STATE OF MICHIGAN

IN THE SUPREME COURT

BANK OF AMERICA, NA,

Plaintiff-Appellant,

v

FIRST AMERICAN TITLE INSURANCE COMPANY, PATRIOT TITLE AGENCY, KIRK D. SCHIEB, WESTMINSTER ABSTRACT COMPANY, WESTMINSTER TITLE AGENCY, INC, PRIME FINANCIAL GROUP, INC, VALENTINO M. TRABUCCHI, PAMELA S. NOTTURNO, f/k/a, PAMELA S. SIIRA, DOUGLAS K. SMITH, JOSHUA J. GRIGGS, STATE VALUE APPRAISALS, LLC, NATHAN B. HOGAN, and CHRISTINE D. MAYS,

Defendants-Appellees,

and

FRED MATSON, MICHAEL LYNETT, JO KAY JAMES, and PAUL SMITH,

Defendants.

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Opn March 27, 2014
Rec 5-22-14

No. 307756
Oakland Circuit Court
LC No. 2010-112606-CK

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PLAINTIFF BANK OF AMERICA, N.A.'S APPLICATION FOR LEAVE TO APPEAL

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STATEMENT OF JUDGMENT APPEALED FROM AND RELIEF SOUGHT

Plaintiff/Appellant Bank of America, N.A. appeals a March 27, 2014 per curiam opinion (with a dissent) by the Michigan Court of Appeals under MCR 7.302(B)(3) and (5). (Ex 1.) Despite agreeing that the Bank lost $7,000,000 as a result of four fraudulent mortgage loan transactions, the Court of Appeals ruled that the Bank could pursue only a fraction of these losses against Defendants – all of whom are real estate professionals who agreed to be contractually liable for the Bank's losses. The Court of Appeals, with Chief Judge William B. Murphy dissenting, misapplied the closing protection letters and closing instructions that governed the contractual duties owed to the Bank by Defendants. These separate and distinct agreements are present in virtually every mortgage loan transaction closed in Michigan, and these standard contracts advance the significant interests of Michigan by protecting lenders and borrowers from mortgage fraud. The majority's approach to the application of these contracts seriously limits the ability of victims of mortgage fraud to hold a closing agent or its authorizing title insurer liable for the losses resulting from the closing agent's misconduct.

The Court of Appeals also ruled that it was required by *New Freedom Mortgage Corp v Globe Mortgage Corp*, 281 Mich App 63; 761 NW2d 832 (2008) to bar the Bank from recovering certain of its losses under the so-called "full credit bid rule." The majority acknowledged that the full credit bid rule was designed to protect mortgagors – not third parties like Defendants – but did not formally request a conflict panel under MCR 7.215(J). In dissent, Chief Judge Murphy stated that he would request a conflict panel to challenge *New Freedom*. The Bank timely filed a motion for reconsideration on April 17, 2014. An order was entered on May 22, 2014 denying the Bank's motion for reconsideration, with Chief Judge Murphy stating that he would have granted the motion. This application for leave to appeal is timely filed within

42 days of the clerk's mailing of the order denying reconsideration as required by MCR 7.302(C)(2).

The Bank respectfully requests that this Court: (1) overrule *New Freedom* and reverse the holdings of the Court of Appeals' March 27, 2014 per curiam opinion as they relate to the full credit bid rule; (2) reverse Parts IV and V of the Court of Appeals' March 27, 2014 per curiam opinion; and (3) remand to the Circuit Court accordingly.

STATEMENT OF QUESTIONS PRESENTED

I. In the typical Michigan mortgage loan transaction, the closing agent agrees to follow all of the lender's written closing instructions before disbursing the lender's funds and closing the transaction. In addition to the agreement with the closing agent embodied in these closing instructions, the lender also typically receives a closing protection letter (or "CPL") from the title insurer that requires the title insurer to reimburse the lender (and its borrower) for actual losses arising out of the limited matters described in the CPL. Did the Court of Appeals err in holding that CPL agreements entered between title insurers and lenders modify the plain language of the separate and distinct closing instruction agreements between lenders and closing agents?

Plaintiff answers: Yes.
Defendant Westminster answers: No.
The Circuit Court and Defendant First American did not answer this question.
The Court of Appeals answered: No (majority) and Yes (dissent).
This Court should answer: Yes.

II. Defendant First American agreed to reimburse the Bank under CPLs for actual losses arising from the "fraud or dishonesty" of Westminster. Title insurers have made similar promises in CPLs issued in countless other Michigan mortgage loan transactions. The Bank presented evidence and unrebutted proposed expert testimony that Westminster must have known that the subject transactions were fraudulent. Should the Bank be allowed to present this evidence to the jury so the jury can decide whether Westminster closed the transactions with the requisite fraud or dishonesty?

Plaintiff answers: Yes.
Defendants First American and Westminster answer: No.
Circuit Court answered: No.
The Court of Appeals answered: No (majority) and Yes (dissent).
This Court should answer: Yes.

III. MCL 600.3280 protects mortgagors and persons liable on secured debt from deficiency judgments and encourages lenders to make full credit bids when foreclosing by advertisement. Defendants are not persons liable on secured debt and § 600.3280 was never intended to shield third party wrongdoers from civil liability unrelated to the secured debt. Should this Court overrule *New Freedom* because it wrongly extended the statutory protections of §600.3280 to relieve third parties from liability arising from their fraud or misconduct?

Plaintiff answers: Yes.
Defendants First American and Westminster answer: No.
The Circuit Court did not answer this question.
The Court of Appeals answered: No (majority) and Yes (dissent).
This Court should answer: Yes

INTRODUCTION AND REASONS FOR GRANTING LEAVE TO APPEAL

This mortgage fraud case presents legal principles of major significance to Michigan's jurisprudence. In the everyday Michigan mortgage loan transaction, a closing agent agrees to be financially liable to the lender for losses resulting from the failure of the agent to comply with *any* of the lender's closing instructions. The lender's closing instructions dictate how the loan is to be closed and allow the lender to place conditions on the closing agent designed to detect and prevent mortgage fraud. To further offset the risk of malfeasance or defalcation by the closing agent, the lender typically demands the additional protection of a closing protection letter (or "CPL"). See Gosdin, Title Insurance: A Comprehensive Overview (3d), p 87. CPLs are indemnity contracts that, in general, require title insurers to reimburse lenders (and their borrowers) for actual losses arising out of the fraud or dishonesty of the closing agent or the closing agent's failure to follow a limited type of closing instructions. Closing instructions and CPLs govern the rights and liabilities of parties in virtually every mortgage loan transaction closed in Michigan. But despite their prevalence, this Court has not had the opportunity to provide guidance on the proper scope of these standard contracts.

In this case, the Bank required closing agents Westminster Abstract Company d/b/a Westminster Title Agency, Inc. and Patriot Title Agency, LLC to comply with *all* of the Bank's written closing instructions with respect to four mortgage loan transactions and required that CPLs be issued from national title insurer First American Title Insurance Company. It is undisputed that the Bank was the victim of a mortgage fraud scheme involving concealed property flips, straw buyers, and inflated property values. In the end, the Bank suffered actual losses of more than $7,000,000 as a result of this fraud. The Bank sought to recover its losses from the third parties responsible for these losses, including Westminster (under the Bank's closing instructions) and First American (under the CPLs). Despite Michigan's significant interest in deterring and combating mortgage fraud, see MCL 750.219d, the Court of Appeals ruled that the Bank could not seek a complete recovery of its substantial losses from those responsible for facilitating the mortgage fraud at issue in this case. The Court of Appeals' decision has broad implications and impairs the rights of victims of mortgage fraud to recover their losses against the responsible parties in three significant ways:

(1) The Court of Appeals (with a dissent) ruled that Westminster only had a duty to comply with the Bank's limited closing instructions to the extent that they would *also* trigger liability under the separate CPL contracts. Nothing in the language of the subject contracts or the conduct of the parties in this case supports such a ruling. This ruling is also directly contrary to the standards of the industry, which require closing agents to comply with *all* of a lender's instructions, and impairs the ability of parties to freely contract. If this decision is allowed to stand, closing agents across the State would be free to ignore countless closing instructions – many of which are designed to detect and prevent mortgage fraud.

(2) The Court of Appeals agreed with the Bank that the "fraud or dishonesty" paragraph of a CPL covers a broad range of misconduct by closing agents, including suppressing material facts or closing a transaction despite knowledge of the underlying fraud. But after finding that the Bank had presented sufficient evidence with regards to the "fraud or dishonesty" of Patriot, the Court of Appeals (with a dissent) ruled that the Bank's CPL claims as to Westminster could not proceed. The Bank, however, had presented evidence and proffered expert testimony that Westminster *must have known that the subject transactions were fraudulent*. In disregarding this evidence, the court improperly created a heightened standard for lenders (and their borrowers) to

meet in order to take CPL claims to a jury, and severely limited the ability of lenders (and their borrowers) to seek recourse for losses caused by mortgage fraud.

(3) Irrespective of the merits of the Bank's claims, the Court of Appeals ruled that it was constrained by *New Freedom* to bar *all* claims against third parties for losses relating to properties purchased with full credit bids at foreclosure sales. Since the Great Depression, Michigan has, *by statute*, protected mortgagors from deficiency judgments and encouraged mortgagees to make full credit bids in order to provide certainty to mortgagors and mortgagees. See MCL 600.3280. *New Freedom's* extension of this rule to immunize certain third party wrongdoers from the consequences of their fraudulent or tortious conduct (unrelated to the secured debt) was unprecedented and clearly erroneous. By its express terms, § 600.3280 is inapplicable to the Bank's claims against Defendants and *New Freedom* should be reversed in order to avoid material injustice to lenders,[1] deter mortgage fraud, and reestablish certainty in the foreclosure process. Lenders should not be required to pursue deficiency judgments against already beleaguered borrowers as a condition precedent to seeking recovery from those contractually liable for the losses caused by mortgage fraud.

In addition to involving legal principles of major significance to Michigan, these rulings are clearly erroneous and will cause material injustice to lenders and borrowers injured by mortgage fraud in Michigan. The Bank respectfully requests that this Court reverse these rulings so as to preserve Michigan's interests in protecting victims of mortgage fraud – as opposed to insulating those responsible for the fraud from civil liability.

[1] Two other appeals are pending in the Court of Appeals directly relating to the application of the full credit bid rule as to multi-million dollar claims under CPLs. See Court of Appeals Case Nos. 311798 and 316538.

STATEMENT OF FACTS AND RELEVANT PROCEDURAL HISTORY

A. Summary of subject mortgage loan transactions.

In late 2005 and early 2006, the Bank received four loan packages from an independent mortgage broker. The loan packages contained representations regarding the borrowers' intended occupancy, the borrowers' income and assets, the value of the properties, and the nature of the transactions in general. (App'x 2, ex 26; App'x 3, exs A, B.)[2] The Bank relied on these representations in agreeing to lend 65-70 percent of the sales price. The Bank required each borrower to finance the remaining sale price with a down payment or earnest money deposit. (App'x 2, exs 6, 9, 15, 19.) The stated income loans were secured by mortgages on residences in Oakland and Genesee Counties. The basic information regarding the subject transactions is as follows:

Address	Borrower	Loan Amount	Closing Agent
1766 Golf Ridge Drive, Bloomfield Township	Smith, Paul	$1,500,000	Patriot
1550 Kirkway Road, Bloomfield Township	Lynett, Michael	$1,500,000	Patriot
13232 Enid Boulevard, Fenton	Matson, Fred	$3,575,000	Westminster
1890 Heron Ridge Court, Bloomfield Hills	James, Jo Kay	$2,800,000	Westminster

The subject mortgage loan transactions were closed by Westminster and Patriot. The Bank provided the closing agents with detailed closing instructions for each transaction. (App'x 4, ex 4.) These instructions required the closing agents to contact the Bank immediately if the agent could not comply with the instructions and stated that the agent would be financially responsible for any losses resulting from the failure to follow the instructions. The closing agents certified compliance with all of the conditions in the closing instructions.

[2] The appendices cited in this application are to the Bank's Brief on Appeal in Court of Appeals No. 307756. The Index of Appendices from the Bank's Brief on Appeal is attached as exhibit 2.

The closing instructions required that an insured closing letter ("CPL"[3]) in a form authorized by the American Land Title Association ("ALTA") be issued in connection with the closings.[4] Westminster and Patriot were issuing agents of title insurer First American and were authorized to issue CPLs in First American's name. (App'x 5, ex 6, O'Connor Dep 97:15-98:25, May 17, 2011.) First American entered into agency agreements with Patriot and Westminster that required the agents to close transactions in accordance with prudent practice and the instructions of lenders. (App'x 4, ex 3, ¶ 2(j).) First American provided its agents with additional instructions to follow when closing mortgage loan transactions. In a 1998 Underwriting Alert, First American warned its agents that double escrow flips suggest fraud and instructed its agents to fully disclose in writing all terms of double escrow transactions to the lender. (App'x 5, ex 1, attached as ex 3.) In this same alert, First American instructed its agents to proceed with land flips only with the guidance of senior management, which would usually require that the closing be cancelled.[5] *See id.*

As instructed by the Bank, the closing agents issued CPLs in First American's name for the subject closings. (App'x 4, ex 2; App'x 6 ex 1, attached as Ex 4.) Each CPL reads in part:

> When title insurance of First American Title Insurance Company is specified for your protection or the protection of a purchase from you in connection with closings of real estate transactions on *land located in the state of Michigan* in which you are to be the seller or purchaser of an interest in the land or a lender secured by a mortgage (including any other security instrument) of an interest in land, the Company, subject to the Conditions and Exclusions set forth below, *hereby agrees to reimburse you for actual loss incurred by you in connection with*

[3] A CPL is sometimes also referred to as an insured closing letter.

[4] ALTA is the national trade association and the voice of the title insurance industry. See American Land Title Association, About ALTA <http://www.alta.org/about/index.cfm> (accessed June 26, 2014).

[5] First American's representative testified that all new agents would be given a disc containing historical Underwriting Alerts. (O'Connor Dep 108:2-10.)

such closing when conducted by the Issuing Agent (an agent authorized to issue title insurance for the Company), referenced herein and when such loss arises out of:

1. Failure of the Issuing Agent to comply with your written closing instructions *to the extent that they relate to* (a) the status of the title to said interest in land or the validity, enforceability and priority of the lien of said mortgage on said interest in land, including the obtaining of documents and the disbursement of funds necessary to establish such status of title or lien, or (b) the obtaining of any other document, specifically required by you, but not to the extent that said instructions require a determination of the validity, enforceability or effectiveness of such other document, or (c) the collection and payment of funds due you, or

2. *Fraud or dishonesty of the Issuing Agent handling your funds or documents in connection with such closings.*

If you are a lender protected under the foregoing paragraph, your borrower in connection with a loan secured by a mortgage on a one to four family dwelling shall be protected as if this letter was addressed to your borrower. [*Id.* (emphasis added.]

Soon after the subject loans were closed, the borrowers defaulted and the Bank foreclosed on its mortgages by advertisement. The Bank purchased the subject properties with credit bids at the foreclosure sales. No evidence was submitted regarding bids made by other parties at these sales. The properties were then sold out of the Bank's real-estate-owned ("REO") inventory. The Bank incurred a total actual loss of approximately $7,000,000 after crediting the proceeds from these REO sales.

B. The properties closed by Patriot.

1. 1766 Golf Ridge Drive, Bloomfield Township.

The Golf Ridge closing was a same day flip. On December 23, 2005, the property was sold by James and Joanna Spear to Michael Kahn for $1.1 million. (App'x 2, ex 5.) Kahn then sold the property to Paul Smith that same day for $2.4 million, with the Bank funding $1.5 million for this purchase. (App'x 2, ex 6.) Patriot closer Jennifer Kojs asserted the Fifth Amendment with regards to her knowledge of this same day flip. (App'x 5, ex.16, Kojs Dep

11:8-15:5, June 20, 2011.) Kojs also asserted the Fifth Amendment with regards to the $325,000 paid to "Titanic Investment Gro [sic]" at closing. (Kojs Dep. p18:12-19:24.) Titanic was affiliated with Randy Saylor and Patriot.[6] Kojs also asserted the Fifth Amendment with regards to the loan payments on the Golf Ridge loan made by Bedford Falls Property Management, another company affiliated with Saylor and Patriot. (Kojs Dep 22:2-25:12).

In May 2012, Kojs and Saylor were charged with conspiracy by the United States Attorney for obtaining fraudulent mortgage loans on numerous properties, *specifically including the Golf Ridge property.* (Ex 5, ¶ 7.) In September 2012, Kojs pleaded guilty to falsifying information regarding straw buyers as charged by the US Attorney. (Ex 6, p 2.)

After the borrower Smith defaulted, the Bank foreclosed by advertisement. In June 2008, the Bank purchased the Golf Ridge property with a credit bid of $1,200,000.00 – $334,834.01 less than the amount owed per the Sheriff's Deed. (App'x 6 p13.) The Bank then sold the property of out REO for $325,000 on or about May 28, 2009, realizing a loss of approximately $1,200,000. (App'x 2, ex 4, Answer Interrog 33.)

2. 1550 Kirkway Road, Bloomfield Township.

The Kirkway transaction was another same day flip. On January 31, 2006, the property was sold by Abby and Keith Kutner to Michael Kahn for $965,000. (App'x 2, ex 10.) According to the warranty deed for this sale, the deed was acknowledged before Kojs. Kojs never disclosed this sale to the Bank. On the same day, Patriot closed the sale of the Kirkway property from Kutner Holdings to Michael Lynett for $2.1 million, with the Bank funding $1.5 million for this

[6] First American alleged in previous litigation that Randy Saylor operated Titanic and Bedford out of Patriot's offices, that Patriot employees Kirk Scheib and Jennifer Kojs prepared, issued, and recorded numerous false and fraudulent documents, and that Kojs allowed Saylor to transfer funds from Patriot's escrow account to Saylor's affiliated companies. (App'x 5, ex 2 at ¶¶ 19, 30-34.)

purchase.[7] Kojs asserted the Fifth Amendment with regards to her knowledge of this same day flip. (Kojs Dep 32:23-33:15.)

In a separate case, borrower Lynett took the deposition of Michael Teaney and questioned him about two HUD-1 settlement statements that were drafted in connection with the Lynett closing. (App'x 5, ex 8.) One version of the HUD-1 represents that Teaney's company, Cobb Financial, received $180,000, which according to Teaney was supposed to be set aside to make loan payments on behalf of Lynett. (App'x 2, ex 9.) Another version of the HUD-1 represents that Cobb Financial received $71,004 and $108,996 went to Westminster. (App'x 2, ex 12.) The $108,996 payment from Patriot was used to close the 1890 Heron Ridge Court transaction. See *infra.* Kojs asserted the Fifth Amendment with regards to moneys being used to make the borrower's loan payments. (Kojs Dep 44).

After the borrower Lynett defaulted, the Bank foreclosed by advertisement. In May 2007, the Bank purchased the Kirkway property with a full credit bid of $1,575,206.02. (App'x 6 p13). The Bank then sold the property of out REO for $440,000 on or about June 18, 2009, realizing a loss of approximately $1,100,000. (App'x 2, ex. 4, Interrogatory no. 33.)

[7] Patriot later recorded an Affidavit (to record lost document) representing that Kahn had quitclaimed the property to Kutner Holdings on January 31, 2006. (App'x 2, ex 11.)

C. The properties closed by Westminster.

1. 13232 Enid Boulevard, Fenton.[8]

The Enid transaction was another same day flip. On December 30, 2005, Michigan Land Development purchased the Enid property for $3.1 million. (App'x 2, ex 21.) Michigan Land Development then sold the property to Fred Matson that same day for $5,500,000, with the Bank funding $3,575,000 for this purchase. (App'x 2, ex 19.) In December 2010, Thomas Keller pleaded guilty to Financial Institution Fraud for using Michigan Land Development to sell inflated real property to straw buyers. (Ex 7.) The final HUD-1 submitted to the Bank by Westminster after funding, shows that the Bank's funds were disbursed to finance both sales of the property, with the first sale being held in escrow until the Bank funded the second sale. (App'x 2, ex 19.) Westminster knew that the Enid transaction was a double escrow flip. (App'x 5, ex 13, Dolan Dep 38, April 21, 2011) And Westminster knew such double escrow transactions were improper, but allowed the closing to proceed. (Dolan Dep 36:12-37:18.)

Westminster's manager Linda Dolan had borrower Matson execute a HUD-1 showing $1,925,000 due from Matson at closing and "debt payoffs" of $360,000 to Andrew Davison, $360,000 to Michigan Land Development, $540,000 to Blue Sky Investments, and $340,000 to Invesco Realty. (App'x 20, ex 20.) The original documents submitted to the Bank indicated that the owner/seller of the Enid property was Raji Zaher. Dolan stopped the closing when the seller name changed from Zaher to Michigan Land Development. (Dolan Dep 22:12-23:1.) Westminster employee Jodie Berbas was then instructed to call the Bank's funder to seek approval for the seller name change. The only record of the conversation is a note by Berbas that says: "Per Kwannah at BOA no survey is needed. She doesn't know anything about an EMD.

[8] Westminster simultaneously prepared a title commitment for Matson's $4 million purchase of another property at 4660 Quarton Road. (App'x 2, ex 24.)

She said it is okay that the seller is different person than originally thought. Owner's policy issued with exceptions." (App'x 5, ex 14, Berbas Dep 9:4-18, March 24, 2011.) Nothing in Berbas's note indicates that Westminster disclosed that the Enid property was being sold to the new seller for $2.4 million less than the reported purchase price or the existence of the double escrow. It was not until days after funding that Westminster sent the Bank a quit claim deed from Zaher to Michigan Land Development disclosing the $3.1 million purchase price. (See App'x 2, ex 4, Answer Interrog 14; App'x 2, ex 22.)

The Bank's closing instructions for the Enid closing state in pertinent part:

> Loan Purpose: Purchase
>
> ***
>
> Contact lender immediately if for any reason you cannot comply with these Instructions . . . . As a closing agent you are financially liable for any loss resulting from your failure to follow these Instructions.
>
> ***
>
> In addition to any conditions listed in the attached Conditions Addendum, the following SPECIAL INSTRUCTIONS must be met:
> MUST APPROVE HUD PRIOR TO CLOSING.
>
> ***
>
> The identity of all payees must appear on the HUD-1.
>
> ***
>
> \+ MAXIMUM 3RD PARTY OR SELLER CONTRIBUTION IS NOT TO EXCEED THE LESSER OF 1) 6.00% OF THE PURCHASE PRICE OR 2) THE ACTUAL CLOSING COSTS.
>
> ***
>
> \+ BANK OF AMERICA MUST REVIEW HUD-1 AND ISSUE AN AUTHORIZATION NUMBER PRIOR TO SIGNING OF CLOSING DOCUMENTS.
>
> \+ BANK OF AMERICA MAY REVOKE THIS COMMITMENT AT ANY TIME IF THERE IS ANY MATERIAL VARIATION OF THE FACTS FROM THOSE STATED IN THE MORTGAGE APPLICATION, CREDIT REPORT, OR ANY OTHER DOCUMENT SUBMITTED IN CONNECTION WITH YOUR APPLICATION.

(App'x 4, ex 4, BOA 370, 375, 376 (emphasis in original).)[9] Westminster made a number of changes to the HUD-1 after the Bank had wired its funds to Westminster without seeking the Bank's approval. (App'x 2, ex 23, Maxwell Dep 144:12-15, March 24, 2011; compare App'x 2, ex 19 (printed December 30, 2005) with App'x 2, ex 20 (printed January 4, 2006).) The revised HUD-1 was not submitted to the Bank until after the Bank's funds had been disbursed by Westminster. (App'x 2, ex 4, Answer Interrog 14). The January 4, 2006 HUD-1 includes changes to lines 103, 201, 206, 220, 301-303, 501, 502, 506, 507, 508, 520, 602, 603, 801, 903, 1302, 1304-1307, and 1400 from the HUD-1 submitted to the Bank for approval. The HUD-1 submitted to the Bank by Westminster for approval did not disclose a "Raji Zaher Land Contract P/O" in the amount of $2,450,884.09 present in the January 4, 2006 HUD-1. (Compare App'x 2, ex 19 line 508 with App'x 2, ex 20 line 508.)

After the borrower Matson defaulted, the Bank foreclosed by advertisement. In June 2007, the Bank purchased the Enid property with a full credit bid of $3,944,267.09. (App'x 6 p13). The Bank then sold the property of out REO for $632,500 on or about September 16, 2009, realizing a loss of approximately $3,300,000. (App'x 2, ex 4, Answer Interrog 33.)

2. 1890 Heron Ridge, Bloomfield Township.

The closing for Heron Ridge was a second generation flip. In May 2005, Mark Conte purchased the Heron Ridge property for $3,850,000. (App'x 2, ex 14.) According to Conte, his daughter Blythe had convinced him to participate in a "property flipping" scheme. (App'x 2, ex 13, Conte Dep 28-29, February 3, 2011.) Conte never visited the home, made a mortgage payment, or paid a utility bill, and was paid $59,000 for acting as the nominal buyer of the property. (Conte Dep 31:4-33:17.)

[9] The Bank detailed some of the violations of its closing instructions for both Westminster transactions in its answers to Westminster's interrogatories. (App'x 2, ex 4, Answer Interrog 8.)

In September 2012, Blythe Conte was charged with conspiracy by a Grand Jury for recruiting straw buyers to purchase inflated properties, *specifically including the Heron Ridge property*, by using fraudulently obtained mortgages. (Ex 8, ¶¶ 4, 7, and 10.) In April 2014, Blythe pleaded guilty to misprision of a felony relating to the fraudulent mortgage scheme. (Ex 9, p 2.)

The previously inflated Heron Ridge property was then sold again on January 31, 2006 to Jo Kay James for $4,000,000. The Bank financed $2.8 million of the purchase price. (App'x 2, ex 15.) James testified that she never occupied the Heron Ridge property, never made mortgage payments, never made a down payment at closing, and was only supposed to own the property for a few months before it was flipped again. (App'x 4, ex 1, James Dep 9, 34, 38-39, 70, February 3, 2011.) James further testified that she thought she was agreeing to purchase a different property, and first learned of the Heron Ridge property at the Westminster closing. (*Id.*, 45.) James was told at closing not to worry about the change in properties. *Id.*, 45-47.) James also testified that everyone at the closing table knew she was purchasing the home as an investment, and not as a primary residence as represented. (*Id.*, 71; App'x 2, ex 26.)

The Bank's closing instructions for the Heron Ridge closing included identical conditions as the Enid instructions quoted above. The HUD-1 for the Heron Ridge transaction represents that James made an earnest money deposit in the amount of $1,260,000 and that Conte had to bring $545,899.53 to close the transaction. (App'x 2, ex 15.) Documents produced by Westminster show that this was not true and that the money required to close had come from an undisclosed second mortgage and a check from Patriot.

Unbeknownst to the Bank, James contemporaneously took out a $420,000 second mortgage closed by Westminster. (App'x 2, ex 17.) This secondary financing was not approved by the Bank. The Bank agreed to loan James $2,800,000 to purchase a home purportedly worth $4,000,000 – for a combined loan-to-value of 70 percent. With James's additional $420,000 loan, the combined loan-to-value was greater than 80 percent. Westminster also received $108,996 from Patriot (from the Kirkway transaction), a third party contribution that was not disclosed to the Bank by Westminster. (App'x 2, ex 18.) The combined total of the funds from the second mortgage and Patriot alone represented third-party contributions in an amount prohibited by the closing instructions since they were greater than the actual closing costs of $17,548.20. (App'x 2, ex 15, line 206.) But Westminster still needed additional funds to balance the transaction. The HUD-1 represented that James had received $27,398.53 at closing, purportedly as a refund of the earnest money deposit. (App'x 2, ex 15.) Westminster's closing file shows that James endorsed the check that she received from Westminster back to Westminster to provide the remaining funds that were represented on the HUD-1 as having been paid by the seller. (App'x 2, ex 27.)

After the borrower James defaulted, the Bank foreclosed by advertisement. In January 2007, the Bank purchased the Heron Ridge property with a credit bid of $2,650,000.00 – $218,979.52 less than the amount owed per the Sheriff's Deed. (App'x 6 p 13). The Bank then sold the property of out REO for $1,150,000 on or about April 22, 2009, realizing a loss of approximately $1,700,000. (App'x 2, ex 4, Answer Interrog 33.)

D. Summary of proceedings.

In August 2010, the Bank filed its complaint in this action. (App'x 7.) The Bank brought claims against Patriot and Westminster for breach of the closing instructions and negligent misrepresentation and claims against First American for breach of the CPLs.[10] Additional claims were asserted by the Bank against the appraisers, the broker, the broker's owner, and Kirk Scheib, the purported owner of Patriot. Only Westminster and First American defended the Bank's claims, and the other defendants were either defaulted or dismissed.

Westminster and First American each moved for summary disposition. The Bank responded to both motions and requested partial judgment pursuant to MCR 2.116(I)(2) as to its CPL claims for the Patriot closings. After full briefing and a hearing on Defendants' motions, the Circuit Court issued an opinion and order granting First American and Westminster summary disposition under MCR 2.116(C)(10). (App'x 8.) The Circuit Court found that there was no breach of contract by Westminster or First American under the Court of Appeals' decision in *New Freedom*. The Bank filed a motion for reconsideration and attached a Declaration of William Jaquinde containing the proffered expert's qualifications and opinions that Patriot and Westminster failed to follow the Bank's closing instructions and closed the transactions dishonestly. (App'x 2, ex 3, attached as exhibit 10.) The Circuit Court denied the Bank's motion for reconsideration, (App'x 9) and issued a final order on December 15, 2011 (App'x 1).

The Bank filed its claim of appeal as of right on December 21, 2011 and filed its appellant brief on February 14, 2012. (COA docket no. 10.) The Court of Appeals took oral argument on August 13, 2013 and issued an unpublished per curiam opinion on March 27, 2014 with a dissent by Chief Judge Murphy. (Ex 1.) The Court of Appeals: (1) reversed the Circuit Court as to First American's liability for the Golf Ridge closing because there was a genuine

[10] The Bank agreed to voluntarily dismiss its negligent misrepresentation claim against Westminster in its response to Westminster's motion for partial summary disposition, in which it argued that a closing agent cannot be held liable in tort under *Wormsbacher v Phillip R Seaver Title Co*, 284 Mich App 1; 772 NW2d 827 (2009). (App'x 12, pp 9-10.) First American filed a concurrence as to Westminster's motion.

question of fact that Patriot knew of the undisputed fraud scheme and the Bank's claims were not barred by the full credit bid rule; (2) held that there was a genuine question of fact that Patriot knew of the undisputed fraud scheme for the Kirkway closing, but also ruled that claims against First American were barred by the full credit bid;[11] (3) affirmed the Circuit Court's granting of summary disposition to First American for the Westminster closings because there was no question of fact as to whether Westminster engaged in "fraud or dishonesty" within the meaning of the CPL; and (4) affirmed the Circuit Court's granting of summary disposition to Westminster because the Bank abandoned its claims under paragraph 1 of the CPLs and failed to establish a causal link between the alleged breach and damages.[12] The Court of Appeals' rulings left only the Bank's claims as to the Golf Ridge closing. The Bank's loss for this closing is approximately $1,200,000, and the deficiency at the time of the foreclosure sale was approximately $335,000. (App'x 6 p 13; Answer Interrog 33.) Chief Judge Murphy agreed with the majority's finding that the Bank's claims for the Kirkway and Enid closings were barred by the full credit bid rule under *New Freedom*, but would have requested a conflict panel challenging *New Freedom*. Chief Judge Murphy disagreed with the majority's findings that there was no question of fact as to whether Westminster engaged in "fraud or dishonesty" for the Heron Ridge and Enid closings and that the Bank could not pursue Westminster for breach of the separate closing instructions.

On April 17, 2014, the Bank timely filed a motion for reconsideration of the Court of Appeals per curiam opinion. (COA docket no. 64.) On May 22, 2014, the Court of Appeals issued an order denying the Bank's motion for reconsideration – with Chief Judge Murphy once

[11] The full credit bid rule was not ruled on by the Circuit Court, but it was briefed to the Circuit Court, addressed in appellate briefs, and discussed at oral argument.

[12] The court also held that the full credit bid rule barred claims relating to the Enid closing.

again dissenting. (COA docket no. 71.) This application for leave to appeal is filed within 42 days of the order denying reconsideration.

ARGUMENT

A. Michigan has a significant interest in combating and discouraging the type of mortgage fraud facilitated by Patriot and Westminster in this case.

Recognizing that mortgage fraud has traditionally been a significant statewide problem, in 2011 the State amended the Michigan Penal Code to create the felony of residential mortgage fraud – codified as MCL 750.219d. (Senate Legislative Analysis, SB 43, 249-252, HB 4462, 4478, 4492, January 18, 2012, p 1, attached as ex 11.) The legislature sought to tailor a statute to specifically criminalize mortgage fraud (*Id.* pp 1, 6-7.) In so doing the State acknowledged the harms caused to borrowers and mortgage lenders by mortgage fraud in its many forms (including property flipping, falsification of borrower information, and inflated appraisals). Under § 750.219d, any person, including a closing agent, who makes a false statement or conceals a material fact during the mortgage lending process is guilty of a felony punishable by 20 years in prison and a $500,000 fine (where as here, the loan exceeds $100,000).

It is undisputed that the subject mortgage transactions were fraudulent. (See Ex 1, Per Curiam Op, p 8.) Multiple individuals, including the closing agent for the Patriot closings, have pleaded guilty to federal crimes relating to these transactions. (See exs 6, 7, 9.) The mortgage fraud in this case (property flips, falsified borrower information, inflated appraisals) is exactly the type of fraud that the State sought to address with § 750.219d. (Senate Legislative Analysis, *supra*, pp 1, 6-7.) If the subject closings occurred today, both Patriot and Westminster could be charged with residential mortgage fraud for concealing material facts from the Bank. See § 750.219d(1)(a). In stark contrast to this legislative history, the Court of Appeals' decisions in *New Freedom* and this case would leave these same parties relieved of civil liability for the millions of dollars in losses caused by the mortgage fraud which they and their agents facilitated.[13] Not only will these erroneous decisions cause a material injustice to the Bank, the decisions condone mortgage fraud and will bar countless other lenders and borrowers from holding third parties civilly liable for their felonious conduct.

B. Closing instructions and closing protection letters serve an important function in protecting Michigan lenders and borrowers from fraudulent transactions and errors by closing agents.

Closing agents perform a necessary and vital function in mortgage loan transactions. Because closing agents have direct contact with the transaction participants and the exchange of money, they are the best and last opportunity to detect and prevent mortgage fraud. Lenders provide these agents with detailed closing instructions to ensure that transactions close to the lender's specifications. If the lender suffers a loss, the lender can pursue the closing agent if the loss resulted from the agent's failure to follow the closing instructions. If, as is customary, the lender also received a CPL, the lender can separately pursue the title insurer if the loss resulted from conduct covered by the CPL. (App'x 2, ex 3, p 3.) These separate contracts – closing instructions and CPLs – govern the vast majority of mortgage loan transactions closed in Michigan.[14] These contracts are entered into between sophisticated entities (lenders, closing agents, and title insurers), and should be enforced according to their unambiguous terms. Such

[13] Both Defendant First American and Westminster have the ability to make the Bank whole. First American is a leader in title insurance services with billions of dollars in assets while Westminster is covered under a $2 million dollar insurance policy and backed by the billions of dollars in assets held by its parent national construction company, Toll Brothers, Inc.

[14] According to the U. S. Department of Housing and Urban Development, in just the 12 months ending September 2011, there were more than 75,000 home sales in the Detroit-Warren-Livonia Housing Market alone. Ex. 12. The Detroit-Warren-Livonia Housing Market is defined as Wayne, Livingston, Oakland, Lapeer, Macomb, and St. Clair Counties.

enforcement of these standard contracts will aid in the prevention of mortgage fraud to the benefit of lenders and borrowers alike.

1. Closing agents are required to follow all the lender's instructions and this duty is not modified or limited by separate agreements by title insurers to indemnify against losses arising out of the failure to follow certain and limited instructions.

As is the custom and practice with residential mortgage loan transactions, the Bank provided the closing agents with written closing instructions prior to the closing of the subject transactions. (Ex 10, Jaquinde Decl, p 1.) Westminster agreed to be financially liable for any losses resulting from its failure to follow *any* of these instructions. (App'x 4, ex 4.) These standard agreements satisfy the elements necessary to constitute valid contracts under Michigan law. See *Thomas v Leja*, 187 Mich App 418, 422; 468 NW2d 58 (1991).[15] In fact, closing agents like Westminster have argued that their *only* duty to lenders is *contractual*. (App'x 12, pp 9-10). And while this argument confuses *title* agents with *closing* agents, it aptly illustrates the importance of closing instructions in defining the expectations of the parties. Compare *Wormsbacher*, p 7-8 with *Smith v First Nat'l Bank & Trust*, 177 Mich App 264, 270; 440 NW2d 915 (1989). The majority, in a mystifying conflation of concepts, only gave these key agreements scant attention, concluding that the closing instructions were "modified and limited" by the separate CPL contracts between the Bank and First American. (Ex 1, Per Curiam Op, pp 15-16.)

The CPLs – separate contracts to which Westminster is not a party – state:

> [First American], subject to the Conditions and Exclusions set forth below, hereby agrees to reimburse you for actual loss incurred by you in connection with such

[15] Other states have expressly held that a lender's closing instructions constitute a contract between the lender and the closing agent. See e.g., *Plaza Home Mortgage, Inc v North American Title Co, Inc*, 184 Cal App 4th 130, 139 (2010) and *Old West Annuity & Life Ins Co v Progressive Closing & Escrows, Inc*, 74 Fed Appx 4 (10 CA 2003), (App'x 4, ex 5).

closing when conducted by the Issuing Agent (an agent authorized to issue title insurance for the Company), referenced herein and *when such loss arises out of*:

1. Failure of the Issuing Agent to comply with your written closing instructions *to the extent that they relate to* (a) the status of the title to said interest in land or the validity, enforceability and priority of the lien of said mortgage on said interest in land, including the obtaining of documents and the disbursement of funds necessary to establish such status of title or lien, or (b) the obtaining of any other document, specifically required by you, but not to the extent that said instructions require a determination of the validity, enforceability or effectiveness of such other document, or (c) the collection and payment of funds due you[.]

CONDITIONS AND EXCLUSIONS

A. The Company will not be liable to you for loss arising out of:

1. Failure of the Issuing Agent to comply with your closing instructions which require title insurance protection inconsistent with that set forth in the commitment issued by the Company. Instructions which require the removal of specific exceptions to title or compliance with the requirements contained in said commitment shall not be deemed to be inconsistent. [Ex 4 (emphasis added.]

Nothing in the closing instructions signed by Westminster indicates an intent to limit Westminster's duty under the agreements to just the *very limited* closing instructions that would *also* trigger liability under this CPL language.[16] (App'x 4, ex 4.) First American itself required Westminster to comply with *all* of the Bank's closing instructions, (see App'x 4, ex 3; COA docket no. 32, ex 2) and the CPLs expressly acknowledge that the Bank may incur losses arising from the failure to follow closing instructions that are *not* covered by the CPLs. But under the majority's clearly erroneous holding, the Bank has no recourse for losses not covered by the CPLs, and the only way for lenders to hold closing agents to their full agreements would be for the lender to forgo "the financial resources of the national title insurance underwriter" provided

[16] See *New Freedom*, pp 82-83 for an analysis of the limited nature of closing instructions that fall under paragraph 1 of a CPL.

by CPLs. *New Freedom*, p 80. This decision is unprecedented, contrary to industry standards, and will drastically reduce the ability of lenders to control closings and prevent mortgage fraud.

For instance, ALTA has for years been working with the Mortgage Bankers Association of America and the American Escrow Association to develop a set of Uniform General Closing Instructions for closing residential real estate transactions. The current draft is 46 pages long and includes numerous instructions that have nothing to do with the status of a lender's mortgage lien, or other items that would trigger liability under paragraph 1 of a CPL like those issued by First American. (COA docket no. 32, ex 3.) Notably, these proposed uniform instructions require a closing agent to stop a closing if it obtains actual knowledge of misrepresentations made by a person to the transaction. (*Id.*, p 35.) Under the majority's holding, closing agents would be free to disregard similar instructions designed to prevent mortgage fraud of the kind addressed by the State in MCL 750.219d.

The Bank's closing instructions required Westminster to get HUD-1 approval *prior* to closing, identify all payees, and limit contributions from third parties. (App'x 4, ex 4.) Westminster was not free to disregard these instructions simply because they do not relate to the (a) status of the Bank's lien, (b) the obtaining of documents, or (c) the payment of funds. The Court of Appeals' failure to give effect to the intentions of the parties in agreeing to these instructions will cause material injustice to the Bank and encourage other Michigan closing agents to disregard important instructions designed to prevent mortgage fraud.

Hedging its unprecedented ruling, the majority ruled in the alternative that the Bank's deficient underwriting policies – and not Westminster's failure to follow the closing instructions – were the cause of the Bank's losses. (Ex 1, Per Curiam Op, p 16.) This alternative ruling is no less clearly erroneous. Defendants did not proffer expert testimony regarding the Bank's underwriting practices in general or as to the specific transactions. Instead, Defendants simply argued that the Bank *might* have discovered the fraud had it verified the borrower's stated incomes. (See Ex 1, Per Curiam Op, pp 3-4.) Not only does this argument falsely assume that Michigan mortgage fraud is limited to stated income loans, it also ignores the growing body of case law that supports the position that a lender's underwriting is irrelevant in the context of breach of contract claims by the lender. (COA docket no. 32, pp 8-9.) See e.g., *Fifth Third Mortgage Co v Chicago Title Ins Co*, 692 F3d 507, 511 (CA 6, 2012) (title policy); *JPMorgan Chase Bank, NA v First American Title Ins Co*, 795 F Supp 2d 624, 633 (ED Mich 2011), aff'd, 750 F3d 573 (CA 6, 2014) (CPL); *FDIC v First American Title Ins Co*, 2011 US Dist LEXIS 94842 (CD Cal, August 24, 2011) (closing instructions); and *FDIC v Property Transfer Service., Inc*, 2013 US Dist LEXIS 144663 (SD Fla, Oct 4, 2013) (CPL).[17]

The Bank introduced sufficient evidence that the subject loans would not have closed had Westminster properly followed these instructions. (See e.g., App'x 2, ex 4, Answer Interrog 8.) Westminster itself argued that this would be an "interesting question" for the jury. (App'x 12, p 6.) Yet, the majority concluded that there was no question of fact as to this issue. The majority clearly erred in finding that reasonable minds could not differ as to the conclusions to be drawn from the evidence in this case. See *Bean v Directions Unlimited*, 462 Mich 24, 34 n 12; 609 NW2d 567 (2000) ("The Court of Appeals role is not to 'find' facts, but rather, to review the trial court's decision without substituting its view of the evidence for the jury's.") The Bank should be permitted to present this evidence to the jury in order to determine if Westminster's breaches were a legal cause of the Bank's losses. *McMillan v State Highway Comm*, 426 Mich 46, 63 n 8; 393 NW2d 332 (1986).

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[17] All unpublished cases are attached as exhibit 13.

(See Ex 1, Dissent Op, p 5.)

2. Closing protection letters provide important and expansive protection for lenders and borrowers against the fraud or dishonesty of closing agents.

It is an unfortunate reality of the lending industry that there is little a lender can do to prevent mortgage fraud if a closing agent, who has direct contact with the perpetrators and the purported exchange of funds, is complicit, or an active participant, in the scheme. For this reason, lenders – nationwide – generally will not entrust money or loan documents to closing agents unless the title insurer has issued a CPL covering the closing. Davis, *The Law of Closing Protection Letters*, 36 Tort & Ins L J 845 (2001); *New Freedom*, p 80.

The subject CPLs read:

> When title insurance of First American Title Insurance Company is specified for your protection or the protection of a purchase from you in connection with closings of real estate transactions on *land located in the state of Michigan* in which you are to be the seller or purchaser of an interest in the land or a lender secured by a mortgage (including any other security instrument) of an interest in land, the Company, subject to the Conditions and Exclusions set forth below, *hereby agrees to reimburse you for actual loss incurred by you in connection with such closing when conducted by the Issuing Agent (an agent authorized to issue title insurance for the Company), referenced herein and when such loss arises out of*:
>
> 2. *Fraud or dishonesty of the Issuing Agent handling your funds or documents in connection with such closings.*
>
> If you are a lender protected under the foregoing paragraph, *your borrower in connection with a loan secured by a mortgage on a one to four family dwelling shall be protected as if this letter was addressed to your borrower*. [Ex 4 (emphasis added).]

In *New Freedom*, the Court of Appeals construed similar CPL language,[18] and held that the title insurer was not liable under Paragraph 2 of the CPLs because the lender "presented no evidence

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[18] The CPLs in *New Freedom* covered the "fraud or dishonesty *in* handling your funds or documents in connection with such closings." (Ex 1, Dissent Op, p 2.)

that [the closing agent] was aware at closing that [the borrower] did not intend to occupy the property," and "there [was] no evidence that [the closing agent] was aware of [the borrower's] misrepresentation.[19]" *New Freedom*, p 82. The *New Freedom* court also found that discrepancies in the HUD-1 were not actionable under a CPL because the document "did not belong" to the lender. *Id.*, p 83.

First American argued that *New Freedom* adopted a very narrow reading of CPLs, and the Circuit Court agreed, finding that the fraud or dishonesty must be linked to "concealed disbursements, shortages, or unpaid prior lien holders." (App'x 8, p 2.) Such a narrow reading is contrary to the overwhelming weight of CPL case law, which has read these indemnity contracts expansively when dealing with fraudulent mortgage loan transactions like those at issue in this case. See e.g., *First American Title Insurance Co v Vision Mortgage Corp*, 298 NJ Super 138; 689 A2d 154 (1997); *JPMorgan Chase Bank, NA v First American Title Ins Co*, 2011 US Dist LEXIS 123716 (ED Mich, Oct, 26, 2011), aff'd, 750 F3d 573 (CA 6, 2014); *Walsh Securities, Inc v Cristo Prop Mgt, Ltd*, 858 F Supp 2d 402, 419 (D NJ 2012); and *FDIC v Property Transfer Services, Inc*, 2013 US Dist. LEXIS 144663 (SD FL Oct. 4, 2013). First American cited no CPL cases to the Court of Appeals, and relied solely on its narrow interpretation of *New Freedom*.

In construing paragraph 2 of the CPLs, the majority correctly disregarded First American's self serving interpretation and found that the protection under paragraph 2 of the CPLs is not limited to "concealed disbursements, shortages, or unpaid prior lien holders.[20]" (Ex

[19] *New Freedom* was originally unpublished, and leave to appeal to this Court was not sought by any party.

[20] The court also stated its belief that the *New Freedom* panel misread the word "your" to modify "documents" rather than only "funds."(Ex 1, Per Curiam Op, p 9 n 5.) As such, the court would have considered discrepancies in all documents (including the HUD-1s) if not for *New Freedom*. (See *id.*)

1, Per Curiam Op, p 10.) According to the majority, the terms "fraud or dishonesty" are "quite broad" and include "constructive fraud – an act of deception or a misrepresentation without an evil intent" and "suppressing facts—silent fraud—where circumstances establish a legal duty to make *full* disclosure." (*Id.*, p 9 [Emphasis added].) This is in line with other authorities interpreting similar CPL contracts. *See supra.*

The Court of Appeals then performed a detailed analysis of the evidence presented by the Bank as to the fraud or dishonesty of Patriot. The court correctly drew an adverse inference from closing agent Kojs's assertion of her Fifth Amendment privilege as to subject closings,[21] and correctly inferred Patriot's knowledge of the fraud from First American's underwriting alert regarding fraudulent double escrows and flips and the proffered expert testimony of William Jaquinde. (See Ex 1, Per Curiam Op, pp 10-11.) Based on this evidence, the court concluded that there was a genuine issue of fact that Patriot engaged in "fraud or dishonesty" in closing the Golf Ridge and Kirkway transactions. Specifically, the majority found that "[t]aken together, plaintiff's proposed expert testimony and First American's underwriting alert would provide *significant* evidence from which to infer that the closing agents in this case knew or *should have known* the transactions at issue were fraudulent." (*Id.*, pp 8-9 (Emphasis added).)

The majority, however, completely disregarded this same "significant" evidence in erroneously concluding that there was no issue of fact that "Westminster knew of or participated in the underlying fraud." (*Id.*, p 14.) Just like Patriot, Westminster was warned by First American to avoid closing double escrows and flips because they "suggest fraud." (Ex 3.) Further, proffered expert William Jaquinde found that *both* Patriot *and* Westminster engaged in dishonest

[21] Clearly, Kojs's assertion was warranted as she later was charged by the US Attorney with conspiracy relating to these fraudulent closings. (Ex 5.)

conduct in closing the subject transactions. (Ex 10.) The majority's finding as to Westminster's dishonesty was clearly erroneous and will cause material injustice to the Bank, and other lenders (and their borrowers) bringing claims under similar CPLs.[22]

The Bank submitted funds and documents to Westminster with the expectation that the closing agents would not commit "fraud or dishonesty." In closing the Enid transaction, Westminster failed to follow First American's instructions regarding the disclosure of suspicious double escrows. (Ex 3.) It was only after the Bank's funds had been disbursed that Westminster provided the Bank with documents disclosing that the property had supposedly increased in value by $2.4 million in one day. (See App'x 2, ex 4, Answer Interrog 14.) Moreover, unapproved changes to the HUD-1 indicate that Westminster knew that the borrower did not provide the required down payment to close the subject transaction.[23] (App'x 2, ex 19.) Westminster had further reason to know that the borrower would not occupy the Enid property as represented because it had simultaneously prepared a title commitment for the borrower's purchase of a $4 million property at 4660 Quarton Road.[24] (App'x 2, ex 24.) In closing the Heron Ridge transaction, Westminster failed to disclose the fact that the borrower made no down payment, or that closing funds came from a second mortgage and Patriot. (App'x 2, ex 17.) The Bank further presented evidence via testimony from the borrower that everyone at closing was aware she was purchasing the Heron Ridge property as an investment – not a primary residence as represented to the Bank. (James Dep 71.)

[22] This opinion contains the Court of Appeals' most comprehensive analysis of the "fraud or dishonesty" CPL paragraph. Similar CPLs are at issue in two other appeals pending in the Court of Appeals. See Court of Appeals Case Nos. 311798 and 316538.

[23] Lenders require borrowers to provide down payments from their own funds because such borrowers are less likely to default (thereby forfeiting their down payment investment).

[24] Lenders have different loan guidelines for loan secured by primary residence as opposed to riskier loans secured by investment properties.

Under the majority's well reasoned definition of "fraud or dishonesty," this evidence (with First American's underwriting alert and William Jaquinde's proffered expert testimony) is sufficient to create an issue of fact as to CPL liability under paragraph 2. This evidence should be presented to the jury, and the majority clearly erred in finding that reasonable minds could not differ as to the conclusions to be drawn from this evidence. See *Bean*, p 34, n 12; *Michigan Nat'l Bank-Oakland v Wheeling*, 165 Mich App 738, 745; 419 NW2d 746 (1988) (state of mind is "hardly ever appropriate" for summary judgment). The majority's uneven application of its reasoning to First American's CPLs leaves the insurer free from liability for the losses arising from Westminster's suppression of material facts (today, such suppression would subject the closing agent to MCL 750.219d). The majority's decision sets an alarming precedent favoring the professionals that facilitate mortgage fraud at the expense of lenders and borrowers who suffer the losses caused by this fraud. This decision is especially chilling when juxtaposed with the majority's opinion to "modify and limit" a lender's closing instructions. In practice, the majority has advocated for a system in which a lender or borrower has no recourse under a CPL unless the closing agent admits to committing fraud or takes the Fifth Amendment to all questions regarding the closing.

C. The full credit bid rule was developed to protect mortgagors – not to relieve third party wrongdoers like Defendants from liability unrelated to the secured debt.

The Bank (as mortgagee) foreclosed on the subject properties by advertisement – a process that has always been governed entirely by statute in Michigan. *Doyle v Howard*, 16 Mich 261, 264 (1867). Under the foreclosure by advertisement act (MCL 600.3201 *et seq.*), a mortgagee has the right to purchase the property securing its debt with a credit bid. MCL 600.3228; *Griffin v Union Guardian Trust Co*, 261 Mich 67, 69; 245 NW 572 (1933) (actual payment to the sheriff by mortgagee would be an "idle gesture"). After the mortgagee bids on the advertised property, the mortgagor, or any person claiming under the mortgagor, has a certain amount of time to redeem the property by paying the bid amount and required fees. § 600.3240. If the property is not redeemed, the mortgagee then gets title to the property (subject to any prior liens). § 600.3236. In addition to receiving title to the property, the mortgagee is permitted to seek a deficiency judgment against the mortgagor, or other person liable on the debt, but the mortgagor can defeat the deficiency judgment to the extent the mortgagor can show the amount bid was substantially less that the true value of the property. § 600.3280.

1. Michigan's anti-deficiency statute is designed to protect mortgagors and it encourages full credit bids in order to bring certainty to the rights and liabilities of mortgagors and mortgagees.

Michigan's anti-deficiency statute provides that a "mortgagor, trustor or other maker of any such obligation, or any other person liable thereon" can defeat a deficiency judgment if it is shown that the property was "fairly worth" the amount of the debt secured or substantially more than the amount bid. See MCL 600.3280. The statute is clear in its intent to affect only the rights of mortgagees and mortgagors, and the statute has remained virtually unchanged since the Great Depression.[25] *Guardian Depositors Corp v Hebb*, 290 Mich 427, 430; 287 NW 796 (1939). At least one principal purpose of the statute was to prevent a mortgagee from obtaining a deficiency judgment and title to property of greater value than the amount of the debt secured by the mortgage.[26] *Bankers Trust Co v Rose*, 322 Mich 256; 33 NW2d 783 (1948).

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[25] Like many states during the Great Depression, Michigan enacted this statute to protect the ever-growing number of defaulting home owners. See Comment, *The Effect of New Deal Real Estate Residential Finance and Foreclosure Policies Made in Response to the Real Estate Conditions of the Great Depression*, 57 Ala L Rev 231, 239-240 (2005).

[26] A previous statute limited the mortgagee's right to seek a deficiency judgment to the balance of the debt remaining "unsatisfied" after the sale. *Winsor v Ludington*, 77 Mich 215, 219; 43 NW 866 (1889).

A corollary of this anti-deficiency statute is that if a mortgagee bids the total debt (a full credit bid), the debt is discharged and there is no right of deficiency against the mortgagor. See *Bank of Three Oaks v Lakefront Properties*, 178 Mich App 551, 555; 444 NW2d 217 (1989). The intent of the legislature was to force an election of remedies by a mortgagee concerning a single debt. See *Church & Church In. v A-1 Carpentry*, 281 Mich App 330, 340; 766 NW2d 30 (2008). One of the major reasons for this rule is to foster certainty as to the mortgagor's rights. See *Smith v General Mortgage Corp*, 402 Mich 125, 129; 261 NW2d 710 (1978). If a full credit bid is made, the mortgagee forfeits the right to pursue the mortgagor for a deficiency and avoids the need for a hearing or trial as to the "fair worth" of the property. See *Talmer Bank & Trust v Parikh*, 304 Mich App 373, *16, 21; __ NW2d __ (2014). And the mortgagor has the certainty of knowing that no deficiency judgment can be had. Both mortgagee and mortgagor benefit from full credit bids. See e.g., *Washington v Bac Home Loans Servicing, LP*, 2013 US Dist LEXIS 142256 (ED Mich Oct 2, 2013) ("such bids actually help a borrower because in such situation the borrower 'is no longer liable for the debt'").

The Bank made full credit bids on the Kirkway and Enid properties. In bidding the full amount of the debt, the Bank merely decided that the best way to mitigate its losses for these loans was to forgo the right to collect any deficiency from the straw buyers and attempt to obtain marketable title to the collateral properties. Defendants did not contend that the Bank's bids were market bids, or that the Bank's bids prevented others from purchasing the properties, or that the properties were worth more than a fraction of the Bank's loaned funds. Defendants merely argued that they were relieved from their contractual responsibility because *New Freedom* extended the full credit bid rule beyond mortgagors and guarantors.

2. *New Freedom's* **extension of the protections provided to mortgagors by Michigan's anti-deficiency statute to shield third party wrongdoers was clearly erroneous and will causes material injustice to victims of mortgage fraud.**

In *New Freedom*, the Court of Appeals ruled that a full credit bid not only discharged a mortgagor's obligations under the secured debt, but it also barred recovery of losses against certain third party wrongdoers.[27] *New Freedom*, p 63. In this case, the dissent noted that the full credit bid rule (and § 600.3280) was designed to protect borrowers and "should not work to the benefit of nonborrower third parties, especially where [like here] fraud is involved." (Ex 1, Dissent Op, p 4.) The majority too expressed its hesitation about *New Freedom* in its "Prologue." (Ex 1, Per Curiam Op, p 7.) Despite this disagreement, the court rejected the Bank's arguments that *New Freedom* should be narrowly applied,[28] and ruled that the full credit bid rule applied to the Bank's claims under *New Freedom* (See Per Curiam Op, p 7, Dissent Op, p 3).

For over a hundred years prior to *New Freedom*, Michigan jurisprudence had applied the full credit bid rule only to mortgagors and those having rights or liabilities under the secured debt being foreclosed. All of the Michigan cases cited in *New Freedom* involved deficiency actions against either mortgagors or guarantors, cases that fall directly within the purview of § 600.3280. Michigan's foreclosure by advertisement system is governed entirely by statute and there is simply no legislative evidence or justification (in § 600.3280 or otherwise) to support the extension of the full credit bid rule to shield third parties from civil liability unrelated to the discharged debt. In making its new rule, the *New Freedom* court plainly missed the crucial distinction that anti-deficiency laws by their plain language were intended to protect mortgagors,

[27] Again, leave to appeal to this Court was not sought in *New Freedom*.

[28] For instance, the court acknowledged that *New Freedom* did not specifically discuss the application of the full credit bid rule to CPL claims. (Per Curiam Op, p 12, Dissent Op, p 3.)

and were never intended to immunize wrongdoers from the consequences of their fraudulent or tortious conduct.

By extending the full credit bid rule in such a broad and unexpected way, *New Freedom* judicially legislated a new rule. This new rule was contrary to long standing Michigan jurisprudence and the State's strong interest in combating mortgage fraud (as confirmed by the enactment of MCL 750.219d). Extending the full credit bid rule to claims against third parties like Defendants First American and Westminster condones mortgage fraud by causing the Bank to bear the full losses caused by the fraud facilitated by Defendants. Mortgage fraud is a significant problem in Michigan (Ex 11, Senate Legislative Analysis, *supra*, p 1), and its perpetrators should not be absolved of civil liability just because the unrelated debt is extinguished. The Bank – which is slated to lose millions of dollars as a result of this unreasonable application of foreclosure law – is not the only one harmed be this unjust rule.

Mortgagors will be harmed by *New Freedo*m's misapplication of the full credit bid rule because they will face greater uncertainty regarding potential deficiency judgments.[29] As recognized by the Michigan legislature, mortgage fraud can take years to discover. (Ex 11, Senate Legislative Analysis, *supra*, p 7.) If *New Freedom* remains the law, it will be in the best interests of mortgagees to avoid full credit bids (and to thereby preserve the right to pursue deficiency judgments against mortgagors) in case the mortgagee later discovers that it was the victim of mortgage fraud.[30] As such, the *New Freedom* rule does not foster certainty as to mortgagor's rights – one of the guiding reasons for the rule in the first place. See *Smith*, p 129.

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[29] The statute of limitations for actions founded upon covenants in mortgages of real estate is ten years. MCL 600.5807(4).

[30] The Federal Housing Finance Agency has suggested that the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) seek to recover more deficiency judgments against borrowers. (Ex 14.)

RELIEF SOUGHT

For the foregoing reasons, Plaintiff/Appellant Bank of America respectfully requests that this Honorable Court:

1. overrule *New Freedom* and reverse the holdings of the Court of Appeals' March 27, 2014 per curiam opinion as they relate to the full credit bid rule;

2. reverse Parts IV and V of the Court of Appeals' March 27, 2014 per curiam opinion;

3. remand to the Circuit Court accordingly; and

4. order such other relief that this Court deems equitable and just.

Respectfully submitted,

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The *New Freedom* rule also creates an incentive for mortgagees to seek recovery from unsophisticated borrowers rather than pursuing sophisticated real estate professionals or fraudsters liable to the mortgagee under contract (like CPLs and closing instructions) or tort law.

Respectfully, the Court should overrule *New Freedom* as clearly erroneous and allow the Bank to pursue Defendants for its actual losses.[31] The Bank's bids should be of no consequence as to the rights and liabilities between the Bank and Defendants. Because no third party monies were received by the Bank in connection with the foreclosure sales, it sustained the same actual loss regardless of what bids were made.[32] If the Court does not overrule *New Freedom*, it should in the alternative, give *New Freedom* only prospective effect. See *Bolt v City of Lansing*, 238 Mich App 37, 44; 604 NW2d 745 (1999). The Bank made its credit bids prior to the decision in *New Freedom* (App'x 6 p 13) and could not have anticipated that the Court of Appeals would create such a drastically new rule. In *Smith*, this Court was asked to apply the full credit bid rule to a new situation involving the rights of insurance proceeds *between the mortgagor and mortgagee*. The Court ruled that the mortgagee's rights to the insurance proceeds were terminated by the full credit bid rule when the debt (which created the insurable interest in mortgagee) was extinguished. *Id.*, pp 126-128. The Court, however, refused to apply the rule retroactively because it would be unfair in that case. *Id.*, p 130. A similar result is even more

[31] "Actual loss" under a CPL equals the total amount owed on the loan minus amounts actually received. See e.g., *JPMorgan Chase Bank, NA v First American Title Ins Co*, 750 F3d 573, pp * 26-27 and *Property Transfer Services*, pp *55-56.

[32] Rather than relying on a legal fiction created to prevent mortgagees from receiving a double recovery against mortgagors, Defendants should instead be required to argue (and prove as an affirmative defense) that the Bank's credit bids somehow amounted to a failure to mitigate damages. See *Reinardy v Bruzzese*, 368 Mich 688, 691; 118 NW2d 952 (1962).

appropriate in this case because the Bank's claims are completely independent of the secured debt and do not involve the rights and liabilities as between mortgagors and mortgagees.[33]

First American entered into contracts to reimburse the Bank for its actual losses and Westminster entered into contracts accepting financial liability for losses resulting from its failure to follow the Bank's closing instructions. Defendants' liability under these contracts has nothing to do with the borrowers' liability under the secured debt as provided by Michigan statute. The Bank should be permitted to pursue its vested substantive rights to what is its due – recovery from Defendants of the Bank's entire losses. See *Rose*, p 261 ("one has a vested substantive right to what is his due").

[33] For this reason it is even more appropriate to reject Defendants' request to create a new rule that further limits the Bank's recoverable losses based on the Bank's *less* than full credit bids for Heron Ridge and Golf Ridge. (COA docket no. 15, p 29.) Such a rule would limit the Bank to less than ten percent of its $7,000,000 actual loss. Understanding that there is no Michigan authority for such a rule, the majority remained silent as to this issue – although, Chief Judge Murphy noted that he would find that the Bank's recovery is not limited by the foreclosure bids on Heron Ridge and Gold Ridge. (Ex 1, Dissent Op, p 4 n 1.)