

2001

Guardian Title Company of Utah v. Stacey Mitchell; Tebbs & Smith P.C.; Douglas L. Rex; Stagg & Associates : Reply Brief

Utah Supreme Court

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GUARDIAN TITLE COMPANY OF
UTAH, a corporation,

VS.

Defendants/Appellees.

Supreme Court No. 20010283-SC
Third District Court No. 990904087

Priority No. 15

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IN THE UTAH SUPREME COURT

GUARDIAN TITLE COMPANY OF
UTAH, a corporation,

Plaintiff/Appellant,

vs.

STACEY MITCHELL, formerly known as
STACEY HOWELL; TEBBS & SMITH
P.C., a corporation; DOUGLAS L. REX;
STAGG & ASSOCIATES, a corporation,

Defendants/Appellees.

APPELLANT'S REPLY BRIEF

Supreme Court No. 20010283-SC
Third District Court No. 990904087

Priority No. 15

**Appeal from the Third District Court
In and For Salt Lake County, State of Utah
Honorable Anne M. Stirba, District Court Judge**

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ARGUMENT

In responding to Guardian Title Company of Utah's (Guardian) appeal, Tebbs & Smith, P.C. (Tebbs), has essentially made three arguments in support of the trial court's decision: (1) Guardian's Complaint alleges only tort claims and not contract claims; (2) Tebbs was entitled to summary judgment because Guardian allegedly caused some of its own damages; and (3) all of Guardian's claims are barred because Tebbs' employee, Stacey Mitchell, was acting outside of the scope of her employment. Each of these arguments will be addressed in turn.

I. GUARDIAN ALLEGED CONTRACT CLAIMS

Tebbs does not dispute that there was a contract between Tebbs and Guardian nor does it apparently dispute that a cause of action for breach of contract for professional services exists in Utah. Rather, it asserts that Guardian has not alleged a contract cause of action. It proffers two reasons to support its premise. First it contends there can be no cause of action in contract because there was no explicit "provision that a Tebbs' employee would not write checks to herself or that Tebbs would indemnify Guardian for the criminal acts of an employee." (Brief of Appellee 6.) Secondly, it asserts that Guardian's claims that Tebbs breached implied covenants are in actuality disguised tort claims.

It is true that there is no record evidence that Tebbs and Guardian expressly agreed that Tebbs' employees would not write checks to themselves. However, as discussed at length in the Appellant's Brief, Guardian has alleged that Tebbs entered into a verbal

agreement with Guardian to provide and perform professional public accounting services, including preparation of checks made payable to Guardian's employees and drawn on Guardian's bank checking account (Payroll Account) and the performance of account statement reconciliation services with regard to the Payroll Account. These facts are undisputed and admitted. (*See* R. at 3, 37, 182-83, 210.) A necessary implication of these contractual terms is that Tebbs was to provide those services for which the parties contracted. Thus, when Tebbs agreed that it would prepare checks made payable to Guardian's employees, the agreement contemplated that Tebbs would perform those services and write such checks exclusively to Guardian employees and not to any other person. In writing checks to a Tebbs employee, Tebbs has breached the express terms of the contract.

Even had Tebbs' actions not violated an express term of the contract, they certainly violated implied terms. In its brief, Tebbs argues, as it did below, that any claim for breach of an implied or constructive covenant, particularly the covenant of good faith and fair dealing, is a claim for a breach of a duty imposed by law. (*See* Brief of Appellee 8.) The primary problem with this argument is that the argument misstates the law clearly established by this Court.

The case law on this point is very clear. If a wrongdoer's obligation "to refrain from" doing a particular act "depend[s] upon any express or **implied** promise arising from the . . . contract," a breach of that obligation gives rise to a cause of action in contract. *Peterson v. Browning*, 832 P.2d 1280, 1284 (Utah 1992) (emphasis added). If, however, the

wrongdoer's obligation to refrain from doing a particular act arises from "a legal duty independently imposed as a result of what the [wrongdoer] undertook to do with relation to the plaintiff's interest," a breach of that obligation gives rise to a cause of action in tort. *DCR Inc. v. Peak Alarm Co.*, 663 P.2d 433, 437 (Utah 1983) (quoting Carl S. Hawkins, *Retaining Traditional Tort Liability in the Nonmedical Professions*, 1981 B.Y.U.L.Rev. 33, 36). Accordingly, if the breach is of an implied promise arising from the contract, it is a breach of a contractual duty.

Additionally, this Court has unambiguously held that a breach of the covenant of good faith and fair dealing "is read into contracts in order to protect the express covenants or promises of the contract, not to protect some general public policy interest not directly tied to the contract's purpose." *Peterson v. Browning*, 832 P.2d 1280, 1284 (Utah 1992) (quoting *Foley v. Interactive Data Corp.*, 765 P.2d 373, 394 (Cal. 1988)); *see also Beck v. Farmers Ins. Exchange*, 701 P.2d 795, 800 (Utah 1985). Hence, this Court has expressly concluded that "a violation of th[e] duty [of good faith and fair dealing] gives rise to a claim for breach of contract." *Beck*, 701 P.2d at 798 (emphasis added); *see also St. Benedict's Dev. Co v. St. Benedict's Hospital*, 811 P.2d 194, 200 (Utah 1991).¹

¹ Tebbs claims that Guardian did not properly plead a breach of the covenant of good faith and fair dealing. (See Brief of Appellee 14.) Of course, the only requirements of a complaint are that it contain a "short plain statement . . . showing that the pleader is entitled to relief" and "a demand for judgment for the relief." Utah R. Civ. P. 8(a). In fact, a complaint is required only to " . . . give the opposing party fair notice of the nature and basis or grounds of the claim and a general indication of the type of litigation involved." It may also frequently be found stated in these cases

Despite these clear holdings, with nothing more than highly selective quotations from two cases, Tebbs conjures a new legal theory from its cauldron of equivocation. Citing the “growing out of” language of *DCR Inc. v. Peak Alarm Co.*, 663 P.2d 433, 435 (Utah 1983), and the inapposite holding regarding the public policy exception to the employment at-will doctrine in the *Peterson* case, (see Brief of Appellee 8-9), Tebbs proposes a new and unsupportable theory: if a court has, as a matter of law, recognized an implied duty in a contract, a breach of that duty necessarily gives rise to a claim in tort. As explained fully in the Appellant’s Brief and briefly above, the rule in Utah is expressly contrary to any such theory.

Finally, without any analysis, Tebbs reiterates its argument that Guardian’s Complaint actually is a disguised tort claim. (See Brief of Appellee 11.) However, this argument demonstrates Tebbs misunderstanding of the Complaint and the facts. Guardian has alleged that (1) when Tebbs failed to pay only Guardian’s employees, it failed to fulfill the terms of its contract with Guardian, and (2) when Tebbs failed to disclose that it had written and paid

that a complaint does not fail to state a claim unless “. . . it appears to a certainty that the plaintiff would be entitled to no relief under any state of facts which could be proved in support of the claim.”

Blackham v. Snelgrove, 3 Utah 2d 157, 280 P.2d 453, 455 (1955). Even a cursory review of the Complaint makes clear that Guardian has alleged the facts necessary to raise the claim. Specifically, the Complaint states that Tebbs “expressly and implicitly covenanted and agreed that it would charge and commission the performance of . . . services and duties by such of its employees as would perform the same accurately, properly, competently and with honesty and fidelity.” (R. at 3, ¶ 11.) This reference to an implied covenant to perform “properly” and “with honesty and fidelity” is certainly sufficient to plead a claim for breach of the covenant of good faith and fair dealing.

unauthorized checks, it failed to fulfill the terms of its contract with Guardian. Guardian does not allege that Tebbs' level of practice fell below a standard of care because it gave Guardian bad accounting advice or it failed to supervise its employees or it failed to follow certain accounting standards. Guardian alleges only that it had a contract with Tebbs to perform certain acts, and Tebbs did not perform those acts or did not perform those acts in good faith. *See, e.g., Clark v. Milam*, 847 F. Supp. 409, 420-21 (S.D. W. Va. 1994). Such a claim is a breach of contract claim. *See* Dan L. Goldwasser & M. Thomas Arnold, *Accountants' Liability* § 3.2, at 3-11, 3-13 (1996) ("Accountants may be held liable for breach of contract where they fail to perform a specific service which they are committed by contract to perform;" and "an accountant may be held liable for failing to perform contractual obligations in a satisfactory manner."); *cf.* Ronald E. Mallen & Jeffrey M. Smith, *Legal Malpractice* § 8.8 (1996) ("The client may instruct the attorney to perform certain tasks or to act in a specified manner. The undertaking then becomes contractual in nature, and the failure to perform can result in virtual strict liability for any resulting injury.")

II. THE QUESTION OF CAUSATION IS A DISPUTED ISSUE OF FACT

Tebbs next argues that "the trial court concluded, as a matter of law, . . . that Guardian could not establish the requisite causation." (Brief of Appellee 6.) In support of this theory, Tebbs, citing *Steiner Corp. v. Johnson & Higgins*, 2000 UT 21, 996 P.2d 531, and Utah Code Ann. § 78-27-38, argues that to determine whether Guardian can prove the requisite "thread of causation" requiring recovery from Tebbs, "the Court should take into consideration

Guardian's own role in causing the loss." (Brief of Appellee 10-12.) Each of the citations relied upon by Tebbs refers to apportionment of fault in a comparative negligence case. Obviously then, although the argument Tebbs has made is couched as a "causation" argument, it is really a mitigation/comparative negligence argument.

The most obvious flaw in this argument is that, even if the trial court had concluded that Tebbs was entitled to summary judgment based upon its causation argument, such a conclusion would be incorrect as a matter of law.² What Tebbs fails to recognize is that whether the plaintiff failed to mitigate is a factual issue which Tebbs bears "the burden of proving." *John Call Engineering, Inc. v. Manti City Corp.*, 795 P.2d 678, 680 (Utah Ct. App. 1990). Viewing all evidence in a light most favorable to Guardian, there is at least a factual issue as to whether Guardian was required to mitigate, and, if so, how much the damages should be reduced. Further, Tebbs cites no authority that given the facts at issue, Tebbs would entitle it to summary judgment.

The facts are simple. Guardian hired Tebbs to do its payroll accounting work, including reconciliation and preparing and filing the taxes. (*See* R. at 388.) Guardian paid Tebbs to do this work. Tebbs had all of Guardian's relevant bank statements, cash disbursement, and bank draft journals. (*See id.* at 385, 392-93.) Because of the contract, Tebbs had the best and only realistic opportunity to discover its breach. However, even

² Another problem with the argument is that the trial court never explicitly ruled that it was granting summary judgment on the basis of the causation argument. (*See* R. at 464, 33-34.)

Tebbs did not discover Mitchell's activity. (*See id.* at 386.) If Tebbs, who had all of the records and relevant documents in its possession and who supervised Mitchell's work, did not discover the activity, it strains common sense to urge that Guardian should have, as a matter of law, discovered it sooner.

Tebbs has also implicitly argued that Guardian's claim is barred by the doctrine of comparative negligence. Comparative negligence applies only to a negligence claim. *See, e.g., Steiner Corp. v. Johnson & Higgins*, 2000 UT 21, ¶4, 996 P.2d 531. In this case, Guardian has not urged a negligence claim but a breach of contract claim. Even if this were a negligence cause of action, however, the question of whether an entity is comparatively negligent is also a question of fact for which Tebbs would bear the burden of proof. *See Lamkin v. Lynch*, 600 P.2d 530, 531 (Utah 1979). As discussed above, the trial court did not, and, viewing the evidence in a light most favorable to Guardian, could not grant summary judgment on the evidence in this case. Genuine issues of material fact exist regarding the actions of Guardian. Again, summary judgment was inappropriately granted.³

³ Tebbs has cited law relating to a bank customer's duty to examine statements and checks for forgery in support of its position that the court can examine the reasonableness of a party's action in preventing fraud. (*See* Brief of Appellee 18-19.) There are several problems with this argument.

First, none of the law cited by Tebbs states that the mere presentation alone of evidence of some negligence by a party who was the victim of a fraudulent act entitles the party presenting the evidence to summary judgment. As described above, there is a substantial factual dispute as to whether Guardian's conduct contributed to its damages, and, even if it did, how much of its conduct could be attributed to its damages.

Second, these authorities are factually inapposite to this case. The law cited by Tebbs relates to a person's obligation to discover a *bank's* payment to a *third-party* who had

III. THE TRIAL COURT INCORRECTLY CONCLUDED THAT THE TORT DOCTRINE THAT AN EMPLOYER IS NOT LIABLE IN RESPONDEAT SUPERIOR FOR THE ILLEGAL ACT OF AN EMPLOYEE IS AN ABSOLUTE DEFENSE TO A BREACH OF CONTRACT ACTION AGAINST THE EMPLOYER

Finally, Tebbs argues that it is entitled to summary judgment because, although it agrees “that principals are bound by the acts of their agents,” “illegal acts by an employee, for the sole benefit and purpose of the employee and not the employer, . . . are not within the actual or apparent scope of authority.” (Brief of Appellee 20.) Accordingly, Tebbs argues, it could not “be liable for such illegal acts.” (*Id.*)

The trial court’s conclusion and Tebbs arguments are based upon an incorrect understanding of the law and Guardian’s arguments. Guardian’s sole contention is that Tebbs breached the terms of its contract with Guardian when it failed to pay only Guardian employees and when it failed to reconcile bank statements. Thus, the question before the trial court was fairly straightforward: Did Tebbs breach its contract by failing to pay only Guardian employees and failing to reconcile bank statements? As discussed fully in the Appellant’s Brief, the resolution of that question does not depend on the reason for the

negotiated a check with an unauthorized signature or had negotiated an altered check. If the bank’s employee had improperly debited a customer’s account or the bank paid money in violation of its contract with the depositor, it would have liability.

A bank is under the duty to disburse funds in accordance with the directions of its depositor. It is implicit in the Uniform Commercial Code that a bank may not charge its customer for any item not properly payable against the customer’s account.

10 Am. Jur.2d, *Banks & Financial Institutions* § 890 (1997) (footnotes omitted).

breach, only that a breach occurred. Further, the tort doctrine of respondeat superior does not apply in a contract claim.

CONCLUSION

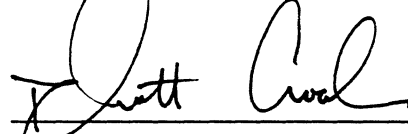
Tebbs' position, reduced to its essential core, is that although Tebbs hired an employee that wrongfully converted money from its client, Tebbs has no liability for that conduct even though it thereby breached its contract with the client. Such a result is obviously contrary to the law and common sense.

The trial court incorrectly concluded that Utah law requires that any action brought against a professional accounting firm must be treated in all respects as a negligence cause of action. The trial court also incorrectly concluded that an action for the breach of an implied covenant of good faith and fair dealing is one sounding in tort. Moreover, the trial court incorrectly concluded that Guardian attempted to use the covenant of good faith and fair dealing to add new, independent terms to the contract. Finally, the trial court incorrectly concluded that Tebbs was not liable in breach of contract for breaches of contract caused by an illegal act committed by an employee.

Accordingly, Guardian respectfully requests this Court to reverse the order granting summary judgment to Tebbs and remand the case for trial.

DATED this 17th day of September, 2001.

NIELSEN & SENIOR

Handwritten signatures of Gary A. Weston and D. Scott Crook in cursive script.

Gary A. Weston

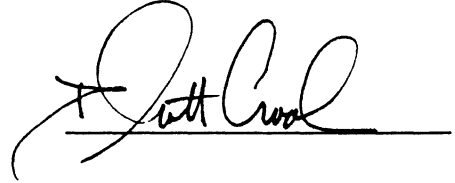
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 18th day of September, 2001, I did cause two true and correct copies of the foregoing **APPELLANT'S REPLY BRIEF** to be mailed, United States mails, postage prepaid, addressed to the following:

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A handwritten signature in black ink, appearing to read "J. T. Hall", is written over a horizontal line.