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CASE NUMBER: 115434

No. 16-115434-A

**IN THE SUPREME COURT OF THE STATE OF KANSAS**

LCL, LLC

*Plaintiffs*

vs.

JAMES W. FALEN, in his capacity as sole Trustee of the James W. Falen Living Trust U/A dated April 30, 2007; JULIE D. FALEN; GREGORY A. FALEN; and MARYL M. WESLOWSKI

*Defendants/Third-Party Plaintiffs – Appellants*

vs.

RICE COUNTY ABSTRACT & TITLE CO., INC.

*Third-Party Defendants - Appellees*

# RESPONSE TO PETITION FOR REVIEW

Appeal from the District Court of Rice County, Kansas
Honorable Steve Johnson
District Court Case No. 2014 CV 35

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II. The Falens' injury was not reasonably ascertainable as per K.S.A. §60-513(b) until August 2014 despite the fact of constructive notice imparted by K.S.A §58-2222.

III. Should this Court find that the Falens' suffered substantial injury in 2008 and their injury was reasonably ascertainable as of the date the defective deed was filed, the case should still be remanded to the District Court to address the Falens' second negligence and breach of fiduciary duty causes of action.

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## STATEMENT of FACTS

Rice County Abstract and Title (hereinafter referred to as "RCAT") continues to disregard the findings of fact the District Court used to determine the viability of RCAT's Motion for Summary Judgment. RCAT sets out numerous facts that purportedly support their position as if there had been a trial or that the District Court had actually made the same findings of fact. Due to RCAT's premature Motion for Summary Judgment, the Falens were precluded from conducting discovery relevant to this portion of the bifurcated case and the District Court found that numerous contentions of fact alleged by RCAT were contested by the Falens and vice versa. The District Court, for the purposes of its Memorandum Opinion, adopted the uncontroverted facts of RCAT in its Memorandum in Support of Motion for Summary Judgment, except to the extent controverted by Falens and adopted the Falens' controverted statements contained in the Falens' Response to Third Party Defendant's Motion for Summary Judgment. (ROA Vol. II p. 396-399; ROA Vol. III p. 530-532; ROA Vol. V. p. 1037-1038). The Court further adopted the additional facts asserted by the Falens in their Response for the purposes of ruling on RCAT's Motion for Summary Judgment, although the District Court did not find all the facts relevant to its analysis. (ROA Vol. III p. 532-551). The facts as relied on by the District Court and Court of Appeals are as follows:

RCAT is a licensed abstract company that provides escrow services for real estate closings and title examinations for title insurance commitments and title insurance policies. (ROA Vol. IV p. 734, ln. 5-25). In connection with its closing services, RCAT prepares deeds, owner's affidavits, closing statements and other types of documents commonly needed to facilitate the close of real estate transactions. (ROA Vol. IV p. 740 ln. 5-22).

In 2008, Defendants/Third-Party Plaintiffs James W. Falen, in his capacity as sole Trustee of the James W. Falen Living Trust U/A dated April 30, 2007, Julie D. Falen, Gregory Falen and Maryl M. Weslowski (hereinafter referred to collectively as 'Falens') sold farm land to a third-party purchaser by written contract with an express reservation of their producing mineral interest. (ROA Vol. II p. 412-413). RCAT was contracted to provide title insurance and closing/escrow services (which included deed preparation) in connection with this 2008 transaction. RCAT expressly understood that the parties intended for the Falens to reserve their mineral interest and knew the impact of failing to express the mineral reservation in the warranty deed. (ROA Vol. II p. 412-413; ROA Vol. IV p. 71, ln. 4-21; p. 139, ln. 17-22;p. 741, ln. 10-25; p. 742, ln. 3-16; p. 744 l. 8-9; p. 745, ln. 11) The transaction closed but the deed prepared by RCAT did not preserve the express mineral reservation. The Falens also claim that RCAT in providing escrow services made many mistakes - in their title search, title insurance commitment, settlement statement, and deed of transfer by failing to reserve the minerals of record. (ROA Vol. IV p. 754 ln. 25- p. 755 ln. 21; p. 769 ln2. – p. 770 ln. 3; p. 830, 831-834). Nevertheless, these multiple deficiencies had no noticeable effect at the time because the Falens and the buyer conducted themselves like the transaction closed as contracted.

From 2008 to 2014 the Falens continued to receive royalty payments from the oil & gas purchaser and paid ad valorem taxes without any claim to minerals by the third party purchaser. (ROA Vol. III p. 704-717, 721-725) In 2014 a successor in interest to the 2008 third-party purchaser contracted to sell the property to Plaintiff LCL, LLC. RCAT was again hired for title insurance and closing/escrow services. (ROA Vol. IV p. 844; p. 876 ln. 9 – p. 877 ln. 22; p. 923). RCAT provided title search, title insurance/commitment, settlement statements and closed the transaction. (ROA Vol. IV p. 737 ln. 4 – p. 768, ln. 16; p. 899 ln. 14-21; p. 959 l 25 – p. 960 ln.

13). Despite documentation in the public record to the contrary, RCAT claims it did not discover its 2008 mistakes and facilitated the close of the 2014 transaction, whereby the Plaintiff acquired the Falens' mineral interest in the property. (ROA Vol. IV p. 771 ln. 8-16; p. 772 ln. 1-9 p. 839-842; p. 858-852; p. 864-865; p. 879 ln. 16 – p. 882 ln. 14; p. 898 ln. 2-11; p. 924). RCAT never notified the Falens that the Falens' minerals had been sold and conveyed to Plaintiff.

After the 2014 closing, when Plaintiff was unable to convince the oil purchaser to change royalty payments to the Plaintiff from the Falens, the Plaintiff made a claim on the title insurance provided through RCAT. (ROA Vol. IV p. 626 ln. 9 – p. 628 ln. 12; p. 636 ln. 17 – p. 637 ln. 1; p. 928-929; p. 764 ln. 1 – p. 766 ln. 1.; p. 972). The title insurance company for both transactions, First American Title, paid the attorney fees and costs for the Plaintiff to file a lawsuit against the Falens in an attempt to quiet title. (ROA Vol. IV p. 930-936).

The Falens defended the action and made a third party claim against RCAT for indemnification and attorney fees. (ROA Vol. I p. 60-78; ROA Vol. II p. 485-492;) The quiet title action was bifurcated from the indemnification claim and, after discovery, was settled with the Falens reserving their indemnification claim against RCAT. (ROA Vol. II p. 386-389) Prior to settlement of the original action, RCAT filed a Motion for Summary Judgment in the third party claim relying on a theory that the two year statute of limitation provided by K.S.A. 60-513(c) began to run at the time the 2008 deed was filed with the Register of Deeds. (ROA Vol. II p. 390-393).

The Court noted in its Memorandum Opinion that the record and statement of uncontroverted facts provided by the Falens is "overwhelmingly convincing that a factual issue has been asserted that they had no actual realization of the injury until this time." (ROA Vol. V p. 1039). Despite this finding, the District Court ruled in RCAT's favor and the Falens

appealed. The third party claims of the Falens were based on breach of contract, negligence (professional), and breach of fiduciary duty.

## ARGUMENTS and AUTHORITIES

**I. Due to the fiduciary relationship between RCAT and the Falens as recognized by *Ford v. Guarantee Abstract Co.*, the Court of Appeal's decision is directly in line with this Court's holding in *Dearborn Animal Clinic P.A. vs. Wilson* and the Falens did not suffer an actionable injury until their title was challenged in 2014.**

RCAT's Petition for Review omits a Kansas Supreme Court case that is central to the Falen's cause of action – *Ford v. Guarantee Abstract Co.*, 220 Kan. 244 (1976). *Ford* stands for the proposition that a company engaged in title insurance and closing services "assumes to discharge the same duties as an individual conveyancer or attorney, [and] *has the same responsibilities and its duty to its employer is governed by the principles applicable to attorney and client.*" *Ford* at 256. (Emphasis added). As such, RCAT had a fiduciary duty to advance the interests of the Falens and use the skill and care of a competent lawyer in similar circumstances, so the Falens reasonably relied on the expertise of RCAT to prepare the deed in a non-negligent manner.

As a consequence of the RCAT/Falen relationship matching that of an attorney and client, *Dearborn Animal Clinic P.A. vs. Wilson*, 248 Kan. 257 (1991) is directly on point and supports the Court of Appeals' decision in this case. *Dearborn* concerned a purchase agreement drafted by an attorney for the sale of a client's veterinary clinic and stock in the client's holding company, with the purchaser making regular installment payments under the contract. The client's explicit desire was for the stock purchase portion of the agreement to be a firm offer, but defendant-attorney Wilson instead drafted it as a straight option contract for the purchase of the holding company stock. Subsequent to the execution of the contract plaintiff-seller continued receiving payments pursuant to the contract without any indication of the contract's defect, but

approximately one year after execution the purchaser put plaintiff on notice that it did not intend exercise the option contained in the purchase agreement. In ruling on attorney-defendant's statute of limitations argument, the Court held that the defendant's negligent act occurred at the time he prepared the agreement and "arguably the plaintiffs suffered injury at the time when they did not get the agreement [they hired defendant to prepare]" but "no actionable injury had occurred because [purchaser] *might* have elected to exercise his option in which case the plaintiffs would have suffered no injury." *Dearborn*, 248 Kan. at 265.

Like *Dearborn*, the present case concerns the negligent drafting of a document that affects the legal rights of parties to the document. The Falens, much like the plaintiff in *Dearborn*, continued to receive the intended benefit of the negligently prepared document up to the point that the defect was brought to light. In *Dearborn* the plaintiff continued receiving payments from the purchaser under the assumption the purchaser was buying the holding company stock under the defective purchase agreement; in the present case, the Falens continued receiving royalties from the producing minerals under the assumption they had reserved a severed mineral interest with the defective deed. RCAT states that the executed deed divested the Falens of its title ownership in the property thereby causing "substantial injury" under K.S.A. §60-513(b) in 2008, but this loss of title is all but immaterial when considering that the Falens were intending to reserve *then-producing* severed minerals, continued receiving the royalties therefrom and never attempted to convey their mineral interest to a third party. This argument attempts to blur the line between the concept of "negligent act" and "actionable injury." Moreover, RCAT argues that the Falen's loss of title in 2008 was in fact an actionable injury, the damage of which can be measured by the difference between the property's value with and

without minerals, but there is presently nothing in the record to support any measurable difference under this proposed formula.

**II. The Falens' injury was not reasonably ascertainable as per K.S.A. §60-513(b) until August 2014 despite the fact of constructive notice imparted by K.S.A §58-2222.**

RCAT's Petition for Review also mischaracterizes the Court of Appeals' analysis of when an injury becomes "reasonably ascertainable" as per K.S.A. §60-513(b). RCAT would have this Court believe that constructive notice pursuant to K.S.A. §58-2222 is the sole inquiry for determining when the Falen's injury was reasonably ascertainable, but as their own petition accurately states "this Court has noted the term reasonably ascertainable . . . suggests an objective standard *based on an examination of the surrounding circumstances*." RCAT's Petition for Review p. 2. The Falens do not disagree with this statement and believe the Court of Appeals, in looking at the facts accepted by the District Court, did an effective job of examining the circumstances surrounding the Falens' injury to find it was not reasonably ascertainable prior to 2014– the continued benefit of the royalties generated from the property, the continued payment of ad valorem taxes and the lack of challenges to the Falens title prior to 2014.

RCAT's exclusive reliance on K.S.A. 58-2222 to determine when the Falens' injury became reasonably ascertainable attempts to present the inquiry as a question of law – if §58-2222 applies, then the negligent of act of RCAT becomes reasonably ascertainable by operation of law. However it is well established that "where the evidence is in dispute as to when substantial injury first appears or becomes reasonably ascertainable, *the issue is for determination by the trier of fact.*" *Gilger v. Lee Const., Inc.*, 249 Kan. 307, 311 (1991). K.S.A. §60-501 states that the scope of Chapter 60, Article Five governs "the limitation of time for commencing civil actions, *except where a different limitation is specifically provided by statute*."

(Emphasis added). By making the question of when an injury becomes reasonably ascertainable a question of law, the Court would simply be engrafting an exception to K.S.A. §60-513(b) for title defects stemming from negligently prepared documents that have been filed of record. "Kansas courts cannot engraft an exception [to the statute of limitations] which the legislature . . . has not included in the statute." *Law v. Law Co. Bldg. Associates*, 295 Kan. 551, 576 (2012).

There is nothing in K.S.A. §60-501 *et seq* to suggest the Legislature intended K.S.A. §58-2222 to be a discovery exception to K.S.A. §60-513. At best, the question of constructive notice is but one factor for determining when an injury becomes reasonably ascertainable and the weight given to constructive notice should necessarily examine *what* notice is provided under K.S.A. §58-2222. "[T]he purpose of the statutes authorizing the recording of instruments of conveyance is to impart to a subsequent purchaser *notice of* instruments which affect the title to a specific tract of land in which the subsequent purchaser is interested at the time." *Luthi v. Evans*, 223 Kan. 622, 629 (1978) (emphasis added). In other words, K.S.A. §58-2222 imparts notice to the world that a document has been executed and filed with the respective register of deeds where the property is situated. The Falens cannot claim ignorance to the *existence* of the deed filed of record, but this is a far cry from notice of the document's unintended legal effect. *See generally Bick v. Peat Marwick & Main*, 14 Kan. App. 2d 699 (1990)(taxpayer's constructive knowledge of a potential tax penalty for underpayment of income tax does not equate to the knowledge of a negligent act by a tax preparer that triggers the tax penalty).

RCAT relies on *Bi-State Dev. Co., Inc. v. Shafer, Kline & Warren, Inc.*, 26 Kan.App.2d 515 (1999) to support the idea that constructive notice pursuant to K.S.A. §58-2222 provides notice to a recorded document's defect, but as the Court of Appeals noted, *Bi-State* is distinguishable from the present case for a number of compelling reasons. First is the nature of

the defect – in *Bi-State* the defect was with the legal description of easement, whereas here the defect is in how the document operates. Second is that *Bi-State* does not concern the creation and recording of a document prepared by the Defendant in its capacity as a fiduciary to the Plaintiff. Defendant in *Bi-State* was hired to prepare a survey to determine where an easement *yet to be created* was supposed run through the property in question. Lastly, the timeline of events in *Bi-State* is such that the Plaintiff had an active role in its own damages by failing to consult with Defendant before executing and filing the document that provided constructive notice. In the present case, the Falens could only be accused of contributing to their own damage by failing to hire an attorney to review the work of RCAT *despite* the facts that RCAT held itself out as capable of this work and that RCAT and the Falens have a relationship tantamount to that of an attorney and client by virtue of *Ford v. Guarantee Abstract.*

**III. Should this Court find that the Falens' suffered substantial injury in 2008 and their injury was reasonably ascertainable as of the date the defective deed was filed, the case should still be remanded to the District Court to address the Falens' second negligence and breach of fiduciary duty causes of action.**

In the present case, the District Court summarily dismissed the Falens' second cause of action against RCAT for breach of fiduciary duty, ruling that RCAT's 2014 actions were nothing more than a continuation of their negligence committed in 2008. However if the Falens were bestowed with constructive notice of the defect in the 2008 deed, then so too was RCAT. Constructive notice to *all parties* pursuant to K.S.A. §58-2222 is not a one-way street; therefore, any action taken by RCAT subsequent to filing the defective deed of record, in accordance with RCAT's theory of discovery, was done with the knowledge of its negligently prepared deed and the transfer of minerals was contrary to the desires of the parties to the 2008 transaction. Because of this constructive notice, RCAT's negligent title examination in the 2014 transaction, its close

of the 2014 transaction and non-disclosure to the Falens of its mistake was not a mere continuation of its alleged 2008 negligence, but rather, a wholly new breach of its fiduciary duty to the Falens.

RCAT knew the contract for the 2008 transaction was such that the Falens were to reserve the mineral interest in the Property and arguably had constructive knowledge of its improperly prepared, executed and recorded deed; therefore, RCAT had notice in 2008 that it breached its duty to the Falens in deed preparation to use the learning, skill and care of a reasonably competent lawyer. Despite the fact of its knowledge that the Falens contracted to retain their minerals in 2008 *and* notice that it breached a duty owed to the Falens, RCAT certified fee title to LCL for the surface and one-half of the minerals with its 2014 title examination and title commitment. As closing agent to the 2014 transaction, RCAT also took an active role in facilitating the mineral transfer of record to LCL, and only after LCL attempted to make a claim on its title insurance policy did RCAT, without notice to the Falens, attempt to correct its 2008 breach of duty to the Falens. Although RCAT breached its duty to the Falens to use the skill and care of a reasonably competent attorney in 2008, its second breach of fiduciary duty did not occur until it closed the transaction in 2014; it took an active role in subverting the interests of the Falens by closing the 2014 transaction, and did so with the constructive notice that it previously breached a duty owed to the Falens.

Moreover, should RCAT's 2014 actions be deemed a mere continuation of their 2008 negligence and not a wholly separate cause of action, RCAT should necessarily be estopped from relying on the statute of limitations due to the fiduciary duty owed to the Falens.

> If a defendant, electing to rely on the statute of limitations, has previously by deception or in violation of his duty toward plaintiff, caused him to subject his claim to the statutory

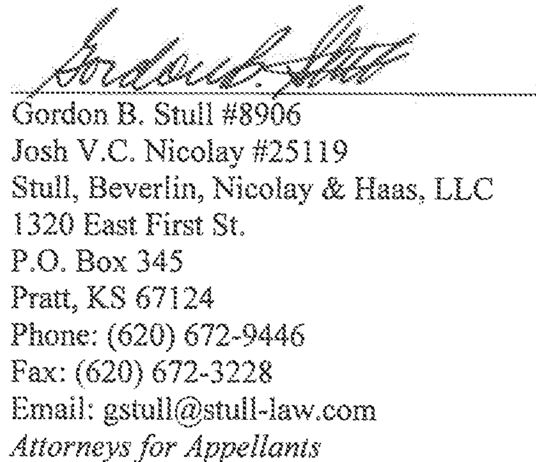
> bar, defendant must be charged with having wrongfully obtained an advantage which the court will not allow him to hold, and this can be done by his silence when under an affirmative duty to speak. *Klepper v. Stover*, 193 Kan. 219, 222, 392 P.2d 957, 959 (1964).

Despite having constructive notice of the negligently prepared deed *and* a fiduciary relationship with the Falens, RCAT took no effort to try and correct its negligently prepared deed, nor did RCAT attempt to notify the Falens that the deed prepared did not reserve the mineral interest as per the Falens' express request. Since RCAT was also hired to conduct a title examination, provide title insurance and closing services in the 2014 transaction, it was in the unique position of being able to correct their 2008 mistake prior to closing the 2014 transaction. Armed with the constructive notice of its 2008 mistake, RCAT nonetheless facilitated the close of the 2014 transaction without any attempt to protect the known interest of the Falens in reserving and maintaining its mineral interest. RCAT had an affirmative, fiduciary duty to protect the interests of the Falens, which would necessarily require RCAT to notify the Falens of its mistake and attempt to remedy the problem. Should the entire world be imparted constructive notice of the 2008 deed's defect, RCAT's failure to attempt to remedy its mistake *and* active role in the 2014 transaction was done with notice of its error and thus was a breach of the fiduciary duty owed to the Falens. If RCAT's position is correct, RCAT's breach of fiduciary duty caused the Falens to subject their negligence claim to the statute of limitations, and thus RCAT should be charged with having wrongfully obtained an advantage and should not be allowed to rely on the statute of limitations to bar the Falens' 2008 claims.

## CONCLUSION

For the aforementioned reasons, the Falens request that RCAT's Petition for Review be denied and that the case be remanded back to the Rice County District Court for proceedings consistent with the holding of the Court of Appeals.

Respectfully submitted,



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## CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 4 day of April, 2016, a true and correct copy of the above and foregoing Response to Petition for Review was mailed to the following:

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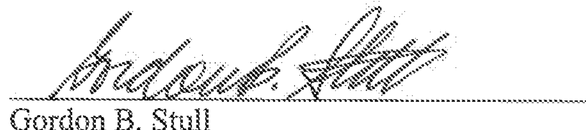

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