

## TITLE INSURANCE

### ARIZONA COURT OF APPEALS RULES AGAINST TITLE INSURER ON DATE OF LOSS ISSUE

by Michael R. Scheurich

In the recent decision in *First American Title Insurance Co. v. Johnson Bank*, 1 CA-CV 14-0190, 2015 WL 3965740 filed June 30, 2015, the Arizona Court of Appeals held that the date for calculating a loss under a lender's title insurance policy is the date of the loan and not the date of the loan foreclosure (as the lender/plaintiff had contended). The court held that, where the undisclosed defect in title (CC&Rs prohibiting commercial development) caused the borrower's default, the date of the loan is the proper date to measure the insured property's diminution in value as a result of the undisclosed title defect. While this issue had been previously resolved in the same fashion by an Arizona federal district court, *Equity Income Partners LP v. Chicago Title Ins. Co.*, 2012 WL 3871505 (D. Ariz. Sept. 6, 2012), no published Arizona court decision had yet ruled.

The Court of Appeals in *Johnson Bank* noted that the failure of the lender's policy to specify the date the loss is to be calculated creates an ambiguity that must be resolved by looking to social policy and the transaction as a whole. Any remaining ambiguity is construed against the insurer. Given this analytical process, the following passage from the decision is noteworthy:

"Unlike an owner, a lender stands to gain nothing when market forces cause property to appreciate. A lender purchases insurance to insure the value of its loan, not the value of a property. A rule that allows the insurer to benefit from market depreciation while facing no risk in the event of a rising market would not reflect the reasonable expectations of the contracting parties. But the rule we adopt here allows certain evaluation of the risks associated with the policy and therefore strikes a fair balance: each party to the insurance policy knows what the policy is worth, and how damages will be calculated. Our holding does not transform lenders' insurance policies into guarantors of future market property values that are the product of subsequent market fluctuation - liability under such policies is simply the difference between the value of the property without the insured defects at the time of the loan and the value of the property with the insured defects at the time of the loan."

The court concluded that, because First American failed to discover and timely disclose the CC&R's, the policy was breached at the time the loan was made. Using the date of the loan to measure any diminution in value will allow Johnson Bank to recover its loss where the default and resulting losses to the lender were caused by a covered title defect.

We may or may not see policy revisions resulting from this decision. As the court noted, quoting the trial court: "[i]nsurance companies know how to write sentences that say 'on the date of foreclosure' in them. I don't know why they don't." However, the language in question by in large remains a part of the standard ALTA 2006 lender policy forms. Therefore, most likely, any changes would come from the ALTA or from a rather significant impetus from the major title insurers.

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