

2004

VESTIN MORTGAGE, INC., Appellant and Petitioner and Plaintiff, vs. FIRST AMERICAN TITLE INSURANCE COMPANY, Appellee and Respondent and Defendant : Reply Brief

Utah Supreme Court

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IN THE UTAH SUPREME COURT

VESTIN MORTGAGE, INC.,

Appellant/Petitioner and Plaintiff,

vs.

FIRST AMERICAN TITLE
INSURANCE COMPANY,

Appellee/Respondent and Defendant.

No. 20041132-SC

APPELLANT/PETITIONER'S REPLY BRIEF

On Writ of Certiorari to the Utah Court of Appeals, Case No. 20030941-CA

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ORAL ARGUMENT REQUESTED

UTAH *Supreme Court*

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ARGUMENT

I. FIRST AMERICAN’S PRINCIPAL ARGUMENTS FAIL.

Ignoring standards of review and arguing facts, First American advances four main points, repeating them *ad nauseam* in its cram-spaced brief:

- A. The Assessment alone caused Vestin’s injury;
- B. The Policies pre-dated the injury;
- C. The authorities all support First American’s position; and
- D. The granting of Vestin’s certiorari petition limits the arguments.

Vestin responds to each in turn. None is accurate.

A. Injury and Causation Are Issues of Fact.

A 12(b)(6) motion is not well taken if any set of facts could support the cause of action. *Christensen v. Lelis Automatic Transmission Serv.*, 467 P.2d 605, 607 (Utah 1970). Reviewing this threshold motion, the Court cannot simply accept First American’s *ipse dixit* assertions of Vestin’s injury and its cause based on a narrow reading of the Complaint. The Court must presume Vestin’s facts are true and view them liberally in their most favorable light. *See St. Benedict’s Dev. Co. v. St. Benedict’s Hosp.*, 811 P.2d 194, 196 (Utah 1991) (dismissal); *Farmers New World Life Ins. Co. v. Bountiful City*, 803 P.2d 1241, 1243 (Utah 1990) (summary judgment).

Given this standard, Vestin has viable grounds for proceeding. (R. 1-10; Opening Br.; *infra*.) Initial pleadings need not set forth all the particulars of a party’s legal position. “[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.” *Christensen*, 467 P.2d at 607. Vestin did this: “Despite demand, First

American has refused to pay the claim of Vestin owing under the Policies of Title Insurance, which constitutes a breach of the Policy by First American. . . . As a result of the breach of the Policy by First American, Vestin and its assignees have been damaged in an amount of . . . not less than \$2,241,348.70.” (R. 10, Aplt. App. 1.) These allegations from Vestin’s complaint are more than sufficient pleading. *See Gill v. Timm*, 720 P.2d 1352, 1353 (Utah 1986).

Ultimately, the Utah courts provide recovery for damages suffered when an insurer fails to disclose a title defect. *Espinoza v. Safeco Title Ins. Co.*, 598 P.2d 346, 347 (Utah 1979). Related injury and causation are issues of fact “triable somewhere else than on summary judgment.” *Russell v. Hooper Irrigation Co.*, 435 P.2d 294, 296 (Utah 1967); *King v. Searle Pharma*, 832 P.2d 858, 864 (Utah 1992). First American played a role in causing Vestin damage; the fact-finder can determine the extent.

Vestin does not argue the sole cause of injury was the post-Policy lien – that is First American’s rhetoric. (Aplee. Br. at 19, *passim*.) That the due-on-sale provision played a part in the sale failing does not mean it was the sole or even the principal cause of the damage alleged in the Complaint. (Aplee. Br. at 27.) “[C]ausation issues are factual issues that generally cannot be resolved as a matter of law. We refuse to prevent these issues from going to the jury when, as here, there is any evidence upon which a reasonable jury could infer causation.” *Nay v. General Motors Corp., GMC Truck Div.*, 850 P.2d 1260, 1264 (Utah 1993) (citations omitted). Certainly a court should not summarily dismiss based on *First American’s* argumentative characterizations. *See, e.g.*,

Farmers New World Life Ins. Co. v. Bountiful City, 803 P.2d 1241, 1243 (Utah 1990)

(facts and inferences viewed in light most favorable to *non-moving* party).

This Court accords no deference to the ruling below. *Brigham Young Univ. v. Tremco Consultants, Inc.*, 2005 UT 19, ¶ 13, 110 P.3d 678. If there is any doubt about the propriety of a dismissal motion, it should not be granted. *King v. Searle Pharma.*, 832 P.2d 858, 864 (Utah 1992). First American's technical assertions regarding divisible injury and cause transpose the appropriate analysis. Reversal is required here.

B. The SID Documents Pre-Date Policy No. 3192 and the Endorsements.

Vestin gives an accurate timeline of events in its opening brief. (Opening Br. at 7-8, 10-11.) The Eagle Mountain SID Documents pre-date Policy No. 3192 and both Endorsements. The treatise relied on by both parties holds the endorsement date controls liability for events between the date of policy and the endorsement:

When, however, the insurer expressly consents to a general endorsement of a policy, **the date of the endorsement controls the liability of the insurer. Defects in title falling within the scope of the endorsement and arising between the original date of the policy and the date of the endorsement are covered by the policy thereafter.** The insurer has the duty to search the title for defects discoverable on the land records filed between those dates before issuing the endorsement. . . . As to the subject of any endorsement for some special coverage, **the date of the endorsement should control the date of issuance of the policy as to a claim made under the special coverage.** . . .

Barlow Burke, *Law of Title Insurance* § 3.03, at 3-51 (3rd ed. 2004) (emphasis added).

Coverage thus exists for Vestin under both Policies.

The Form 104 Endorsements say they do not “extend” the “effective date” of the Policies or of any other endorsement. (R. 24, 44.) This means adopting these

Endorsements does not “lengthen,” “prolong,” or “add to” the time the Policies are in effect. *Merriam-Webster’s Collegiate Dictionary* 411 (10th ed. 1999). It does *not* mean the original policy date measures liability for events occurring before the endorsement date. (Aplee. Br. at 15-16.) The undefined “effective date” is not synonymous with the defined “Date of Policy” start date. (R. 80, 84, 100, 104); *see Hansen v. Wilkinson*, 658 P.2d 1216, 1217 (Utah 1983) (“[O]rdinarily when people say one thing they do not mean something else.”). Reference to “extending” endorsements would otherwise be nonsensical. *See Okelberry v. W. Daniels Land Ass’n*, 2005 UT App 327, ¶ 24 (contract will not be construed to reach absurd result). If there is any question, this is at least ambiguous and therefore factual. *See infra* part III.B.

The record is silent on the precise dates First American issued the Endorsements. Discovery will establish this and other facts crucial to the parties’ respective positions. The Court should not dismiss beforehand.

C. The Record In This Case Requires Reversal.

First American overstates the weight and effect of the authorities. They neither uniformly nor unanimously support First American. This Court judges cases on their individual merits; it does not blindly follow string cites.

The coverage in *Edwards v. St. Paul Title Ins. Co.*, 563 P.2d 979 (Colo. App. 1977), **specifically excluded** “Taxes and assessments not yet due or payable and Special Assessments not yet certified to the Treasurer’s office.” *Id.* at 980. Little wonder, then, the intermediate Colorado court found no liability for “the mere existence of the district and the prospect of taxes in the future.” *Id.* There is no similar exclusion in this case.

Moreover, Eagle Mountain did more than simply create a special district as in *Edwards*: it actually decided to assess, resolved objections, adopted and recorded an ordinance, and notified the public of impending assessments, all before the Endorsement clauses and the second Policy went into effect. (R. 121-123, 127-143.)

Strass v. District-Realty Title Ins. Corp., 358 A.2d 251 (Md. Sp. App. 1976), held pre-lien assessment decisions were “encumbrances” if “inevitable.” *Id.* at 258. In the instant case, the Notice of Intention said improvements “**shall be paid by special assessments to be levied against the property.**” (R. 121, emphasis added.) In a section titled “**Levy of Assessments**” the Notice said, “**The assessments shall be levied according to the benefits to be derived by each property within the District.**” (R. 122, emphasis added.) The Assessment was in fact levied directly. (R. 335-345.) Adopting *Strass*’s approach and viewing the evidence favorably to Vestin, a jury could find the Eagle Mountain Assessment was inevitable.

Strass labored to distinguish *Manor Real Estate Co. v. Jos. M. Zamoiski Co.*, 246 A.2d 240 (Md. 1968). In *Manor*, Maryland’s highest court properly rejected the very argument First American makes, that coverage is invoked only if an “encumbrance” has first ripened into a “lien”:

Manor further declares that “if the future charges are encumbrances, it is only because they are first liens,” which seems to us to be another way of saying that unless an encumbrance is also a lien it cannot be an encumbrance. But there are many encumbrances, such as easements, that are not liens. As Judge Carter put it “a lien is always an encumbrance, but an encumbrance need not necessarily be a lien.”

...

It has been said that the mere fact that property becomes liable for the payment of a benefit charge for municipal improvements may constitute an

encumbrance even before the amount thereof has been ascertained. 4 H. Tiffany, *The Law of Real Property* § 1003, n.3 at 135 (3d ed. 1939). It has been said also that present liability to an eventual lien may be sufficient to establish an encumbrance. 20 Am.Jur.2d, *Covenants* § 87 (1965).

Id. at 242-43, 245. The *Manor* court cited approvingly an earlier decision from Massachusetts' highest court finding a pre-lien encumbrance when "[t]here was a liability which was sure to become absolute and enforceable against the land as soon as the work was completed and the expense ascertained. *This was an incumbrance from which the plaintiffs were entitled to be protected under the covenant.*" *Id.* at 247 (quoting *Cotting v. Commonwealth*, 91 N.E. 900, 902 (Mass. 1910)) (emphasis modified). These cases, like *Strass*, confirm liability is soundly based on failure to disclose assured forthcoming assessments.

Other cases First American cites, however, contradict these cases, confuse encumbrances with liens – as so many cases do – and reach unsustainable holdings. (Aplee. Br. at 31 n.19.) *Butcher v. Burton Abstract & Title Co.*, 216 N.W.2d 434, 436 (Mich. App. 1974), for example, acknowledged "the broadest definition of the word 'encumbrance' might include prospective charges." *Butcher* nevertheless held a special assessment must be a "lien" before it is an "encumbrance." This same court subsequently found statutory use of the word "encumbrance" to be ambiguous given post-*Butcher* cases applying its broader meaning. See *Lakes of the N. Ass'n v. Twiga P'ship*, 614 N.W.2d 682, 685-86 (Mich. App. 2000).

Cummins v. United States Life Ins. Co., 357 N.E.2d 975, 976 (N.Y. 1976), is one of a string of New York cases perpetuating the error that "[e]ncumbrance" is

synonymous with ‘lien’” *Invest Enters. v. TRW Title Ins., Inc.*, 573 N.Y.S.2d 239, 242 (N.Y. Sup. Ct. 1991) (discussing *Cummins*); see *Metropolitan Life Ins. Co. v. Union Trust Co.*, 27 N.E. 2d 225, 227 (N.Y. 1940) (same); *Mayers v. Van Schaick*, 197 N.E. 296 (N.Y. 1935) (same). The oft-cited foundational decision in *Mayers v. Van Schaick* held an assessment was not an encumbrance or defect *even though it had already been assessed*. 197 N.E. at 296 (1935). Even First American does not argue as much. These cases are not only demonstrably wrong, they contradict *Strass*’s holding. Moreover, they allow First American to suggest there are numerous supporting authorities when in fact the vast majority reflect the decisions of only one state. (Aplee. Br. at 31 n.19); see Burke § 3.05[A], at 3-76.1 (noting New York provides much of the case law). In the only soundly reasoned opinion among the incestuous New York cases, the *Mayers* dissent pointed out: “It is not necessary that the objection or requirement should amount to a *lien*, but what is stated in the policy of title insurance is that any *defect* is insured against except those noted.” 197 N.E. at 298 (emphasis added).¹

Medeiros v. Guardian Title & Guar. Agency, Inc., 387 N.E.2d 644 (Ohio App. 1978), construed a contract requiring the seller to pay for any special assessments “certified” with the county auditor at the time title transferred. *Id.* at 645. The court easily held a subsequent special assessment was not “certified” by the policy date. *Id.* at

¹ Only “liens” were covered in *Cole v. Home Title Guar. Co.*, 29 A.D.2d 552 (N.Y. App. Div. 1967), *aff’d*, 244 N.E.2d 470 (N.Y. 1968). This unremarkable holding was correct on its facts. First American puffs its authorities by citing this inapposite New York case twice. (Aplee. Br. at 31 n.19.)

647. Despite First American’s aspersions, cases construing limitations in conveyances are analogous to title insurance cases – and are included in First American’s citations.

Lastly, First American inexplicably cites *Burman v. Richmond Homes, Ltd.*, 821 P.2d 913, 921 (Colo. App. 1991) – a case that very much supports Vestin. *Burman* relied specifically on an affidavit identifying Colorado’s custom and practice for disclosing special improvement districts. *Id.* at 921. Vestin has submitted just such (unrebutted) evidence showing the governing custom and practice here – which is to disclose special improvement districts. (R. 355-361, 396-397.) Furthermore, the record in *Burman* showed the defendant *did* disclose the district in the title commitments and policies. 821 P.2d at 913. Vestin itself could not have picked a better case.

Notably, most if not all of First American’s cases enforce assessment statutes. *A priori*, this Court should enforce Utah’s assessment statute, which requires recording of pre-lien SID assessment documents that create an “encumbrance” on title. Utah Code Ann. § 17A-3-307(6).

The treatises add little, if anything, to the weight of the authorities. Burke, Palomar, Couch, and AmJur cite and then discuss the reasoning from the same cases cited by First American. Virtually all the major points First American makes about the state of the law are derived in this way. (Aplee. Br. at 23, 25, 31, 46-47.) This no more demonstrates unanimous opinion among the jurisdictions than the cases themselves. These same authorities admit the question here is a factual one. *See, e.g.*, 43 Am. Jur. 2d *Insurance* § 526 (2002) (“What constitutes a defect in title, or a lien or encumbrance thereon, depends upon the facts of the individual case.”); *Couch on Insurance* 3d

§ 159:38 (1998) (when assessment may be considered to exist “is generally a factual question requiring analysis of all laws, ordinances, and regulations concerning the authority to levy the specific assessment that is in dispute”).

First American tries to distinguish *Bel-Air Motel Corp. v. Title Ins. Corp.*, 444 A.2d 1119 (N.J. Sup. Ct. 1981), on grounds the improvements had been completed. (Aplee. Br. at 33 n.20.) The court held, however, “the local improvement ordinance itself created a title defect” because of state title search legislation. 444 A.2d at 1122. Like *Bel-Air*, *Lafferty v. Milligan*, 30 A. 1030 (Pa. 1895), was held to be a sufficiently definite encumbrance *because an existing statute made the improvement an encumbrance* even though a lien had not yet attached. *See id.* at 1031. These cases are both analogous here, where the Utah Legislature has required recording of the local improvement ordinance as an *encumbrance* in the county real property records where title insurers search. Utah Code Ann. § 17A-3-307(6).

Bel-Air’s analysis is cogent, extensive, and worthy of review and emulation, both on the coverage and recorded police power exception issues. *See infra* part II. No decision contradicting *Bel-Air* has come down from any high court within the last 25 years. This Court has a virtual tabula rasa on which to decide a leading case to guide other jurisdictions in this century. The Court should take advantage of supervening scholarship that has properly defined defects and encumbrances as different than liens. Moreover, the Court should apply *Utah*’s statutory scheme. The Court should not mindlessly regurgitate holdings such as those First American cites, especially those based on faulty premises exposed by actually reading the cases.

Vestin’s case law stands for the propositions cited and is the better reasoned. To quote *Leh v. Burke* and the cases it relies on:

Encumbrance is a broad term and has been defined as “every right or interest in the land which may subsist in third persons to the diminution of the value of the land, but consistent with the passing of the fee by the conveyance.” *Ritter v. Hill*, 282 Pa. 115, 118, 127 A. 455, 456 (1925), *quoting from Lafferty v. Milligan*, 165 Pa. 534, 537, 30 A. 1030, 1031 (1895). It may be either “one which affects the physical condition or use of the property, or one which affects the title of the property.” *Ziskind v. Bruce Lee Corp.*, 224 Pa.Super. 518, 521, 307 A.2d 377, 379 (1973). Examples of encumbrances have been said to include assessable benefits which have not yet become liens, *Ritter v. Hill, supra*

331 A.2d 755, 762 (Pa. 1974). In *Ritter v. Hill*, the court concluded planned improvements constituted an encumbrance. 127 A. at 456. Construing this term to include all claims which affect market value, the court concluded the conveyance breached a covenant against encumbrances, even though the parties did not know precisely when, if ever, the land would be occupied. *Id.* at 457; *see Lafferty*, 30 A. at 1031-32 (same).

Finally, and separately, the record in the instant case must be considered. This Court should take into account the threshold procedural posture; the allegations; the affidavit evidence; and First American’s parallel disclosure of this and other special improvement districts. Given *this* record, it was legal error to dismiss, notwithstanding the holding of any other case. *See also infra* part II.A (discussing Utah legislative scheme).

D. Vestin’s Arguments Each Support the Certiorari Issue.

Vestin’s arguments fall squarely within the purview of the certiorari review. This Court should consider whether it is reviewing a summary judgment or 12(b)(6) dismissal. (Opening Br., part II.A & B.) It should also examine contract law and public policy, giving thought to the impact on Vestin and similarly situated parties. (Opening Br., part II.C.) Controlling legal principles are woven throughout these discussions.

The Court should also decide whether the Eagle Mountain SID documents constituted a “recorded encumbrance” on Vestin’s title as the Legislature said in Utah Code Ann. § 17A-3-307(6) (c). This case from the outset has involved application of the Utah Municipal Improvement District Act, Utah Code Ann. § 17A-3-301, *et seq.* (R. 71, 236-37, 415.) This Court’s review of legislation is “plenary,” with all that word denotes. *Covington v. Board of Review*, 737 P.2d 207, 209 (Utah 1987). As the U.S. Supreme Court observed, “We do not construe statutory phrases in isolation; we read statutes as a whole.” *United States v. Morton*, 467 U.S. 822, 828 (1984).

In *Thurston v. Box Elder County*, 835 P.2d 165, 168 & n.3 (Utah 1992), this Court *sua sponte* identified, analyzed, and applied a controlling statute that was not raised to or considered by the district court. Here as there, prudential appellate maxims should not undermine the overarching objective to render a correct decision on an issue directly addressed by the lawmaking branch. *See id.* (holding it would be “contrary to public policy” to ignore statute on point).

Neither plain error nor extraordinary circumstances are needed to consider the statute. The underlying defect argument raised below is the same argument Vestin

advances now. Vestin highlighted its “new argument” for the Court out of an abundance of caution. On appeal, parties are not (and should not be) prevented from identifying additional law to elucidate the issues. Statutory law differs in kind from case law only in that it trumps in a conflict. *See* Utah Code Ann. § 68-3-2. This Court’s dictums on appellate review have consistently focused on preventing the wholesale raising of brand new *issues*, not on stifling the identification of additional *legal authority* that helps decide the proper outcome of the issues on review. *See, e.g., Carrier v. Salt Lake County*, 2004 UT 98, ¶ 43, 104 P.3d 1208; Aplee. Br. at 35 n.21.

The statute is highly relevant – it could not be more on point – and if it employs a “slightly cavalier use” of the word “encumbrance,” it does so in precisely the same context as the Policies with respect to the publicly recorded documentation at issue. (Aplee. Br. at 38.) If “encumbrance” here does not mean “encumbrance” there, an ambiguity exists. *See, e.g., Lakes of the N. Ass’n*, 614 N.W.2d at 685-86 (holding statutory reference to “encumbrance” was ambiguous in light of differing case law usages); *infra* part III.B (ambiguity analysis). That First American identifies two separately acceptable constructions of a word not defined in the Policies makes ambiguity all the more apparent.

An encumbrance can include “any *right* in a third party which diminishes the value or limits the use of the land granted.” *Magraw v. Dillow*, 671 A.2d 485 (Md. 1996) (citing 3 *American Law of Property* § 12.128 (1952) (emphasis added)). This definition is not synonymous with “lien” and the statute does not make it so. (Aplee. Br. at 39 n.24.) “[W]hen reading a statute, we presume that the legislature used each word

advisedly.” *Gottling v. P.R. Inc.*, 2002 UT 95, ¶ 11, 61 P.3d 989. If “encumbrance” meant “lien” in the statute, a lien would arise on the filing of the Notice of Intention. *See* Utah Code Ann. § 17A-3-307(6).

In sum, none of First American’s principal arguments is right.

II. THE POLICIES AND ENDORSEMENTS PROVIDE COVERAGE.

A. Vestin’s Title Had a “Defect” and Was “Unmarketable.”

1. First American Failed to Disclose a “Defect” in Vestin’s Title.

The recorded Eagle Mountain SID documents were evidence of a sufficient “claim” against title to constitute a defect and require disclosure in Utah. This is best demonstrated by the statutory scheme.

Municipalities create special districts to improve real property pursuant to the Municipal Improvement District Act, Utah Code Ann. § 17A-3-301, *et seq.* Notice of intent must be given to the public and an opportunity to object provided. *Id.* § 17A-3-305 to -307. After considering all protests, the governing body creating the district must **record** the final approved resolution in the County Recorder’s office, identifying the “legal description and tax identification number of each property to be assessed.” *Id.* § 17A-3-307(6)(a)(i). If additional properties are added, a new recording must be filed in the County Recorder’s office. *Id.* § 17A-3-307(6)(b). If the governing body deletes any properties to be assessed after the district has been created, it must “record a release and discharge of the **recorded encumbrance** created as a result of the recording required by this section.” *Id.* § 17A-3-307(6)(c) (emphasis added). The district then contracts for

improvements and levies assessments. *Id.* § 17A-3-308 to -312. An assessment becomes a lien when the assessment is levied. *Id.* § 17A-3-323.

In light of this comprehensive statute and its modernizing purposes, *see id.* § 17A-3-302, the reasons First American gives for not disclosing the “recorded encumbrance” are inapplicable. (Aplee. Br. at 25-26.) Vestin responds to each:

- “[I]n some jurisdictions, local legislative history for tax bills is just too unreliable.... Local legislative records are neither uniformly nor sufficiently maintained to enable insurers to perform such searches well.” Burke § 3.05[A], at 3-77. Not so under the Utah statute, which requires recording of the key documents. First American found the Eagle Mountain SID in the county records and excepted it when issuing a title policy to another purchaser. (R. 396-97.)
- “Taxpayers might object.” Under Utah’s statute, recording is not required until *after* protests are heard. *See* Utah Code Ann. § 17A-3-306 to -07.
- “There may be an error in the political process.” There may also be invalidating errors in recorded liens. This is hardly justification for not disclosing what is required by law to be recorded as an encumbrance against specific property.
- “An alternate source of funding may be found.” Burke himself all but rebuts this justification in explaining the purpose for which policyholders purchase insurance:

The purpose of title insurance is to protect a transferee of real estate from *possible losses* through defects that *may cloud title*. The prospective real estate purchaser relies on the title insurer’s search when he decides whether or not to purchase the property; accordingly, he expects the insurer (1) to have researched the applicable law, *as well as the records*, before issuing the commitment, and (2) *to provide warnings about areas in which he might find title surprises*. Burke, § 3.05[A], at 3-85 & n.291 (emphasis added, citations omitted).

- “Notices of intent might not provide an accurate estimate of the amount of the planned levy.” Burke § 3.05[A], at 3-76.2 to 3-78. This fails on its own merits as a compelling reason. Many encumbrances appearing of record do not carry a dollar amount at all. The purpose of recording has never been to liquidate claims but to warn of potential exposure.

Burke’s arguments are more a justification for when a legislature, as a matter of statutory policy, should conclude a *lien* arises. But the Policies are not limited to liens. The Utah Legislature required the “encumbrance” at issue here be recorded in the very place where title companies search. *See* 1 Joyce Palomar, *Title Insurance Law* § 5:5 (county real property records are “the only public records the title insurer is obligated to search”). The law in Utah – which was modernized deliberately – is different from other jurisdictions where authorization for special assessments is generally not filed in county real property records. *See id.* Given this law, summary dismissal is most inappropriate. *See Oak Park Tr. & Savings Bk. v. Intercounty Title Co. of Ill.*, 678 N.E.2d 723, 725-27 (Ill. App. Ct. 1997) (whether an estimate of unpaid taxes was a public record requiring disclosure by an insurer was not appropriate for determination on summary judgment).

First American claims it could not negotiate premiums if it had to disclose publicly recorded SID documents. (Aplee. Br. at 27.) This Court has more faith in the market than that. Vestin is not asking for a guaranty or warranty. (Aplee. Br. at 49.) Vestin wants only what First American obligated itself to do: indemnify for “on-record and off-record defects found in the title or interest in an insured property to have existed on the date on which the policy is issued.” (Aplee. Br. at 49, quoting Burke.) Vestin bargained for and is entitled to this. It asks for nothing more. First American and other title companies need only disclose what industry custom and practice say they should.

“Defect” is a broad term encompassing any adverse impact on title. *United Fire & Cas. Co. v. Fidelity Title Ins. Co.*, 258 F.3d 714, 719 (8th Cir. 2001). Utah cases have identified numerous “defects” under a wide variety of circumstances. *See, e.g., Neves v.*

Wright, 638 P.2d 1195 (Utah 1981) (seller did not own property during entire executory period of contract); *Castagno v. Church*, 552 P.2d 1282 (Utah 1976) (buyer ordered to stop pumping water from conveyed land by state engineer); *Bott v. Reeder*, 369 P.2d 932 (Utah 1962) (subject land in probate estate); *Stewart v. Lesin*, 302 P.2d 714 (Utah 1956) (restriction on transfer of franchise accompanying auto sales business); *Kiahtipes v. Mills*, 649 P.2d 9 (Utah 1982) (junior lienholder). This is helpful Utah precedent from which to mold the rule of decision here.²

Vestin has pointed out the term “defect” is meaningless if a “lien” is required. (Opening Br. at 18-19.) First American argues “encumbrance” is meaningless if a “defect” is enough. (Aplee. Br. at 36-37.) This is a prototypical ambiguity scenario. *See infra* part III.B.³

Finally, First American argues that because the terms of payment were not known until after the assessment ordinance, Vestin was harmed *only* because of the due-on-sale requirement. (Aplee. Br., *passim*.) This is not true. Utah’s statutory scheme, in place since 1990, holds property owners liable for the full amount of an assessment regardless of installment payment requirements. *See* Utah Code Ann. § 17A-3-323. Moreover, following First American’s reasoning to its logical extreme, there would be no actual

² First American’s own list of defects, taken from Palomar’s treatise and Utah case law, is facially incomplete. (Aplee. Br. at 23 n.13); *see* Palomar § 5.5, text accompanying nn.10-11 (identifying *Bel-Air* holding as one type of defect and encumbrances such as “easement[s]” as another).

³ “[C]ourts tend to use the terms [“defect,” “lien,” and “encumbrance”] **loosely** and interchangeably in cases pertaining to title insurance coverage.” Palomar § 5.5, at 5-19 (emphasis added); *cf.* Aplee. Br. at 30 n.18. This does not mean courts *should*. That they do is a problem, not a rationale. *See also Manor Real Estate*, 246 A.2d at 245 (lamenting “the tendency of the courts to equate or confuse liens with encumbrances”).

harm until foreclosure. At this stage of the proceedings, Vestin gets the benefit of the doubt on all such arguments.

2. Vestin's Title Was "Unmarketable."

Even if no defect exists, title may be unmarketable if a reasonable buyer with knowledge of all the facts would be deterred from accepting the title. *See Bel-Air*, 444 A.2d at 1122-23. In *Bel-Air*, the court held the plaintiff's title unmarketable because the plaintiff would be exposed to litigation concerning its title if it challenged the assessment or pressed a claim against its vendor based on the assessment. *Id.* Vestin was in precisely that predicament.

First American overlooks Vestin itself as a purchaser in arguing the title was marketable. Vestin would have structured the transactions differently or not purchased at all had it known of the impending assessment. (R. 360.) In this sense, what Vestin would have done had the SID documents been disclosed is not "irrelevant." (Aplee. Br. at 17-18 n.7.) Moreover, Vestin alleges its buyer actually failed to perform because of the previously undisclosed SID itself. (R. 9.)

That the SID's intent to assess affected Vestin's title is evidenced by its recording against the property in the County Recorder's office. This occurred *before* the second Policy and the Endorsements issued and raises at least a substantive question of fact. *See Mellinger v. Ticor Title Ins. Co. of Ca.*, 113 Cal Rptr. 2d 357, 360 (Cal. App. 2001) (unmarketability is factual).

Finally, unmarketability is determined "without reference to the beneficial purpose" creating the restriction. *George v. Colvin*, 219 P.2d 64 (Cal. App. 1950)

(quoting 57 A.L.R. 1414). “It is no defense to show by the opinion of experts that the value of the property is not diminished by the restrictions.” *Id.* This issue should clearly move forward.

B. The Existence of the SID Made Incorrect First American’s Representations.

First American says the Eagle Mountain SID and intended assessment “could not” cut off, subordinate, or otherwise impair Vestin’s lien at the time of the second Policy. (Aplee. Br. at 42.) They most certainly could, and did. Coverage was provided for any condition capable of impairing Vestin’s interest. It was wholly unnecessary for the “covenants, conditions, or restrictions” to have *already* subordinated, impaired, or cut off Vestin’s interest. This would make the “incorrectness” provision superfluous: the Policies would need only provide coverage for already existing liens. The Utah appellate courts do not interpret contracts this way. *See Kraatz v. Heritage Imps.*, 2003 UT App 201, ¶ 26, 71 P.3d 138 (court will not interpret contract to have superfluous terms).

C. The Eagle Mountain SID Documents Were “Other Matters” that First American Failed to Disclose.

First American equates “other matters” with “defects, liens, or encumbrances.” (Aplee. Br. at 43.) But in the Policies, “other matters” does not come at the end of a list of specific items that includes defects, liens, or encumbrances. Instead, it comes in a separate clause insuring against the existence of matters “*other than those shown in the policy.*” (R. 111, emphasis added.) The doctrine of *ejusdem generis* applied in *Lombardo v. Pierson*, 852 P.2d 308 (Wash. 1993), does not control. (Aplee. Br. at 43 n.26.) To the contrary, the rules of contract law dictate construing the “other matters”

clause to have significance independent of the other insuring clauses. *See, e.g., Stewart Title Guar. Co. v. Greenlands Realty, L.L.C.*, 58 F. Supp. 2d 370, 382 (D.N.J. 1999).

First American tries to turn Vestin's arguments around, suggesting the "subsisting tax or assessment lien" language is surplusage if a "defect" is enough. (Aplee. Br. at 34.) These items appear in different provisions altogether. Had First American missed an existing lien, it undoubtedly would have been liable. But if First American meant only to exclude liens, it could have limited its Policies to that language.

The steps taken to assess Vestin's property were "matters" completed and recorded that merited disclosure. Claims based on such grounds are fact-intensive:

A claim based on a tax lien is not usually susceptible to resolution at the summary judgment stage. This is so because the complexities of assessing the lien will not likely be resolved without testimony from the insurer's [or the insured's] personnel, who are familiar with both the mechanics of assessment and the underwriting of the policy.

Burke § 3.05[A], at 3-85. Such evidence may include "[e]vidence that the lien was inchoate, but nonetheless was customarily included in the policy." *Id.*

First American suggests Vestin would have suffered no injury had it sold the Property after the SID was created but before a lien attached. (Aplee. Br. at 11-12.) Whether it even could have after a proper title search is pure speculation. Vestin likewise would have suffered no injury if its purchaser had completed the sale or if First American had disclosed the SID documents. These are factual arguments to be supported by evidence yet to be developed. Vestin suffered injury by purchasing land subject to an impending assessment that had been statutorily noticed and recorded and against which Vestin no longer had any statutory right to protest.

D. The Police Power Exception Helps Define Coverage.

An exception to an exclusionary clause need not provide independent coverage for the clause to cover the insured. The insuring agreement defines the type of risks covered; the exclusions remove coverage; exceptions to such exclusions limit the breadth of those exclusions. *Collin v. American Empire Ins. Co.*, 21 Cal. App. 4th 787, 802-3 (1994).

It would be pointless to except from exclusion uncovered risks. The very existence of the exception signals the intention recorded police power actions affecting real property were included in coverage in the first place. *See Big Cottonwood Tanner Ditch Co. v. Salt Lake City*, 740 P.2d 1357, 1359 (Utah App. 1987) (contract construed to give meaning to all provisions). Exceptions to exclusions should be considered when determining coverage. *See Crane v. State Farm Fire & Cas. Co.*, 485 P.2d 1129 (Cal. 1971).

Here, the recorded police power exception should be considered in determining the scope of coverage. *See Bel-Air*, 444 A.2d at 1122. Moreover, the exception should be construed liberally in determining coverage for Vestin. *See Taylor v. American Fire & Cas. Co.*, 925 P.2d 1279, 1282 (Utah App. 1996) (exclusionary clauses construed strictly against insurer); *New England Fed. Cr. Union v. Stewart Title Guar. Co.*, 765 A.2d 450 (Vt. 2000); *Radovanov v. Land Title Co.*, 545 N.E. 2d 351, 354-55 (Ill. App. 1989); *Bel-Air*, 444 A.2d 1119.⁴

⁴ *Bel-Air* and the other cited cases fully support Vestin's police power argument. Burke's "rejection" of *Bel-Air* makes no sense: Burke cites the case as if it were a supporting authority for the opposite proposition. Burke § 4.02[B], at 4-28 and n.103.

First American concedes “the Policies cover ‘loss or damage’ caused by the exercise of a governmental police power if a notice of the exercise of the police power that caused the loss or damage was recorded in the public records on the policy date.” (Aplee. Br. at 44-45.) That is this case. The Assessment was not simply a post-policy exercise of police power distinct and separate from the pre-policy “steps.” It specifically implements the pre-lien ordinances. (R. 200, 202-03.) This further distinguishes those authorities relying on *Cummins v. U.S. Life Title Ins. Co.*, 357 N.E.2d at 976-77, which held on its facts that a post-policy lien was a new exercise of legislative authority that did not relate back to an expired authorization made six years earlier.

In sum, coverage or factual issues about coverage exist under multiple Policy provisions.

III. PROPER AMBIGUITY ANALYSIS REQUIRES REVERSAL.

A. This Court Construes Insurance Policies in Favor of the Insured.

“Since 1921 this Court has expressed its commitment to the principle that insurance policies should be construed liberally in favor of the insured and their beneficiaries so as to promote and not defeat the purposes of insurance.” *United States Fid. & Guar. Co. v. Sandt*, 854 P.2d 519, 521-22 (Utah 1993) (citations omitted); *see also McCoy v. Blue Cross & Blue Shield*, 2001 UT 31, n.1, 20 P.3d 901 (same). Only if a policy is unambiguous does the presumption in favor of coverage disappear. *S.W. Energy Corp. v. Continental Ins. Co.*, 1999 UT 23, ¶¶ 12-14, 974 P.2d 1239. Evidence of ambiguity keeps the presumption intact, and “all ambiguities are construed against the

insurer and are ‘resolved in favor of coverage.’” *Hill v. Farmers Ins. Exch.*, 888 P.2d 138, 140 (Utah App. 1994) (quoting *Nielsen v. O’Reilly*, 848 P.2d 664, 666 (Utah 1992)).

There is no basis for departing from the settled rules based on First American’s factual characterization of Vestin as “sophisticated.” (Aplee. Br. at 19 n.10.) These form policies should not be applied differently to Vestin, who was in the same position as any other policyholder purchasing title insurance.

B. This Court Should Consider the Record Evidence in Determining the Policies Are Ambiguous.

First American’s ambiguity analysis is wrong. That ambiguity is a question of law does not make extrinsic evidence irrelevant. To the contrary, proffered evidence is considered. *Ward v. Intermountain Farmers Ass’n*, 907 P.2d 264, 268 (Utah 1995).

This Court recently reaffirmed this analysis. *See Nielsen v. Gold’s Gym*, 2003 UT 37, ¶ 7, 78 P.3d 600 (citing *Ward* inter alia). Yet the Court of Appeals uses this maxim notoriously selectively. *Compare Novell, Inc. v. The Canopy Group, Inc.*, 2004 UT App 162, ¶ 21, 92 P.3d 768 (citing *Ward* and looking to extrinsic evidence) with Ct. App. Op., ¶¶ 9, 19 & n.9 (suggesting court may only consider extrinsic evidence after finding contract ambiguous). This breeds unfairness and confusion. Indeed, inconsistency of this sort contributed to the Tenth Circuit’s believing “Utah law is unsettled on the issue whether the court may go beyond the four corners of the contract to determine whether the contract is ambiguous.” *Flying J, Inc. v. Comdata Network, Inc.*, 405 F.3d 821, 831 (10th Cir. 2005). Ultimately, however, the Tenth Circuit applied *Ward* because Utah counsel recognized it governed. *See id.* at 832.

This Court should affirm the *Ward* rule unequivocally. Parties and their counsel in Utah are entitled to consistent application of one rule – not differing rules reaching different results in comparable contexts.

Vestin’s extrinsic evidence is compelling. First American’s litigation position contradicts industry practice *and* First American’s own practice. (R. 359, 396-97.) First American disclosed to Vestin a different SID and revealed the assessment status. (R. 18, 86.) First American also disclosed and excepted *this very SID and this very Notice of Intention to levy special assessments to a different policyholder*. (R. 396-97.) Why? First American plainly determined it was required to do so under its standard policy. First American also warned Vestin of pre-lien charges and assessments that *could be*, but had not yet been, levied by non-SID governmental authority. (R. 18, 86.)⁵

First American has no answer for this evidence but to malign it without contrary evidence. First American weakly suggests Vestin’s affidavits violate the parol evidence rule. (Aplee. Br. at 18 n.8.) This evidence demonstrates how the Policy terms are to be construed, not varied or contradicted. Indeed, First American itself relies on industry custom and practice in arguing *its* construction, telling the Court the Policies are “standard form” documents “used throughout the country” and approved by ALTA. (Aplee. Br. at 24 & n.14; *see also id.* at 28.) This evidence, viewed in its most favorable

⁵ The Eagle Mountain SID is a separate arm of the government from Eagle Mountain City, with separate power to assess. *See Tygesen v. Magna Water Co.*, 226 P.2d 127, 131, 139 (Utah 1950). Consequently, this statement did *not* disclose the SID or its ability to levy charges and assessments. (Aplee. Br. at 22 n.12.) Given this language, however, any reasonable policyholder would be justified in believing entities with assessment power would be disclosed.

light to Vestin, cuts against First American. Because the Policies are standard forms, evidence of how First American generally interprets them demonstrates at least an ambiguity when First American advances a contradictory position here. *See also AIS Insurance Online Glossary*, www.aisinsurance.com/pltp/pages/glossary (“policy jacket” is preprinted form with standard language).⁶

First American also relies on matters outside the pleadings, including facts unsupported by the record. It argues, without record citation, “the improvements obviously have caused the value of the benefited property to increase.” (Aplee. Br. at 3.) It says Vestin “obviously” will “enjoy” the “benefit” bestowed and wants First American to “pay for the benefit.” (Aplee. Br. at 3.) It relies on the very evidence submitted by Vestin to argue Vestin’s people were experienced and sophisticated. (Aplee. Br. at 19 n.10.) It characterizes Vestin’s testimony, calling it “self-serving.” (Aplee. Br. at 17 n.7.) These are factual jury-type arguments (or completely unsupported by evidence), inappropriate for summary dismissal of a non-moving plaintiff at the pleading stage.

First American also says Vestin’s neighbors have to pay for their improvements and Vestin is not bearing its fair share. (Aplee. Br. at 48.) This is completely unsupported by the record. Perhaps each adjoining landowner had title insurance that disclosed the Eagle Mountain SID and Notice of Assessment, maybe even from First

⁶ First American did not put IFA’s policy in the record. *See Rivera v. TRW Title Ins. Co.*, 765 N.Y.S.2d 257 (App. Div. 2003) (affirming judgment against insurer after trial court drew negative inference from its failure to present evidence of its underwriting practices). There is no record basis for First American’s suggestion it “negotiated” different policy language with IFA. (Aplee. Br. at 18 n.7.)

American. It will be revealing to see what discovery turns up. There is no “windfall” in a policyholder actually receiving the benefit of the bargain for which it pays premiums.

First American argues Vestin’s evidence does not show Vestin or First American *subjectively* intended disclosure of the SID or Notice of Assessment. (Aplee. Br. at 17 n.7.) The correct standard is *objective*, asking what a reasonable purchaser would anticipate. *See, e.g., Christensen v. Farmers Ins. Exch.*, 443 P.2d 385, 387 (Utah 1968). Vestin’s evidence certainly shows this. Even if the standard were subjective, the evidence shows the parties so intended because: (1) First American and the industry as a whole typically disclose; and (2) Vestin’s officers were familiar with these standards.

“To demonstrate ambiguity, the contrary positions of the parties must each be tenable.” *R & R Energies v. Mother Earth Indus., Inc.*, 936 P.2d 1068, 1074 (Utah 1997). Given the evidence, Vestin’s position is more than tenable – it is most probable. The construction of disputed contract terms is a question of fact after an evidentiary ambiguity determination. *See Flying J*, 405 F.3d at 832 (applying Utah law). The Court of Appeals erred in prematurely preempting factual findings.

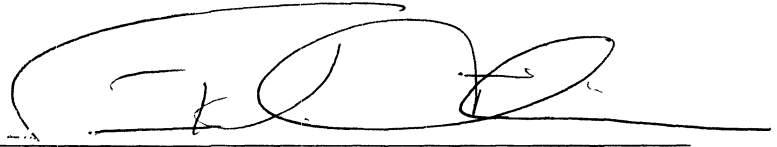
CONCLUSION

For all of the foregoing reasons, individually and collectively, the judgment of the Court of Appeals should be reversed and the case remanded for further proceedings.

DATED this 2nd day of September, 2005.

VAN COTT, BAGLEY, CORNWALL & McCARTHY

By:

A handwritten signature in black ink, appearing to be "John A. Snow", written over a horizontal line.

John A. Snow

Stephen K. Christiansen

Cassie Wray

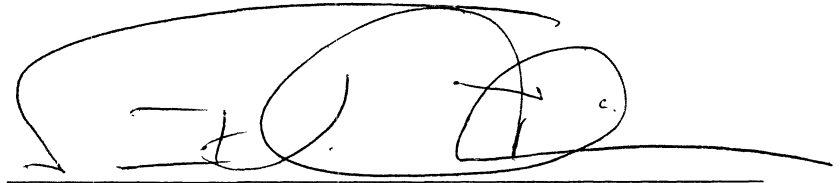
Attorneys for Appellant/ Petitioner

Vestin Mortgage, Inc.

CERTIFICATE OF SERVICE

I hereby certify that I caused two (2) true and correct copies of the within and foregoing **APPELLANT/PETITIONER'S REPLY BRIEF** to be mailed, postage prepaid, this 2nd day of September, 2005, to the following counsel of record:

Alan L. Sullivan
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A handwritten signature in black ink, appearing to be "Alan L. Sullivan", written over a horizontal line.