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Bank of Idaho v. First American Title Insurance Company Respondent's Brief Dckt. 41157

IN THE SUPREME COURT OF THE STATE OF IDAHO

BANK OF IDAHO, an Idaho banking corporation, Plaintiff/Appellant, v. FIRST AMERICAN TITLE INSURANCE COMPANY, a corporation, Defendant/Respondent	Supreme Court Docket No. 41157 District Court Case No. CV-12-603

RESPONDENT'S BRIEF

Appeal from the District Court of the Seventh Judicial District for Bonneville County

Honorable Joel E. Tingey, District Judge, Presiding

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I. STATEMENT OF THE CASE

A. Summary

This matter arises out of a dispute about whether First American Title Insurance Company ("First American") is liable to Bank of Idaho ("BOI") under a loan policy of title insurance (the "Loan Policy") issued by First American's predecessor in interest, United General Title Insurance Company ("United General"). The District Court, in its Memorandum Decision and Order in this case, granted First American's motion for summary judgment, concluding that BOI did not incur losses for which First American is liable under the Loan Policy. (R. Vol. 2, p. 461.) In accordance with the District Court's Memorandum Decision and Order, the District Court issued a Judgment of Dismissal. (R. Vol. 2, pp. 463-64.) BOI has appealed from the District Court's decision. (R. Vol. 2, pp. 470-73.) First American seeks to have the District Court's decision upheld.

B. Factual Background and Procedural History

On or about January 8, 2007, BOI extended two construction loans to the Petersons. (R. Vol. 2, p. 168, ¶ 4; R. Vol. 2, pp. 173-81.) The first loan, in an amount not to exceed the principal amount of $227,041.30, was secured by a Deed of Trust, covering Lot 1, recorded as Instrument No. 1249619 in the records of Bonneville County, Idaho (the "Lot 1 Deed of Trust"). (R. Vol. 2, p. 168, ¶ 5; R. Vol. 2, pp. 182-88.) The second loan, in an amount not to exceed the principal amount of $226,737.80, was secured by a Deed of Trust covering Lot

2, recorded as Instrument No. 1249621 in the records of Bonneville County, Idaho (the "Lot 2 Deed of Trust"). (R. Vol. 2, p. 168, ¶ 6; R. Vol. 2, pp. 189-95.)

The two deeds of trust and the two loans to the Petersons were cross-collateralized, meaning that both Lot 1 and Lot 2 constituted collateral securing payment of either of the two loans. See the fourth paragraph, entitled "CROSS-COLLATERALIZATION", in both the Lot 1 Deed of Trust and the Lot 2 Deed of Trust. (R. Vol. 2, pp. 183, 190.) On or about March 17, 2009, such cross-collateralization was reconfirmed when the Petersons and BOI executed and recorded a Modification of Deed of Trust with respect to each deed of trust. (R. Vol. 2, pp. 168-69,¶ 7-8; R. Vol. 2, pp. 196-201.)

United General issued the Loan Policy, bearing Policy No. 64092871, with respect to the Lot 1 Deed of Trust and a loan policy of title insurance with respect to the Lot 2 Deed of Trust (R. Vol. 1, p. 69, ¶ 7; R. Vol. 2, p. 169,¶ 9; R. Vol. 2, pp. 291-305.) At some point United General issued Endorsement CLTA Form 116 ("Endorsement 116") to the aforementioned title policies. (R. Vol. 1, p. 69, ¶ 7; R. Vol. 2, pp. 285-86, ¶ 5, R. Vol. 2, pp. 291-305.)

The Petersons originally planned to construct one four-plex on Lot 1 and one four-plex on Lot 2. (R. Vol. 1, p. 69, ¶ 3.) However, as required by the City of Idaho Falls, the Petersons changed their plans and constructed both four-plexes on Lot 2 and common parking, storm water retention, and landscaping on Lot 1. (R. Vol. 1, pp. 37-44.)

The Petersons defaulted on the aforementioned loans and BOI foreclosed on the property. (R. Vol. 1, p. 70, ¶ 11.) The foreclosure sale took place on March 11, 2010. At the foreclosure sale, BOI made a credit bid on Lot 1 "for all amounts due and owing as of March 11, 2010, under the terms of the [Lot 1] Deed of Trust and Modification of Deed of Trust." (R. Vol. 2, p. 169, ¶ 10; R. Vol. 2, pp. 211-13.) At the foreclosure sale, BOI made a credit bid on Lot 2 "for all amounts due and owing as of March 11, 2010, under the terms of the [Lot 2] Deed of Trust and Modification of Deed of Trust." (R. Vol. 2, pp. 169-70, ¶ 11; R. Vol. 2, pp. 214-16.)

BOI provided a Notice of Title Insurance Claim to United General on June 10, 2010, demanding payment of the full amount of the Loan Policy, notwithstanding the fact that the indebtedness secured by the Lot 1 Deed of Trust had been satisfied in full at the foreclosure sale. (R. Vol. 1, p. 7, ¶ 14; R. Vol. 2, p. 312, ¶ 11; R. Vol. 1, pp. 30-31.) First American, successor in interest to United General, reviewed BOI's claim and, by letter dated March 10, 2011, denied BOI's claim for failure to state a loss for which First American was liable under the Loan Policy. (R. Vol. 1, pp. 65-67.)

BOI sold the property to a third-party buyer for $360,000. (R. Vol. 2, p. 454.) Less than a year after BOI sold the property, Jeffrey L. Kelley, an Idaho State General Certified Appraiser and the only certified appraiser to offer an opinion in this matter, performed an appraisal of the property. (R. Vol. 2, p. 227, ¶ 2-4.) He also gave his professional opinion

as to whether there would be a difference in the value of the property if one four-plex, its parking area, and its water retention area had been built on Lot 1 and one four-plex, its parking area, and its water retention area had been built on Lot 2, as opposed to the "as is" condition with both four-plexes built on Lot 2 and the parking and water retention areas for the two four-plexes built on Lot 1. After inspecting and appraising the property, Mr. Kelley determined that the property's value would not change from the "as is" value reflected in Mr. Kelley's appraisal if one four-plex, its parking area, and its water retention area had been built on Lot 1 and one four-plex, its parking area, and its water retention area had been built on Lot 2. (R. Vol. 2, pp. 227-28, ¶ 5-6.)

II. ADDITIONAL ISSUES PRESENTED ON APPEAL

In addition to responding to the issues raised in BOI's Brief, as set forth in statements (1) through (3) below, First American also includes a fourth issue, set forth in statement (4) below:

(1) The District Court did not err in concluding that BOI's full credit bid at the trustee's sale constituted a "voluntary satisfaction or release of the insured mortgage" which terminated First American's liability under the Loan Policy's Conditions and Stipulations.

(2) The District Court did not err in finding that BOI's full credit bid was correctly applied as a payment on the secured obligation and that it satisfied in full any and all obligations to BOI with respect to the secured indebtedness.

(3) The District Court did not err in its application of Section 7(a)(ii) of the Loan Policy in concluding that BOI did not suffer a "loss or damage" for which First American was liable to BOI under the Loan Policy.

(4) First American is entitled to attorneys fees and costs on appeal.

III. ATTORNEY FEES ON APPEAL

First American requests an award of attorney's fees and costs on appeal, pursuant to Rules 40 and 41 of the Idaho Appellate Rules, and Idaho Code § 12-123 and Idaho Code § 41-1839(4), as further explained and supported in First American's Argument section below.

IV. ARGUMENT

A. Introduction

A loan policy of title insurance, such as the Loan Policy at issue in this case, is a contract of indemnity against actual monetary loss or damage incurred by reason of matters insured against in the policy and only to the extent described in the policy. Multiple provisions of the Loan Policy quoted by BOI in its brief make it clear that the amount of coverage is limited to, at most, the amount of the outstanding debt secured by the insured deed of trust.

BOI alleges that it suffered damages at various points in time and that such damages were of the kind insured against under the Loan Policy. First American disputes that BOI has suffered any damages covered under the Loan Policy. Even if it is assumed, for the sake

of argument, that BOI at some point incurred covered damages, First American's liability to BOI under the Loan Policy was extinguished when BOI made a full credit bid at the foreclosure sale and thereby reduced the amount of the outstanding debt to zero.

B. The District Court did not err in concluding that BOI's full credit bid at the trustee's sale constituted a "voluntary satisfaction or release of the insured mortgage" which terminated First American's liability under the Loan Policy Conditions and Stipulations.

In this matter, the parties agree that the question of whether First American is liable to BOI is to be decided based on the terms, conditions, and provisions of the Loan Policy. Like other kinds of insurance, title insurance does not protect the insured against every kind of loss that the insured may incur in connection with the subject property. A title insurance policy "is a contract for indemnity against actual monetary loss or damage sustained by the insured claimant who has suffered loss or damage by reason of matters insured against by [the title] policy and only to the extent [therein] described." (R. Vol. 2, p. 455.) "Title insurance policies are contracts between insureds and insurers. As such, absent ambiguity, they are normally governed by the same rules as applied to contracts generally." *Boel v. Stewart Title Guar. Co.*, 137 Idaho 9, 13, 43 P.3d 768, 772 (2002).

With regard to interpreting insurance contracts, this Court has stated:

> It is the function of the Court to construe a contract of insurance as it is written, and the Court by construction can not create a liability not assumed by the insurer, nor make a new contract for the parties, or one different from that plainly intended, nor add words to the contract of insurance to either create or avoid liability. *Thomas v. Farm Bureau Mut. Ins. Co. of Idaho*, 82 Idaho 314,

318, 353 P.2d 776, 778 (1960) (quoting *Miller v. World Ins. Co.*, 76 Idaho 355, 357, 283 P.2d 581, 582 (1955)).

Where a title policy is clear and unambiguous, it should be interpreted and enforced in accordance with its plain meaning.

An analysis of the terms and conditions of the Loan Policy, in light of the undisputed facts of this case, reveals that First American is not liable to BOI. To determine whether a title insurance company is liable to an insured, the natural starting point for the analysis is Section 7 of the Loan Policy Conditions and Stipulations, entitled "Determination and Extent of Liability". Section 7 provides:

> **7. DETERMINATION AND EXTENT OF LIABILITY.**
>
> This policy is a contract for indemnity against actual monetary loss or damage sustained by the insured claimant who has suffered loss or damage by reason of matters insured against by this policy and only to the extent herein described.
>
> (a) The liability of the Company under this policy shall not exceed the least of:
>
> (i) the Amount of Insurance stated in Schedule A, or, if applicable, the amount of insurance as defined in Section 2(c) of these Conditions and Stipulations;
>
> (ii) the amount of the unpaid principal indebtedness secured by the insured mortgage as limited or provided under Section 8 of these Conditions and Stipulations or as reduced under Section 9 of these Conditions and Stipulations, at the time the loss or damage insured against by this policy occurs, together with interest thereon; or

(iii) 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 by this policy.

(b) In the event the insured has acquired the estate or interest in the manner described in Section 2(a) of these Conditions and Stipulations or has conveyed the title, then the liability of the Company shall continue as set forth in Section 7(a) of these Conditions and Stipulations.

(c) The Company will pay only those costs, attorneys' fees and expenses incurred in accordance with Section 4 of these Conditions and Stipulations. (R. Vol. 2, p. 294.) (emphasis added)

As quoted above, the liability of First American to BOI under the Loan Policy "shall not exceed . . . the amount of the unpaid principal indebtedness secured by the insured mortgage . . . as reduced under Section 9 of [the] Conditions and Stipulations."

Section 9 of the Conditions and Stipulations provides:

9. REDUCTION OF INSURANCE: REDUCTION OR TERMINATION OF LIABILITY

(a) All payments under this policy, except for payments made for costs, attorneys fees and expenses, shall reduce the amount of insurance pro tanto. However, any payments made prior to the acquisition of title to the estate or interest as provided in Section 2(a) of these Conditions and Stipulations shall not reduce pro tanto the amount of insurance afforded under this policy except to the extent the payments reduce the amount of the indebtedness secured by the insured mortgage.

(b) Payment in part by any person of the principal of the indebtedness, or any other obligation secured by the insured mortgage, or any voluntary partial satisfaction or release of the insured mortgage, to the extent of the payment, satisfaction or release, shall reduce the amount of insurance pro tanto. The

amount of insurance may thereafter be increased by accruing interest and advances made to protect the lien of the insured mortgage and secured thereby, with interest thereon, provided in no event shall the amount of insurance be greater than the Amount of Insurance stated in Schedule A.

(c) Payment in full by any person or the voluntary satisfaction or release of the insured mortgage shall terminate all liability of the Company except as provided in Section 2(a) of these Conditions and Stipulations. (R. Vol. 2, p. 294-95.) (emphasis added)

As discussed in greater detail below, when BOI acquired the subject property at a nonjudicial foreclosure sale by winning the auction with a full credit bid, the indebtedness secured by the insured deed of trust was paid in full and the insured deed of trust was satisfied and released. As noted in Section 9(c) above, the voluntary satisfaction and release of the deed of trust terminated all liability of First American to BOI "except as provided in Section 2(a) of [the] Conditions and Stipulations."

Section 2(a) describes the parties who are eligible for continued coverage after acquisition of title. Section 2(b) describes the limited situations in which coverage will continue in favor of such parties. Section 2(c) describes the amount of insurance available in the limited situations described in Sections 2(a) and 2(b).

Section 2 states:

2. CONTINUATION OF INSURANCE.

(a) **After Acquisition of Title.** The coverage of this policy shall continue in force as of the Date of Policy in favor of (i) an insured who acquires all or any part of the estate or interest in the land by foreclosure,

trustee's sale, conveyance in lieu of foreclosure, or other legal manner which discharges the lien of the insured mortgage; (ii) a transferee of the estate or interest so acquired from an insured corporation, provided the transferee is the parent or wholly-owned subsidiary of the insured corporation, and their corporate successors by operation of law and not by purchase, subject to any rights or defenses the Company may have against any predecessor insureds; and (iii) . . .

(b) **After Conveyance of Title.** 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 or interest.

(c) **Amount of Insurance.** The amount of insurance after the acquisition or after the conveyance shall in neither event exceed the least of:

(i) the Amount of Insurance stated in Schedule A;
(ii) the amount of the principal of the indebtedness secured by the insured mortgage as of Date of Policy, interest thereon, expenses of foreclosure, amounts advanced pursuant to the insured mortgage to assure compliance with laws or to protect the lien of the insured mortgage prior to the time of acquisition of the estate or interest in the land and secured thereby and reasonable amounts spent to prevent deterioration of improvements, but reduced by the amount of all payments made;
or
(iii) . . . (R. Vol. 2, p. 293.) (emphasis added)

In BOI's Brief, BOI noted that coverage continued after BOI acquired title by foreclosure, as stated in Section 2(a), but failed to note the limitation on the amount of insurance described in Section 2(c). After acquisition of title, the amount of insurance does

not exceed the sum of the principal of the indebtedness and the other amounts described in Section 2(c)(ii), "***reduced by the amount of all payments made.***" (emphasis added)

The amount of BOI's winning bid at the foreclosure sale was "all amounts due and owning as of March 11, 2010 [the date of the foreclosure sale], under the terms of the Deed of Trust and Modification of Deed of Trust." (R. Vol. 2, pp. 212-13.) The amounts due and owning under the terms of the Deed of Trust included "all principal, interest, and other amounts, costs and expenses payable under the Note . . . and any amounts expended or advanced by [BOI] to discharge Grantor's obligations or expenses incurred by Trustee or [BOI] to enforce Grantor's obligations under the Deed of Trust, together with interest on such amounts as provided in this Deed of Trust." See definition of "Indebtedness" in the Lot 1 Deed of Trust. (R. Vol. 2, p. 188.) In other words, BOI's winning bid was for all of the amounts described in Section 2(c)(ii) quoted above. As explained more fully below, credit bids such as BOI's winning credit bid in this case, constitute payments on the secured indebtedness. Because credit bids constitute payments and BOI's credit bid was for all amounts due and owing, BOI's credit bid in this case reduced the amount of insurance under Section 2(c) to zero.

The same conclusion is reached by applying Section 7(b) of the Conditions and Stipulations, which states:

> (b) In the event the insured has acquired the estate or interest in the manner described in Section 2(a) of these Conditions and Stipulations or has

> conveyed the title, then the liability of the Company shall continue as set forth in Section 7(a) of these Conditions and Stipulations. (R. Vol. 2, p. 294.)

As noted above, Section 7(a)(ii) provides that the amount of insurance is not to exceed the amount of the unpaid principal indebtedness secured by the insured mortgage, reduced by payments received as described in Section 9. Section 9(b) specifically provides:

> Payment in part by any person of the principal of the indebtedness, or any other obligation secured by the insured mortgage, or any voluntary partial satisfaction or release of the insured mortgage, to the extent of the payment, satisfaction or release, shall reduce the amount of insurance pro tanto. (R. Vol. 2, p. 294.)

As previously mentioned, Section 9(c) provides that payment in full terminates all liability of the Company, except as provided in Section 2(a). (R. Vol. 2, p. 295.) The amount of any liability under Section 2(a) is specifically described in Section 2(c), which states that the amount of liability after the insured's acquisition of title under Section 2(a) is reduced by the amount of all payments made. (R. Vol. 2, p. 294.)

In BOI's analysis of the Loan Policy's Conditions and Stipulations, found on pages 11-14 of BOI's Brief, BOI prematurely ends its discussion of Section 2(a) by failing to consider Section 2(c), which defines the amount of insurance available to a party who has acquired title as described in Section 2(a). Section 2(c) states that the amount of insurance is the least of three alternatives, one of which is the amount of the secured indebtedness "reduced by the amount of all payments made." (R. Vol. 2, p. 293.) Under the facts of this

case, the amount of insurance available to BOI under Section 2(c) was reduced to zero when BOI purchased the subject property at foreclosure auction with a credit bid equivalent to all amounts secured by the insured deed of trust. (R. Vol. 2, pp. 212-13.)

Read in their entirety, Sections 2, 7, and 9 of the Loan Policy's Conditions and Stipulations clearly and unambiguously provide that the amount of insurance under the Loan Policy is reduced by payments made on the secured indebtedness. Below, we discuss the fact that credit bids, such as the winning bid made by BOI at the foreclosure sale, do indeed constitute payments made on secured indebtedness. When BOI won the auction by making a full credit bid, the amount of insurance, as set forth in Sections 2, 7, and 9 of the Conditions and Stipulations, was reduced to zero. Therefore, First American is not liable to BOI under the Loan Policy.

C. The District Court did not err in finding that BOI's full credit bid was correctly applied as a payment on the secured obligation and that it satisfied in full any and all obligations to BOI with respect to the secured indebtedness.

As discussed above, payments made on indebtedness secured by an insured deed of trust clearly affect the extent of liability under a loan policy of title insurance. It is well established that a lender's credit bid at a foreclosure sale is treated as an actual payment on the underlying debt.

> It makes no sense to require the note holder to bring cash to the sale in order to pay himself. His bid, if successful, immediately reduces or eliminates the debtor's obligation. We hold that where the holder of the deed of trust note is the bidder, crediting the bid against the note is the equivalent of a cash sale.

> *Fed. Home Loan Mortg. Corp. v. Appel*, 143 Idaho 42, 45, 137 P.3d 429, 432 (2006).
>
> At a nonjudicial foreclosure sale, if the lender chooses to bid, it does so in the capacity of a purchaser. The only distinction between the lender and any other bidder is that the lender is not required to pay cash, but is entitled to make a credit bid up to the amount of the outstanding indebtedness. The purpose of this entitlement is to avoid the inefficiency of requiring the lender to tender cash which would only be immediately returned to it. *Alliance Mortg. Co. v. Rothwell*, 900 P.2d 601, 608 (Cal. 1995) (internal quotations and citations omitted).
>
> A beneficiary's credit bid, whether full or partial, is actual payment to the beneficiary to the extent of the bid, just as a cash bid and payment by a non-beneficiary would be. A beneficiary who bids high, drives out other bidders, and takes the property for the amount of its bid may not then say it was not really paid because it paid itself too much. *M&I Bank, F.S.B. v. Coughlin*, 805 F. Supp. 2d 858, 868 (D. Ariz. 2011).

The public policy behind the doctrine that credit bids constitute payments on outstanding indebtedness is clear. If credit bids were not applied as payments, the integrity of nonjudicial foreclosure sales would be undermined, as explained in the above quotations.

When a lender makes a winning credit bid at a foreclosure sale, it is the same as if the lender received a cash payment in the amount of the credit bid. *Appel*, 143 Idaho at 45, 137 P.3d at 432; *Coughlin*, 805 F. Supp. 2d at 868. In Idaho, such payments are applied as set forth in Idaho Code § 45-1507, which provides:

> **45-1507. PROCEEDS OF SALE -- DISPOSITION.** The trustee shall apply the proceeds of the trustee's sale as follows:
> (1) To the expenses of the sale, including a reasonable charge by the trustee and a reasonable attorney's fee.
> (2) To the obligation secured by the trust deed.

(3) To any persons having recorded liens subsequent to the interest of the trustee in the trust deed as their interests may appear.
(4) The surplus, if any, to the grantor of the trust deed or to his successor in interest entitled to such surplus.

Among the undisputed facts of this case is that BOI made a full credit bid at the foreclosure sale. (R. Vol. 2, pp. 212-13.) In Idaho and in other jurisdictions, credit bids constitute payments made on the secured indebtedness. *Appel*, 143 Idaho at 44, 137 P.3d at 431-32; *Rothwell*, 900 P.2d at 608; *Coughlin*, 805 F. Supp. 2d at 867-68. As a payment, BOI's winning credit bid was applied in accordance with Idaho Code § 45-1507, quoted in full above, and the amount of the outstanding indebtedness was reduced to zero.

Noticeably absent from the above analysis, and from the District Court's Memorandum Decision and Order, is any mention of, or reliance on, the Idaho anti-deficiency statute found in Idaho Code § 45-1512. On pages 14-19 of BOI's Brief, BOI argues that the Idaho anti-deficiency statute does not protect First American from liability to BOI in this case. The anti-deficiency statute protects borrowers from excessive deficiency claims asserted by lenders who credit bid at foreclosure an amount that is lower than the fair market value of the property. The statute protects borrowers by limiting the judgment to which the lender is entitled to the lesser of (i) the difference between the fair market value of the property and the amount of the indebtedness, and (ii) the difference between the amount for which the property is sold at foreclosure and the amount of the indebtedness. *See* Idaho Code § 45-1512.

As noted above, First American has not invoked the protection of the anti-deficiency statute in this case, which renders the BOI's arguments regarding the inapplicability of the anti-deficiency statute moot. However, for the sake of argument, we consider both of the cases cited by BOI in support of its assertion that BOI's credit bid is not relevant in this case. As a preliminary matter, it is important to note that neither *First Sec. Bank of Idaho, N.A. v. Gaige*, 115 Idaho 172, 765 P.2d 683 (1988), nor *Willis v. Realty Country, Inc.*, 121 Idaho 312, 824 P.2d 887 (Ct. App. 1991) (pet. rev. denied, February 28, 1992), support the notion that a lender's credit bid should not be applied as a payment on the secured indebtedness.

In *Gaige*, the court found that the Idaho anti-deficiency statute does not protect a guarantor from liability on his guaranty. *Gaige*, 115 Idaho at 173-75, 765 P.2d at 684-86. Importantly, the Court in *Gaige* did not hold that the lender's credit bid did not reduce the amount of the outstanding indebtedness. In fact, the Court's recitation of the facts of the case indicates that the lender's credit bid was applied to reduce the amount of the indebtedness and that the guarantor's obligation on his guaranty was reduced by the amount of the credit bid so applied.

> First Security was the highest bidder, bidding $300,000. After crediting the amount bid to the notes and accrued interest, a principal balance remained on the August 24, 1984, note of $351,104.37 . . . . First Security chose not to repossess or foreclose upon any remaining collateral or attempt collection of any remaining accounts receivable. No deficiency judgment was sought against the company. Instead, First Security sued Gaige and his wife on the personal guaranties for the balance owing. *Gaige*, 115 Idaho at 173, 765 P.2d at 684.

Therefore, while the Court in *Gaige* found that the guarantor was ineligible for the protection of the anti-deficiency statute, the Court also recognized the fact that credit bids made by lenders at foreclosure sales are applied to reduce the amount of the secured indebtedness. *Id.*

In *Willis*, while the foreclosure was pending, the assignor of a deed of trust allowed fixtures to be removed from the property and damaged the property, actions which amounted to unlawful conversion. *Willis*, 121 Idaho at 313-15. After taking assignment of the deed of trust but before the foreclosure sale, the assignee of the deed of trust repaired the damage to the property. *Id.* Having repaired the property, the assignee then made a full credit bid at the foreclosure sale. *Id.* The court held that the Idaho anti-deficiency statute did not prevent the assignee from recovering the cost of the repairs incurred because of the assignor's unlawful conversion of property during the pendency of the foreclosure. *Id.*

In *Willis*, the court held that the anti-deficiency statute does not preclude recovery in tort. *Id.* at 316-17. Importantly, the court did not hold that the full credit bid made at the foreclosure sale should not be applied to the secured indebtedness. The impact of the credit bid on the indebtedness secured by the deed of trust was not discussed in the court's opinion and formed no part of the court's holding. It is difficult to see how *Willis*, a case about the inapplicability of the anti-deficiency statute in the defense of a tort claim, has any bearing on

the present case in which the anti-deficiency statute has not even been raised by First American in its defense against BOI's contract claim.

On pages 14-19 of BOI's Brief, BOI cites *Gaige* and *Willis* in support of the notion that the protections of Idaho's anti-deficiency statute are not available to non-borrowers. As explained above, neither *Gaige* nor *Willis* support the notion that a lender's credit bid should not be applied to reduce outstanding indebtedness. As noted above, in Idaho and elsewhere, a lender's credit bid at a foreclosure sale is the equivalent of a cash payment and is applied to reduce the amount due on the secured indebtedness. *Appel*, 143 Idaho at 45, 137 P.3d at 432; *Rothwell*, 900 P.2d at 608; *Coughlin*, 805 F. Supp. 2d at 867-68; Idaho Code § 45-1507. BOI has not cited any authority that would contravene such doctrine.

When BOI acquired the subject property with a winning full credit bid, the proceeds of sale were applied to reduce the underlying indebtedness to zero. As discussed above, Sections 2, 7, and 9 of the Loan Policy's Conditions and Stipulations make it clear that payments made on the indebtedness secured by the insured deed of trust reduce the amount of insurance. Where, as here, payments made reduce the amount of the secured indebtedness to zero, the amount of insurance available under the Loan Policy is likewise reduced to zero. As a result, First American is not liable to BOI under the Loan Policy.

D. The District Court did not err in its application of Section 7(a)(ii) of the Loan Policy in concluding that BOI did not suffer a "loss or damage" for which First American was liable to BOI under the Loan Policy.

In pages 19-24 of BOI's Brief, BOI argues that, through a misapplication of the terms of the Loan Policy, the District Court mistakenly equated the "time of loss" with the time at which losses could be "determined" and therefore failed to recognize that BOI incurred losses and damages at various points in time long before the foreclosure sale. Even if it is assumed, for the sake of argument, that BOI incurred a loss or damage as a result of the failure to locate a four-plex on Lot 1, BOI's supposed loss or damage was mitigated to zero at the foreclosure sale when the debt secured by the insured deed of trust was paid in full.

BOI's argument that BOI incurred covered loss or damage at various times, including when a four-plex was not built on Lot 1, when BOI could not sell its loans on the secondary market, and when the borrowers defaulted on their loans, reflects a fundamental misunderstanding of the nature of the coverage afforded by the Loan Policy. A loan policy of title insurance does not guarantee that the loan will be repaid or that the property securing the debt is of a certain value.

> For a mortgagee, title insurance undertakes to indemnify against loss or damage sustained by reason of defects of title or liens upon the land, but does not guarantee either that the mortgaged premises are worth the amount of the mortgage or that the mortgage debt will be paid. *Blackhawk Prod. Credit Ass'n v. Chicago Title Ins. Co.*, 423 N.W.2d 521, 525 (Wis. 1988).

Likewise, a loan policy of title insurance does not insure against a reduction in the security property's market value or the diminution in profits potentially obtainable from resale of the property.

> [W]hile a title insurance policy insuring the interest of a real estate owner and a title insurance policy insuring the interest of a mortgagee are both contracts of indemnity, . . . , substantive differences between the insured interest of an owner and that of a mortgagee results in a significant difference in what constitutes "loss or damage" under each type of title policy. Title defects and liens directly and adversely affect the property owner because the owner is entitled to the full market value of the property and that value is immediately reduced by outstanding title defects and liens. A mortgagee's loss is measured by the extent to which the insured debt is not repaid because the value of the security property is diminished or impaired by outstanding lien encumbrances or title defects covered by the title insurance. Therefore, superior liens or title defects in claims may exist which reduce the market value of the security property (the value to the owner) yet result in no loss or damage to the insured mortgagee because the effect of the title problems does not reduce the value of the security property below the amount of an indebtedness secured or because the indebtedness is otherwise secured or paid. *CMEI, Inc. v. Am. Title Ins. Co.*, 447 So. 2d 427, 428 (Fla. Dist. Ct. App. 5th Dist. 1984).
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> Title insurance indemnifies a lender only against loss with respect to the secured indebtedness, not a diminution of profits potentially obtainable from resale of the property. *Cale v. Transamerica Title Ins.*, 275 Cal. Rptr. 107, 109 (Cal. Ct. App. 1990).

From the foregoing it can be inferred that neither the value of the mortgage nor the marketability of the mortgage on the secondary market fall within the coverage afforded by a loan policy of title insurance.

What is insured is a loss with respect to the secured indebtedness resulting from an insured defect in the security. *Falmouth Nat'l Bank v. Ticor Title Ins. Co.*, 920 F.2d 1058,

1063 (1st Cir. 1990); *Cale*, 275 Cal. Rptr. at 109; *CMEI*, 447 So. 2d at 428; *Green v. Evesham Corp.*, 430 A.2d 944, 946 (N.J. Super. Ct. App. Div. 1981). Where an insured mortgagee does not incur a loss on the secured indebtedness, there is no loss under a loan policy of title insurance.

> The law clearly states that a title insurance policy is a contract of indemnity, not one of guarantee. The insurer . . . only agrees to indemnify to the extent the insured suffers a loss caused by defects in the title . . . . [If a lender] fully recouped all amounts due them the fact that title to the property was not as represented did not cause any cognizable loss. *Karl v. Commonwealth Land Title Ins. Co.*, 24 Cal. Rptr. 2d 912, 915, 917 (Cal. Ct. App. 1993).
>
> The fee interest of an owner is immediately diminished by the presence of a [defect] since its resale value will always reflect the cost of removing the [defect]. It is otherwise with a mortgage lender whose loss cannot be measured unless the underlying debt is not repaid and the security of the mortgage proves inadequate. To say that the loss here consisted of the diminution in the security misses the point that the diminished security is now supplied by the title policy, but only to the extent that there has been a debt loss which remained unsatisfied from the proceeds of the mortgaged property. *Green*, 430 A.2d at 946.

If the secured indebtedness is paid in full despite some defect in the security, the lender has not suffered actual monetary loss or damage. *Falmouth*, 920 F.2d at 1063; *Karl*, 24 Cal. Rptr. 2d at 915-17; *Cale*, 275 Cal. Rptr. at 109; *Blackhawk*, 423 N.W.2d at 525. This is true even if the borrower defaults, the lender takes title to the property, and the debt is satisfied or deemed satisfied.

> [I]n the context of an owner's policy, the insured sustains a "loss" when the existence of a title problem reduces the fair market value of the insured interest; conversely, in the context of a loan policy, the insured generally has

> no compensable "loss," despite the existence of a title problem, unless the loan is not repaid and, as a result of the title problem, the lender receives less for the land than the amount of the debt. In other words, existing case law almost unanimously holds that an insured owner has a loss as soon as its legal rights in the property are diminished, without an out-of-pocket cost; but a lender has no loss until it sustains an out-of-pocket loss. This distinction is expressly made in the cases of *Green v. Evesham Corp.*, *Blackhawk Production Credit Ass'n v. Chicago Title Ins. Co.*, *CMEI, Inc. v. American Title Ins. Co.*

Joyce Palomar, *Title Ins. Law* § 6:20 (2011) (emphasis added) (citations omitted).

As noted above, BOI recouped all amounts due to BOI through application of the full credit bid at the foreclosure sale. BOI took title to the property and the debt was satisfied. Therefore, the alleged defect in title in this case, namely that one of the multi-family residences was not located on Lot 1 as set forth in Endorsement 116, did not result in any loss or damage within the indemnity afforded by the Loan Policy. The Loan Policy's "EXCLUSIONS FROM COVERAGE" expressly state that defects that do not result in a loss to the claimant are excluded from coverage.

> The following matters are expressly excluded from the coverage of this policy and the Company will not pay loss or damage, costs, attorneys' fees or expenses which arise by reason of:
> . . . 3. Defects, liens, encumbrances, adverse claims or other matters:
> . . . (c) resulting in no loss or damage to the insured claimant. (R. Vol. 2, p. 293.)

As noted above, the overwhelming weight of existing case law confirms that there are two indispensable prerequisites to recovery under a loan policy of title insurance: (i) the existence of an insured defect, and (ii) a loan loss resulting from the insured defect. If either

prerequisite is missing, there is no loss or damage within the indemnity provided by the loan policy of title insurance. It is therefore important to note, with respect to the matters complained of on pages 21-24 of BOI's Brief, such as diminution in value of the collateral, inability to market the insured deed of trust on the secondary market, default by the borrowers, necessity of foreclosure, and so forth, that none of such matters are defects insured under the Loan Policy. However, even if it is assumed, for the purposes of argument, that any one or more of such matters constituted an insured defect, BOI would not now be entitled to recover from First American under the Loan Policy because such alleged defects did not result in a loan loss as explained below.

On pages 19-20 of BOI's Brief, BOI makes much of the fact that there is a difference between when a loss occurs and when the amount of such loss can actually be determined. BOI alleges that its loss occurred at various points in time before the foreclosure sale, but acknowledges that determining the amount of such loss "may not have been possible until after it attempted to mitigate its loss by finally selling the property to a third party in November of 2010." (Appellant's Br., p. 20.) BOI apparently recognizes that its supposed losses were mitigated, but fails to acknowledge the important event at which such mitigation took place — the foreclosure sale.

At the foreclosure sale, a purchaser, BOI, purchased the property for "all amounts due and owning" under the insured deed of trust as of the date of the foreclosure sale. As noted

above, by law, BOI's credit bid was equivalent to cash. When the bid was applied, the indebtedness secured by the insured deed of trust was satisfied in full. Therefore, whatever losses BOI supposedly incurred prior to the foreclosure sale were mitigated in full at the foreclosure sale. That being the case, even if BOI at one time sustained a loss covered by the Loan Policy, such loss has been effectively mitigated to zero, and First American is not liable to BOI under the Loan Policy.

E. First American is entitled to attorneys fees and costs on appeal.

Pursuant to Rules 40 and 41 of the Idaho Appellate Rules, First American request its attorneys fees and costs on appeal. In support of First American's request for attorneys fees on appeal, First American relies on Idaho Code § 12-123 and Idaho Code § 41-1839(4), which are the Idaho Code sections that provide for awarding attorney fees in disputes arising out of insurance policies. *Mortensen v. Stewart Title Guar. Co.*, 149 Idaho 437, 447, 235 P.3d 387, 397 (2010). Under Idaho Code § 12-123 and Idaho Code § 41-1839(4), attorney fees may also be awarded, if the appeal was "brought, pursued or defended frivolously, unreasonably or without foundation." In *Mortensen*, the Court found that an award of attorney fees in favor of the defendant/respondent title company was appropriate where the plaintiff/appellant was "merely asking [the] Court to second-guess the district court's ruling despite unambiguous controlling language in the insurance policy." *Mortensen*, 149 Idaho at 448, 235 P.3d at 398.

In BOI's Brief, BOI has not introduced any arguments not already considered and disposed of by the District Court and has not cited any authority not already considered by the District Court. BOI is therefore asking the Court to review the same arguments and authority considered by the District Court and reach a different conclusion. Clearly, then, BOI is merely inviting the Court to second-guess the findings of the District Court despite unambiguous controlling language in the Loan Policy.

In addition, it should be noted that BOI's entire argument hinges on the Court ignoring BOI's full credit bid at the foreclosure sale. Not applying BOI's full credit bid at the foreclosure sale to the subject indebtedness would defy clear and longstanding principles of law recognized in Idaho and elsewhere. BOI presents no authority or persuasive argument to contradict such principles of law. Instead, BOI appears to argue that because the anti-deficiency statute grew out of a common law rule called the "full credit bid rule", and because the anti-deficiency statute is inapplicable in this case, then BOI's full credit bid must not be relevant in this case. This argument is lacking in both logic and persuasive merit. Therefore, First American respectfully urges the Court to find that BOI's appeal is brought frivolously, unreasonably, or without foundation and, as a result, award attorneys fees and costs on appeal to First American.

V. CONCLUSION

Based on the foregoing, First American respectfully requests that this Court find the following:

(1) the District Court's grant of Summary Judgment in favor of First American and Judgment of Dismissal dismissing BOI's Complaint were proper and should be upheld;

(2) the District Court's denial of BOI's Motion for Partial Summary Judgment was proper and should not be reversed; and

(3) First American is entitled to attorneys fees and costs on appeal against BOI.

RESPECTFULLY SUBMITTED this 30th day of October, 2013.

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CERTIFICATE OF SERVICE

I hereby certify that I served a copy of the following described pleading or document on the individual listed below in the manner indicated on this 30th day of October, 2013.

DOCUMENT SERVED: **RESPONDENT'S BRIEF**

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