DIVISION ONE
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IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

THOMAS L. THORNTON and NANCY K. THORNTON, husband and wife, Plaintiffs/Appellants, v. CHICAGO TITLE INSURANCE COMPANY, a foreign corporation, Defendant/Appellee.	No. 1 CA-CV 10-0014 DEPARTMENT C **MEMORANDUM DECISION** (Not for Publication - Rule 28, Arizona Rules of Civil Appellate Procedure)

Appeal from the Superior Court in Maricopa County

Cause No. CV2008-011540

The Honorable Bethany G. Hicks, Judge

AFFIRMED IN PART; REVERSED IN PART; REMANDED

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B R O W N, Judge

¶1 Thomas and Nancy Thornton appeal the trial court's order dismissing their complaint against Chicago Title Insurance Company. For the following reasons, we affirm the court's

dismissal of the Thorntons' claims for negligence and aiding and abetting, but we reverse the dismissal of the claim for breach of fiduciary duty, and remand for further proceedings.

BACKGROUND

¶2 For purposes of reviewing a motion to dismiss, we assume the truth of the factual allegations as set forth in the complaint. *Cullen v. Auto-Owners Ins. Co.*, 218 Ariz. 417, 419, ¶ 7, 189 P.3d 344, 346 (2008).

¶3 Thomas and Nancy Thornton, husband and wife, agreed to make two loans to Darren Hartwick. The loans were to be secured by deeds of trust on two parcels of real property. Chicago Title served as the escrow company for both transactions. Terms of the first loan, in the amount of $125,000, were reflected in a promissory note prepared by Chicago Title. The note was to be secured by a deed of trust on real property located in Mohave County. Escrow instructions for the transaction provided that Chicago Title: (1) would serve as the escrow agent; (2) would issue a standard lender's title insurance policy for $125,000, insuring that the Mohave property was owned by Hartwick, "free from encumbrances"; and (3) would "insure[] the lien of the Mohave Deed of Trust which secured the $125,000 loan."

¶4 The Thorntons remitted $125,000 to Chicago Title, believing that Hartwick owned the Mohave property, that the proceeds of the loan were to be used to improve the property,

and that the Deed of Trust was to be the first lien on the property. Prior to close of escrow, Chicago Title did not provide the Thorntons with a commitment for title insurance or documents reflecting the title or lien status of the Mohave property.

¶5 At closing, Chicago Title recorded documents in the following order: (1) a warranty deed from GHB Investments conveying title to Hartwick; (2) a deed of trust from Hartwick as trustor to Sir Mortgage & Finance and others as beneficiaries; (3) a deed of trust from Hartwick as trustor, to the Thorntons as beneficiaries. Because of the recording sequence, the Thornton's Deed of Trust became subordinate to the Sir Mortgage Deed of Trust, which had a principal balance of $195,000 plus interest and other potential charges if Hartwick defaulted.

¶6 The second loan transaction was in the amount of $185,000. The promissory note was to be secured by a deed of trust on property located in Needles, California. In accordance with the escrow instructions, the Thorntons remitted $185,000 to Chicago Title. They believed that the property was subject to a first position deed of trust in the amount of $575,000 and that their loan of $185,000 was to be used to subdivide and improve the property. The Needles property, however, was subject to a first lien of $1,060,500, and Hartwick used at least some, if

not all, of the proceeds of the Thorntons' loan to pay the first lien holder. At no time prior to closing did Chicago Title provide the Thorntons with a commitment for title insurance or other documents reflecting the title or lien status of the Needles property.

¶7 Hartwick defaulted on both of the loans made to him by the Thorntons, in addition to the other loans on the two properties. The first position lien holders conducted foreclosure sales of the Mohave and Needles properties, extinguishing the subordinate property interests with no funds available for payment on either of the Thorntons' loans.

¶8 The Thorntons filed suit against Hartwick, Premier Realty Services, Chicago Title, and the individual escrow agent. Before an answer was served, an amended complaint was filed that removed Hartwick[1] and Premier Realty Services as defendants and corrected the name of the individual escrow agent. As to Chicago Title, the complaint alleged breach of fiduciary duty, negligence, and aiding and abetting fraud.

¶9 As relevant here, the Thorntons alleged in their complaint that Chicago Title breached its fiduciary duty by failing to disclose, in advance of the Mohave loan, that

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[1] A Chapter 11 bankruptcy was filed by Hartwick, requiring an automatic stay in this case until he was removed as a defendant by the amended complaint. 11 U.S.C. § 362(a)(1) (West 2011) (providing for automatic stay of judicial proceedings arising before the commencement of a bankruptcy case).

Hartwick was insolvent; that he had a history of defaulting on other loans; that all or part of the proceeds of the Mohave loan were to be used to purchase the property and pay creditors; and that the Thorntons' lien was subordinate to a prior lien in the amount of at least $195,000, which over-encumbered the property because it left no equity to secure the Thorntons' $125,000 note. The Thorntons further alleged that Chicago Title intentionally failed to provide, prior to closing, a commitment of title insurance and thus withheld material information regarding the true ownership of the Mohave property.

¶10 Regarding the Needles loan, the Thorntons alleged breach of fiduciary duty based on Chicago Title's failure to disclose, prior to closing, Hartwick's insolvency; his history of defaulting on loans; that all or part of the $185,000 would be used to pay arrearages owed to the first lien holders or other creditors; that the first lien on the Needles property was substantially higher than expected; and that the amount of the first lien caused the Needles property to be over-encumbered. The Thorntons also alleged that Chicago Title intentionally failed to provide them with a commitment of title insurance prior to closing, thus withholding material information regarding the amount of the Sir Mortgage Deed of Trust.

¶11 Chicago Title moved to dismiss the breach of fiduciary duty claim,[2] arguing that the complaint: (1) did not allege any breach of a duty of disclosure; and (2) failed to contain the requisite particularity required by Arizona Rule of Civil Procedure 9(b) because any alleged breach was necessarily based on an underlying fraud claim. Without comment, the trial court granted the motion to dismiss. The Thorntons filed a motion to amend or supplement the judgment. *See* Ariz. R. Civ. P. 52(b). The Thorntons argued that because the judgment included Hartwick as a listed defendant and did not reflect the reasoning of the court, it appeared as though the court may have granted the motion to dismiss based on the bankruptcy stay that no longer legitimately applied to the amended complaint. Alternatively, if the court had decided the motion on the merits, the Thorntons requested that the court provide the grounds for dismissal, and additionally moved for leave to file an amended complaint to avoid the dismissal.

¶12 Before the court ruled on the Thornton's motion, Chicago Title lodged a form of judgment that included language

[2] Chicago Title also moved to dismiss the negligence and aiding and abetting claims and the trial court granted the motion in its entirety. On appeal, the Thorntons do not challenge the court's ruling as to those two counts and therefore we do not disturb that portion of the dismissal order. *City of Tucson v. Clear Channel Outdoor, Inc.*, 218 Ariz. 172, 193 n.10, ¶ 80, 181 P.3d 219, 240 n.10 (App. 2008) (recognizing that issues not raised in an opening brief are waived).

clarifying that the dismissal was based on the merits, and the Thorntons objected. The trial court signed the proposed order on August 24, 2009, dismissing the case with prejudice over the Thorntons' objection, but the judgment was not filed by the clerk until September 25, 2009. The court denied the Thorntons' motion to supplement or amend in an unsigned minute entry and this appeal followed.[3]

DISCUSSION

¶13 A trial court's grant of a motion to dismiss for failure to state a claim is reviewed de novo. *Phelps Dodge Corp. v. El Paso Corp*., 213 Ariz. 400, 402, ¶ 8, 142 P.3d 708, 710 (App. 2006). We assume the allegations in the complaint are true, and will "uphold dismissal only if the plaintiffs would not be entitled to relief under any facts susceptible of proof in the statement of the claim." *T.P. Racing, L.L.L.P. v. Ariz. Dep't of Racing*, 223 Ariz. 257, 259, ¶ 8, 222 P.3d 280, 282 (App. 2009) (quoting *Mohave Disposal, Inc. v. City of Kingman*, 186 Ariz. 343, 346, 922 P.2d 308, 311 (1996)).

[3] A notice of appeal was prematurely filed on November 9, 2009, because the September 25, 2009, minute entry was unsigned. Pursuant to *Eaton Fruit Co. v. Cal. Spray-Chem. Corp.*, 102 Ariz. 129, 130, 426 P.2d 397, 398 (1967), we suspended the appeal and re-vested jurisdiction in the superior court for the purpose of allowing the court to sign the order. An order was entered and signed by the trial court on May 7, 2010, and we now have jurisdiction over this appeal.

¶14 The Thorntons assert the trial court erred in granting Chicago Title's motion to dismiss because Chicago Title, as the escrow agent handling the loan transactions, had a duty to disclose facts that presented substantial evidence of fraud, and that their complaint presented sufficient facts in support of the claim. We agree.

¶15 "An escrow agent has a fiduciary relationship of trust and confidence to the parties to the escrow." *Maxfield v. Martin*, 217 Ariz. 312, 314, ¶ 12, 173 P.3d 476, 478 (App. 2007) (citing *Maganas v. Northroup*, 135 Ariz. 573, 576, 663 P.2d 565, 568 (1983)). As such, the escrow agent is obligated to perform his responsibilities with "scrupulous honesty, skill, and diligence." *Id.* at 315, ¶ 14, 173 P.3d at 479 (quoting *Berry v. McLeod*, 124 Ariz. 346, 351, 604 P.2d 610, 615 (1979)). "The escrow relationship gives rise to two specific fiduciary duties to the principals: to comply strictly with the terms of the escrow agreement and to disclose facts that a reasonable escrow agent would perceive as evidence of fraud being committed on a party to the escrow." *Id.* at 314, ¶ 12, 173 Ariz. at 478.

¶16 As it did in the trial court, Chicago Title argues "there is no duty to disclose information received by an escrow agent unless such a duty is required by the terms of the escrow agreement." Chicago Title further contends that the duty to disclose information arises "if, and only if," an escrow agent

actually knows that a fraud is being committed on a party to an escrow. These arguments, however, are not consistent with Arizona law. *See Burkons v. Ticor Title Ins. Co. of Cal.*, 168 Ariz. 345, 813 P.2d 710 (1991).

¶17 In *Burkons*, Pyramid purchased real estate with a small down payment and a carry-back deed of trust against the property as collateral on the loan. *Id*. at 347-48, 813 P.2d at 712-13. A subordination agreement was prepared by Pyramid and signed by the plaintiffs. *Id*. at 348, 813 P.2d at 713. Pyramid used the loan for a down payment to purchase the property, receiving the rest of the purchase price from Tower, a different lender. *Id.* The defendant title company recorded the Tower lien document first, and then the plaintiff's lien document followed by the subordination agreement, so that the plaintiff's lien was junior to Tower's lien. *Id.* The title company did not inform the plaintiffs that the property was over-encumbered, meaning that the combination of liens exceeded the property's value and sale price and that the loan proceeds were not used to improve the property but to purchase it. *Id.* at n.5.

¶18 Our supreme court, in analyzing whether the facts and circumstances known to the title company could support a finding that a reasonable escrow agent would have perceived them as evidence of fraud, concluded that the facts left the question "easily answered." *Id.* at 354, 813 P.2d at 719. The court

found that the transaction itself provided sufficient suspicious indicia triggering the obligation to disclose:

> Certainly the trier of fact would be entitled to consider that no reasonable business purpose was served by Pyramid's scheme, that no reasonable seller would have agreed to it if he had understood it, and that the documents——particularly the letter of intent——were misleading because they implied the funds would be used for construction. The factfinder could conclude that the escrow agent, with all its experience, must have been aware of these circumstances.

Id. The court explained further that "it is difficult to imagine why a seller would agree to the destruction of his or her own security," and that such an arrangement would be unusual and unlikely and might be required to be spelled out with particularity for enforcement. *Id.* at 350, 813 P.2d at 715 (citing *Miller v. Citizens Sav. & Loan Ass'n,* 248 Cal. App. 2d 655, 663 (1967)). The court then concluded that entry of summary judgment against the plaintiffs, on their claim that the title company breached its fiduciary duty by failing to disclose that the property was over-encumbered, was improper. *Id.* at 354, 813 P.2d at 719. Finally, the court expressly rejected the notion that an escrow agent must have actual knowledge that fraud is being committed:

> We reject [defendant's] suggestion that there is no duty to disclose unless the escrow agent actually knows that a fraud is being perpetrated. Parties perpetrating

> fraud rarely confess to their escrow agents, and absolute knowledge of fraud can seldom be established. Such a rule is so unrealistic that it would actually make escrow agents reluctant accomplices to land fraud schemes. Because of the principle of confidentiality, the escrow agent would act at its peril in making any disclosure without an actual confession of fraud. We prefer as a matter of common law policy to rely on *Berry's* point: if the facts *actually known* to the escrow agent present substantial evidence of fraud, there is a duty to disclose.

Id. at 354-55, 813 P.2d at 719-20.[4]

¶19 Applying these principles here, the Thorntons alleged that Chicago Title knew that the Mohave property would be over-encumbered once it recorded two liens against the property. The Thorntons further alleged that they did not have knowledge of or agree to the Mohave lien subordination, and that they never received a title commitment that would have shown outstanding liens and property ownership prior to the loan closing. Concerning the Needles transaction, though the Thorntons knew of a prior lien, they believed that the proceeds of their loan were to be used to subdivide and improve the Needles property. They

[4] We reject Chicago Title's attempt to distinguish *Burkons* by pointing to the internal title company policy violation concerning over-encumbered loans in that case that is not present in this record. As this case is only in the beginning stages, it is premature to attempt to divine what company policies may or may not exist. And, the existence of any particular policy is but one factor that may be considered in determining whether the escrow agent had a disclosure obligation under the principles set forth in *Burkons*.

also alleged that Chicago Title knew that some or all of the loan proceeds would not be used for that purpose but to pay arrearages to the first lien holders with a significantly higher prior loan amount than the Thorntons expected.

¶20 These specific allegations are sufficient to withstand a motion to dismiss for failure to state a claim. *See id.* at 353-54, 813 P.2d 718-19 (finding that the relevant inquiry is whether a reasonable escrow agent would have perceived the facts and circumstances as "evidence of fraud"); *Manley v. Ticor Title Ins. Co. of Cal.*, 168 Ariz. 568, 573, 816 P.2d 225, 230 (1991) (finding that even in a loan to purchase contract, if there are contractual indications that the buyer agrees to use the loan to construct specific improvements, a breach of fiduciary duty may occur if a title company allows the loan proceeds to be used otherwise). Accordingly, we hold that the trial court erred in granting Chicago Title's motion to dismiss the Thorntons' claim for breach of fiduciary duty.

II. Inapplicability of Rule 9(b)

¶21 Chicago Title asserts that the Thorntons failed to sufficiently plead the underlying fraud of Hartwick or Chicago Title's knowledge of fraud, in violation of Rule 9(b) of the Arizona Rules of Civil Procedure. We disagree.

¶22 The Thorntons' claim of breach of fiduciary duty is not an actual claim of fraud; rather, it is based on

nondisclosure by the escrow agent. Thus, the requirement for greater particularity imposed by Rule 9(b) is inapplicable because the alleged breach is not premised on Chicago Title's own fraudulent conduct. For their breach of fiduciary duty claim, the Thorntons were only required to provide a short and plain statement showing they are entitled to relief, which they have done. *See* Ariz. R. Civ. P. 8(a); *Mobilisa, Inc. v. Doe 1*, 217 Ariz. 103, 111, ¶ 23, 170 P.3d 712, 720 (App. 2007).

CONCLUSION

¶23 Because the Thorntons' complaint stated a claim for relief for breach of fiduciary duty, we reverse the court's dismissal of that claim and remand for further proceedings. We affirm the court's dismissal of the Thorntons' claims of negligence and aiding and abetting.

/s/

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MICHAEL J. BROWN, Judge

CONCURRING:

/s/

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DANIEL A. BARKER, Presiding Judge

/s/

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MARGARET H. DOWNIE, Judge