it should apply one choice-of-law analysis to both claims.

The court then used the Restatement analysis to decide which state had the most significant relationship to this insurance contract. Restatement (Second) of Conflict of Laws section 188 addresses "Law Governing in Absence of Effective Choice by the Parties." That section lists seven principles and five contact factors that courts are to consider. The Restatement comments emphasize the importance of several types of contacts. One is the state where the contract was performed. Also, comment (e) says:

> *When the contract ... affords protection against a localized risk ... the location ... of the risk is significant. ... Indeed, when ... the risk is the principal subject of the contract, it can often be assumed that the parties, to the extent that they thought about the matter at all, would expect that the local law of the state where the thing or risk was located would be applied to determine many of the issues arising under the contract.*

The same comment says that a business's place of business is more important than its state of incorporation.

Commonwealth recited a long list of factors weighing in favor of applying Michigan law. That state's laws should be used to resolve the question raised by Buhl about the building's title and legal description. Commonwealth had searched the real estate and tax records of Wayne County in issuing the policy, and the claim was based on the Wayne County tax description. Michigan had an interest in interpreting an insurance policy issued in that state and filed with its insurance commissioner. Buhl's place of business is in the building, located in Detroit.

Commonwealth said that the negotiation and performance of the contract was done mainly by telephone, mail and facsimile, involving people in Michigan, Pennsylvania and Florida, so no one state predominated and that factor should not control. It also said that the states in which the companies were domiciled and incorporated should not control.

Commonwealth also emphasized that the insurance risk was located in Michigan. This is an important factor in the Section 188 analysis. Further, Section 193 of the Restatement, entitled “Contracts of Fire, Surety or Casualty Insurance,” says that courts should presume that the applicable law is that of the site of the risk.

Buhl's argued that Section 193 should not apply because title is not a casualty insurance policy. It said that Pennsylvania law should apply because some of the negotiations over the policy occurred there and Commonwealth was domiciled there when the policy was issued. Alternately, it said, Delaware law should apply because that state has a strong interest in protecting its residents against an insurer's

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breach of the covenant of good faith and fair dealing. It cited two product liability decisions as support for the latter contention.

The court said that Michigan law applies. It said:

> *The Court notes that the Contract does not have a choice-of-law provision. At the time of contracting, the Court finds that the reasonable expectations of the parties would have been that Michigan law would apply to disputes regarding the Property. This is because the Contract involves commercial property located in Michigan—the Property—and much of the parties' performance on the Contract was in Michigan. Applying Michigan law promotes certainty and predictability. Moreover, Delaware, Pennsylvania or Michigan have not articulated a particular interest in applying their laws to the resolution of a breach of an insurance contract claim for title insurance. So, the Court weighs the parties' justified expectations as the most significant principle in its choice-of-law analysis and finds that Michigan law applies.*
>
> *The Court finds that because the places of contracting and negotiation were spread across several states and mostly performed using mail, phone, etc. these factors are not dispositive in its choice-of-law analysis. Second, as the Defendants noted, the places of performance were also spread between several states. But, the place of performance suggests that Michigan law applies because Buhl paid its premiums from Michigan, Commonwealth referenced land records in Michigan, and the parties formed the Contract using Michigan forms. Third, the Court finds that the subject matter of the Contract is located entirely within Michigan. This is clear because the Contract solely functions to provide title insurance for the Property which is located in Detroit, Michigan. All relevant land records are also located in Michigan.*
>
> *The Court follows the guidance in the comments to Restatement § 188, which state that the subject matter of the contract is a significant factor in a choice-of-law analysis. Finally, the Court notes that the comments to Section 188 state that the principal place of business is more significant than the place of incorporation, unless the place of incorporation has specially applicable policies. Delaware's only contacts in this civil action are that Buhl and FNC are incorporated in Delaware. The Court notes that Buhl's principal place of business in Michigan, although not dispositive, supports applying Michigan law.*

The court also dismissed Fidelity National Financial as a defendant. Buhl argued that "FNF disregarded Commonwealth's separate legal personality and exercised control over the specific transaction at issue—FNF took control of the claim process." The court noted that there was no contract between Buhl and FNF. Buhl could only reach FNF by a claim of piercing of the corporate veil, which claim would have to be brought in the Delaware chancery court.

This decision is one of the very few to address the lack of a governing law provision in older ALTA policies, and perhaps the only one to consider choice of law in relation to a bad faith claim. The court's analysis illustrated how complex and expensive it is for the parties to resolve the issue when there is no such provision in the policy form.

There are three related choice-of-law issues that may be addressed in an insurance contract: the law that governs disputes about the contract, the underlying law controlling the real estate issues that trigger coverage, and the forum in which a lawsuit must be filed in a dispute over the insurance contract. The 2006 ALTA policy forms address all three subjects, as do the 2015 versions of the ALTA closing protection letter. Those provisions are quite thorough, and would have eliminated most of the analysis performed by the Delaware court in this case.

The current ALTA choice-of-law provisions do not specify the state in which suit must be filed. Condition 17(b) of the 2006 policies says this:

> *Choice of Forum: Any litigation or other proceeding brought by the Insured against the Company must be filed only in a state or federal court within the United States of America or its territories having appropriate jurisdiction.*

This provision likely would not have precluded Buhl from filing suit in Delaware, if that court could conclude that it had "appropriate" jurisdiction over the dispute. The ALTA forum choice provision could be modified to specify that an action be filed in a federal or state court having jurisdiction over the Land. Fidelity National Title has developed a policy form, used in Carribean countries, that contains a jurisdictional provision mandating that actions be filed in New York courts.

Escrow Matters

Delayed Return of Escrowed Money Leads to Host of Claims

Appel v. Boston Nat'l Title Agency, LLC, ___ F.Supp.3d ___, 2019 WL 3858888 (S.D.Cal. 2019) (not yet released for publication).

A California federal court has dismissed most of the claims brought against an escrowee due to its seeming reluctance to return deposited money, but some claims survive despite the money's return.

In 2017, Howard Appel, David Cohen and Ke'e Partners LLC signed a Bidder Registration Agreement with Concierge Auctions LLC to participate in an auction of properties. The Agreement said that escrow services would be provided by Boston National Title. The Appel group wired $100,000 to Boston National's escrow account, and bid on a property in Fiji.

On July 1, 2017, the Appel group was declared the winning bidder for the Fiji property. Concierge sent them an email asking them to wire the balance of $185,000 to the escrow account. They sent the money. Concierge also sent an email to the owners of the

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Fiji property, congratulating them on the sale and sending them a purchase contract. The owners replied that they were surprised to get the email, since Concierge had said that the auction would not go forward. Boston National was copied on these emails.

The Appel group soon learned that the owners now did not want to sell. The Appel group told Boston National not to release the $285,000 from escrow without their permission. They negotiated with the owners until September of 2017. When the negotiations failed, the Appel group asked Boston National to send them the escrow instructions. Boston National responded that there was no signed escrow agreement between them. Boston National told the Appel group it had "a fiduciary relationship with Concierge."

Boston National then asked Concierge to tell the Appel group what would happen if the seller refused to sign a contract. The company said that, if an agreement could not be reached, it would interplead the money with the appropriate court. In the complaint later filed by the Appel group, they "infer that Concierge instructed Boston National not to disburse the funds until Concierge said so."

At the end of September, the Appel group demanded that Boston National send back their money. Boston National did not send the money. The bidder group sued Concierge for the return of the money and their attorneys' fees. In the arbitration of that action, Concierge allegedly told the Appel group that, if they paid $37,500, Concierge would instruct Boston National to release the money. The bidders did not pay, and the *Concierge* case proceeded.

Then the bidders sued Boston National. It made several allegations that range from fanciful to conspiratorial, including that Boston National did not return the money because it was using the cash "for the benefit of itself, Concierge, or another third party." Boston National returned the full amount to the bidder group in May 2018.

The Appel group demanded Boston National's escrow account bank statements and records, based on their theory that the title company did not return the money right away because there was a shortage in the account. The court ordered Boston National to turn over redacted bank statements to prove that the escrow account had a positive balance.

Still, the Appel group amended its complaint to add new claims. Boston National sought to dismiss the amended complaint in its entirety. In this decision, the court dismissed most but not all of the claims.

The court refused to dismiss the claim for an accounting, even though the money has been returned in full. The plaintiffs want the accounting so they can figure out if Boston National earned any money from their money. It claims the right to be paid whatever profit the company made from the money. The court said that it let the claim stand because Boston National did not respond sufficiently to the argument made by the Appel group. This decision now stands alone in even countenancing this type of claim against an escrowee.

The Appel group brought a claim under the California Unfair Competition Law. They asserted that Boston National falsely advertised that it was licensed to do business in California, "that it was the exclusive escrow agent for Concierge, that it could conduct business and perform escrow services in the State of California, and that it was an expert in the field." They say that these claims induced them to sign the Bidder Agreement.

The court dismissed this claim. It agreed with Boston National that it was not responsible for the claims made in the Bidder Agreement. Concierge wrote that agreement and signed it. Boston National did not write those statements. The court dismissed a similar claim under the California False Advertising Law for the same reasons.

The Appel group also sued under the Unfair Competition Law, claiming that the Boston National website says that the company can conduct escrows in California. The court agreed with Boston National that that claim failed because the bidders did not claim to have viewed the website before they deposited their money.

The court dismissed the Appel group's claims of fraudulent concealment, fraudulent misrepresentation and negligent misrepresentation because those claims were predicated on the false notion that Boston National knew when the money was deposited that the Fiji owners had refused to sell. The court said the facts showed that the Appel group learned this at the same time as did Boston National, and spent two months trying to convince the owners to sell before they asked for the return of the money.

The court refused to dismiss the conversion claim. The Appel group asserted that Boston National "substantially interfered with Plaintiffs' ownership and possession of the Escrow Funds by intentionally taking possession of, preventing Plaintiffs from having access to, and refusing to return the Escrow Funds after Plaintiffs demanded their return, to which Plaintiffs did not consent." The court said that, although the money was returned, this did not moot the plaintiffs' claims for the attorney's fees they incurred in getting the money, or the alleged interest on the money. The court also refused to dismiss the claims of negligence and breach of fiduciary duty.

The plaintiffs' most fanciful and frightening claim was based on the doctrine of the tort of another. In this complaint, the plaintiffs alleged that Boston National's refusal to immediately return the money *forced* them to spend "hundreds of thousands of dollars in attorneys' fees" in suing Concierge, which money they now sought from Boston National "pursuant to the tort of another doctrine."

The tort of another doctrine is an exception to the American rule about attorneys' fees. The seminal California case establishing the tort of another doctrine was *Prentice v. North American Title Guaranty Corp.*, 59 Cal. 2d 618 (1963), wherein the California Supreme Court held:

> *A person who through the tort of another has been required to act in the protection of his interests by bringing or defending an action against a third person is entitled to recover compensation for the reasonably necessary loss of time, attorney's fees, and other expenditures thereby suffered or incurred.*

Id. at 620. Later decisions have emphasized, however, that "the *Prentice* exception was not meant to apply in every case in which one party's

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wrongdoing causes another to be involved in litigation with a third party." Rather, the rule is limited to cases involving "exceptional circumstances."

The court said that the plaintiffs "have pled themselves out of using the tort of another doctrine." The doctrine does not apply "to one of several joint tortfeasors." *Vacco Indus. Inc. v. Van den Berg*, 5 Cal. App. 4th 34 (1992). The doctrine "does not reach so far as to allow plaintiffs to pick and choose which one of several joint tortfeasors should absorb the costs of the plaintiffs litigating with the other tortfeasors." *Gorman v. Tassajara Dev. Corp.*, 178 Cal. App. 4th 44, 81 (2009); see *MJT Secs., LLC v. Toronto Dominion Bank*, No. 04-16362, 2006 WL 123661, at *2 (9th Cir. 2006) (holding the doctrine can be used if two parties commit "separate and distinct tort[s]" but not if they are joint tortfeasors).

The court said that the Appel group had alleged the same conduct by Concierge and Boston National (not returning the funds) that contributed to a single injury (the loss of the use of the money). The court said that they had thus alleged that Concierge and Boston National were joint tortfeasors. Therefore, their attorney's fees against Concierge "were caused by its decision to pursue a joint tortfeasor, rather than simply seek a recovery based on [Boston National's] negligence."

Finally, the court dismissed the Appel group's demand for punitive damages. The court had already found that they had not sufficiently alleged fraudulent conduct. Beyond their allegations of fraud, the plaintiffs merely used "buzzwords" suggesting fraud or malicious conduct.

Unfortunately, this case likely bears monitoring by California escrow companies. It certainly illustrates the difficulties that can flow from the deposit of money prior to the signing of enforceable escrow instructions, or even an enforceable purchase contract.

Escrow Matters

Attorney Closer Personally Liable for Assisting in Loan Fraud

Fifth Third Mortgage Co. v. Kaufman, ___ F.3d ___, 2019 WL 3759395 (7th Cir. (Ill.) 2019) (not yet released for publication).

The owner of a title agency who also personally conducted loan closings is liable to the lender for having failed to report to the lender that the borrowers were straw buyers and had made misrepresentations in their loan applications.

Yaseen Ahmed was the president of High Point Developers Inc. and the co-owner of a condominium on South Michigan Avenue in Chicago. Ahmed and Eliot Higueros recruited people to pose as buyers for the units. The straw buyers submitted loan applications to several lenders, including Fifth Third Mortgage, that made false statements about employment, assets and income. The applications also falsely said that the buyers would make the units their primary residences, which was likely the most obvious misrepresentation since each person bought more than one unit.

Attorney Ira Kaufman conducted the closings on 26 unit sales, involving nine borrowers, at the South Michigan property. The closing agent for those sales was Traditional Title, a company owned by Kaufman. Kaufman also closed four other loans made by Fifth Third for buyers of units in other buildings owned by Ahmed. He served as the seller's attorney in all the sales.

Ahmed arranged for a total of 35 mortgage loans. He and his fraud partners kept all the loan money. No payments were made on the loans. Ahmed and five others pled guilty to criminal charges.

Fifth Third Mortgage sued several people and businesses tied to the scheme, including Kaufman. After a bench trial, the court entered a money judgment in favor of Fifth Third against Kaufman.

The crux of Fifth Third's case was the loan closing instructions it had issued to Traditional Title, which required the title company to tell the bank about "any misrepresentations that would influence the bank's decision to make the loan," as the court phrased it, including an instruction to suspend the transaction and notify Fifth Third if "the loan is owner occupied and the closing agent has knowledge that the borrower does not intend to occupy the property." The trial court held that Kaufman violated those instructions by concealing the buyers' misrepresentations from Fifth Third and telling closing agents "to complete closings even when buyers were purchasing multiple properties."

At trial, Kaufman testified that he was not aware of the loan fraud scheme. He said he reviewed the numbers on the closing statements but "didn't really look at the people." He also said that it was not his job, as the seller's attorney, to review the closing instructions or the buyers' loan applications.

Ahmed, however, testified that Kaufman knew the buyers were part of the scheme. Two closing agents, Julio Martinez and Michael Lee, testified that they informed Kaufman about the misrepresentations in the loan applications. Kaufman testified that they never gave him that information. (It is often the case that the fraudsters receive better plea deals from prosecutors if they implicate other parties such as loan closers.)

Kaufman appealed. His first argument was that he should be shielded from personal liability for the aiding and abetting claims because he was merely the owner of Traditional Title. The appeals court affirmed the judgment, and the finding by the trial court that Kaufman was sued for his own acts in conducting the loan closings, not solely in his role as manager or owner of Traditional Title. The court especially observed that Kaufman had been involved personally in all the closings, as counsel for the seller, and had personally "directed Traditional Title's employees to conceal the fraud from Fifth Third."

The appeals court also rejected Kaufman's argument that an attorney cannot be found personally liable for aiding and abetting a fraud perpetrated by his client. The court quoted an Illinois decision to the contrary:

> *… we see no reason to impose a per se bar that prevents imposing*

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liability upon attorneys who knowingly and substantially assist their clients in causing another party's injury. As we have recognized, one may not use his license to practice law as a shield to protect himself from the consequences of his participation in an unlawful or illegal conspiracy. The same policy should prevent an attorney from escaping liability for knowingly and substantially assisting a client in the commission of a tort.

Thornwood, Inc. v. Jenner & Block, 344 Ill.App.3d 15, 278 Ill.Dec. 891, 799 N.E.2d 756, 768 (2003). The court further held that the record supported the district court's conclusion that Kaufman was substantially involved in the scheme, by reviewing closing statements, hosting the closings, and attending the closings "despite knowing the loans were obtained using straw buyers to defraud the lenders as a part of Ahmed's scheme." The court found a but-for causation in Kaufman's involvement, saying that "[w]ithout his participation, the scheme would have failed entirely."

This is another sobering decision placing the blame and the financial liability for borrower loan fraud squarely on the closing agent.

Escrow Matters

Escrow Claims Filed Late; Could Have Been Discovered in Time

Sky Station Holdings I, LP v. Fidelity Nat'l Title Ins. Co., 2019 WL 3786569 (Tex.App.-Austin) (unpublished).

The limitations period for claims made by a lender concerning the closing of an allegedly fraudulent loan began running when the lender received several documents asserting fraud. The lender's claims against the escrowee were dismissed because the action was filed after the limitations period had run.

In the summer of 2006, J&T Development Group LP bought a 367-acre tract of land in the Austin, Texas area. A short time later, J&T transferred 200 acres of that parcel to Waterfall Gallery of Austin LP. Vitaly Zaretsky and Gennady Borokovich were the principals of both J&T and Waterfall.

Interim-HZ Funding LLC lent $11 million to Waterfall when it "bought" the 200 acres. Fidelity National Title served as escrowee for the sale and loan. About $1.5 million of the loan money was delivered by Fidelity to J&T's attorney after escrow closed.

In December 2006, Alexandra and Alexander Krot III sued Zaretsky, Borokovich, Waterfall and others, claiming that they had delivered money to buy the Waterfall parcel and that they were supposed to be partners in the owner entity. They claimed that J&T had fraudulently transferred the property to Waterfall, controlled by Zaretsky and Borokovich. The Krots filed a notice of lis pendens against the property.

Waterfall defaulted in 2007. Interim Funding started a foreclosure proceeding. It got a title report that listed the Krot lis pendens. The loan was assigned to Sky Station Holdings I LP in May 2008.

Waterfall filed for bankruptcy in June 2008, the day before the foreclosure sale was to take place. Sky Station received a copy of a motion filed by Borokovich in the bankruptcy, claiming that the case should be dismissed because Zaretsky had "engaged in a pattern of fraud and perjury." He claimed that J&T bought the bigger tract for $11.5 million three months earlier, that Zaretsky inflated the $17.6 million price for the purported sale to Waterfall, that he had represented to potential investors that the land was worth $27 million, and that the deed from J&T to Waterfall was not a sale at all.

The Krots also got involved in the bankruptcy, asserting their claims in that forum. Also during the bankruptcy, Sky Station had the property appraised, and its value was ascribed as being $8.1 million. In mid-2008, Sky Station got the bankruptcy court to lift the stay, and it foreclosed on the property in November of 2008.

About four years later, in April 2012, Interim Funding filed a Pre-Suit Petition to Take Deposition to Investigate Potential Lawsuit, seeking to depose a Fidelity corporate representative. At the hearing on the motion, Fidelity's lawyer explained that he did not believe the procedural rule allowed Interim to subpoena documents, but that Fidelity would produce its escrow file if Interim gave it the escrow number. The trial court signed an order in July 2012 requiring the production of the file, and Fidelity provided the file 30 days later.

In December 2012, Sky Station filed suit against Fidelity, bringing claims for breach of fiduciary duty, common law fraud, constructive fraud, fraudulent inducement, negligence, negligence per se and breach of contract. Fidelity moved for summary judgment, because of all Sky Station's claims were barred by limitations. The longest limitations period for those claims was four years. Sky Station resisted the motion on the assertion that the limitations periods were tolled under the discovery rule until it obtained the escrow file. The trial court ruled in Fidelity's favor.

Sky Station appealed, and the court affirmed the holding in Fidelity's favor. It rejected Sky Station's claims that the limitations period was extended under either the discovery rule or the fraudulent concealment doctrine.

The appeals court began by noting that, despite these two special rules, the plaintiff's "actual knowledge of alleged injury-causing conduct starts the clock on the limitations period" and "triggers the putative claimant's duty to exercise reasonable diligence to investigate the problem, even if the claimant does not know the specific cause of the injury or the full extent of it." *Exxon Corp. v. Emerald Oil & Gas Co.*, 348 S.W.3d 194, 209 (Tex. 2011). In some cases, a court can decide as a matter of law that reasonable diligence would have uncovered the alleged wrong.

The court ruled as a matter of law that the summary judgment evidence had established that Sky Station learned in 2008 that there likely had been fraud in the sale and loan. Sky Station received the Krot motion for relief from stay that described their lawsuit against Waterfall, Zaretsky, Borokovich and J&T. It also received Borokovich's motion detailing his allegations against

Zaretsky of several types of fraud in the sale and loan. Sky Station also got a copy of the Krot lis pendens, which put it on inquiry notice of what they had alleged in that case. Sky Station also received its own appraisal showing that the property was worth about half of the purported sale price from J&T to Waterfall. The appeals court said:

> *In 2008, Sky Station may not have known all of the details of Fidelity's and Serebro's involvement and alleged misconduct, but it knew of its likely injury—that its predecessor had been the victim of fraud in the real estate transaction.*

The court then observed that Sky Station did not even attempt to obtain Fidelity's file until four years later, in May 2012. It rejected Sky Station's after-the-fact assertion that Fidelity might not have given the escrow file to it, noting instead that the company turned over the file when so ordered. The court concluded:

> *Thus, having been informed of fraud and missing funds related to the transaction, the record indicates that Sky Station could have discovered Fidelity's … alleged involvement in the misconduct had it looked into the transaction in 2008. … [Fidelity] therefore defeated Sky Station's attempted defenses to limitations by establishing as a matter of law that Sky Station's responsibility to use reasonable diligence to investigate its possible claims related to the loan transaction arose no later than July 2008, more than four years before it filed suit.*

The court also found that there was no evidence that Fidelity had ever had actual knowledge "that a wrong had occurred or an intent to conceal the facts necessary for Sky Station to know it had a claim." Therefore, the fraudulent concealment doctrine did not extend the limitations period.

Conveyance News

Oregon Supreme Court Tempers Test for Reformation of Deed of Trust

Troubled Asset Solutions, LLC v. Wilcher, ___ P.3d ___, 365 Or. 397, 2019 WL 3491209 (Or. 2019).

The Oregon Supreme Court has held that a lender is entitled to reformation of a deed of trust that failed to name one of the property owners as a grantor. The court provided a gentler interpretation of its longstanding rule that a party guilty of gross negligence is not entitled to reformation.

Sierra Development LLC borrowed $5 million from The Mortgage Exchange. The promissory note said that the loan would be secured by several properties in Oregon, including the land owned by Sierra that was to be developed with the loan money plus several other properties owned by Eddie Wilcher. The note specifically identified Wilcher's house in Keno. Wilcher was a member of Sierra, and he signed a personal guaranty for the loan.

The Mortgage Exchange drafted the trust deed. It included the legal description for the Keno house and acreage, and Wilcher signed the instrument. However, the only grantor named on the deed of trust was Sierra; Wilcher was not named.

Sierra defaulted on the loan. The loan was sold to Troubled Asset Solutions. TAS tried to foreclose on one of the properties owned by Wilcher. He raised the drafting problem as a defense.

Wilcher sued to quiet title, asking the court to declare that the deed of trust did not encumber the Keno house or other land owned by him individually. TAS counterclaimed, seeking to reform the trust deed. The trial judge reformed the trust deed, holding that the drafting error was "easily missed" and that the evidence was overwhelming that both parties had intended the trust deed to encumber Wilcher's properties.

Wilcher appealed. That court reversed. The appeals court relied on Oregon's longstanding rule that reformation requires proof of an agreement, a mutual mistake in the contract, and the absence of "gross negligence" by the party seeking reformation. It announced that "no factfinder could conclude that failing to name Wilcher as a grantor was 'mere oversight, inadvertence, or mistake.'"

The Oregon Supreme Court accepted review of the case. It reversed again and reinstated the trial court ruling reforming the trust deed. TAS asserted that, since reformation is an equitable remedy, the court must balance the equities in deciding whether to grant the remedy. It also invited the court to abandon the gross negligence element and adopt the reformation test espoused by the *Restatement (Second) of Contracts*.

Wilcher responded that gross negligence has been interpreted in Oregon to mean "heightened negligence," and that "it does not incorporate other equitable principles." He asserted that, while a party is not grossly negligent for failing to read a document, a party drafting a document is automatically grossly negligent if it fails to insert an important term in that instrument.

The high court admitted that Wilcher "is not necessarily inaccurate in quoting some of the formulations of the 'gross negligence' requirement" in prior Oregon decisions. However, it concluded that he was advancing "a cramped and abstract interpretation of that requirement that is inconsistent with our case law."

The high court said the court of appeals had erred "by focusing only on the conduct of MEX and its agents and by failing to consider the equities of the case, notably whether anyone would be prejudiced by reformation of the contract." The appeals court had said that "the omission of a crucial term when drafting a trust deed can rise to the level of gross negligence." The person at The Mortgage Exchange who drafted the deed of trust was experienced. Its only justification was that it had expected the title company to "catch any errors before closing," which apparently did not happen. The high court said that what was missing from the appeals court analysis was any consideration of harm

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in not granting reformation to make the trust deed enforceable.

The Supreme Court gave a lengthy discussion of its prior reformation decisions, going all the way back to the first use of the term "gross negligence" in relation to that remedy, in *Lewis v. Lewis*, 5 Or. 169, 174 (1874). The court kept emphasizing the fact that reformation is granted to prevent injustice, and to keep a party to the contract from gaining an advantage by the oversight of the other party. It noted a 1943 decision that held that "[s]ome mistakes prejudice no one except those who commit them, and therefore, cancellation will prejudice no one. In such a case a considerable degree of carelessness can be tolerated." In the 1952 *Edwards Farms* decision, in which a party drafted a contract with the wrong terms, the court had said that the party opposing reformation had to prove it would be harmed before the court even considered the issue of negligent drafting.

The high court also observed that the term gross negligence has been criticized because it is so hard to define or quantify. It quoted with approval a comment in the Restatement that a party should be barred from seeking reformation only when his or her fault "amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing." The court concluded that the facts showed that nothing about the lender's conduct "was anything other than a careless mistake, of the type that we never have found to bar reformation absent prejudice to the other party."

The court also held that the lender's use of a highly qualified person to draft the trust deed "supports the argument of a party seeking reformation that it was not negligent at all, let alone grossly negligent, when a mistake is made in one of the transaction documents." It said that the appeals court had it all wrong in concluding that the use of an experienced draftsperson was evidence of gross negligence:

> *Combined with the Court of Appeals' suggestion that a party responsible for a drafting error will find it difficult to prove lack of gross negligence, the court's comments on using qualified personnel suggest that it would view any substantive mistake by the party that prepared the documents, or an agent acting on that party's behalf, as likely to constitute gross negligence attributable to that party. Such a standard would dramatically alter the landscape of contract reformation by collapsing gross negligence into ordinary negligence, as well as explicitly jettisoning the prejudice and equitable considerations inquiry that we have discussed at length above.*

However, the court refused to simply abandon its reformation standard in favor of adopting the Restatement position wholesale. It said: "Imperfect as the term 'gross negligence' may be, understood as we have applied it here and in cases going back more than a century, we believe it is sufficient to guide courts of equity in determining whether reformation is appropriate in a given case."

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Title Insurance

Arizona Measures Loss as of Policy Date on Some Lender Claims

First American Title Ins. Co. v. Johnson Bank, ___ P.3d ___, 2016 WL 3247545 (Ariz. 2016) (permanent citation not yet available).

The Arizona Supreme Court has ruled that loss is measured based on the value of the property on the policy date, for a claim on a loan policy, when the claim involves an encumbrance on title and the lender can establish that the borrower defaulted due to the encumbrance. The court found the policy ambiguous because it does not say what date is used to measure loss.

In 2005 and 2006, Johnson Bank made loans on two parcels in Arizona and First American Title issued two policies in the combined amount of $2,050,000. The policies did not except a recorded declaration of restrictions that prohibited commercial development of the parcels.

The borrowers defaulted on the loans. Johnson Bank now claims that the default was directly caused by the restrictions, which prohibited the borrowers from developing the parcels as they had intended.

The owners sued First American and recovered under their owner's policies. Then, in 2010, Johnson Bank took title through its trustee's sale, at which it made a credit bid of $102,000 for both parcels. In 2011, Johnson Bank made a demand on its loan policies, based on the same restrictions.

The bank and insurer agreed to arbitrate the claims. However, they disagreed about how to measure loss, with Johnson pushing the policy date as the valuation date and First American asserting that loss should be measured as of the date of the foreclosure. The court admitted that the property's value plummeted between 2005 and 2010, based solely on the real estate market.

Because of this disagreement, Johnson Bank and First American Title agreed to ask the superior court to decide the measure of loss issue. Both sides filed motions for summary judgment. The superior court agreed with First American Title, ruling that the parcels should be valued as of the foreclosure date. Johnson Bank appealed. The court of appeals reversed, holding that the policy date should be used because the policy was ambiguous due to the fact that it does not prescribe the loss date. See the decision at 237 Ariz. 490, 353 P.3d 370 (Ariz.App. 2015), reported in the September 2015 issue.

First American appealed to the state supreme court, which accepted the case. The Land Title Association of Arizona filed an amicus brief, as did two private lenders with a pending case on the same issue, who urged the court to affirm the court of appeals decision.

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The appeals court had ruled flatly that, because the policy did not set a date of loss, the date of policy should be applied to any claim on a loan policy. [Arizona held more than 20 years ago that loss under an owner's policy is measured as of the date of discovery of the title issue, in *Swanson v. Safeco Title Ins. Co.,* 186 Ariz. 637, 925 P.2d 1354 (Ariz.App. 1995).] The supreme court narrowed the ruling of the appeals court, tailoring the result to the allegations made by Johnson Bank.

The supreme court acknowledged that the majority of courts have said that loss under a loan policy is measured either as of the date the insured's lien is extinguished by the foreclosure of a senior lien for which the policy provides coverage, or the date on which the insured takes title by foreclosure. Because the issue in this case was a use restriction, the court adopted a novel but very narrow principle: that loss is measured as of the policy date when the policy does not except an encumbrance, and the borrower defaults on the loan solely due to the existence of that covered risk. A dissenting justice made the simple but compelling point that this formula converts the policy from a contract of indemnity to a guaranty that title is as stated in the policy, contrary to the Arizona title code's definition of a title insurance policy and of long-accepted case law.

The majority opinion began with Johnson Bank's twisted argument that Conditions & Stipulations 7(a)(iii) of this 1992 form ALTA loan policy impliedly does contain a loss date. That provision says that loss is "the difference between the value of the insured estate or interest as insured and the value of the insured estate or interest subject to the defect, lien or encumbrance insured against this policy." Johnson argued that the phrase "as insured" indicated "when the property is to be valued" and means that "the property should be valued as of the date that the insurance policy issued." First American responded that the phrase "as insured," which is used throughout the policy, refers only to the state of title as depicted in the policy, particularly in Schedule B if the subject of the claim is a recorded instrument that is not excepted. The supreme court at least impliedly agreed with First American, by holding that Conditions 7 does not set a loss date.

Johnson Bank also argued that the policy was ambiguous if it does not set a loss date, and therefore the high court should adopt any reasonable interpretation of the policy that would penalize the insurer for having issued the ambiguous policy. First American countered this argument with decisions that have held that the lack of a date of loss does not create an ambiguity, including *First Tenn. Bank, N. A. v. Lawyers Title Ins. Corp.*, 282 F.R.D. 423 (N.D. Ill. 2012). First American urged the court to accept the date of foreclosure as the loss date, because of the substantial body of law holding that no loss is payable to the lender until it takes title to the property.

The supreme court held that the lack of a loss date did make the policy ambiguous, "[u]nder the facts of this particular case." It then began to thread the needle between all of the prior decisions and the facts of this case, in order to arrive at a different conclusion under these facts without rejecting the reasoning of the other courts. The court said that the courts that found the policy unambiguous were different because, "[u]nlike this case, those cases involved undisclosed senior liens in which courts found that the policy unambiguously requires using the date of foreclosure as the valuation date." Dissenting Justice Bales said, by contrast, that the policy was "facially ambiguous" because the loss date was missing, but that all loan policies should be construed under the same rules, all of which point to loss being measured on the date the lender

The majority said that First American's argument that the date the bank took title should be the loss date "conflates two concepts." It rejected the reasoning of many other courts that had adopted this principle, saying that:

> *Although the insured lender's exact loss might not be calculable until foreclosure occurs, that calculation can be made using the property's value, with and without the defect, as of the policy date to determine the actual loss on the date of foreclosure.*

It supported that argument with the fact that "the policy contains several contractual prerequisites" to the making of a claim, not just that the lender come into title. The lender, for example, must send a claim notice and proof of loss. The court said that, because loss is not measured on the date the claim notice is sent, neither should it be measured as of the date the insured takes title. It cited no decision that had used a similar analysis.

The court nonetheless agreed with First American that the loss date "might well be" when the insured lender takes title, if the issue is a lien rather than a restriction. It said:

> *When the title defect is an undisclosed lien, the foreclosure date might well be the appropriate valuation date because the lender's damage results from not having priority in the foreclosure proceeds. See First Tenn. Bank, 282 F.R.D. at 427; see generally Christopher B. Frantze, Equity Income Partners LP v. Chicago Title Insurance Co. and Recovery Under A Lender's Title Insurance Policy in A Falling Real Estate Market, 48 Real Prop. Tr. & Est. L.J. 391, 392 (2013) (surveying cases). But to the extent the foregoing cases suggest that, regardless of circumstances, lenders' title insurance policies like that at issue here clearly establish the date of foreclosure as the only damage-valuation date because the existence and extent of any loss is unknown before then, we find them unpersuasive.*
>
> *In any event, the title defect in this case is not an undisclosed lien, but is instead undisclosed CC&R's that prevented the borrowers/owners from developing the property, which in turn allegedly caused them to default on their loans. The policy does not clearly identify the appropriate valuation date for calculating the lender's loss in these circumstances, and thus the court of appeals did not err in finding the policy ambiguous on that issue.*

The Arizona high court has stated previously, in the context of a title insurance policy, that an insurance

contract ambiguity is not resolved simply by finding that there are two possible "reasonable" interpretations of the policy, and then adopting the one proposed by the insured in order to punish the insurer for having allowed the ambiguity to exist. It paid lip service to the rule that, "[i]n interpreting an insurance policy, we apply 'a rule of common sense' thus, 'when a question of interpretation arises, we are not compelled in every case of apparent ambiguity to blindly follow the interpretation least favorable to the insurer.'" Rather, the court has said that:

> *If a clause appears ambiguous, we interpret it by looking to legislative goals, social policy, and the transaction as a whole. If an ambiguity remains after considering these factors, we construe it against the insurer.*

First Am. Title Ins. Co. v. Action Acquisitions, LLC, 218 Ariz. 394, 397 ¶ 8, 187 P.3d 1107, 1110 (2008) [reported in the January, 2009 issue].

However, the court had trouble justifying its result based on statutory intent and social policy. First, the majority put on blinders as it considered how its interpretation of the policy's terms matched "legislative goals." It said that there was "no statute or other binding legal precedent in Arizona that determines the starting date of comparative valuation of property for calculating covered losses under a lender's title insurance policy." Of course, if the Arizona title insurance act had set the loss date under a loan policy, the court would not have needed to make any ruling. Dissenting Justice Bales said that the legislative intent was expressed in the fact that Arizona statutes say that a title insurance policy is not an abstract of title, and that a commitment and policy do not guaranty that every title encumbrance that affects the property is excepted from coverage. The majority replied that "no identifiable legislative goals affect or resolve the issue before us," because Johnson Bank's claim was based on the contract, not a claim for abstractor negligence.

However, in the very next paragraph, the majority said that the "social policy" in support of its conclusion was that a title insurer should pay the lender for a reduction in market value as if a title insurance policy did guaranty the state of title shown in the policy:

> *In this case, social policies and fundamental aspects of the parties' transaction support using the date of the policy as the valuation date. The insurer has complete control of the title defects against which it insures; it is in the best position to avoid such risks and prevent resulting loss by conducting thorough and accurate title searches. Here, First American's deficient title search resulted in its failure to discover and disclose the adverse CC&R's that had been recorded against the property in 1985.*

The court buttressed its notion of the "social policy" in favor of having the insurer pay for a decline in market value with the comments of law professors. It quoted professor Burke's book for these nuggets of folk wisdom:

> *Using the foreclosure date as the damage-valuation date would allow the insurer to profit from a depreciating market even when the title defect caused the borrower to default. See Barlow Burke, Law of Title Insurance § 7.04 (3d ed. Aspen Publishers 2004) (noting that if an insurer collects a premium based on the loan's face amount and then, when title fails in a falling market, argues the decrease resulted from market conditions and thus "seeks to pay less than the amount of the insurance purchased and the loss of capital sunk in the purchase price," "the insurer is in a 'tails I win, heads you lose' position").*
>
> *... Finally, using the foreclosure date when the title defect caused the borrower to default would unfairly allow the title company to avoid the insured's actual, resulting consequential damages. Id. ("The choice of a date for measuring damages should not provide the insurer with an opportunity to shield its eyes from the insured's actual, economic, and consequential losses.").*

The court got the idea that it could adopt different dates of loss for *different* types of title issues from a similar bit of homespun philosophy found in professor Palomar's book:

> *Finally, the lack of a specific valuation date in title insurance policies allows a case-by-case approach to value the insured's loss. Joyce Palomar, 1 Title Ins. Law § 10:16 (2015 ed.) ("Because ALTA policies have not specified the date the value of the property is to be assessed to measure an insured's loss, courts need to determine the insured's actual loss in the particular circumstances."). If the foreclosure date were the universal valuation date to be used regardless of circumstances, then courts and the parties could not evaluate the insured's actual loss in a particular case.*

The court concluded this part of its analysis by again reminding title insurers that, if they want rationality, they should simply insert a date of loss provision in the policy:

> *And if title insurers desire to avoid all uncertainty by establishing the foreclosure date or specifying some other damage-valuation measure to uniformly apply in all situations, they can modify their policies accordingly.*

Further, the court concluded that it was not unfair to make an insurance company pay the insured the amount by which the property declined in value due to market conditions for two reasons. The first was that the policy does not exclude that "risk" from coverage:

> *Under the policies, First American did not expressly agree to indemnify or otherwise insure against the risk of a drop in the real estate market. But the policies also do not exclude coverage for loss resulting partly from such risk, nor do we hold that a title company, as a general commercial matter, bears that risk.*

Second, the court said that, although a lender does inherently assume the risk that its collateral will fall in value, the insurer must take over that risk when the policy fails to exclude an encumbrance that frustrates the borrower's intended improvement of the property:

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When an undisclosed, material title defect completely frustrates the borrowers/owners' intended use of the property and directly causes their default and the subsequent foreclosure, an insured lender's recoverable damages may include loss resulting from a declining real estate market. We acknowledge that, for purposes of § 7(a)(iii) of the policy, measuring the difference in value at the time of policy issuance for a loss that does not occur until foreclosure in a down market may effectively shift to the title insurer part of the loss attributable to the market downturn (which could occur irrespective of any title defect or error in the title search). Under these particular circumstances, however, that consequence offends neither the policy language nor the relevant, identified social policies. As a leading treatise has explained, reasons that support using the policy date to measure the lender's loss in a falling market include: "the purpose of the policy from the standpoint of the insured is future indemnification;" and "the policy date is consistent with fully compensating the insured for his or her 'actual losses' under the policy." Id.

The "leading treatise" on which the court relied for this novel conclusion was, again, professor Burke's book.

The court said this was not unfair, because although banks "are in the business of assessing the risk that their loans will not be repaid, including the risk of market declines," they make that risk assessment "when banks enter into a loan contract, not when a default and foreclosure occur sometime later." Therefore, "in determining damages caused by First American's incomplete title search under the facts presented here, social policy does not preclude using the date the policies were issued as the valuation date." In other words, the court said, part of the "loss" that a title insurer has contracted to pay is the decline in market value, if it conducts an "incomplete title search" that causes the borrower to lose the ability to develop the land as it intends. Nonetheless, the court protested that:

... Using the date of the policy does not convert the indemnification policy into a guarantee of title. First, the insurer will be liable only if the loss results due to a discoverable defect or encumbrance on the title. ... Second, under the policy, the lender must demonstrate an actual loss. ... Third, the title insurance policy applies only if a title defect caused the insured's loss. ... Using the date of policy issuance as the valuation date under the circumstances here does not change the nature or scope of the policy's coverage.

* * * *

...[I]n resolving the ambiguity in First American's policy by evaluating relevant social policies and the parties' transaction as a whole, we quite properly consider that First American was in the best position to timely discover and disclose the title defect, and to thereby avoid the risk of loss in a depreciating real estate market, but failed to do so. ... Because evaluation of relevant social policies and the parties' transaction as a whole does not resolve the policy's ambiguity, and because we must then construe the policy against the insurer, First American should bear that risk.

Finally, the high court said its reasoning was not the same as that used by the appeals court, which relied on a federal court decision that set the date of policy as the date of loss. In *Equity Income Partners v. Chicago Title Ins. Co.*, 2012 WL 3871505 (D. Ariz. Sept. 6, 2012), the federal court "embraced the reasoning of" *Citicorp Savings of Illinois v. Stewart Title Guar. Co.*, 840 F.2d 526 (7th Cir. 1988). *Citicorp*, which also concerned a policy issued just before a real estate downturn, held that loss should be measured as of the date of policy because the insured lien was invalid when granted.

First American had labeled *Citicorp* and its progeny as the "minority view," which it is. The Arizona supreme court said it looked at the issue not as a matter of majority or minority positions, but rather as two basic classes of claim types: senior liens versus issues that made title worthless. It said that most of the courts that have rejected *Citicorp* involved unexcepted senior liens. Because this case did not involve a senior lien, the majority said, "those cases are not persuasive or particularly helpful."

The court then said that *Citicorp* was the vanguard of the decisions concerning the other class of claims, those that "involved situations where, as here, a total failure of title occurred and courts used the loan date to measure damages." However, the decisions it cited as falling under that category are not unified by any fact other than that they involved something other than a senior lien. In *Citicorp*, the insured mortgage was invalid, but the title insurer replaced it with an equitable lien that the lender could have foreclosed but which it refused to accept. *In re Evans*, also cited by the court, involved a good lien on land that had been subdivided without the necessary approvals. *Equity Income Partners* involved a valid deed of trust granted on land that had no recorded access easement. This case concerned a valid deed of trust secured by land subject to a use restriction that did not render the property valueless but that was contrary to the subjective intended use by the borrower.

The majority nonetheless lumped these decisions together under the banner of claims involving title issues that "rendered the property essentially worthless," which the majority said was "a different species of breach." This creative new categorizing of the decisions, devoid of their reasoning, allowed the majority to conclude that "the case law from other jurisdictions does not influence the relevant social policies for determining the appropriate valuation date in this case."

However, the majority justices did significantly limit the reasoning of *Citicorp*, by holding that loss is measured on the policy date only if the title issue *causes* both the loan default and the foreclosure by the lender. It reached this conclusion:

There is no evidence demonstrating that the undisclosed title defect caused the borrowers' default. Although Johnson Bank points to the unpublished court of appeals' decision that affirmed judgment in favor of the borrowers/owners in their action against First

American, that case does not establish as a matter of fact or law that the title defect caused the borrowers' default. ... Accordingly, the court of appeals erred by directing entry of summary judgment in favor of Johnson Bank. ...

On remand, Johnson Bank will have to prove that the title defect caused the borrowers' default and subsequent foreclosure to justify using the date of the policies as the valuation date. If Johnson Bank fails to satisfy this burden, then the proper valuation date is the foreclosure date.

The majority opinion does not acknowledge that the policy is silent on the two issues on which its loss formulation depends: the intended use of the property by the borrower (who is not the insured under a lender's policy), and the reasons why the borrower stopped making payments. Both of those subjects are well beyond the ambit of the policy. A title insurance policy insures title and not use. A loan policy certainly does not "insure" the *borrower's* right to construct a future improvement for an undisclosed and unstated intended use of the property. The policy also does not insure the debt or protect the lender against the borrower's default on that debt. The idea of incorporating these two subjective elements into the analysis of how to measure loss due to an encumbrance on title is foreign to the actual terms of the policy. It also means that both lender and insurer must measure the amount of loss based on what the foreclosed borrower says about his or her intentions and actions.

The most rational statement by the majority was that a title insurer could avoid this lunacy by inserting a loss date in the policy.

Title Insurance

Title Insurer Did Not Violate E-recording Agreement by Recording Copy of Lost Deed

Estate of Myrman v. U.S. Bank, N.A., 2016 WL 3264120 (Ariz.App. 1 Div.) (unpublished).

An insured deed of trust was not invalid because the deed transferring the property from the borrowers as trustees to themselves as individuals was not recorded. Also, the title insurer's later electronic recording of a copy of that deed did not violate its trusted-submitter agreement with the recorder or amount to the recording of a sham conveyance in violation of an Arizona statute. The court also explained that a deed is effective on delivery, not recording, so the self-serving arguments of the borrower seeking to void the deed of trust were unavailing.

In 2006, Earl and Virginia Myrman got a loan from Downey Savings & Loan and granted a deed of trust on their home to the lender. Downey insisted that the Myrmans sign the deed of trust as individuals, which meant that they had to convey the property as trustees of their living trust to themselves as individuals. The Myrmans signed the deed and handed it to the escrow company. However, the deed was not recorded with the deed of trust.

First American Title, which was not the escrowee, issued a policy to Downey even though the deed had not been recorded. U.S. Bank took an assignment of the loan from Downey Savings.

Both of the Myrmans died. Virginia Myrman survived her husband. She stopped making loan payments shortly before she died in 2011.

When the bank started gearing up to conduct a trustee's sale, it realized that the quit claim deed had not been recorded. It made a claim on the First American policy. The insurer found a copy of the Deed and recorded it electronically.

Ladien Steelman, the Myrmans' daughter, became the trustee of the Myrman trust and the personal representative for her parents' estates. In 2013, Steelman as personal representative sued herself as trustee of the trust, asking the court to declare the deed void because it did not contain certain trust-related disclosures required by statute. Steelman did not name either U.S. Bank or First American in that lawsuit. The court entered the requested order, declaring the quit claim deed void.

A few months later, U.S. Bank started a foreclosure by recording a notice of trustee's sale. Steelman sued U.S. Bank and First American, this time as both trustee and personal representative. She alleged that the deed had been "fraudulently recorded and contained false statements and [was] therefore void and of no effect." The court issued a preliminary injunction staying the trustee's sale. U.S. Bank counterclaimed to quiet title. Then all parties moved for summary judgment.

The trial court granted U.S. Bank's and First American's motions, finding the deed valid despite Steelman's objections, and quieted title to the property in favor of U.S. Bank. It lifted the injunction, and awarded attorney's fees to U.S. Bank and First American. Steelman appealed, and the bank agreed to reinstate the injunction until the appeal was decided.

Steelman argued that the deed of trust was invalid because record title was held by her parents as trustees when the deed of trust was signed by them as individuals. She argued that title was never transferred because the original deed was lost. Steelman based her argument on A.R.S. § 33-412(A) (2014), the recording law, which says that conveyances of land "shall be void as to creditors and subsequent purchasers for valuable consideration without notice, unless they are acknowledged and recorded in the office of the county recorder."

The appeals court began by noting that "U.S. Bank's right to foreclose is not based on the Quitclaim Deed, but on the Deed of Trust." Thus, it said, the deed was "relevant only insofar as it affected the transfer of the property from the Trust to the Myrmans individually." It declared flatly that the deed was valid. Steelman was relying on the wrong statute. A.R.S. § 33-412 (B) says that "[u]nrecorded instruments, as between the parties and their heirs ... shall be valid and

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APP044

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binding." Therefore, the court said, the deed did not have to be recorded at all for the deed of trust to be valid.

Steelman's only counter was that U.S. Bank fell under the recording law because it was a "subsequent purchaser for valuable consideration." The court noted, however, that Arizona has a race-notice law, not a pure race recording statute. Thus, if U.S. Bank had notice of the deed, it was bound by it. Moreover, it said, the recording law's purpose is to provide a shield to the subsequent buyer or lender, not a sword to be wielded against them by the property owner. It said that "Steelman's argument is contrary to § 33-412(A)'s clear purpose, which is to protect subsequent purchasers' interests, not void them." The 1982 decision on which Steelman based her argument involved the conventional situation in which the recording law was used to settle the rights of a competing buyer and creditor, and thus did not apply to these facts.

The court also ruled that the judgment declaring the deed void, in Steelman v. Steelman, had no effect on U.S. Bank's rights, since the bank had not been a party in that action. The court also said that the judgment was based on a faulty premise. A.R.S. § 33-404(B) (2014) says that a deed from a trustee must disclose the names and addresses of the trust's beneficiaries. However, the statute also says that the failure to include this information on a deed does not void a conveyance to a party who pays value for the property. The court concluded that Steelman again sought to turn a protection for the buyer into a tool to extinguish its rights, contrary to the purpose of the statute.

The court also held that the deed had been delivered, though not recorded. Steelman tried to put the burden on the bank to prove delivery of the deed. The court responded with the rule that "[n]o specific procedure or action is required to complete delivery of legal title." Instead, Arizona case law has established that delivery is any action or conduct that "clearly manifests the intention of the grantor and the person to whom it is delivered that the deed shall presently become operative ... and that the grantor loses all control over it, and that by it the grantee is to become possessed of the estate." The bank had proven that the Myrmans signed the deed and gave it to the escrow agent for recording, that they did so to induce Downey to lend them the money, and that the Myrmans affirmed the deed by making payments on the loan for about five years. The court found this conduct more than adequate to establish delivery of the deed.

Having ruled that the deed and deed of trust were both valid, the court rejected Steelman's arguments that the bank and title insurer had violated the law by recording the copy of the deed. Steelman's first argument was that both the bank and the insurer had broken the law by recording a "sham" copy of the deed. A.R.S. § 33–420(A) makes a person liable for recording a document asserting an interest in real property while "knowing or having reason to know that the document is forged, groundless, contains a material misstatement or false claim or is otherwise invalid." The court said that the deed was not forged, groundless, or otherwise invalid. The Myrmans delivered the deed to induce Downey to lend them money, "and that is exactly what the Quitclaim Deed accomplished." The court also said that the statute did not even apply, because neither the bank nor the title insurer claimed to own the property by virtue of the deed.

Steelman's second argument was that First American violated the recording law by recording only an image of the deed rather than the original. The court responded that Arizona law allows the recording of a copy of an instrument if the copy is "sufficiently legible for the recorder to make certified copies from the photographic or micrographic record." A.R.S. § 11-480(A)(2) (2012).

Steelman also argued that First American violated a fiduciary duty to her parents by recording the copy of the deed. This claim was premised on an unsigned Memorandum of Understanding between First American and the Maricopa County Recorder's Office about electronic recordings, which is commonly termed a "trusted submitter" agreement. That MOU said that the two parties "desire to operate and maintain a secure recording system that safeguards parties to recordation from deceit, fraud and forgery." Steelman claimed that First American failed to live up to its duties by submitting the deed copy rather than the original.

The court said that Steelman had not even proven that the MOU had been signed and was in effect. Second, it said, First American Title was not a fiduciary, because it did not conduct the escrow and was merely the insurer that issued the policy to U.S. Bank, which is not done in a fiduciary capacity. Third, it said that Steelman and her parents were not members of a class of people who were third party beneficiaries of the MOU even if it was in effect. The court said, referring to the trusted submitter agreement:

> *The language Steelman cites does not confer any direct benefit on the Trust or the Myrmans' estates. At most, taking all inferences in Steelman's favor, the MOU does not support a private cause of action, but merely confers an incidental benefit on Steelman by reducing "deceit, fraud and forgery."*

The court lifted the injunction and allowed U.S. Bank to proceed with the foreclosure on the home.

This decision contains a series of well-reasoned and refreshingly conventional statements about conveyancing law and the purpose of the recording statutes. This is the first decision reported in this newsletter about the purpose and effect of a trusted-submitter agreement.

ALTA Calendar

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October 4-7, 2016
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2017 ALTA Springboard
March 8-10, 2017
Omni Fort Worth, Fort Worth, TX

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Title Insurance

Insurer Cannot Get Attorneys' Fees Against New York Notary

Chicago Title Ins. Co. v. LaPierre, ___ N.Y.S.3d ___, 2016 WL 3177206, 2016 N.Y. Slip Op. 04379 (N.Y.A.D. 2 Dept. 2016) (permanent citation not yet available).

Attorney's fees are not part of the damages that a title insurer can recover from a New York notary public for having acknowledged a forged instrument.

Chicago Title paid out over $100,000 in attorneys' fees and costs to defend an insured because of a forged deed. It sued the notary for its damages. After a trial, the court entered judgment for the notary, on the basis that the insurer was required to prove that it had detrimentally relied on the false notarial act, which it had not proven. In a 2013 decision, the appellate division reversed, finding that the title insurer need not prove detrimental reliance on the notarial act. It sent the case back to the trial court.

Chicago Title moved for judgment before the trial court, based on the $103,000 in fees and costs it had paid to defend title. The notary argued that Chicago Title could not recover what it sought, because it was trying to get paid attorneys' fees contrary to the American rule that parties each pay their own fees in litigation. The trial court agreed with the notary, and appellate division affirmed.

The "American Rule" says that "[a]n attorney's fee is merely an incident of litigation and is not recoverable absent a specific contractual provision or statutory authority." New York's Executive Law § 135 provides that "[f]or any misconduct by a notary public in the performance of any of his [or her] powers such notary public shall be liable to the parties injured for all damages sustained by them… ." The appellate division said that the "plain language of the statute does not explicitly permit recovery of attorneys' fees and costs." It also said that, even if the law might support such an award, "the public policy of the American Rule 'militate[s] against adoption of that interpretation.'"

The court did not even discuss the fact that the fees claimed by Chicago Title were to defend its insured's title which was conveyed by the forged deed, rather than its fees in suing the notary. Attorneys' fees spent to defend title are the most commonly-incurred form of damage resulting from a forged deed.

Agent Focus

Tort Claims Against Agent as Insurance Broker Not Barred by Economic Loss Doctrine

Bank of America, N.A. v. Bailey, ___ F.Supp.3d ___, 2016 WL 3410174 (D.Nev. 2016) (permanent citation not yet available).

Several types of claims against a title insurance agent survived a motion to dismiss because they were premised on its duties as an insurance broker, not as an escrowee. In Nevada, the economic loss doctrine bars escrow negligence claims, but not a claim that an insurance "professional" breached a fiduciary duty.

Pete Aguilar got a roughly $370,000 loan from Bank of America in January 2010 and gave the bank a deed of trust on his house in Las Vegas. In June of 2010, the B of A deed of trust still was not recorded. A business owned by Aguilar and Samuel Bailey got a $500,000 loan from Meadows Bank in June 2010, and Aguilar gave that bank a deed of trust on his house. Meadows Bank bought a title insurance policy from Nevada Title Company, agent of Westcor Land Title Insurance Company, which understandably contained no exception for the unrecorded B of A deed of trust.

In November 2010, the busy Mr. Aguilar refinanced the B of A loan with Franklin America Mortgage. He gave a new deed of trust on his house. The B of A loan was paid off and Bank of America released its deed of trust.

After the Franklin loan was closed, Franklin asked Meadows Bank to subordinate its lien to the Franklin deed of trust, which it refused to do. However, in October 2011, Bank of America recorded its deed of trust, which had been released of record a year earlier. Franklin says that, in December 2012, it assigned its deed of trust to Bank of America.

In June 2013, Meadows Bank assigned its deed of trust to Samuel Bailey, Aguilar's business partner. Bailey claims that he was not aware of "any dispute" about what liens were on the property or in what position, except that he believed the Meadows Bank deed of trust was on top. Three months later, Bailey recorded a notice of default and election to sell, and sent a notice to Bank of America. In May 2014, Bailey recorded a notice of trustee's sale and sent a notice to B of A.

The trustee's sale notice got a rise out Bank of America, which sued Bailey asking the court to rule that its lien had priority over his. However, the bank did not ask the court to stop the trustee's sale, which Bailey conducted in September, and at which he made the only bid.

Bailey demanded that Westcor defend him in the Bank of America action and asked for indemnification. Westcor "denied the claim for indemnification," according to the court. Westcor's denial was based on the fact that, when Bailey bought the Meadows Bank loan in 2013, Westcor issued a new policy rather than endorsing the existing policy to name him as an insured. The new policy contained exceptions for the Bank of America and Franklin deeds of trust.

Bailey sued Westcor and Nevada Title because the 2013 policy "downgraded Bailey's insurance coverage and Westcor's obligations to Bailey, and reduced Bailey's rights under the Meadows-Bailey assignment." Bailey sued Westcor and Nevada Title on a number of theories, which included breach of the implied covenant of good faith

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and fair dealing arising from either the Meadows Bank or the 2013 title policy, breach of fiduciary duty, negligence, and intentional interference with the "contractual relationship between Bailey and Meadows" Bank.

The appeals court dismissed some but not all of these claims in response to motions filed by Westcor and Nevada Title. The main basis for those motions was the economic loss doctrine, which bars tort claims for purely economic losses that arise from duties that are contractual in nature.

Most fiduciary duty claims are barred by the economic loss doctrine. However, Nevada has said that duties that are fundamentally professional rather than contractual do not fall under the rule. Westcor and Nevada Title argued that they were acting as escrowees, which this same federal court found is a contractual duty that does not fall under the professional services exception to the doctrine. *First Magnus Fin. Corp. v. Rondeau*, No. 2:07-CV-132-JCM (PAL), 2012 U.S. Dist. LEXIS 23549 (D.Nev. February 24, 2012).

The court disagreed in part. It said that Nevada Title was acting as an insurance broker, which is one of the professions whose special duties are not strictly contractual. It cited *Terracon Consultants Western, Inc. v. Mandalay Resort Group*, 125 Nev. 66 (2009) as its support. It looked to this definition of an insurance broker, from *Appleman on Insurance Law*:

> *Generally, "the legal distinction between an 'agent' and a 'broker' is that an 'agent' transacts insurance as the agent of the insurer and a 'broker' transacts insurance as the agent of the insured with regard to a particular insurance transaction."*

The court held that Bailey had alleged that Nevada Title was an insurance broker because Bailey had solicited the company to get insurance, and it did so by causing Westcor to issue the 2013 policy. However, the court said that Bailey had alleged that Westcor was an insurer, not an insurance broker. Thus, it dismissed his negligence claim against Westcor only.

The court refused to employ the economic loss doctrine to dismiss Bailey's claims against both Westcor and Nevada Title based on intentional interference with his supposed "contract" with Meadows Bank and intentional breach of fiduciary duty. The court said simply that the economic loss doctrine, as formulated by Nevada, "does not bar intentional tort claims." It refused to delve deeper into the nature of those claims on motions to dismiss. The court specifically held that Bailey had made a facially sufficient claim that the issuance a title insurance policy with exceptions for recorded deeds of trust "interfered" with his supposed contract with Meadows Bank for the assignment of its loan.

This is one of the few decisions to examine the issue of a title agency as an insurance broker. One element the court glossed over is that a broker is customarily defined as a party having the authority to bind insurance for more than one carrier, and who is retained by the insured to negotiate coverage for certain identified risks. Nevada Title was not retained by Bailey to obtain certain specified coverages from a carrier, and it does not place insurance with an array of carriers. Bailey dealt with Nevada Title only because Meadows Bank already had obtained a Westcor policy from Nevada Title three years before Bailey bought its loan.

Agent Focus

Insured Lender's Judgment Against Title Agent Does Not Stop Insurer From Suing Agent for Loss

Fidelity Nat'l Title Ins. Co. v. Home Equity Title Services, Inc., 2016 IL App (1st) 141098-U, 2016 WL 3249097 (Ill.App. 1 Dist.) (unpublished).

A title insurer was not blocked from suing its agent for failing to pay off a prior loan at a refinance closing because the lender had already obtained a default judgment against the agent for breach of closing instructions. Also, the agent's liability survived the mutual termination of the agency contract and was not limited to a deductible amount in that agreement.

Home Equity Title Services, Inc. was an agent for Fidelity National Title in Illinois. In 2006, Home Equity closed a refinance loan made by JPMorgan Chase secured by a house in Aurora. Home Equity searched title and discovered the prior lien in favor of Valley Community Bank. However, it did not pay off that loan at closing. Home Equity then issued a Fidelity policy to Chase with no exception for the Valley mortgage.

Fidelity National and Home Equity signed a mutual termination of the agency agreement in March 2008. In December of that year, Valley filed a foreclosure of the Aurora mortgage, and named Chase as the holder of a junior lien.

Fidelity defended Chase, which filed a third party complaint against Home Equity for breach of closing instructions. Home Equity did not appear, and the court granted Chase's motion for default judgment in October of 2010. Then Fidelity paid Valley's successor in interest, First State Bank, $60,000 for a release of its mortgage and dismissal of the foreclosure action.

Fidelity then sued Home Equity and its owner, Henry Kiely, under the agency agreement and Kiely's personal guaranty of that contract. It demanded the $60,000 it had paid for the release of the prior mortgage, and roughly $38,000 in attorneys' fees it had paid to defend Chase's lien.

Home Equity and Kiely defended the Fidelity action by claiming that that lawsuit was barred by the doctrines of res judicata and claim preclusion, because the court had already entered the default judgment in favor of Chase. They also argued that the settlement between Fidelity, Chase and the other bank was an accord and satisfaction that released the agent. The trial court did not buy either argument, and neither did the appeals court.

The appeals court said that a default judgment was not a final judgment on the merits that would bar relitigation of

the dispute. In Illinois, a default judgment is res judicata as to the parties in that action. However, it is not a judgment on the merits. Rather, the judgment bars the defaulting defendant "from making any further defenses regarding liability." The default judgment in favor of Chase did not terminate the litigation or serve as a final judgment on the merits. Further, Fidelity was not a party to that action, and the Chase suit was not based on the agency contract but on the loan closing instructions.

The appeals court also said that the stipulation and order dismissing the foreclosure action after the settlement was not a final judgment on the merits that would stop Fidelity from suing its agent. Although several Illinois decisions have held that a dismissal with prejudice pursuant to a settlement agreement operates as a final judgment on the merits, others have said that such an order does not invoke res judicata because "an agreed order is not a judicial determination of the parties' rights, but rather is a recordation of the agreement between the parties." Thus, the court said, the order dismissing the complaint did not bar Fidelity's later suit.

The court also said that "it is significant that the stipulation and order to dismiss specifically provided that Chase's third party complaint was voluntarily dismissed without prejudice." Because of that wording, the court said, the order "did not constitute a final judgment as to Chase's third party claim." The court again noted that Fidelity's claims were not based on the same contract on which Chase had sued, and Fidelity had not been a party to the first action. Thus, the title agent had not proven the required elements of res judicata of identical causes of action and that Chase had "adequately represented" the interests of Fidelity in its action.

The court also found that the doctrine of claim splitting did not bar Fidelity from suing Home Equity Title and Kiely. Under that doctrine, a plaintiff cannot "sue for part of a claim in one action and then sue for the remainder in another action." The court said that Chase and Fidelity were not, in effect, the same plaintiff bringing two claims that should have been brought in one action.

The court also held that Fidelity did not void or waive Kiely's liability under his personal guaranty by settling with the banks without his consent. An Illinois decision on a loan guaranty said that the guarantor's obligation for the debt is discharged dollar-for-dollar to the extent that the lender "takes any action to vary the terms of the principal obligation, to increase the guarantor's risk or to deprive the guarantor of the opportunity to protect himself." Kiely argued that Fidelity did not inform him of the settlement until "the die was cast." The appeals court disagreed, saying that "Home Equity and Kiely were informed early enough in the litigation to protect their interests, had they chosen to do so." Instead, they did nothing in the first lawsuit and allowed the default judgment to be taken against them. Also, Kiely had not shown that the agency contract guaranty contained a provision requiring notice to him or his prior consent to the settlement of a policy claim.

Finally, the court held that the mutual termination of the agency agreement did not void the guaranty. The trial court had found that the mutual termination would discharge any obligations which were still executory on both sides, but that "any right based on prior breach or performance survives," citing the Uniform Commercial Code–Sales. See 810 ILCS 5/2–106(3) (West 2008). The circuit court also held that Kiely's liability as guarantor for the 2006 breach survived the 2008 mutual termination.

The appeals court held that the Uniform Commercial Code did not apply, because the agency agreement was not a contract for the sale of goods. However, it affirmed the trial court because the agency agreement specifically stated that a termination of that contract would not cancel the agent or guarantor's duty to reimburse the insurer for losses payable under the contract. It said that the mutual termination did not void that provision.

Home Equity Title and Kiely also argued that the agency contract limited their liability to $10,000. Paragraph G of the agency agreement said:

> *Subject to the provisions of Paragraph 8, Agent shall be liable for the first $10,000.00 of any Loss sustained or incurred by Principal as a result of the issuance of the Title Assurances by Agent.*

The appeals court agreed with Fidelity and the circuit court that Paragraph 8 controlled. That provision said that Home Equity:

> *shall be liable to and agrees to indemnify and to save harmless [Fidelity] for all attorneys' fees, ... and loss or aggregate loss resulting from ... [e]rrors or omissions in any commitment, policy, endorsement or other title assurance which were disclosed ... by the abstracting, examination or other work papers or which were known to [Home Equity]... .*

The appeals court said this provision applied. The circuit court had found that the defendants admitted they made errors or omissions in the Chase policy. The Chase loan was a refinance, after all, so there should have been a prior mortgage and a payoff from closing. The appeals court affirmed the judgment against the title agency and its owner for the $60,000 payment and the attorneys' fees paid for Chase's defense.

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APP048

Escrow Matters

Escrowee Did Not Breach Recording Duty Because Escrow Never Closed

Spring Gardens Inc. v. Security Title Ins. Agency of Utah Inc., ___ P.3d ___, 2016 UT App 113, 2016 WL 3034080 (Utah App. 2016) (permanent citation not yet available).

An escrow company did not violate its instruction to record a deed of trust on close of escrow because the escrow never closed.

In 2006, Spring Gardens Inc. lent a "substantial sum of money" to Blaine and Jessie Johnson, secured by a first lien on their property in Burmester, Utah. By March 2008, the Johnsons still owed Spring Gardens about $85,000 and Spring Gardens wanted to be paid in full. The Johnsons and Spring Gardens signed an agreement saying that the Johnsons would pay off the loan within a month, and give first trust deeds on two additional parcels (the Skull Valley property), in exchange for Spring Gardens' subordination of its first lien on the Burmester property to two other liens.

The Johnsons signed the Skull Valley trust deed. Spring Gardens deposited the documents into an escrow it opened with Security Title Insurance Agency of Utah.

Not long after the escrow was opened, Spring Gardens agreed to accept a partial payment from the Johnsons in exchange for the recording of its subordination agreement for the Burmester property. Spring Gardens collected the money and gave the signed subordination to Security Title, with the instruction to record it.

The Johnsons did not make another payment, and the escrow never closed. Security Title never recorded the Skull Valley trust deed.

The Johnsons then defaulted. Spring Gardens could not foreclose on the Skull Valley property because that trust deed had not been recorded, and its lien on the Burmester property was subordinate to two other liens securing debts of more than that property's value.

Spring Gardens sued the Johnsons and Security Title. Its theory against the escrow company was that it had violated an instruction to record the Skull Valley trust deed. In the complaint, Spring Gardens repeatedly alleged that escrow had closed. Security Title disagreed. It submitted requests to Spring Gardens, asking it to admit that the escrow had not closed. Spring Gardens never responded. Under Utah's discovery code, the party is deemed to have admitted the truth of statements made in requests to admit if no response is provided.

Security Title moved for summary judgment based on the admissions. Spring Gardens responded that Security Title should still be required to prove the lack of a closing on the escrow in order to get the case dismissed. The trial court disagreed, and dismissed Security Title. The appeals court agreed.

The appeals court began its analysis by noting that Spring Gardens' complaint said that Security Title had a duty to record the deed "following the closing." However, Spring Gardens had admitted that no closing had occurred. The court said that a lawsuit "explicitly premised upon the existence of a fact later admitted not to exist by the party making the claim is a weak claim indeed." The court also noted that Spring Gardens had threatened to amend its complaint and withdraw the closing allegations, or recant its admissions, but never did either.

Thus, the court said that "Security Title could not have a duty to record premised upon the occurrence of such a closing and the giving of such instructions." Spring Gardens had neither amended its own pleading or supplied the trial court with a cogent argument as to why the deed of trust should have been recorded in advance of the close of escrow. The appeals court refused to consider the "interesting arguments" made for the first time at oral argument, by Spring Gardens' new lawyer hired for the appeal.

Conveyance News

Federal Forfeiture Beats Interest of Spouse Who Was Not a Record Owner

United States v. Meadows, ___ F.Supp.3d ___, 2016 WL 3014652 (D.Minn. 2016) (permanent citation not yet available).

The wife of a man accused by the federal government of running a "fraudulent enterprise" had no standing to contest the forfeiture of real estate seized because the husband used some crime money to buy the property. The wife claimed that most of the purchase price was paid with money she withdrew from her separate 401(k) account. Because she was not a record owner of the property, however, she had no standing to even dispute the forfeiture, or seek a division of the sale proceeds.

Sean Meadows married Michelle Meadows in 2000. The Meadowses had bought a number of houses in the Twin Cities and had flipped them. In 2010, Sean Meadows became the sole record owner of one such house, in St. Paul.

In 2014, Sean Meadows pled guilty to several criminal charges, including money laundering. The decision does not describe the criminal charges, but a *Star Tribune* article from December 2014 said that Meadows was a financial planner, and had "admitted to swindling more than 50 people in several states out of at least $10 million, using some of the money on gambling and sex-oriented entertainment in Minnesota and Las Vegas." Meadows had operated Meadows Financial Group LLC.

The federal government seized the Atwater and St. Paul real estate, claiming that some of the money used to buy both of them had come from Sean Meadows' illegal businesses. The government agreed to split the proceeds of sale for one

house with Mrs. Meadows, because she was a joint record owner of that property.

However, the government claimed the sole right to be paid from the sale of the St. Paul property, located at 973 Payne Ave. Mrs. Meadows also claimed an interest in that property, because she had borrowed $50,000 from her 401(f) account to purchase and rehab that house. The district court said that Michelle Meadows had no standing to contest the forfeiture or share in the proceeds of sale for the Payne Avenue house, however, because she was not a record owner and did not hold a lien on that property.

The purchase price for the Payne Avenue property was $40,000. The $10,000 down payment came from a TCF National Bank account in the name of Meadows Financial Group LLC, the entity that Sean Meadows used to defraud his financial planning customers. Michelle Meadows did borrow $50,000 from her 401(k) account. She said that money was supposed to be used to "replenish" the down payment made from the TCF financial planning account, pay the balance of the purchase price, and to fund $10,000 in renovation costs.

Michelle Meadows deposited the 401(k) money into the couple's joint checking account, which was also at TCF Bank. Sean Meadows did use $30,000 from that account to buy the property. He got a deed vesting title in himself only. The contractors who rehabbed the house in the fall of 2010 were paid mainly in cash. In October 2010, Sean Meadows withdrew the remaining $20,000 that Michelle had deposited and put it in an account at Wells Fargo in his name only. According to the government, Sean Meadows then spent that money not on renovating the house but for gambling at a horse track and casino and to pay Ponzi-type returns to some of his clients.

The federal district court ruled that Michelle Meadows had no cognizable interest in the Payne Avenue property, and thus no standing to contest the forfeiture or share in the proceeds from its sale. The federal forfeiture law has a heightened standing requirement. A person must assert "a legal interest" in the property. 21 U.S.C. § 853(n)(2). Standing under that law consists of two parts, termed constitutional standing and statutory standing. Constitutional standing is derived from Article III of the United States Constitution. A person has constitutional standing if he or she has "actual possession, control, title" or a "financial stake" in the land. The government did not contest Michelle Meadows' constitutional standing.

Statutory standing, under the forfeiture law, requires proof that the petitioner has a "legal interest in" the property. The law does not define "legal interest." The case law says that the term "encompasses only legally protected rights, not equitable rights." The federal courts look to state law to determine if the petitioner has a legally protected right in the property.

Michelle Meadows' problem was that her claims were equitable, not legal. Minnesota law recognizes the usual categories of "legal" interests in property: lien holders and owners of recognized estates in land granted by written conveyances. Michelle Meadows had no written instrument giving her an estate in the Payne Avenue property or a lien on it.

The court said that the fact that she had "some dominion and control" over the house may give Mrs. Meadows the financial stake necessary for constitutional standing, but it did not rise to the level of a legal interest that is necessary for statutory standing. Similarly, while Michelle Meadows might claim an equitable interest in the house because her money was used to buy it, that equitable interest did not confer statutory standing. It relied on *United States v. Caruthers*, 765 F.3d 843, 845 (8th Cir. 2014) and *United States v. Basurto*, No. 10–cr–0304(2), 2013 WL 1331983 (D.Minn. Mar. 29, 2013) (unpublished), both of which rejected that argument.

Similarly, the court said that Michelle Meadows could not establish that she had a legal interest in the property by her assertion that her husband was a straw owner. Rather, the government sometimes challenges the standing of the record owner to contest a forfeiture, on the grounds that the record owner is a mere straw buyer, and the criminal defendant is the true owner. The court said that Michelle Meadows could not argue that her husband was a mere nominee owner to assert that she was the true legal owner of the house.

The only other avenue under Minnesota law for Michelle Meadows to claim a legal interest in the property was to prove that she had such an interest "by act or operation of law… ." Minn. Stat. § 513.04. She argued that she was entitled to a constructive trust and that she had a "marital interest" in the house. The court said that neither theory produced a legal interest in the real estate by operation of law.

Minnesota says that a constructive trust may be imposed on real estate as an equitable remedy "intended to prevent the unjust enrichment of a person holding property under a duty to convey it or use it for a specific purpose." The court acknowledged that, although a constructive trust is an equitable remedy, it arises by operation of law and constitutes a legal interest under 21 U.S.C. § 853(n). The court cited *United States v. Shefton*, 548 F.3d 1360 (11th Cir. 2008), which catalogued the decisions that have held that a constructive trust constitutes a legal interest under the forfeiture statute.

Although the theory was a good one, the court said that the facts did not support the imposition of a constructive trust in favor of Michelle Meadows. She had not alleged, much less proven, the necessary elements that her husband had obtained title by defrauding her, that he had agreed to convey the house to her, or that the government would be unjustly enriched if it got the money from the sale of the house.

The court also said that the marital interest recognized by Minnesota in a non-homestead property was not enough to give Michelle Meadows a legal interest in the house. Minnesota says that a spouse gets rights in real estate other than the couple's homestead only on the filing of a divorce petition. Further, a prior decision involving a forfeiture held that a spouse could claim an interest in an asset owned by her husband, the criminal, only if she did not know about the crime when she filed for divorce, or she was a bona fide purchaser of the asset. Mrs. Meadows was aware of Sean Meadows' criminal conduct before she filed for divorce, and there still was no judgment of divorce dividing their property. Thus, her "marital interest" in the Payne Avenue house, though it existed by operation of law, did not give Michelle Martin standing to attack the forfeiture or to share in the proceeds of sale.

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The TITLE INSURANCE LAW NEWSLETTER

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Title Insurance

Oil Leak Notice is a Defect in Title, Causing Large Loss

Old Republic Nat'l Title Ins. Co. v. RM Kids, LLC, ___ Ga.App. ___, ___ S.E.2d ___, 2019 WL 5257548 (2019) (not yet released for publication).

A recorded notice saying that oil had leaked into the ground water was found by a jury to be a defect in title, triggering policy coverage. The appeals court also upheld the jury verdict of $4,200,000 as the diminution in value to the insured lender. A central issue in the case was that the loan was assigned and the insurer could not prove that the assignee knew of the notice when it bought the loan.

An earlier decision in this case was reported in the September 2016 issue, and is found at 337 Ga.App. 638, 788 S.E.2d 542 (Ga.App. 2016).

Colonial Pipeline Company's pumping station in Gwinnett County, Ga., near the city of Dacula, leaked oil into the groundwater in the 1990s. Colonial bought 114 acres of adjacent land known as Black Hawk Ranch. Colonial cleaned up the spill, installed monitoring wells on Black Hawk Ranch, and arranged for public water service for the area so that no one would drill a well that might allow more oil to leach into the groundwater.

Colonial's testing of the groundwater showed that by 2003, the contamination was sufficiently reduced so that it would be safe to sell Black Hawk Ranch for development. It contracted to sell the property to Black Hawk Ranch, LLC in 2005. The Georgia Environmental Protection Division approved the sale, but required that Colonial attach to the deed an "Exhibit C," which gave notice of the contamination and said that Colonial had the continued duty to remediate and to take samples from the monitoring well on the property. Exhibit C also said that the property owner could not use the groundwater "for any purpose whatsoever," that Colonial was reserving an easement to get to and use the monitoring well, and that Colonial had a right of first refusal on the property. It also reserved a 25-foot riparian buffer easement along two streams that run through the property.

Black Hawk Ranch LLC got the City of Dacula to annex the parcel and rezone it for high density single-family development. One year later, in 2006, Black Hawk Ranch sold the property to BBC Partners LLC. BBC got a $7.3 million purchase money loan from Peachtree Bank. There were "indications" that the bank knew about the property's environmental issues, but the Old Republic policy issued to Peachtree did not contain an exception for the Exhibit C notice, easement and restrictions.

Later in 2006, BBC bought a second 37-acre parcel next door, known as the Wages Tract, that was not subject to the Exhibit C limitations. In 2007, Peachtree Bank made

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The Title Insurance Law Newsletter, which is distributed electronicly each month by the American Land Title Association (ALTA), reports on cases addressing title insurance coverage, class actions and regulatory enforcement, escrow and closing duties, agent/underwriter disputes, conveyancing law, and RESPA and TILA compliance and violations.

This publication provides helpful information for title agents, approved attorneys, underwriters, claim administrators and attorneys who practice in title insurance defense work or conveyancing disputes.

J. Bushnell Nielsen serves as editor. Please submit news and guest columns to ***bnielsen@reinhartlaw.com***.

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a new loan to BBC for $11.4 million, which paid off the purchase money loans for both parcels. Old Republic issued a policy on that mortgage also, which again did not contain an exception for Exhibit C.

In April 2008, RM Kids LLC bought the $11.4 million loan, which was already in default. A few months later, the borrower told RM Kids about Exhibit C. RM Kids made a claim on the Old Republic policy in January of 2010. The insurer denied the claim, asserting that Exhibit C was not an encumbrance on title, among other defenses.

In November 2010, RM sued Old Republic on the policy and for bad faith. In December 2012, RM Kids finally foreclosed on the ranch and bid $750,000 at the foreclosure sale.

The case went to trial. RM Kids hired an appraiser who set a claimed diminution in value as of the policy date. Old Republic moved to exclude the appraiser because he used the wrong loss date, and asking the court to rule as a matter of law that loss should be measured on the date of foreclosure. The court denied both motions, and ruled that loss should be measured as of the loan closing date. Old Republic moved for a directed verdict at the close of the evidence, because RM Kids as a loan purchaser did not suffer a loss when Peachtree Bank closed the loan. The court denied the motion. The jury rendered a verdict in favor of RM Kids and awarded over $7 million as loss.

Old Republic appealed. In 2016, the court reversed the verdict based on the key issue of the date of loss. It began by noting that Georgia had not previously addressed the issue of date of loss under a lender's title insurance policy. It noted, however, that:

> *… "a majority of courts from other jurisdictions have held that, in the absence of specific policy language, a title insurer's liability to a mortgagee should be measured using the foreclosure date," reasoning that the foreclosure date is "appropriate because the foreclosure is when the insured actually incurs a covered loss."*

The appeals court said that this rule follows from the fact that a lender cannot suffer a loss due to a title defect until the borrower has defaulted and the lender has taken title to the property. The court rejected RM Kids' argument that loss on a loan policy should be measured on the policy date because Georgia adopted that rule for owner's policies in *U.S. Life Title Ins. Co. of Dallas v. Hutsell*, 164 Ga.App. 443, 296 S.E.2d 760 (1982). The court said that this merely illustrated the fact that losses under owner's and loan policies have different conditions, which leads inexorably to the conclusion that there must be different loss dates.

Thus, in the 2016 decision, the court reversed and remanded the case for retrial. However, the court refused to find that the RM Kids appraiser was using junk science that should be barred, because his opinion about diminution in value was based largely on how he believed the average consumer would react to the "environmental stigma" on the property. The appraiser, Jeffrey Miller, based his stigma opinions on consumer focus group testing he performed.

A second trial was held in 2018. The closing attorney testified that, when his legal assistant was preparing the paperwork to close the loan, she mistakenly removed all the items listed in Exhibit C instead of only removing the right of first refusal. The Old Republic title agent testified that Exhibit C "should have been included in the coverage exceptions, but was erroneously omitted."

Old Republic twice moved for a directed verdict, arguing that the notice was not an encumbrance on title and that RM Kids had not suffered a loss. The trial court denied both motions. The jury found in favor of RM Kids, and awarded it $4.2 million.

Old Republic appealed. The court upheld the jury's finding that the notice of remediated contamination was either a defect in title or an encumbrance on title.

The court began with a lengthy discussion of why insurance policy exclusions are construed narrowly and against the insurer, even though no exclusion was at issue. It also gave a lengthy discussion of why ambiguities are construed against the insurer as drafter. The court then declared that the policy was ambiguous, because the terms defect and encumbrance are not defined in the policy:

> *Given our case law, the rules of contract interpretation, and our standard of review, we cannot say, as a matter of law, that the restrictions and easements on the property were not "defects" or "encumbrances" in the title. To the extent that these terms are ambiguous because they are not defined in the policy, we turn to our rules of contract interpretation.*
>
> *Here, reading the policy using ordinary language, coverage extended to "any defect in or lien or encumbrance on the title"*

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and "unmarketability of the title." Generally, an easement is an "encumbrance" that is a defect on the title. … Moreover, encumbrances are defects that are separate and distinct from unmarketability because the policy uses both "defect in or lien or encumbrance" and "[m]arketability of the title," as alternate methods to trigger coverage. To consider marketability the same as an encumbrance would make the language superfluous. … Indeed, as Old Republic's counsel acknowledged in its reply brief and at oral argument before this Court, an easement can be a title defect.

Moreover, as we explained in our prior opinion, where the facts of the case raise a question of coverage, the policy is ambiguous, and the decision rests with the jury. … Thus, any ambiguity in the language and definition of "defect" or "encumbrance" was for the jury to resolve. Here, RM Kids submitted expert testimony of a real estate attorney who opined that easements and encumbrances on a property were title defects and if not listed on the title insurance policy would be covered. He further testified that Exhibit C was, in fact, a title defect. This evidence was sufficient for the jury to conclude that the restrictions and easements were title defects and were covered by the policy.

The court also rejected Old Republic's argument, based on other decisions construing the title insurance policy, that contamination is a physical condition that affects the property but not its title. The court said this, in distinguishing the Georgia Investguard decision on physical condition:

Old Republic's reliance on Chicago Title Insurance Company v. Investguard, Ltd., 215 Ga. App. 121, 449 S.E.2d 681 (1994), does not alter our analysis. In that case, the property was located in a flood plain, and the purchaser argued that this defect rendered its title to the property unmarketable. … This Court held that defects in the physical condition of property, such as its location in a flood plain, do not constitute a title defect. … But the instant case is distinguishable. First, the alleged defect in Investguard was not omitted from the chain of title as it was here. Additionally, an easement is an "encumbrance" on the property and not merely a "physical defect." Moreover, in the instant case, RM Kids has not invoked the coverage provision regarding unmarketability of title; rather, the claim is that the property is subject to these undisclosed encumbrances that rendered the title defective.

Old Republic's argument conflates the concepts of marketability of title and economic marketability. … Because the basis of RM Kids's claim was not marketability of title, Old Republic's argument that the property could still be bought and sold is misplaced. This was not a case involving a simple defect in the physical condition of the property; it was an encumbrance on the property in the form of a restriction on use and the existence of easements, which were omitted from the chain of title and which, as Old Republic acknowledged, can be title defects. In any event, we note that the measure of damages per the terms of the contract is the difference between the value of the land with and without the defect. We fail to see how the economic marketability of the land as encumbered with these defects in title would not be a factor to consider in determining value.

The real crux of Old Republic's claim is that the alleged defect resulted in no damages and, therefore, is expressly excluded from coverage by the policy. … [W]e cannot say as a matter of law that the encumbrances in Exhibit C were not title defects. Rather, on this record, the jury was authorized to find that the easements and use restrictions constituted title defects that would trigger coverage under the policy.

The court then affirmed the jury verdict. It chose to characterize the issue as being "whether or not RM Kids has proved its damages and whether Old Republic met its burden to show the exclusion applied." The court referred to the "no loss" exclusion. It reiterated that an insurance policy exclusion is narrowly and strictly construed in favor of coverage, ignoring the fact that proof of loss is not a coverage issue. Further, the court applied the light burden of the "any evidence" standard of review. The court concluded limply that "there was evidence from which a jury could find damages."

The RM Kids appraiser said the value of the property without the notice of contamination was $6 million, and the property's highest and best use was as a subdivision with over 300 homes. However, subject to the notice of contamination, the property's best use was as four to six large lots, with a value of $680,000. The appraiser treated the notice of contamination and the contamination itself as being one issue. His opinion was again based largely on consumer sentiment and fear.

Old Republic's appraiser said the property had the same value with and without the notice, of $1,910,000. He noted that both property owners were aware of the contamination, and there was no evidence that it affected their purchase prices. He also said that RM Kids' appraiser overvalued the property. Although he was forced by the 2016 decision to value the property as of foreclosure in 2012, RM's appraiser did not admit the full reduction in value from 2006 to 2012 caused by the Great Recession.

The court said this in affirming the verdict:

It was for the jury to evaluate this testimony and make a determination of damages. Although the stigma from the contamination may have played a role in the jury's verdict, we look only to see whether there was "any" evidence to support the jury's findings. … Given the specific expert testimony that the use restrictions and easements contained in Exhibit C reduced the value of the property, there was evidence from which the jury could conclude there were damages flowing from the title defects.

Accordingly, we conclude that the easements and restrictions constituted defects in title that are

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covered by the policy, and there was sufficient evidence to establish damages. The trial court properly denied the motion for directed verdict.

This decision illustrates the persistent problem in the use of the term "defect" in title in the ALTA policies, without any definition for that term. A term so fundamental to this type of insurance should be well-defined in the policy so that everyone knows the scope of policy coverage.

Most states have fairly well-developed case law about what constitutes an encumbrance on title. Those matters that burden the title are encumbrances. However, there is little discussion by courts as to defects in title. A defective title should be construed to mean that there is a question about the insured's ownership of the property. A notice saying that the ground water is polluted by leaking oil does not create a question about the ownership of the property.

This court was wrong in saying that the policy is ambiguous because "defect" is not defined. However, there is no valid reason why the policy does not clearly define the term, if it is necessary to use the term at all.

Your editor questions the use of the term "defect." For one thing, it is found in the wrong Covered Risk. The word "defect" is found in the second Covered Risk, which deals with matters that burden the title. By contrast, the first Covered Risk addresses the failure of title. A customer could be excused from understanding the difference, because that coverage is less than obvious, reading "Title being vested other than as stated in Schedule A." The current definition of "Title" only increases the confusion, by defining "Title" as simply "[t]he estate or interest described in Schedule A." Title means ownership; the definition does not say that. The estate in the land held by the insured is one aspect of title, but does not define the term. The result is that neither Title nor Defect in Title are adequately defined in the ALTA title insurance policy.

In 2012, your editor proposed to ALTA that the "vesting" coverage be replaced by something more to the point: "There is a Defect in Title." Your editor also proposed a definition for Defect in Title, being:

"Defect in Title": a failure or flaw in the Title of the Insured to the Land that causes the Insured to be unable to transfer the estate or interest insured by this Policy, whether in full or in part; or, an ownership right or estate held by a party other than the Insured in the Title to the Land, including a fee simple interest, a life estate, leasehold estate or remainder interest.

Had the Old Republic policy contained these terms, it seems unlikely that a real estate lawyer could have testified to the jury that a recorded notice saying that oil had leaked into the ground water was a defect in title.

The very interesting issue addressed only in a footnote was the question of what RM Kids knew that could invoke Exclusion 3(a). The property owner borrowers both knew about the contamination and the recorded notice; the notice was listed in their deeds as a title encumbrance. Peachtree Bank may also have known about the oil leak. It almost certainly had copies of the deeds to its two borrowers. However, RM Kids insisted that the contamination was not disclosed to it when it bought the loan, asserting that Peachtree Bank did not give it a copy of the recorded deed. Therefore, Old Republic was barred from asserting Exclusion 3(a) as a defense. This would not be the first time that a successor insured under a loan policy escaped Exclusion 3(a) simply because the policy puts the burden of proof on the insurer to show that a successor insured had the same knowledge as did the named insured.

Title Insurance

Policy Limits Access Judgment Reversed

Rio Mesa Holdings, LLC v. Fidelity Nat'l Title Ins. Co., 2019 WL 4639103 (Cal.App. 5 Dist.) (unpublished).

A jury verdict giving the insured policy limits of $25 million has been reversed because it was based on a ruling by the trial court that the insured had no access to the property, which misconstrued a prior ruling saying the insured *did* have access rights. However, the case was sent back for a new trial on the issue of what loss, if any, is payable under access and contiguity endorsements.

Sumner-Peck Ranch Inc. owned and operated Peck Ranch, a cattle ranch composed of 1,500 acres lying between Highway 41 and the San Joaquin River in Madera County, Calif. In 1985, Sumner-Peck developed about 160 acres of the ranch on a bluff overlooking the river into a 49-lot subdivision known as Sumner Hill. There were also 10 surrounding outlots identified on the Sumner Hill plat.

Madera County make Sumner-Peck install a security gate and perimeter fence to keep lot owners' pets away from the ranch cattle and for privacy.

Outlots A and B in the plat are on the west side of the residential lots. Outlots C and D lie to the east, between the lots and the San Joaquin River. Killarney Drive is the main road in Sumner Hill, and leads to the nearest public street, Road 204. Killkelly Road is a dirt road that branches off Killarney Drive inside the subdivision, and runs through Outlots C and D to the river.

Sumner-Peck installed a security gate on Killarney Drive and some no-trespassing signs on the fence. The lots were sold. The only people who knew the pass code for the gate were the lot owners and Sumner-Peck employees. The lot owners use Killkelly Road to go to the river.

Madera County vacated the roads, returning them to private ownership and maintenance. The subdivision restriction declaration was amended in 1988 to make the Sumner Hill Homeowners' Association responsible for maintaining the gate and fence.

In 2003, Sumner-Peck sold the balance of the Peck Ranch, including the Sumner Hill outlots, to Rio Mesa Holdings LLC for $25 million. Fidelity National Title issued a policy to Rio Mesa containing access and contiguity endorsements.

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Rio Mesa knew that Sumner Hill was a private, gated community and that its residents used Killkelly Road to go to the San Joaquin River. Nevertheless, the court said,

> *… in 2005, it announced plans for Tesoro Viejo, a massive residential and commercial development that would feature an access route to the San Joaquin River through the 49-Lot area via Killkelly Road. Rio Mesa hoped river access would boost the marketability and value of Tesoro Viejo's residential lots. It installed its own locked gate near the top of Killkelly Road and hired private security guards to patrol for trespassers, preventing the 49-Lot residents from visiting the river.*

In 2006, the lot owners sued Rio Mesa, claiming among other things that Rio Mesa should be prevented from developing the outlots as planned because that would violate the rights they held, and that use of the roads by hundreds of new lot owners would be inconsistent with Sumner-Peck's access rights.

The trial court ruled that Rio Mesa became the owner of Killarney Drive and Killkelly Road when the county vacated them as public roads. The appeals court reversed that ruling in 2012, finding that the lot owners took title to the adjoining portions of the streets when they were vacated. 205 Cal.App.4th 999. It also said the lot owners could exclude the general public from the roads. However, the appeals court also ruled that Rio Mesa had prescriptive easement rights to use the roads.

Rio Mesa then sued Fidelity, claiming a policy-limits loss due to its alleged lack of access over the roads within the Sumner Hill subdivision. On summary judgment, the trial court held that the appeals court had already ruled that Outlots C and D, which lie between the subdivision and the river, had no access rights in the two roads inside the subdivision. Also, the trial court said, Rio Mesa was a member of the "general public," and the appeals court decision gave the lot owners the right to keep Rio Mesa from using any of the subdivision roads.

The case then went to trial. The judge gave the jury the following instruction: "You are advised that it has been determined, as a matter of law, that Rio Mesa ... has no right of access through the Sumner Hill subdivision."

The jury also heard from John Sanger, Rio Mesa's attorney, who negotiated policy coverage and "drafted the customized endorsements." Sanger said he wanted "particular endorsements that assured access between Road 204 and to Outlots A and B and C and D and among the [O]utlots... ." He told the jury that he wrote a contiguity endorsement that also insured access:

> *To me a contiguity endorsement ensures that there is contiguity, whether physical or legal – well, certainly legal, and usually physical, among all of the different legal parcels that make up the property being acquired to ensure against any gaps that would prevent treating ... the entire acquired area as one unit. ... [T]he contiguity endorsement assures that there are no gaps ... between the various parcels being acquired such that you can treat the entire property as a unit, and that naturally leads also to the ability to move freely among the parcels, to have access, legal access, among the parcels.*

Title officer Gary Walker said that the "customized" contiguity endorsement was intended "to make sure that all of the parcels were either touching or that there was some way to get between them... ." He said that Sanger also customized an access endorsement "to insure an easement for Rio Mesa to travel over Killarney and Killkelly to reach Outlots C and D... ."

In fact, however, the Fidelity policy contained standard contiguity and access endorsements. The contiguity endorsement merely insured against:

> *… loss or damage which [Rio Mesa] shall sustain by reason of the failure of any [of] the parcels of land ... to be contiguous to each other.*

That endorsement said nothing about access, including "access" from one contiguous parcel to another. The access endorsement was likewise a standard limited CLTA access endorsement that insured against:

> *… any loss or damage which [Rio Mesa] shall sustain by reason of lack of ingress and egress to and from Outlots C and D, lying within and adjacent to Killkelly Road (vacated) and lack of ingress and egress to and from Outlots A and B lying within and adjacent to Killarney Road (vacated).*

The jury found that Rio Mesa suffered a loss of policy limits. Fidelity filed a motion for judgment notwithstanding the verdict, which the trial court denied.

Fidelity appealed. The appellate court struck the jury verdict and remanded for a new trial. The appeals court said that, in its 2012 decision, it had held that Rio Mesa, as the owner of Outlots A through D, had access rights over the subdivision roads. Further, the court had ruled that, in the alternative, Rio Mesa had a prescriptive easement to use the roads. Thus, the trial court simply misread the 2012 decision.

The appeals court also agreed with Fidelity that the trial court's summary judgment ruling and its instruction to the jury that the property lacked a right of access "effectively directed a verdict on liability in favor of Rio Mesa," which mandated a new trial.

Fidelity asked the appeals court to instruct the trial court that certain findings were binding on it under collateral estoppel at the new trial. One requested instruction was that "Rio Mesa and its invitees have access through the 49-Lot area security gate." The appeals court said that it did not hold in 2012 that "it was granting access through the 49-Lot area to either Rio Mesa's invitees or the future owners of its lots located outside of the private, gated subdivision." It instructed the trial court that, at the new trial, the following findings were to be given conclusive effect:

> *(1) Outlots C and D enjoy an easement by necessity through the 49-Lot area to Road 204; (2) Rio Mesa, the holder of this easement by necessity, may enter and use the roads within the 49-Lot area in a manner consistent with the 49-Lot residents and*

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the Association's rights to use the subdivision roads and maintain the 49-Lot area as a private, gated community; and (3) Rio Mesa may develop Outlots A through D in a manner consistent with the 49-Lot residents and the Association's aforementioned rights.

The appeals court's formulation of Rio Mesa's access rights appears to be entirely consistent with and as broad as the rights insured in its access endorsement. Neither the CLTA nor the ALTA access endorsement assures that an access right exists for the benefit of a future owner of a parcel subdivided from the insured parcel(s), or the right of any invitee of the insured to gain access to the insured parcel.

This decision highlights the risk in giving an access endorsement, whether standard or "custom," when the insured's intent is to develop the insured parcel in a way that might overburden whatever access rights it then enjoys.

Title Insurance

Subrogated Insurer May Collect Against Loan Guarantor

Uddin v. Cunningham, 2019 WL 4065273 (Tex.App.-Houston) (unpublished).

A title insurer is entitled to recover from a loan guarantor despite numerous defenses raised by the guarantor, including that the insurer had no standing to sue him on the guaranty before it paid the claim.

Shakeel Uddin guaranteed a $1.4 million loan made by Sterling Bank to Nabeel & Amaan Investments, Inc. Uddin was Nabeel & Amaan's president. The company used the money to buy real estate in Houston.

NAI defaulted. The bank then learned that a creditor of Nabeel & Amaan's, JLE Investors, had obtained a lien on the property that primed the Sterling Bank deed of trust. That lien was not excepted in Sterling Bank's policy. JLE foreclosed on the property in October of 2011, wiping out Sterling Bank's deed of trust.

The bank made a claim under its policy, issued by Southern Title Insurance Company. By that time, Southern had troubles of its own. In fact, in a footnote, the court observed that the Southern policy at issue was issued by agent American National Title. That company's director was Syed Rizwan Mohiuddin. The court said that Mohiuddin and Uddin were business partners. "Ray" Mohiuddin brought down Southern Title almost single-handedly, as the court noted:

STIC filed a complaint in an adversary proceeding against Mohiuddin in United States Bankruptcy Court, seeking a determination that Mohiuddin was liable to STIC for his fraudulent issuance of eight title policies—including the two involved with this case. STIC was ultimately awarded a $8,497,832.62 nondischargeable judgment against Mohiuddin.

The State Corporation Commission of Virginia was appointed Southern's receiver in December 2011. In May 2012, Southern Title's receiver filed an action against Uddin in Harris County District Court, claiming to be subrogated to Sterling's rights under the loan guaranty. The case was then stayed until Sterling's insurance claim with Southern Title was "settled or resolved such that the exact amount of damages sought by [STIC could] be confirmed."

In 2015, Southern Title's receiver informed Sterling Bank that it was entitled to $710,000 under the policy, but that it could only afford to pay $250,000 at that time. The insurer made a series of payments to the bank. In June of 2016, Sterling assigned the note and guaranty to Southern.

In August 2016, Southern amended its petition against Uddin seeking full recovery under the guaranty. It asserted that, when it filed its 2012 action, Southern Title had the right under the policy to bring that action, because the policy says the insurer has the right to "institute and prosecute any action or proceeding" that may be "necessary or desirable" to, among other things, "prevent or reduce loss or damage to the insured." Southern said that its lawsuit sought to "reduce loss or damage to Sterling by holding [Uddin] accountable for matters related to the Lender's Policy, specifically, the related Loan Documents."

Uddin raised a plethora of defenses, including the statute of limitations and counterclaims that sought an offset to liability under the guaranty. Eventually, the trial court entered judgment against Uddin, requiring him to pay Southern Title about $1.65 million.

Uddin appealed. The court affirmed.

Uddin's first argument on appeal was that Southern Title had no standing to sue Uddin for breach of contract when it filed its 2012 action, but that by the time it obtained standing to sue, it was too late under the Texas four-year breach of contract limitations period of Texas Civil Practice and Remedies Code section 16.004(a)(3). Sterling Bank accelerated the note in February 2011, which Uddin said was the trigger for enforcement of the guaranty. Thus, the time to sue under the guaranty expired in February 2015. Uddin asserted that Southern Title did not validly sue under the guaranty until August 2016, which was too late.

Southern Title asserted that its 2016 petition related back to the 2012 petition, so its claim was not time-barred. The court agreed. Texas Civil Practice and Remedies Code section 16.068 says that an amended pleading relates back to the filing of the action for limitations purposes. Southern Title had alleged all of the important facts in 2012. The addition of new allegations in 2016 did not disturb the relation-back effect of the new pleading.

Uddin countered, however, that Southern Title's 2012 petition was essentially void, because the insurer filed it before it was rightly subrogated to the guaranty and note. The court said that "Uddin correctly states that standing cannot be waived or cured by the relation-back doctrine." Still, it rejected his argument, because it found that Southern Title was in fact a subrogee in 2012. It quoted the policy subrogation provision, which said:

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The Company's right of subrogation against noninsured obligors shall exist and shall include, without limitation, the rights of the insured to indemnities, guaranties, other policies of insurance or bonds, notwithstanding any terms or conditions contained in those instruments that provide for subrogation rights by reason of this policy.

Based on that language, the court said that Southern Title "was subrogated to Sterling's rights and interest in the note securing NAI's indebtedness, including Sterling's rights under Uddin's Guaranty Agreement with Sterling." It said that "[s]ubrogation allows a party who otherwise lacks standing to step into the shoes of and pursue the claims belonging to a party with standing." The court quoted a number of Texas decisions that have so held. The court also rejected Uddin's argument that Southern Title lacked standing in 2012 because it had not yet paid the claim, saying:

First, although STIC had not paid the claim, it had nevertheless incurred an interest in the matter because of its role as Sterling's insurer. See Heckman v. Williams Cty., 369 S.W.3d 137, 155 (Tex. 2012) (holding that, for plaintiff to have standing, it must be personally injured in concrete and particularized way by conduct "fairly traceable" to defendant and redressable by its requested relief). Second, although there is a general rule "that a person who is subrogated to the rights or securities of another many not enforce the same until the claim of the latter against the debtor has been paid in full," Providence Inst. for Sav. v. Sims, 441 S.W.2d 516, 519 (Tex. 1969), the purpose of that rule is to protect the prior creditor (here, Sterling). Id. The rule does not exist to protect a party in Uddin's position, i.e., the third party liable for the injury to the prior creditor. See id. ("If the prior creditor consents to pro tanto subrogation of one who makes partial payment, ... no one else is entitled to object."). Finally, the concern about whether STIC had paid Sterling's claim is more properly a question of STIC's capacity to sue on Sterling's behalf, not its standing. The parties agreed to an abatement following STIC's filing of its original petition so that the amount of damages under the policy could be determined. STIC's receiver determined that Sterling was entitled to payment under the terms of the Lender's Policy and paid a portion of the amount due while this litigation continued in an effort to recuperate some portion of the losses caused, in relevant part, by Uddin's failure to abide by the Guaranty Agreement. Therefore, at the time the trial court granted STIC's motion for summary judgment, Uddin's complaints regarding STIC's capacity to sue in place of Sterling had been cured. See, e.g., In re Bridgestone Am. Tire Operations, LLC, 387 S.W.3d 840, 848 n.7 (Tex. App.—Beaumont 2012) (orig. proceeding) ("A defect in capacity is curable and after-acquired capacity will relate back to the inception of the suit.").

Further, the court held, the statute of limitations was an affirmative defense and not jurisdictional in nature. It said:

Because nothing in section 16.004 of the Texas Civil Practice and Remedies Code or related statutes suggest a legislative intent to impose a jurisdictional requirement, we hold that subsection 16.004(a)(3)'s four-year limitations period is not jurisdictional. Rather, it presents an issue of capacity, and deficient capacity can be cured by the relation-back doctrine.

The court also held that Uddin was not entitled to assert various offset type claims, including misrepresentation, conversion, negligence and breach of contract, because all such claims were waived in the guaranty. In Paragraph 11 of the guaranty, Uddin waived "all defenses given to sureties or guarantors." Accordingly, the court said, "Uddin waived his offset defense and its underlying theories."

Title Insurance

Insurer That Changed Legal on Deed of Trust Not Liable for Constructive Fraud

Carver v. RBS Citizens, N.A., 2019 WL 4733437 (Md.Sp.App.) (unpublished).

A title insurer that added parcels to a deed of trust by rerecording it after closing was not liable to the borrowers on their claim of constructive fraud, because the insurer had no contractual relationship with the borrowers.

Lawrence and Nancy Carver bought a farm in Cecil County, Maryland in 1998, made up of three parcels. They got several loans from Central Maryland Farm Credit and granted deeds of trust on all of their parcels. Later, they split off a 3.5-acre parcel from their 41-acre parcel, which the court referred to as Property A.

In 2005, the Carvers refinanced their loans with one loan from RBS Citizens of $576,000. The RBS deed of trust described the encumbered land as being "part of" the 41-acre parcel, having a total area of 3.505 acres. Also, Lawrence Carver was the only person named on the deed of trust. Security Title Guarantee Corporation of Baltimore issued a policy insuring the RBS deed of trust.

Later, the Carvers got four loans from Christiana Bank & Trust. The Carvers gave deeds of trust on all four of their parcels to Christiana Bank. Those loans were assigned to Penn Lenders LLC.

The Carvers defaulted on their RBS loan. In 2010, RBS started a foreclosure action. The substitute trustee told Security Title that RBS could not complete the foreclosure because the deed of trust contained "conflicting information." The trustee asked Security Title to "clarify the number of acres subject to the deed of trust because the document described

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the encumbered property as being part of 41.072 acres, but separately identified the encumbered property as a 3.505-acre plot." The trustee also asked why Nancy Carver was not listed as a borrower.

Security Title fixed the problem by rerecording the deed of trust with a new legal description, covering all the Carver parcels, and listing Nancy Carver as a borrower, without informing the Carvers.

The Carvers discovered the modification when they tried to sell the properties. The buyer allegedly walked because he was not sure if RBS held a valid lien on the added parcels. The Carvers then defaulted on the loans held by Penn Lenders. That lender sued for a declaratory judgment about whose lien was first on the added parcels. The circuit court ruled that the rerecording was a nullity and the RBS deed of trust encumbered only the original Property A.

The Carvers went on the offensive, suing RBS and Security Title for the allegedly lost sale. They brought claims of misrepresentation, fraud, constructive fraud, and conspiracy. There was a trial. RBS made some sort of deal during trial and was dismissed. The court dismissed the claims against Security Title for misrepresentation, fraud, and conspiracy, but held that the Carvers prevailed on their constructive fraud claim. It reasoned that "[t]itle examiners owe a duty to use a reasonable degree of skill and diligence in supplying information to their customers and to others." The court awarded the Carvers $6,726 in damages.

Security Title and Carver both appealed. The appeals court struck the judgment based on constructive fraud, holding that Security Title did not have the requisite confidential relationship with the Carvers to support the claim.

In Maryland, a claim of constructive fraud is based on a "breach of a legal or equitable duty which, irrespective of the moral guilt of the fraud feasor, the law declares fraudulent because of its tendency to deceive others, to violate public or private confidence, or to injure public interests." *Canaj, Inc. v. Baker & Div. Phase III, LLC*, 391 Md. 374, 421-22 (2006). The person bringing the claim must demonstrate the existence of a confidential relationship. *Chassels v. Krepps*, 235 Md.App. 1 (2017). A confidential relationship exists only if the defendant was an advisor to the plaintiff and the plaintiff relied on the defendant's advice. The existence of a confidential relationship must be established by clear and convincing evidence.

The appeals court said the Carvers failed to establish the existence of a confidential relationship. Indeed, the court said, "the Carvers did not present any evidence to demonstrate that they had any type of relationship with Security Title." The court refused to apply a case concerning a tax sale, in which the tax buyer was found to have committed fraud by failing to give the owner the statutorily-mandated redemption notice. The court said a title insurer's duty is more general and not based on trust:

> *Although title examiners and mortgagees have an obligation to file accurate liens, "[m]ere non-compliance with a legal duty is not necessarily constructive fraud[.]" ... This is not to say that title examiners and mortgagees may file inaccurate liens without incurring any liability. Indeed, under certain circumstances, individuals who file inaccurate liens may be held criminally liable. See Md. Code (2013, 2018 Suppl.), § 3-808 of the Criminal Law Article. Moreover, plaintiffs may bring negligence claims against title examiners even in the absence of a confidential relationship. See 100 Inv. Ltd. P'ship v. Columbia Town Ctr. Title Co., 430 Md. 197, 230-31 (2013). The damages suffered by the Carvers are not—as a matter of law—the result of constructive fraud.*

This court recognized an important limitation in a Maryland title company's searching and recording duties. It could have, but did not directly, observe that Security Title's duties ran only to the insured, RBS, and not to its borrowers.

Title Insurance

Insurer Gets Judgment Against Forger

First American Title Ins. Co. v. Chavannes, ___ N.Y.S.3d ___, 2019 N.Y. Slip Op. 07053, 2019 WL 4849440 (N.Y.A.D. 2 Dept. 2019) (not yet released for publication).

A title insurer that paid a claim based on a forged power of attorney was entitled to enforce a judgment against the people who forged the instrument.

Robert Comond and his ex-wife, Marie L. Chavannes, owned property in New York. The property was conveyed to Golden Grand Developers LLC by a deed signed by Robert's son Marvin Comond and Chavannes.

Robert sued Golden Grand, Marvin, and Chavannes, claiming that Chavannes forged his signature on the purchase contract and that Marvin forged his signature on a power of attorney that Marvin used to sign the deed. He said that Chavannes and Marvin split the sale proceeds.

Golden Grand agreed to settle with Robert by paying him $190,000 to abandon his claim to the property, and for an assignment of his fraud claim against Chavannes and Marvin. Chavannes then filed for bankruptcy.

After the bankruptcy case was dismissed, Golden Grand settled with its title insurer, First American, and then filed a motion in Robert's action to have the title insurer named as the substitute plaintiff. The court granted the motion and then entered a judgment against Chavannes and Marvin of $190,000.

Chavannes appealed. The court affirmed the judgment. It approved the assignment of the claims to First American, and the entry of the judgment against Chavannes. It said that "Golden Grand submitted clear and convincing evidence that the signatures on the contract of sale and the power of attorney used to execute the deed were forged and that Chavannes forged the signature on the contract of sale, among other things." Conversely, it said, "Chavannes failed to raise a triable issue of fact in opposition."

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Title Insurance

Title Policy May Be a Financial Record, But Can Be Produced Under Subpoena

Nationwide Investments, LLC v. Pinnacle Bank, ___ Tenn.App. ___, ___ S.E.2d ___, 2019 WL 4415188 (Tenn.App. 2019) (not yet released for publication).

A bank did not violate state or federal financial record privacy laws by producing a copy of a title insurance policy in which it was the insured, because it did so in response to a subpoena.

Pinnacle Bank made several loans to Charles Walker, a Tennessee resident and attorney. Walker owned about 40 residences, most of them rental properties. Walker filed a bankruptcy petition immediately after a creditor, Family Trust Services LLC, got a prejudgment attachment order that applied to his rental properties. Pinnacle Bank was a secured creditor in his bankruptcy case.

Family Trust served a subpoena on Pinnacle Bank asking it to produce its loan title insurance policy for one of Walker's properties. The bank produced the title insurance policy. Walker got into a pitched battle in the bankruptcy case with Pinnacle Bank and its attorney. After the court entered orders against Walker, his entity Nationwide Investments sued the bank in this action, claiming that its turnover of its title policy violated the federal Right to Financial Privacy Act and the Tennessee Financial Records Privacy Act.

The district court granted the bank's summary judgment motion and its request for Rule 11 sanctions against both Nationwide and Mr. Walker. Walker appealed, and the court affirmed. The court said it did not need to decide if a title insurance policy is a financial record, because the bank responded to a subpoena and Walker did not object. The Tennessee law specifically allows a bank to respond to a subpoena without violating the law. See Tenn. Code Ann. § 45-10-107(c).

The court also held that the federal Right to Financial Privacy Act did not apply, because that law applies only to records sought by a department or agency of the Federal government, and not records sought by a private individual or entity. See 12 U.S.C. § 3402 ("Except as provided by section 3403(c) or (d), 3413, or 3414 of this title, no Government authority may have access to or obtain copies of, or the information contained in the financial records of any customer from a financial institution unless ...."). The court also cited *United States v. Zimmerman*, 957 F. Supp. 94, 96 (N.D.W.Va. 1997) ("Under the Right to Financial Privacy Act, financial institutions are prohibited from providing access to the financial records of any customer of the financial institution to a government authority."); and Lawrence A. Young, *The Landscape of Privacy*, 55 Consumer Fin. L.Q. Rep. 4, 13 (2001) (noting that the Right to Financial Privacy Act focuses "on the disclosure of information to government agencies and not to private entities").

Escrow Matters

Escrowee Entitled to Full Formulaic Fee Although Escrow Did Not Close

Bong Je Choi v. Prima Escrow, Inc., 2019 WL 5157124 (Cal.App. 2 Dist.) (unpublished).

The parties to an escrow have been required to pay escrow fees based on the proposed sale price even though escrow did not close. However, the escrowee was not entitled to also collect prevailing-party attorneys' fees.

Bong Je Choi and his wife, Hung Yeon Choi, owned the Pasadena Inn in Pasadena, Calif. In 2014, they contracted to sell the hotel to CMA Real Estate Investments Inc. for $13.5 million. Prima Escrow Inc. was retained to serve as escrowee. CMA delivered an initial deposit of $100,000 to Prima. The close of escrow was extended several times at CMA's request, in exchange for which CMA delivered an additional $300,000 into escrow and agreed to an increase in the purchase price.

The last amendment extended the close of escrow to Jan. 16, 2015 and said that escrow would be cancelled if CMA did not deliver its deposits by January 15. Prima was allowed to release $300,000 of the $400,000 deposit to the Chois on Dec. 19, 2014.

CMA did not make the required deposits. However, Prima refused to release any of the money to the Chois because CMA had not agreed to cancel the escrow.

The Chois sued CMA and Prima, asking the court to order the turnover of the $400,000 deposit. The Chois dismissed Prima from the action before it was required to answer the complaint. The court entered a default judgment against CMA, ordering Prima to deliver the $400,000 deposit to the Chois.

Before releasing the money, Prima sent the Chois a demand for $64,846.60 in escrow fees, which was a discounted version of the fee formula stated in the supplemental escrow instructions. The Chois refused to pay the fees because escrow had not closed. Prima released $300,000 to the Chois and told them it would keep the balance of $100,000 until the escrow fee dispute was resolved.

The Chois sued Prima a second time, for conversion, breach of fiduciary duty and money had and received. The Chois claimed that Prima was not entitled to any escrow fee because escrow did not close and the supplemental escrow instructions did not recite a cancellation fee.

There was a trial. Mr. Choi testified that he did not think he would have to pay Prima a fee if the escrow was

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cancelled. A Prima employee testified that the Chois owed the fee even though escrow did not close, because the company had done a lot of work in the initial escrow and the five extensions. Prima put on an expert witness, an experienced escrow officer, who testified that escrow fees are owed whether an escrow is closed or cancelled. The expert also testified it would be appropriate to deduct the escrow fees from the deposit owed to the proposed seller.

The trial court issued a decision holding that the Chois and CMA were jointly and severally liable for escrow fees of $64,846.60. The court also held that Prima acted properly in withholding the $100,000 balance, because resolving the fee dispute was a condition precedent to release of the initial deposit. The court also awarded Prima its attorney fees of $61,692.50 as prevailing-party fees.

The appeals court affirmed some of these rulings. It said the escrow instructions clearly stated that the escrow fee would be calculated based on $2.50 per thousand of the purchase price, and did not condition payment of that fee on close of escrow. Also, the instructions said that the initial deposit of $100,000 would be disbursed only "after deducting cancellation fees and expenses without any further instructions necessary." In a "seller only" provision of the instructions, the Chois agreed to pay Prima's "escrow charges ... whether or not this escrow is consummated."

However, the court noted that a different paragraph in the general instructions said that, if escrow was cancelled, the parties would pay Prima "a sum sufficient to pay you for any expense which you have incurred pursuant to forgoing instructions and a reasonable cancellation fee for services rendered by you."

The court analyzed the escrow instructions based on contract principles, which is the standard of interpretation in California under *Rideau v. Stewart Title of California*, Inc. (2015) 235 Cal.App.4th 1286, 1294. The court said that it was "irrelevant" that Mr. Choi "may have subjectively believed escrow fees referred only to fees due at the closing of an escrow." The court held that the instruction clearly stated that the Chois were to pay the escrow fees whether or not escrow closed.

The court dealt with the cancellation fee provisions this way:

> *Finally, although we believe the ordinary meaning of the terms is clear, any possible ambiguity created by use of both the terms "escrow fees" and "cancellation fees" in the parties' agreement was resolved by the undisputed opinion testimony of Prima's expert witness, who explained that in the escrow industry "escrow fees" and "cancellation fees" are "the same" and may be used interchangeably.*

Further, the court rejected the Chois' argument that the full escrow fee was unreasonably large as a cancellation fee. It said:

> *The formula to be used by Prima to calculate its fees is clearly stated on the first page of the supplemental escrow instructions, and the Chois agreed to pay those fees when they signed the instructions. Moreover, Prima's expert witness testified the fees charged, discounted by Prima from the agreed-to formula, were reasonable. No other evidence of the reasonable value for Prima's services was presented to the trial court. Whether measured by the formula itself or assessment on a reasonable basis, the court's determination that Prima was entitled to that $64,846.60 for the services performed by Prima is supported by substantial evidence and was well within its discretion.*

The court also held that the fee did not violate Financial Code section 17421.5, which permits an escrow company to charge a fee for administering an escrow that has been cancelled only if certain requirements are met. The court said those requirements were met, in that cancellation resulted from an act or omission of a party to the escrow, the fee formula was described in written instructions in not less than eight-point type on the first page of the document, and the instructions were signed and initialed by the Chois.

The appeals court also held that the trial court had properly dismissed the Chois' claims for conversion, breach of fiduciary duty and money had and received.

Finally, however, the court reversed the trial court's order giving Prima attorneys' fees. In a lengthy discussion, the court ruled that the fee provision on which Prima relied was an indemnity provision pertaining to escrow performance disputes, and not a prevailing-party provision that overrides the American rule, under which each party pays its own attorneys' fees.

Escrow Matters

Escrow Disbursement to be Made Only After Final Order Entered

Flandreau Santee Sioux Tribe v. Terwilliger, ___ F.Supp.3d ___, 2019 WL 4452246 (D.S.D. 2019) (not yet released for publication).

When an escrow was set up to hold money claimed by the State of South Dakota for taxes on products sold by the Flandreau Santee Sioux Tribe, the money had to stay in escrow until the final order was entered in the lawsuit between the state and the tribe over whether that tax was owed.

The tribe owns and operates a casino, hotel, RV park, gift shop and store in South Dakota. The state claims that it is entitled to collect taxes on products sold to people who are not tribal members. It conditioned renewal of the tribe's liquor license on payment of those taxes.

The tribe sued the state. An escrow was set up to hold the tax money claimed by the state. In 2017, a federal court ruled that the Indian Gaming and Regulatory Act preempts the state from taxing nonmember purchases at the casino, but not at the store. The court entered an amended judgment in October of 2017, paragraph 4 of which read:

> *In accordance with the Parties' Deposit Agreement, the escrow agent may now, subject to any stay granted pursuant to an appeal, disburse to the Tribe the funds held in escrow which represent the use tax imposed on nonmembers' use of purchased goods and services as to the Casino's slots, table*

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games, food and beverage services, hotel, RV park, live entertainment events, and gift shop.

The state appealed to the Eighth Circuit Court of Appeals and asked the district court to stay disbursement under paragraph 4. It argued that, if the stay was not entered, it would have a hard time collecting the money from the Tribe because of its sovereign immunity. The Tribe opposed the granting of the stay. Then it sent a letter to the escrow agent, asking it to disburse the money from escrow based on the amended judgment. The escrow instructions included a provision stating that disbursement was not to be made until there was "a final determination by a court of proper jurisdiction." The state wrote its own letter to the escrow agent, telling it not to disburse because there had been "no final determination by a court of proper jurisdiction" as to who was entitled to the money, and the state was appealing the district court decision.

The escrow agent hired a lawyer. It appears that section eight of the escrow instructions contained a "contradicting instruction" provision. The escrowee wrote to both parties, saying that under Section Eight, it was entitled to refuse the Tribe's request for disbursement because the Tribe and State "are not in agreement" about whether the matter has been "finally adjudicated." The escrow agent said that, based on its lawyer's advice, "disposition of the funds cannot be made until there is a final, non-appealable judgment directing disposition as set forth in Judge Piersol's ruling."

The Tribe asked the court to issue a writ ordering the escrowee to disburse the money immediately. Just as briefing on the motion for stay was completed, the Eighth Circuit issued its ruling, partly affirming and partly reversing the district court's rulings about the taxes. The district court held that this rendered the request for a stay moot. However, it did rule on the tribe's motion for a writ, which it denied. It said:

The relief sought by way of writ of assistance is ordinarily addressed to the sound discretion of the court. … The Court declines to grant the Tribe's writ of assistance at this time. The Court did not contemplate when issuing its judgment that the Tribe would be entitled to disbursement of the funds until, as provided in the Deposit Agreement, the parties agreed to the disbursement, or until there has been "a final determination by a court of proper jurisdiction." The State has ninety days to petition for a writ of certiorari with the United States Supreme Court after the Eighth Circuit Court of Appeals issued its judgment in this matter.

This is a solid decision, and one of the few to have construed a final determination provision in an escrow agreement. Such provisions are routine in escrows tied to litigation.

RESPA Alert

RESPA Affiliated Business Claim Dismissed

Cantrell v. New Penn Financial, LLC, ___ F.Supp.3d ___, 2019 WL 4689226 (D.S.C. 2019) (not yet released for publication).

A borrower's claim against a title company based on RESPA's Section 8 was dismissed because the agent proved the requirements for an affiliated business arrangement had been met.

Kevin Cantrell contacted New Penn Financial to get a refinance of his Veteran's Administration home loan at a lower rate. New Penn gave Cantrell a RESPA affiliated business disclosure concerning closing company Avenue 365 Lender Services. Cantrell now says that his contact person at New Penn, Jake Brown, never told him that he could use a different closing or title company.

Attorney Ryan Breckenridge came to Cantrell's house to close the loan. Breckenridge was an independent closing attorney retained by Avenue 365.

After the loan closed, Cantrell sued New Penn, Avenue 365 and Breckenridge for fraud, violation of RESPA Section 8 and other claims. The defendants filed summary judgment motions. In this decision, the court granted Avenue 365's motion concerning the RESPA and fraud claims, as well as other claims. The court held that Cantrell had failed to alleged that Breckenridge, as Avenue 365's appointed closer, misrepresented anything or perpetrated a fraud.

Cantrell's RESPA claim was based on a fact he learned in discovery, that Avenue 365 paid $25,000 a month to New Penn. Cantrell argued that Avenue 365's monthly payment to New Penn "has not been connected to any goods or facilities actually furnished or for services actually performed," and that "New Penn automatically sends all of its business to Avenue 365 for the lucrative title insurance commission."

The court dismissed the RESPA claim because it found that Avenue 365 had proven the three required elements for the affiliated business safe harbor. Section 8(c) of RESPA states that payments made to an owner of an affiliated business is not a referral fee as long as "a disclosure is made of the existence of such an arrangement to the person being referred," a written estimate of the charge is provided, the person is not required to use any particular provider of settlement services, and the only value received by the affiliates are payments for services rendered and "a return on the ownership interest." 12 U.S.C. § 2607(c).

The court said the payments to New Penn fell under the safe harbor, and that all elements of the affiliated business exemption had been established without controverting evidence:

Defendants have offered specific evidence that they disclosed their business relationship to Plaintiffs, made Plaintiffs aware of the fees, and did not require Plaintiffs to use Defendant Avenue 365. In fact, Plaintiffs acknowledge that "Defendants made affiliated business disclosures and explicitly stated that Plaintiffs were not required to use Avenue 365." … As to the $25,000 payment, Defendants have offered evidence that it covered bona fide business expenses and administrative fees. … Plaintiffs have offered no specific evidence to the contrary. Accordingly, Defendants' Motion is granted as to Plaintiffs' RESPA claim.

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Conveyance News

Court Thwarts Attempt to Use Torrens to Undo Foreclosure

Matter of Warren, 448 P.3d 820 (Wash.App. 2 Div. 2019).

A Washington appeals court has held that borrowers cannot undo a foreclosure sale by filing a Torrens petition for the property they no longer own.

Frank and Cheri Schnarrs bought a house in Olympia, Washington. They borrowed money and gave a deed of trust on the house as collateral. They stopped making payments on the loan. Wilmington Savings Fund Society conducted an auction sale and recorded a trustee's deed.

The Schnarrses appear to have hired a quack foreclosure consultant. Four months after Wilmington recorded its deed, Micah James Anderson, on behalf of the Schnarrses, signed and filed a Torrens Act petition and application seeking to register the Schnarrses' title to the land under the Act. Anderson signed the Torrens petition and other documents. He is not an attorney. Anderson and the Schnarrses then attempted to bring a series of default motions, all of which were ultimately denied for various reasons.

Frank Schnarrs eventually signed and filed an amended Torrens Act petition and application for registration of land titles almost eight months after Wilmington had recorded its trustee's deed. The amended petition named Cheri Schnarrs as a party and applicant.

The superior court dismissed the petition because the Torrens Act requires petitioners to be owners of the property. The Schnarrses appealed and the court affirmed.

The appeals court began by noting that Washington adopted its Torrens Act in 1907, and that law created a system for recording land titles separate from the recording act. Under the Torrens Act, chapter 65.12 RCW, proper registration with the office of the registrar of titles provides conclusive evidence that the person recorded on the register is the owner of the registered property. The court said that Torrens "has apparently fallen into disuse as a result of modern title recording systems, including the use of title companies and private electronic registration systems such as the Mortgage Electronic Registration System, Inc." It cited *Bain v. Metro. Mortgage Group, Inc.*, 175 Wash.2d 83, 88, 285 P.3d 34 (2012), for that novel proposition.

RCW 65.12.005 says that the "owner" of property may apply to have his or her title registered. The Torrens Act does not define the term "owner." The court said that Wilmington became the owner at the trustee's sale. Frank Schnarrs filed his claims under the Torrens Act four months after Wilmington recorded its deed. The court said that, because the Schnarrses no longer owned the property, they did not have any title to register under the Torrens Act.

The Schnarrses argued on appeal that they still owned the property when they filed their Torrens Act petition because they still lived in the home and had declared it their homestead. The court rejected that argument, because the homestead exemption is not available "against an execution or forced sale in satisfaction of judgments obtained ... [o] n debts secured (a) by security agreements describing as collateral the property that is claimed as a homestead or (b) by mortgages or deeds of trust on the premises that have been executed and acknowledged by both spouses." RCW 6.13.080(2); *Washington Fed. v. Harvey*, 182 Wash.2d 335, 337 n.1, 340 P.3d 846 (2015).

Mr. Anderson's Torrens scheme might have received internet fame. Title insurers might do well to warn examiners and title officers that a Torrens registration by a borrower after foreclosure is invalid and does not divest the lender of title.

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CLAIMS HANDBOOK

compiled by the FNF Legal Staff

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APRIL, 2005
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CLAIMS HANDBOOK

compiled by the FNF Legal Staff

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4. unmarketability of title.

D) The claim must not be barred by the exclusions or exceptions from coverage, or by any other provision of the policy.

In other words, coverage under the policy exists only to the extent set forth in the insuring clauses. And the protection afforded thereby is limited by the exclusions, exceptions and other terms and conditions of the policy. Thus, the existence or non-existence of a particular exclusion or exception does not (in general) cause additional coverage to arise by implication.[1] It has been said that the burden is placed upon the *insured* to establish that the claim falls within the insuring clauses. But once he or she has done so, the burden is cast upon the *insurer* to demonstrate that the claim is excluded or excepted from coverage or otherwise barred under the terms of the policy. *See* §3.02 [D].

Both the insurer and the insured must bear in mind that the policy must be read as a whole, so if a claim is presented based upon a matter which appears to fall within the insuring clauses, it still may not be valid, because the subject-matter thereof may be excepted or excluded from coverage. Examples of this type of situation include a lien which is excepted in Schedule "B" or a claim of unmarketability based upon non-compliance with a zoning regulation. Thus, in one decision, it was held that the assignee of a mortgage, which was unenforceable for lack of consideration, had no cause of action against the title insurer. The risk occasioned by the lender's failure to advance the funds was determined to have been beyond the scope of the coverage afforded by the policy. *Gerrold v. Penn Title Ins. Co.*, 637 A. 2d 1293 (N.J. App.1994).

On the other hand, insurance policies are sometimes referred to by our courts as **contracts of adhesion**, because the insured is frequently unable to negotiate the scope of coverage. For this reason, ambiguities may be construed *in favor of the insured* and *against the insurer*. Furthermore, the **reasonable expectations of the insured doctrine** is sometimes invoked to expand the scope of policy coverage. Thus, if it is unclear from the wording used in the policy whether a particular problem is covered or not, the courts may utilize the principles enunciated above to hold the insurer liable. *See* §2.01[D]. But where the policy fails to contain wording which has been agreed upon by the parties, owing to a scrivener's error (for example), it is subject to reformation, just as is any other contract. *Paz v. DeSimone,* 352 A 2d 609 (N.J. Ch. 1976).

There are nevertheless some limitations on how far the courts are willing to go in interpreting the policy. For example, in a leading case, the court rejected the insured's contention that a general survey exception was insufficiently broad to insulate the insurer from liability for a shortage of acreage, and reached the following conclusion: "...courts should not write for the insured a better policy of insurance than the one purchased".

1 *See, e.g., Elysian Investm. Group v. Stewart Title Co.*, 105 Cal. App. 4th 315, 129 Cal. Rptr. 2d 372 (2003) ("[the insured"] cannot rely upon an exclusion to extend coverage").

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Thus, the policy (a) is one of indemnification, not guaranty; (b) which insures against actual loss or damage; (c) sustained by the insured; (d) which is caused by matters insured against; and (e) which is measured by the formula set forth in the policy.

The title insurance contract is one of indemnity, not guaranty. *See* § 2.01 [C]. This means that in order to recover under the policy or to maintain a cause of action against the insurer, the insured has to demonstrate that it suffered *actual loss or damage* by reason of a matter falling within the insuring clauses of the policy. *See* § 2.03 [C]. Thus, it is insufficient for the insured to demonstrate that title is not held as insured; rather, the insured must show that title is not held as insured, and that, as a result thereof he or she has suffered compensable loss or damage. Consistent with the foregoing, Exclusion from Coverage No. 3(c) expressly excludes defects, liens, encumbrances, adverse claims, or other matters "resulting in no loss or damage to the insured claimant".

The policy's formula for measurement of loss or damage under the loan policy is the *least* of:

- the amount of insurance stated in Schedule A (or, if applicable, C&S, ¶ 2(c)) ; or
- the amount of the unpaid mortgage debt, as limited by C&S, ¶ 8 or as reduced by C&S, ¶ 9 (with regard to loss payments made following the insured lender's acquisition of title), at the time the loss occurs; or
- the difference in value of the estate or interest insured with and without the defect giving rise to the claim.

The measure of damages under the *loan* policy should be contrasted with the measure of damages under the *owner's* policy. Under an owner's policy, the measure of damages is typically the difference in the value of the land with and without the defect which gave rise to the claim. But the estate or interest insured under a loan policy (*i.e.*, the mortgage) is only security for the repayment of the underlying debt. Accordingly, in order for an insured lender to demonstrate that it has suffered loss or damage compensable under a loan policy, it must show that, by reason of a lien, defect or encumbrance not excluded or excepted from coverage, there is insufficient value in the insured land to support the mortgage.

In contrast to an insured owner, an insured lender will not necessarily be able to demonstrate actual loss or damage -- even though a non-excepted, non-excluded lien is being foreclosed – because the insured lender must demonstrate causation; *i.e.*, that its actual loss or damage arises from the title defect. There may be no actual loss or damage under a loan policy (even if a prior lien exists), because there may be enough value in the land so that both the prior lien and the insured mortgage can be satisfied from the sale thereof. As long as the insured lender is repaid the existing indebtedness, or obtains title to the land, which (even with the defect) has value equal to or greater than the secured debt, there is no loss or damage within the meaning of the policy. *Green v. Evesham Corp.*, 430 A.2d 944 (N.J. App. 1981).

So if the insured lender holds a $75,000 mortgage on land having a value of $100,000, and a prior lien in the amount of $10,000 is discovered, the lender has not suffered a loss.

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