Michael K. Jeanes, Clerk of Court
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SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2008-021749 07/22/2009

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HON. EDWARD O. BURKE

CLERK OF THE COURT
L. Nixon
Deputy

SCOTT JACOBY MARK E LINES

v.

H S B C BANK U S A LEONARD J MCDONALD

ARI RAMRAS

MINUTE ENTRY

The Court, having heard oral argument on Plaintiff, Scott Jacoby's ("Jacoby") Motion for Judgment on the Pleadings and/or Motion for Summary Judgment, Intervenors, James V. Orlandini, II (Orlandini) and First American Title Insurance Company's ("First American") Response and Cross-Motion for Summary Judgment, and Plaintiff's Motion to Dismiss Counterclaims, and, having these matters under advisement, issues the following rulings.

Plaintiff, Jacoby's Motion for Judgment on the Pleadings and/or Motion for Summary Judgment is DENIED.

Plaintiff, Jacoby's Motion to Dismiss Counterclaims is DENIED.

Intervenors, Orlandini and First American's Cross-Motion for Summary Judgment is GRANTED.

FACTS

Plaintiff, Jacoby sued to quiet title to a parcel of real property described as Lot 67, CYPRESS ON SUNLAND, according to the plat of record in the office of the County Recorder of Maricopa, Arizona, in Book 617 of Maps, page 31, which is also known as 5413 South 7th Drive, Phoenix (the "Property"). Jacoby's claim of title is based on a recorded warranty deed he

received from Robert Draper who had purchased the Property at a Sheriff's sale held after a suit filed by the Cypress On Sunland Homeowners Association (the "HOA") to foreclose its lien for delinquent assessments.

The somewhat complex facts run on parallel tracks but are boiled down chronologically as follows:

January 6, 2003. A Declaration of Covenants, Conditions, Restrictions & Easements of Cypress on Sunland Homeowners Association (the "CC&Rs") was executed by Great Western Communities, Inc. on Lots 1 through 137 of Cypress On Sunland. The CC&Rs were recorded in the Maricopa County Recorder's Office at Instrument No. 2003-0070365. (Intervenors' Statement of Facts, Exhibit 5).

Section 7.9 of the CC&Rs states:

> "Section 7.9 Subordination of the Lien to First Mortgages. The lien of the Assessment(s) provided for herein shall be subordinate to the lien of any first mortgage. Sale or transfer of any Lot shall not affect the Assessment(s) lien. However, the sale or transfer of any Lot pursuant to mortgage foreclosure, foreclosure or trustee's sale, or any proceeding in lieu thereof, shall extinguish the lien of such Assessment(s)s as to payments which become due prior to such sale or transfer. No sale or transfer shall relieve such Lot form liability or any Assessment(s)s thereafter becoming due or from the lien thereof."

June 2, 2006. Derrick W. Spearman, the Property owner, executed a first deed of trust on the Property to American Lending Corporation ("ALC") to secure the sum of $190,400.00 (the "First D/T"). The First D/T was recorded on June 8, 2006, at Instrument No. 2006-778589. (Intervenors' Statement of Facts, Exhibit 1). On June 2, 2006, Spearman also executed a second deed of trust to ALC to secure the sum of $23,800.00, which was recorded June 8, 2006 at Instrument No. 2006-778590.

June 6, 2006. ALC assigned the First D/T to Alliance Bank Corp. Alliance Bank Corp did not record this assignment. (Intervenors' Statement of Facts, Exhibit 4).

June 12, 2006. Alliance Bank Corp. assigned the First D/T to Defendant HSBC Bank USA ("HSBC"). This assignment was not recorded until November 10, 2008. (Intervenors' Statement of Facts, Exhibit 4).

April 9, 2007. The HOA sues Derrick W. Spearman in CV2007-090828 (the "HOA Action") to foreclose its assessment lien in the sum of $2,436.28 on the Property. The complaint, drafted by attorney Charles E. Maxwell of Maxwell & Morgan, P.C., alleges:

> "11. American Lending Corporation is named as a Defendant pursuant to the Deeds of Trust recorded June 8, 2006, at Document Nos. 2006-778589 and 2006-778590, as the debt herein arose prior to said Deeds of Trust." (Intervenors' Statement of Facts, Exhibit 6).

The complaint also recites that the HOA had obtained a real estate foreclosure title search and that the litigation guarantee obtained by the HOA lists Spearman as the purported record title holder. Neither the foreclosure title search nor the litigation guarantee are attached to the complaint. The complaint does not state that the First D/T at Instrument No. 2006-778589 is a first deed of trust on the Property, nor does it disclose that the CC&Rs, which provides for the assessment lien, specifically states that the assessment lien is subordinate to the lien of any first mortgage.

ALC is served but, having previously assigned its interest in its two deeds of trust, does not answer and is defaulted.

May 17, 2007. Brian W. Morgan, a partner in Maxwell and Morgan, P.C., as attorney for the HOA signs a Motion and Affidavit For Entry of Judgment by Default With Hearing in the HOA Action (Intervenors' Statement of Facts, Exhibit 9). The motion states in part:

> "B. This party's claim is for a sum certain, and the relief sought is for money only and grants no other form of relief…
>
> 2. Plaintiff's claim is for a sum certain and/or a sum for which computation can be made certain and the Judgment submitted herewith is for money only and grants no other form of relief".

Both of these statements are false because the HOA was not seeking a money judgment but only to foreclose its assessment lien on the Property and the judgment submitted was for foreclosure.

June 4, 2007. A default hearing in the HOA Action was held before the Honorable M. Scott McCoy, a Maricopa County Superior Court Commissioner. This Court takes judicial notice of the proceedings at the default hearing through the court's audio recording thereof. The plaintiff HOA was represented by attorney, Arika Brooks Hover

who was associated with Maxwell and Morgan, P.C. Ms. Hover was sworn as a witness and testified:

> "Ms. Hover: Your Honor, again, we have a verified complaint in this matter and I believe the *** here today *** verified complaint. Form of judgment reflects ***. There's been proper service. Defendants have failed to answer. *** request attorney fees 100 percent to client followed by a China Doll affidavit. The costs are supported by a statement of costs and notice of taxation. And the plaintiff asks the court to enter judgment as submitted ***
>
> The Court: Okay. Did you serve American Lending separately?
>
> Ms. Hover: I did." (Partial transcript of audio recording of the June 4, 2007, default hearing before Commissioner McCoy).

Commissioner McCoy signed a judgment on foreclosure against Spearman and ALC which states in part:

> "2. As to the Defendants, the Court finds that said sums are secured by a lien against the Property and that the lien is a valid first lien on the Property and on the whole thereof, which lien is not subject to any homestead pursuant to A.R.S. § 33-1807(C);
>
> 3. As to these Defendants, the Association's lien is adjudged to be a first lien upon the Property and is prior and superior to any right, title, interest, lien, equity or estate of the Defendants herein;
>
> 4. The interests of the Defendants herein are hereby foreclosed, or any of them, and all persons claiming under any of them, and the Defendants herein are forever barred from any or all right, title, claim, interest or lien in and to the Property or with respect thereto, except such rights of redemption as they may have by law." (Intervenors' Statement of Facts, Exhibits 9 and 11).

The statements in the motion and judgment that the HOA's lien is superior to the First D/T are false.

Ms. Hover did not advise Commissioner McCoy that both the HOA CC&Rs and A.R.S. § 33-1807(B) state that a first deed of trust has priority over the HOA lien and that as a matter of law the HOA lien could not foreclose the First D/T.

July 26, 2007. A Sheriff's Sale on Foreclosure is held under a Writ of Special Execution issued in the HOA Action and Robert Draper purchased the Property for $5,599.00. (Intervenors' Statement of Facts, Exhibit 9). Intervenor, Orlandini's attorney had the Property appraised at $190,000.00 as of July 26, 2007. (Intervenors' Statement of Facts, Exhibit 12).

October 9, 2007. A "Substitution of Trustee" naming Michael Bosco ("Bosco") as the successor trustee on the First D/T is recorded at Instrument No. 2007-1105008. (Plaintiff's Statement of Facts in Support of Motion For Summary Judgment, Exhibit D)

October 9, 2007. Bosco records a Notice of Trustee's Sale to foreclose the First D/T on behalf of HSBC at Instrument No. 2007-1105009. (Plaintiff's Statement of Facts in Support of Motion For Summary Judgment, Exhibit E).

January 31, 2008. A Sheriff's Deed to the Property is issued to Robert Draper which was recorded on February 20, 2008, at Instrument No. 2008-0147189. (Plaintiff's Statement of Facts in Support of Motion For Summary Judgment, Exhibit H).

March 27, 2008. Robert Draper conveys the Property to Plaintiff, Scott Jacoby by warranty deed. The deed is recorded at Instrument No. 2008-0267813. (Intervenors' Statement of Facts, Exhibit 20). Jacoby testifies that he knew at the time of his purchase that HSBC was asserting a valid, enforceable first position lien on the Property. (Intervenors' Statement of Facts, Exhibit 13, Deposition of Scott Jacoby, p.137).

April 30, 2008. Bosco issues a Trustee's Deed of Sale of the Property to HSBC which is recorded at Instrument No. 2008-0480285. (Intervenors' Statement of Facts, Exhibit 22).

September 22, 2008. Plaintiff files his Complaint in this quiet title action against HSBC and records a Notice of *Lis Pendens*.

September 26, 2008. HSBC executes and delivers a Special Warranty Deed on the Property to Orlandini.

October 8, 2008. The Special Warranty Deed from HSBC to Orlandini is recorded at Instrument No. 2008-0873140. (Intervenors' Statement of Facts, Exhibit 24).

November 10, 2008. Alliance Bank Corp. records an assignment of the First D/T to HSBC, which had been executed on June 12, 2006, at Instrument No. 2008-0965066. (Intervenors' Statement of Facts, Exhibit 4).

February 26, 2009. Plaintiff files a Motion For Judgment On The Pleadings and/or Motion For Summary Judgment in this case.

March 6, 2009. Orlandini and First American move to intervene in this case. The Court grants the Motion To Intervene.

May 29, 2009. Orlandini and First American respond to Plaintiff's Motion For Judgment On The Pleadings and/or Motion For Summary Judgment and file a Cross-Motion For Summary Judgment.

DISCUSSION

Plaintiff, Jacoby and Intervenor, Orlandini each claim to have valid title to the Property. Counsel for the parties stipulated at oral argument that there is no genuine issue of material fact that would prevent the entry of summary judgment. Plaintiff's counsel acknowledged at oral argument that Maxwell & Morgan, P.C. specializes in representing homeowners associations.

Plaintiff claims the HOA's judgment in the HOA Action is valid on its face and is not subject to review on the basis of an error of fact or law. Real Estate Board v. Dalessandro, 17 Ariz. App. 181, 496 P.2d 607 (App. 1972) and International Ass'n of Machinists and Aerospace Workers v. Petty, 22 Ariz. App. 539, 529 P.2d 251 (App. 1974). Plaintiff also contends that the HOA's judgment is *res judicata* and not subject to collateral impeachment. Dairyland Insurance Co. v. Richards, 108 Ariz. 89, 492 P.2d 1196 (1972). Finally, Plaintiff contends that sound and strong policy favoring the stability of judicial service. Uptown Federal Sav. and Loan Ass'n of Chicago v. Vasavid, 94 Ill. App. 3d 531, 418 N.E. 2nd 831 (Ill App. 1981).

Plaintiff's Motion to Dismiss Counterclaims asserts that there is a failure to join indispensable parties, the Court does not have jurisdiction over the subject matter, intervenors do not have standing and intervenors have failed to state an actionable claim. The Court does not agree.

Intervenors' Cross-Motion for Summary Judgment claims that Orlandini is the legal owner of the Property because: 1) his title derives from a trustee's sale to foreclose the First D/T on the Property originally in favor of ALC; 2) the HOA's judgment of foreclosure in the HOA Action through which Plaintiff, Jacoby claims title should be set aside because it was signed in violation of A.R.S. § 33-1807(B) and an express provision in the CC&Rs and is a fraud on the court; 3) the amount Robert Draper paid at the Sheriff's Sale was grossly inadequate; and 4) the HOA's unlawful default judgment" against First American's insured may have exposed First American to unnecessary liability under the bank's title insurance policy.

This case involves the following issues:

1. Can the HOA's judgment be challenged and set aside because it was obtained by a fraud on the Court?
2. Can the HOA's judgment be set aside under Rule 60(c) of Civil Procedure?
3. Was the amount bid and paid by Robert Draper at the Sheriff's Sale grossly inadequate?
4. Is Plaintiff, Jacoby a bona fide purchaser for value?

The Court finds that the HOA committed a fraud on the court. Evidence of the fraud consists of the following: 1) Mr. Maxwell, who admittedly drafted the complaint to foreclose the homeowners assessment lien is a specialist in homeowner association law which his firm practices exclusively; 2) He had to have known that the CC&Rs he based his claim on contained the provision stating that first mortgages had priority over the HOA's assessment lien; 3) He was aware of the provisions of A.R.S. § 33-1807(B) (See Exhibit 4 to Jacoby's Reply); 4) He claimed in the HOA's complaint that the HOA's lien had priority over the First D/T; 5) While he recited the instrument numbers of the two ALC deeds of trust he did not plead or point out that one of them was in fact a first mortgage on the Property; 6) Brian W. Morgan of Maxwell & Morgan, P.C. submitted a Motion and Affidavit on Default claiming twice that he sought no relief other than money only which was false; 7) Another attorney in Maxwell & Morgan, P.C., Arika Hover gave sworn testimony in front of Commissioner McCoy that her client was entitled to the relief requested in the judgment, which was false for two reasons; 8) Ms. Hover neither informed Commissioner McCoy that the CC&Rs, on which she relied and which were not attached to the Complaint, prohibited the very relief that she was seeking; and 9) Maxwell & Morgan, P.C.'s alleged belief that the First D/T did not have priority under A.R.S. § 33-1807(B) is not a legal claim that was made in good faith given the legislative history of that statute and § 2.8.1 of Scott B. Carpenter's treatise, "Community Association Law In Arizona," Third Edition, 2008, published by the State Bar of Arizona.

The Court takes judicial notice that the Maricopa County Superior Court has four civil court commissioners in downtown Phoenix alone. In addition to the other cases they handle, they each consider approximately 300 civil default applications each month. If court commissioners can not rely on attorneys, as officers of the court, to honestly and candidly present their cases as required by both the Rules of Professional Conduct and Rule 11 of Civil Procedure, the civil justice system in this County would grind to a halt because civil commissioners would then have to independently research each of the claims brought before them and require a great deal more proof than was presented to Commissioner McCoy in the HOA Action. The Court finds that Maxwell & Morgan, P.C. and the three attorneys who were involved in the HOA's case had an obligation both as officers of the Court and under Rule 11 of Civil Procedure to clearly advise Commissioner McCoy of the true status of the facts and the

law. Their obligation is no different than that set forth in Haisch v. Allstate Insurance Company, 197 Ariz. 606, 610, 5 P.3d 949 (2000):"where the defendant has a legal or equitable obligation to reveal material information, his failure to do so is equivalent to a misrepresentation and may therefore support a claim of actionable fraud or the remaining elements of that tort are proved."

The fraud in this case is so severe that Maxwell & Morgan, P.C.'s lack of candor in failing to advise Commissioner McCoy of the contents of the CC&Rs and to state that they were arguing against the plain language of an Arizona statute which prohibited the relief they were seeking, justifies setting aside that judgment for fraud. A judgment obtained by fraud can be attacked in an independent action. In Re Adoption of Frantz, 21 Ariz. App. 36, 515 P.2d (1973) and State ex. rel. Corbin v. Arizona Corporation Commission, 141 Ariz. 219, 693 P.2d 362 (App. 1984). That result is arguably barred by Rule 60(c)(3) of Civil Procedure because it was not presented to this Court within 6 months from the date of the entry of the judgment.

After the judgment was obtained a Sheriff's Sale was conducted at which the purchase price was $5,599.00. The amount the First D/T secured was $190,400.00, and the amount the second deed of trust secured was $23,800.00. Orlandini's appraisal states that the Property was worth $190,000.00 at the time of the Sheriff's Sale. The bid of $5,599.00 was only 2.6% of the original mortgage amounts and 2.95% of the appraised value. In Krohn v. Sweetheart Properties Ltd., 203 Ariz. 205, 52 P.3d 774 (2002) our Supreme Court discussed a finding that an amount paid at a trustee's sale which was less than 20% of the property's fair market value was grossly inadequate. In discussing that question, the Supreme Court stated that "the general rule in Arizona dealing with vacation of execution sales because of inadequate bids is that mere inadequacy of price, where the parties stand on an equal footing and there are no confidential relations between them, is not, in and of itself sufficient to authorize vacation of the sale unless the inadequacy is so gross as to be proof of fraud or shocks the conscience of the court." The Supreme Court went on to say "while the rationale of setting aside judicial foreclosure sales for gross inadequacy is well understood, it is not the only basis for upsetting such sales. Judicial foreclosure sales have been set aside even in the absence of gross inadequacy where there has been some irregularity." Krohn, at 207. The irregularity in this case is the fraud on the Court in obtaining the foreclosure judgment. See also, Zurich American Insurance Company v. International Fibercom, Inc., 503 F.3d 933 (9th Cir, 2007).

Maxwell & Morgan, P.C.'s conduct in presenting the HOA's claim to Commissioner McCoy, plus the grossly inadequate purchase price paid at the execution sale, which itself shocks the conscience of the court, constitute grounds to set the sale aside and to set the judgment aside under Rule 60(c)(6) of Civil Procedure.

Plaintiff, Jacoby cannot complain of this result because he took title with knowledge that HSBC was claiming a valid first position lien on the Property and he has a claim against Draper

based on the warranty deed he received from Draper. As a matter of law, the Court finds that Jacoby is not a bona fide purchaser for value.