No. 89925-8

SUPREME COURT OF
THE STATE OF WASHINGTON

NO. 69644-I

COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION I

ERIK D. ESBERG,

Plaintiff - Appellant,

v.

JASON D. NELSON and FRANCINE E. NELSON

Defendants - Respondents

ON APPEAL FROM SNOHOMISH COUNTY SUPERIOR COURT
(Hon. Judge Janice E. Ellis)

RESPONDENTS' PETITION FOR REVIEW

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Appendix A	Opinion of Court of Appeals, Division I, dated December 16, 2013	n/a
Appendix B	Declaration/Argument of David C. Hammermaster RE: Motion to Publish Pursuant to RAP 12.3	n/a

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I. IDENTITY OF PETITIONERS

Petitioners, Jason D. Nelson and Francine E. Nelson, were the Defendants at trial and the Respondents before the Court of Appeals.

II. COURT OF APPEALS DECISION

An unpublished decision terminating review (the "Decision") was entered on December 16, 2013 (copy attached as App. A). The Court of Appeals on January 14, 2014 granted the Appellant's motion to publish the opinion.

III. STATEMENT OF ISSUES PRESENTED FOR REVIEW

In this real estate dispute, the Petitioners ask this Court to review the following issues.

1. Marketable title. Whether a judgment against a homeowners' association which the owners of lots in a plat are members and is reported on a title commitment, is a matter that renders the title unmarketable.

2. Duty to Investigate. Whether one asserting unmarketability of tile must prove that the title is in fact unmarketable.

For the reasons set forth below, these issue warrants review under RAP 13.4(b)(1) and (4) because the Court of Appeals decision is in

conflict with a decision of the Supreme Court and involves an issue of substantial public interest.

IV. NATURE OF THE CASE AND DECISION BELOW

This case arises out of a conveyance of an unimproved lot in Chelan County by the Appellant ("Ensberg") to Respondents ("Nelson") and the Nelson's attempt to re-sell that real property. At the time of the sale from Ensberg to Nelson, there was a judgment recorded against the homeowners' association governing the plat in which the lot was a located. When the Nelsons attempted to re-sell the lot, the judgment was reported as an exception to title on a title commitment ordered as part of that sale. The party offering to purchase the Nelson's lot refused to close the transaction because of the judgment.

As part of the original sale from Ensberg to Nelson, Nelson executed a promissory note in favor of Ensberg as part of the selling price. When the Nelson's could not sell the property because of the judgment, Nelson refused to pay the remaining balance on the note and Ensberg sued. Nelson counterclaimed claiming breach of the statutory warranty deed and Ensberg's failure to convey marketable title.

Following a bench trial, the trial court dismissed Ensberg's complaint on the promissory note and entered a judgment in favor of

Nelson for Ensberg's breach of the statutory warranty deed. Ensberg appealed and Division I of the Court of Appeals reversed the trial court and remanded the matter to the trial court to enter judgment in favor of Ensberg on the promissory note.[1]

The petitioners now seek review by this Court of a single issued raised by the Court of Appeals published opinion.

Following are the facts material to those issues:

At the time of the sale of lot 18 in Key Bay from the Ensberg to the Nelson there was a judgment against the Key Bay Homeowners' Association (hereafter 'HOA') of record with the Chelan County Auditor. (EX. 6). The HOA is the governing body for the Key Bay subdivision in which lot 18 is located. The judgment was entered on March 17, 2008 and was in the amount of $523,474.00 with interest accruing on the judgment at 12% per annum. It was recorded with the Chelan County Auditor on April 8, 2008. (F/F 1.6) That judgment was not shown as an exception on the statutory warranty deed from Ensberg to Nelson (EX 2).

After the purchase of lot 18 from Ensberg in February 2009,

[1] The Court of Appeals originally issued an unpublished opinion but Ensberg filed a motion in the Court of Appeals asking the Court to publish the decision on the ground that the decision affected the general public. The Court of Appeals granted Ensberg's Motion to Publish on January 14, 2014. (Ensberg's Motion to Publish is attached as App. B.)

Nelson listed the property for sale. (RP 13, lines 20 - 22) In early October 2009, Nelson received an offer on the lot and after some negotiations back and forth with the potential buyers, an agreement was reached to sell the lot for $216,000.00 (RP 13, lines 22 – 24; EX 15). This amount would have been sufficient to pay the underlying debt on the property, the closing costs, real estate commissions, taxes and so forth and provide a small profit to Nelson. After the purchase and sale agreement was signed, the transaction was placed with escrow in Wenatchee and a title commitment was obtained.

The title commitment listed various encumbrances on the title including the deed of trust in favor of Ensberg. (EX 26). The title commitment also listed as an encumbrance the March 17, 2008 judgment against the Key Bay Homeowners' Association. Paragraph 12 of Schedule B of the title commitment provided the following exception:

12. JUDGMENT:

AGAINST:	KEY BAY HOMEOWNERS ASSOCIATION,ET AL
IN FAVOR OF:	DEEP WATER BREWING, LLC
AMOUNT:	$523,474.00
CHELAN COUNTY JUDGMENT	NO: 08-9-00369-8

The buyers exercised their contractual right to disapprove any matter on the title report and on October 24, 2009 they executed an addendum to the purchase and sale agreement requiring the removal of the judgment against the homeowners' association as an encumbrance. (EX 31). The buyers also required Nelson to agree to the following:

> Buyer shall not be liable for any judgment settlement amount presently or in the future owed by the Key Bay Homeowners Association et al in regard to exception #12 in Schedule B involving the judgment in favor of Deepwater Brewing, LLC. Seller will pay off their share of any judgment settlement amount related to their liability due from them as a result of the judgment in favor of Deepwater Brewing LLC prior to closing.

(EX 31; RP 18, lines 2 – 5). Nelson did not agree to this, but urged the title company to revisit the judgment issue. On October 29, 2009, the judgment under Schedule B of the title report was removed as an exception and instead it was included as a "Note" in the title commitment (EX 27):

NOTE 10: JUDGMENT:

AGAINST: KEY BAY HOMEOWNERS ASSOC. ET AL

IN FAVOR OF: DEEP WATER BREWING LLC.

AMOUNT:	$523.474.00
CHELAN COUNTY JUDGMENT	NO: 08-9-00369-8
SUPERIOR COURT CAUSE	NO: 02-2-00848-2

THE JDUGMENT AGAINST THE KEY BAY HOMEOWNERS' ASSOCIATION, A WASHINGTON NONPROFIT CORPORATION (THE "ASSOCIATION"), HAS NOT ATTACHED TO THE TITLE TO THE LAND DESCRIBED IN SCHEDULE A HEREIN. IF, AFTER APPEAL, THE JUDGMENT ATTACHES TO THE ASSOCIATION'S INTEREST. THE ASSOCIATION MAY LEVY ASSESSMENTS AGAINST EACH LOT TO RECOVER THE FUNDS OWED TO THE JUDGMENT CREDITOR. THIS NOTE PROVIDES NOTICE OF THE POTENTIAL FUTURE LIABILITY FOR SUCH ASSESSMENT(S).

On November 4, 2009, the buyers sent Nelson a Rescission of the purchase and sell agreement, which Nelson signed on November 7, 2009, the original closing date of the transaction (EX 32).

V. REASONS FOR GRANTING REVIEW

A. The Court of Appeals decision is not consistent with this Court's decision in *Hebb v. Severson*, 32 Wn.2d 159, 201 P.2d 156 (1948).

Although the trial court rendered judgment against Ensberg based on a breach of the statutory warranty deed's covenant against encumbrances, the judgment against the HOA also affected the market value of the real property and Nelson argued that Ensberg also breached

his duty to convey good and marketable title. A seller of real property is required to convey good and marketable title to a purchaser:

> Even in the absence of any provision in the contract indicating the quality of the title provided for, the law implies an undertaking on the part of the vendor to make and convey a good and marketable title to the purchaser. 55 Am. Jr. 619, Vendor and Purchaser, § 149; notes (1928), 57 A.L.R. 1256, 1260, wherein Washington cases in support of the rule are collected.

Hebb v. Severson, 32 Wn.2d 159, 169, 201 P.2d 156 (1948). In *Shinn v. Thrust IV, Inc.* 56 Wn. App. 827, 786, P.2d 286 (1990), Division I of the Court of Appeals, relying on *Hebb v. Severson, supra.,* held that the mere possibility of enforcement of restrictions that might not even apply to the land in question, was enough to make the title unmarketable. The Court of Appeals noted that

> The Washington Supreme Court has defined marketable title as one being free of reasonable doubt and such as a reasonably informed and intelligent purchaser, exercising ordinary business prudence, would be willing to accept. Such a title need not be perfect in the sense that it is free from every conceivable technical criticism or suspicion, but only from those possibilities of a defect which would give rise to a reasonable question as to its validity.

Shinn v. Thrust IV, Inc., supra, 786 P.2d at 296. The Court of Appeals went on to quote a portion of the Supreme Court's decision in *Hebb v. Severson*:

> [e]very purchaser of land has a right to demand a title which shall put him in all reasonable security, and which shall protect him from anxiety, lest annoying,
>
> if not successful suits be brought against him, and probably take from him or his representative, land upon which money was invested. He should have a title which shall enable him not only to hold his land, but to hold it in peace; and if he wishes to sell it, to be reasonably sure that no flaw or doubt will come up to disturb its marketable value.

Hebb v. Severson, supra at 166-67. Like the restriction at issue in the *Shinn* case, the judgment here cast serious doubts about whether any purchaser of lot 18 had reasonable security that his or her investment in lot 18 would not be in jeopardy. The proof at trial clearly established that the effect of the judgment against the HOA was uncertain and that, based on the title company's representation as to the possible effect of the judgment, it was not unreasonable to assume that litigation might ensue to force the HOA to assess lot owners to pay the judgment. The judgment against the HOA was a "flaw or doubt" which, when Nelson attempted to sell lot 18, came up to "disturb its marketable value."

In its decision, the Court of Appeals rejected the Nelsons' argument and held that without proof that the HOA had the authority to levy assessments to pay the HOA judgment, or certainty of the amount that might be owing on the judgment, the title was not unmarketable.

The defect in *Hebb v. Severson* was an apparent violation of covenants that prohibited structures within 5 feet of the property boundary. The title company's inspection of the property indicated that the house on the property was within 5 feet of the boundary. Nevertheless, the title company indicated in the title report that it would insure against any loss as a result of the enforcement of the restriction.

This Court held in *Hebb v. Severson,* that despite a title insurer's willingness to insure against loss, the title to the property was nonetheless unmarketable. Here, the title company went out of its way to disclose the judgment against the HOA and there was no indication that the title company was willing to insure title to the lot without referencing the judgment in the title policy. The Court of Appeals concluded that the title to the Nelson's lot was marketable. A title is unmarketable even if a title company is willing to insure it (*Hebb v. Severson),* but is marketable when the title company is not willing to insure it (*Ensberg v. Nelson).* That makes no logical sense.

B. <u>The decision of the Court of Appeals presents this Court with an opportunity to clarify the role of title insurance in real estate transactions and the effect of matters shown on a title report on the issue of marketability.</u>

In support of his motion to publish the decision of the Court of Appeals, Ensberg argued that the opinion of the Court of Appeals clarifies a "growing misconception" about the role of title insurance in real estate transactions, and particularly the title commitment or preliminary report issued before the sale is closed. (See Appendix B, Declaration/Argument of David C. Hammermaster Re: Motion to Publish Pursuant to RAP 12.3, page 2). The "misconception", according to Ensberg and now the Court of Appeals, is that the title report is a statement about the legal condition of certain real property. Ensberg went on to argue that "[i]n reality, the title insurance company simply assesses the level or degree of risk it is willing to take for the premium it receives. In that instance, the title insurance company lists everything that they believe poses an unacceptable level of risk as an exception to their coverage." Appendix B, page 2.

The Court of Appeals decision creates doubt whether the general public can or should rely on a title report to assist them in deciding whether to purchase a particular piece of real property.

That is not how normal real estate transactions are conducted. Most purchasers do rely on the title insurance

commitment to determine whether to proceed with the transaction. A prospective purchaser in dealing with a title insurer does expect a professional title search, an opinion as to the title's status, and a guarantee that the title is good. Unlike casualty insurance where the insurer assumes an unknown future risk, title insurers don't insure against future risks, but rather insure against matters affecting title at the time the real estate transaction is closed. Title insurers are about loss prevention rather than risk assumption. Title insurers do title searches for the very purpose of preventing losses and the payment of claims. Indeed, state law requires title insurers to maintain a complete set of tract indexes in the county where it does business. RCW 48.29.020. It is reasonable for prospective buyers to assume that a title insurer searches those indexes and reports its findings.

Consistent with what Ensberg characterizes as this "misconception" by the general public about the role of title insurance in real estate transactions, most real estate purchase and sale agreements provide that the seller will procure a title report, deliver it to the buyer and the buyer will be given the opportunity to object to matters disclosed by the title report. That is what

happened in the instant case. Indeed, it is likely that a prospective buyer is more concerned about what the title report says than the fact of the insurance itself. If the Court of Appeal's decision is correct that a prospective buyer in a real estate transaction cannot rely on a title report in deciding whether to proceed with the transaction, then it would serve the public's interest in knowing that more "due diligence" is required of a buyer than a buyer may now reasonably expect. If a title commitment cannot be relied upon, then a prospective buyer would have to determine on his or her own whether matters that may be disclosed by a title commitment are real, or simply "risk assessments" by the title company.

The Court of Appeals refused to hold that the judgment against the homeowners association rendered the title unmarketable because Nelson had not shown that the judgment creditor could have compelled the homeowners' association to levy assessments to pay the judgment. The Court of Appeals decision shifts the burden on the one claiming an unmarketable title to investigate and establish that the title is in fact not arketable. That is inconsistent with prior decisions of this Court.

In *Moore v. Elliot,* 76 Wash. 520, 136 P. 849 (1913) this Court held that the only issue with regards to marketable title was whether a reasonably well-informed and intelligent purchaser, exercising ordinary business caution would be willing to accept a questionable title.

> We are not called upon to decide whether the title offered is in fact good or whether we would so hold it were that question before us. Granting that is was, the question remains: **Was that fact so free from doubt that a reasonably well-informed and intelligent purchaser of ordinary business caution would accept it?**

Id, 76 Wash. at 522 (Emphasis added). In the instant case, the Court of Appeals held against Nelson because Nelson did not present evidence that the HOA had the power to assess homeowners and compel the homeowners to pay the judgment. In prior decisions of this Court, one asserting unmarketability is never under a duty to investigate the issue further. See, *Scott v. Stanley,* 149 Wash. 29, 270 P. 110 (1928) (". . . a purchaser is not required to accept conveyance, even upon a reasonable showing that he can go out and hunt up evidence sufficient to establish in a lawsuit that his title is good.") and *Coonrod v. Studebaker,* 53

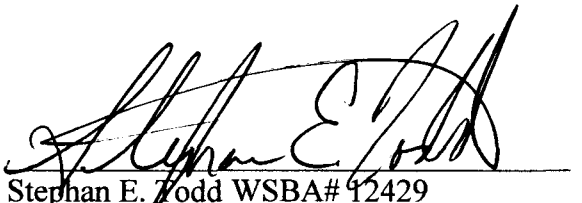
Wash. 32, 101 P. 489 (1909) ("The purchaser cannot be put to the peril of hunting up testimony outside of the record . . .").

The only question on appeal should have been whether the information provided by the title company to the prospective purchaser about the judgment against the HOA and the potential effect on the title to the lot was "that fact so free from doubt that a reasonably well-informed and intelligent purchaser of ordinary business caution would accept it?" The fact is that the purchaser from Nelson would not accept the conveyance. The title was not marketable.

VI. CONCLUSION

The Court should grant review to clarify Washington law pertaining to the role of title insurance in real estate transactions and what constitutes a defect that renders title unmarketable.

RESPECTFULLY SUBMITTED this 12th day of February, 2014.



Stephan E. Todd WSBA# 12429
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APPENDIX A

IN THE COURT OF APPEALS FOR THE STATE OF WASHINGTON

ERIK D. ENSBERG, Appellant, v. JASON D. NELSON and FRANCINE E. NELSON, husband and wife and the marital community comprised thereof, Respondents.	)	No. 69644-1-I DIVISION ONE UNPUBLISHED OPINION FILED: December 16, 2013

SPEARMAN, A.C.J. — The main question on appeal is whether a seller of property breaches the statutory warranty deed covenant against encumbrances when, at the time of conveyance, the property is part of a homeowner's association and there is a judgment against the homeowner's association, but the owner of the property is not a judgment debtor, there is no lien against the property, and there is no evidence of the association's ability to assess the property owner to pay the judgment. We hold that the seller does not breach the warranty against encumbrances in such circumstances. We also hold that the seller does not convey unmarketable title. Therefore, we reverse the trial court's judgment in favor of the buyers of the property, respondents Jason and Francine Nelson, and remand for entry of judgment in favor of the seller, appellant Erik Ensberg, on his claim for breach of the promissory note. We also reverse the trial

court's award of attorney's fees to the Nelsons below and award attorney's fees to Ensberg on appeal based on a provision in the promissory note.

FACTS

In 2004, Erik Ensberg purchased a vacant lot ("the Property") in Chelan County at the encouragement of Jason and Francine Nelson, who had already purchased two lots adjacent to the Property. The purchase was orchestrated by the Nelsons' friend, Jack Johnson, whose company, Key Development Corporation, was developing and selling the lots.

Several years later, on January 25, 2009, the Nelsons bought the Property from Ensberg for $195,000. They made a down payment of $10,000 and financed the balance in the amount of $185,000, which was comprised of an assumption of the underlying debt owed by Ensberg of $129,603.40. Ensberg received a promissory note and deed of trust (in second position) for the balance owed by the Nelsons of $55,396.60. Ensberg was not involved in selecting the escrow or title companies or in drafting the documents, including the statutory warranty deed. The title company performed a title search prior to closing and found no judgment encumbering the Property.

Unbeknownst to the parties, at the time of the sale there was a judgment of $523,474 against Jack Johnson, Key Bay Development Corporation, and Key Bay Homeowners' Association (the HOA) of record with the Chelan County Auditor. The HOA is the governing body for the Key Bay subdivision in which the Property is located. The judgment was entered in Chelan County Superior Court on March 17, 2008 and recorded with the Chelan County Auditor on April 8,

2008. The judgment did not appear on the statutory warranty deed from Ensberg to the Nelsons.

Approximately six months after they bought the Property, the Nelsons listed it for sale. In October 2009, the Nelsons accepted an offer to purchase for $216,000. After the purchase and sale agreement was signed, a title commitment was obtained. The two prior sales of the Property had involved the same escrow agent and title company. The transaction between Ensberg and the Nelsons was to be closed using a different escrow agent and title company, the latter being North Meridian Title and Escrow, LLC.

North Meridian's preliminary title commitment listed various encumbrances on the title, including the deed of trust in favor of Ensberg. Exhibit (Ex.) 26 at 4. Paragraph 12 of Schedule B stated the following "special exception":

> 12. JUDGMENT:
>
> AGAINST: KEY BAY HOMEOWNERS ASSOCIATION, ET AL
> IN FAVOR OF: DEEP WATER BREWING, LLC
> AMOUNT: $523,474.00
> CHELAN COUNTY JUDGMENT NO.: 08-9-00369-8
> SUPERIOR COURT CAUSE NO.: 02-2-00848-2

Id.

The prospective buyers exercised their contractual right to disapprove any matter on the title report. On October 24, 2009, they executed an addendum to the purchase and sale agreement, requesting the Nelsons to remove the

judgment against the HOA as an exception from title[1] and to agree that:

> BUYER SHALL NOT BE LIABLE FOR ANY JUDGEMENT [SIC] SETTLEMENT AMOUNT PRESENTLY OR IN THE FUTURE OWED BY THE KEY BAY HOMEOWNERS ASSOCIATION, ET AL IN REGARD TO EXCEPTION #12 IN SCHEDULE B INVOLVING THE JUDGEMENT [SIC] IN FAVOR OF DEEP WATER BREWING LLC.
>
> SELLER WILL PAY OFF THEIR SHARE OF ANY JUDGEMENT [SIC] SETTLEMENT AMOUNT RELATED TO THEIR LIABILITY DUE FROM THEM AS A RESULT OF THE...JUDGEMENT [SIC] IN FAVOR OF DEEP WATER BREWING LLC PRIOR TO CLOSING.

Ex. 31. The Nelsons did not agree, but urged North Meridian to revisit the judgment issue.[2] North Meridian then removed the judgment against the HOA as an exception from Schedule B and instead referenced the judgment in the following "Note" in the preliminary title commitment:

> NOTE 10: JUDGMENT:
> AGAINST: KEY BAY HOMEOWNERS ASSOCIATION, ET AL
> IN FAVOR OF: DEEP WATER BREWING, LLC
> AMOUNT: $523,474.00
> ENTERED: MARCH 17, 2008
> CHELAN COUNTY JUDGMENT NO.: 08-9-00369-8
> SUPERIOR COURT CAUSE NO.: 02-2-00848-2
>
> THE JUDGMENT AGAINST THE KEY BAY HOMEOWNER'S ASSOCIATION, A WASHINGTON NONPROFIT CORPORATION (THE "ASSOCIATION"), HAS NOT ATTACHED TO THE TITLE TO THE LAND DESCRIBED IN SCHEDULE A HEREIN. IF, AFTER APPEAL, THE JUDGMENT ATTACHES TO THE ASSOCIATION'S

[1] The prospective buyers also objected to exceptions 14, 15, and 16 and requested the Nelsons to clear those exceptions from the title. These exceptions, as listed in the preliminary title commitment, Schedule B, related to (1) general property taxes and service charges in the amount of $1,335.07, (2) a lien claimed by the State of Washington, Department of Social and Health, against Jason Nelson in the amount of $4,534.38, and (3) a lien claimed by the State of Washington, Department of Social and Health, against Jason Nelson in t the amount of $14,455.43. Ex. 26.

[2] It is unclear whether the Nelsons agreed to the prospective buyers' other requests.

> INTEREST, THE ASSOCIATION MAY LEVY ASSESSMENTS AGAINST EACH LOT TO RECOVER THE FUNDS OWED TO THE JUDGMENT CREDITORS. THIS NOTE PROVIDES NOTICE OF THE POTENTIAL FUTURE LIABILITY FOR SUCH ASSESSMENT(S).

Ex. 27. On November 4, 2009, the prospective buyers sent the Nelsons a rescission of the purchase and sale agreement, which the Nelsons signed on November 7. The Nelsons made no further effort to sell the Property.

The Nelsons defaulted on the underlying note and deed of trust and on Ensberg's promissory note. The Property was sold at a trustee's sale in August 2010 for an unknown amount. The foreclosure had the effect of removing Ensberg's deed of trust against the Property, but the balance on the promissory note was still due and owing. The last payment, made on September 1, 2009, brought the balance on that date to $50,012.34.

Ensberg filed suit against the Nelsons for breach of the promissory note. The Nelsons counterclaimed, alleging he breached the statutory warranty deed and failed to convey marketable title. The trial court held a bench trial, upon which the court entered written findings of fact and conclusions of law. It concluded that the judgment against the HOA was an encumbrance on the Property and that Ensberg breached the covenant against encumbrances, though it also concluded that the judgment did not render title to the Property unmarketable. The court concluded that the Nelsons' damages consisted of the difference between the market value of the Property without the encumbrance and the market value of the Property with the encumbrance. For the former, the court used the sale price of the failed sale to the prospective buyers ($216,000).

For the latter, the court used the principal amount owing to the first lien holder at the time of the trustee's sale ($129,733). The difference was $86,267.00.[3] The court next concluded that Ensberg's claim for breach of the promissory note failed because there was a failure of consideration at the time the parties entered into their contract. The court awarded the Nelsons attorney's fees and costs under a provision in the promissory note and entered judgment. Ensberg appeals.

DISCUSSION

Ensberg contends the trial court erred in concluding that (1) he breached the warranty against encumbrances and (2) his claim for breach of the promissory note failed due to a lack of consideration.[4] We review de novo a trial court's conclusions of law following a bench trial. Edmonson v. Popchoi, 155 Wn. App. 376, 382, 228 P.3d 780 (2010), aff'd, 172 Wn.2d 272, 256 P.3d 1223 (2011).

Breach of Statutory Warranty Deed

A grantor conveying land by statutory warranty deed makes the following covenants to the grantee:

> (1) That at the time of the making and delivery of such deed he or she was lawfully seized of an indefeasible estate in fee simple, in and to the premises therein described, and had good right and full

[3] The trial court nonetheless recognized that the amount of any potential encumbrance against the Property (as one of 42 lots) was unknown. It stated, in Conclusion of Law 2.3, "Here the exact amount of the encumbrance may not be known. It appears to have been anywhere from zero to $523,474.00 at the time the plaintiff sold the property to the defendants, but it was nevertheless a burden upon the land." Clerk's Papers (CP) at 20.

[4] Ensberg also argues that the judgment below must be reversed because damages were based on insufficient and speculative evidence. We do not reach this argument given that we reverse based on the trial court's erroneous conclusion that he breached the warranty against encumbrances.

> power to convey the same; (2) that the same were then free from all encumbrances; and (3) that he or she warrants to the grantee, his or her heirs and assigns, the quiet and peaceable possession of such premises, and will defend the title thereto against all persons who may lawfully claim the same, and such covenants shall be obligatory upon any grantor, his or her heirs and personal representatives, as fully and with like effect as if written at full length in such deed.

RCW 64.04.030. "These covenants include both 'present' covenants, such as the warranty of seisin, which are breached at conveyance, and 'future' covenants, which may be breached or become effective after conveyance." Mastro v. Kumakichi Corp., 90 Wn. App. 157, 163, 951 P.2d 817 (1998) (citation omitted). The covenant against encumbrances is a present covenant, "and, if breached at all, is broken at the time it is made." Moore v. Gillingham, 22 Wn.2d 655, 661, 157 P.2d 598 (1945) (citations omitted).

An encumbrance has been defined by the Washington Supreme Court as

> any right to, or interest in, land which may subsist in third persons, to the diminution of the value of the estate of the tenant, but consistent with the passing of the fee; and, also, as a burden upon land depreciative of its value, such as a lien, easement, or servitude, which, though adverse to the interest of the landowner does not conflict with his conveyance of the land in fee.

Hebb v. Severson, 32 Wn.2d 159, 167, 201 P.2d 156 (1948) (citations omitted). In addition to liens, easements, and servitudes, encumbrances include outstanding mortgages, leaseholds, restrictive covenants, and existing violations of a restrictive covenant are encumbrances. 18 WASHINGTON PRACTICE REAL PROPERTY § 14.3 (citing Schaad v. Robinson, 59 Wash. 346, 109 P. 1072 (1910) (outstanding mortgages); O'Connor v. Enos, 56 Wash. 448, 105 P. 1039 (1909) (leaseholds); Williams v. Hewitt, 57 Wash. 62, 106 P. 496 (1910) (restrictive

covenants); Hebb, 32 Wn.2d 159 (existing violation of restrictive covenant)). Unpaid property taxes have also been held to be encumbrances. Moore, 22 Wash. at 660-61 (warranty against encumbrance broken upon delivery of deed because of unpaid property taxes due at the time of delivery of deed).

Ensberg contends the trial court erred in concluding that he breached the warranty against encumbrances when he conveyed the Property to the Nelsons. We agree. The judgment against the HOA was not an encumbrance against the Property because the evidence did not show that the judgment constituted a "right to, or interest in" the Property subsisting in the HOA or other judgment debtors. There is no dispute that Ensberg, the owner of the Property, was not a judgment debtor in the judgment against the HOA. There is no dispute that, at the time he conveyed the Property to the Nelsons, there was no lien on the Property as a result of the judgment against the HOA.[5]

The Nelsons contend that, nonetheless, the possibility of a future assessment by the HOA from lot owners—as noted in the preliminary title commitment—to pay the judgment meant the judgment was an encumbrance on the Property. They cite a California decision, O'Toole v. Los Angeles Kingsbury Court Owners Ass'n., 126 Cal.App.4th 549 (2005), in support of their position.

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[5] By statute, a judgment can attach as a lien against real property owned by a judgment debtor:

> The real estate of any judgment debtor, and such as the judgment debtor may acquire, not exempt by law, shall be held and bound to satisfy any judgment of the district court of the United States rendered in this state and any judgment of the supreme court, court of appeals, superior court, or district court of this state, and every such judgment shall be a lien thereupon to commence as provided in RCW 4.56.200 and to run for a period of not to exceed ten years from the day on which such judgment was entered . . . .

RCW 4.56.190.

We reject the Nelsons' contentions. There was no evidence below that the HOA had the definite right, power, or authority to assess the owner of the Property to pay the judgment or the authority to attach a lien on the Property for any failure to pay an assessment. The HOA's bylaws, covenants, and governing documents were not exhibits in the trial, and the note in the preliminary title commitment is not evidence of the HOA's power to assess lot owners. As Ensberg notes, by statute, a judgment against a condominium association is a lien in favor of the judgment lienholder against all of the units in the condominium.[6] But this case does not involve a condominium association, the statute does not apply, and the Nelsons point to no statutes that do apply. The evidence establishes, at most, that the judgment against the HOA could, in the future, if the HOA had the power to assess lot owners, result in a lien (of a presently unknown amount) against lot owners. This fails to show the existence of a present breach of the warranty against encumbrances at the time Ensberg conveyed the Property to the Nelsons.

O'Toole, aside from being non-binding, is inapposite. There, a plaintiff obtained a judgment against a condominium homeowner's association, but the association refused to pay the judgment and refused to levy a special emergency

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[6] The statute provides,

> (1) Except as provided in subsection (2) of this section, a judgment for money against the association perfected under RCW 4.64.020 is a lien in favor of the judgment lienholder against all of the units in the condominium and their interest in the common elements at the time the judgment was entered. No other property of a unit owner is subject to the claims of creditors of the association.

RCW 64.34.368.

assessment against its members. O'Toole, 126 Cal.App.4th at 551. The plaintiff obtained an order appointing a receiver and compelling the association to levy the assessment. Id. On appeal, the court interpreted and applied a California statute in holding that the association could be compelled to impose an assessment to pay the judgment in question. See id. at 553-59. The Nelsons point to no analogous Washington statutes that apply here so that the HOA could be compelled to impose an assessment against lot owners to pay the judgment.

Marketability of Title

The Nelsons argue that even if Ensberg did not breach the warranty against encumbrances, this court should affirm the judgment on the basis that he breached his duty to convey marketable title.[7] The Nelsons rely primarily on Shinn v. Thrust IV, Inc., 56 Wn. App. 827, 786 P.2d 285 (1990).

In Shinn, a buyer of property refused to close, advising the seller that building restrictions constituted an unacceptable encumbrance and/or defect. Shinn, 56 Wn. App. at 830-32. The buyer was also concerned about the potential for litigation by third parties because the property was part of a replat that was done without the required approval of other lot owners. Id. at 831-32. The trial

[7] The parties disagree as to whether this argument can be raised on appeal as a basis for affirming the trial court's judgment. The Nelsons contend that it can, citing Barber v. Peringer, 75 Wn. App. 248, 877 P.2d 223 (1994) for the proposition that an appellate court can decide a case on any legal theory established by the pleadings and supported by the proof. Ensberg contends that because the issue of marketable title was argued and rejected below and neither party appealed on that issue, the Nelsons cannot raise it on appeal. We agree with the Nelsons and will consider their argument regarding marketability of title. The Nelsons prevailed below and seek no further relief from this court. As such, they were not required to file a cross-appeal of the trial court's ruling on marketable title to argue that this court may affirm on that basis. See State v. Bobic, 140 Wn.2d 250, 257, 996 P.2d 610 (2000) (State not required to file cross-appeal to argue alternative ground for sustaining trial court's order where State prevailed below and did not seek affirmative relief from court on appeal).

court concluded that the buyer breached the purchase and sale agreement. Id. at 841. On appeal, the buyer argued that its performance was excused because the sellers failed to deliver marketable title as required by the agreement, which stated that "'title of seller is to be free of encumbrances or defects except those acceptable to Purchaser.'" Id. This court held that there was a defect in title because, due to the replat, the building restriction was a potential restriction on the buildable area of the replatted lots, and the legal uncertainty as to whether the "'one dwelling per lot'" restriction applied to the replatted lots raised a "real prospect of litigation" and put the purchaser in the position of not knowing where a dwelling could legally be built on the lot. Id. at 845-46. The court also agreed with the buyer that the replat's violation of RCW 58.12.030 clearly exposed a purchaser of the property to litigation. It concluded, "Here, the record demonstrates that real doubts exist regarding the title to Lot 2, and that there is a reasonable probability of litigation arising from the plat restriction and the violation of RCW 58.12.030." Id. at 848. Therefore, title was not marketable.

The Nelsons cite the following statement from the court's discussion in Shinn:

> The Washington Supreme court has defined marketable title 'as one being free of reasonable doubt and such as a reasonably informed and intelligent purchaser, exercising ordinary business prudence, would be willing to accept. Such a title need not be perfect in the sense that it is free from every conceivable technical criticism or suspicion, but only from those possibilities of a defect which would give rise to a reasonable question as to its validity.'

Shinn, 56 Wn. App. at 847 (quoting Brown v. Herman, 75 Wn.2d 816, 823, 454 P.2d 212 (1969) (internal citation omitted)).

We conclude that Ensberg did not provide unmarketable title. For the same reasons he did not breach the warranty against encumbrances, the title to the Property was not unmarketable due to the judgment against the HOA. Unlike in Shinn, where there was a known, present violation of a statute and present uncertainty as to where a purchaser could legally build on the lot, here, a judgment against the HOA that might at some point result in an assessment (of an unknown amount) on lot owners did not "give rise to a reasonable question as to" the validity of title to the Property.

Breach of Promissory Note Claim

Ensberg next contends the trial court erred in concluding that there was a lack of consideration exchanged in the underlying contract due to the encumbrance against the Property and that, therefore, his claim for breach of the promissory note failed. We agree. The Nelsons contend that Ensberg's failure to convey unencumbered and marketable title constituted a failure of consideration for the promissory note. But because we hold that Ensberg did not breach the warranty against encumbrances or provide unmarketable title, we necessarily conclude that the Nelsons' argument is without merit. We reverse and remand for entry of judgment on Ensberg's claim.[8]

[8] The Nelsons do not dispute that they failed to make all of the payments required under the promissory note and that the total payments they made left a balance owing of $50,012.34 plus interest at the default rate of 18 percent per annum. The Nelsons do not dispute that Ensberg made a demand for payment or that they failed to pay.

Attorney's Fees

The trial court awarded attorney's fees to the Nelsons under a provision in the promissory note that states:

> 10. ATTORNEYS' FEES AND COSTS: Maker shall pay all costs incurred by Holder in collecting sums due under this Note after a default, including reasonable attorneys' fees, whether or not suit is brought. If Maker or Holder sues to enforce this Note or obtain a declaration of its rights hereunder, the prevailing party in any such proceeding shall be entitled to recover its reasonable attorneys' fees and costs incurred in the proceeding (including those incurred in any bankruptcy proceeding or appeal) from the non-prevailing party.

Ex. 3. Because we reverse and remand the judgment in favor of the Nelsons, we reverse the trial court's award of attorney's fees to the Nelsons and remand with instructions to award attorney's fees incurred below to Ensberg. We also award attorney's fees on appeal to Ensberg.

Reversed and remanded.

Spearman, A.C.J.

WE CONCUR:

Cox, J.

APPENDIX B

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

ERIK D. ENSBERG, **Plaintiff/Appellant,** -vs- JASON D. NELSON and FRANCINE E. NELSON, husband and wife, and the marital community comprised thereof, **Defendants/Respondents.**	**NO. 69644-1-I** **DECLARATION/ ARGUMENT OF DAVID C. HAMMERMASTER RE: MOTION TO PUBLISH PURSUANT TO RAP 12.3**

The undersigned hereby declares as follows:

That at all times hereinafter mentioned, I was and am now a citizen of the United States and of the State of Washington, a resident of Pierce County in said State, over the age of eighteen years, and competent to be a witness therein. That your Declarant is the attorney for the Plaintiff/Appellant in this cause of action. That your Declarant's statement is made based upon personal knowledge and/or argument.

SIX CRITERIA FOR PUBLISHING THIS COURT'S OPINION:

(1) Since the movant in this case is a party to the case, the first criteria is not applicable.

(2) The movant believes that publication is necessary for the following reason:

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The issues addressed in this case affect the general public and their involvement in the sale and purchase of real estate. At one time or another, the vast majority of people are involved in the purchase and sale of real estate. As part of those transactions, virtually the majority of transactions involves a title insurance company providing title insurance to the purchaser. There is a growing misconception that the title insurance report is a statement about the law or the legal condition of certain real property. In realty, a title insurance company simply assesses the level or degree of risk it is willing to take for the premium it receives. In that instance, the title insurance company lists everything that they believe poses an unacceptable level of risk as an exception to their coverage.

There is the mistaken interpretation that any item identified in a title insurance company's list of exceptions acts as a legal and enforceable lien against the property. This Court's opinion clarifies that misconception and places the purchaser and seller on a proper playing field in understanding the distinction between liens and risk assessment by a title insurance company.

(3) The issue raised by this case and the Court's opinion is one that has never been addressed by an Appellate Court in the State of Washington. In fact, the movant (through his attorney) could not find any case throughout the United States that landed directly on point. That is,

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whether a judgment against a homeowner's association acts as a judgment lien thereby affecting a warranty granted by a warranty deed of one (1) of the lot owners within that association. The legislature has seen fit to specifically address this issue as relates to condominiums and condominium associations, but the issue (to date) had not been addressed by the legislature or any other appellate decisions. In that way, this settles a previously unsettled issue and/or resolves a particular question of law.

(4) For the same reasons set forth in Paragraph (2) herein, this Court decision specifically clarifies the general principles relating to warranties granted by a Statutory Warranty Deed. It more fully and clearly identifies what items on a title report may or may not act as an encumbrance or breach of a warranty deed conveyed by a homeowner.

(5) As previously asserted in (3) hereinabove, the issues addressed in this Court's opinion is of general public interest and importance. It is believed that the vast majority of Washington State residents have or will in the future involve themselves in a real estate transaction. Title insurance companies are often used in those transactions. This case helps clarify and reduce the potential "rush to the Courthouse" problem when addressing liens and other notes identified in a title insurance report as an exception to what the insurance company will cover.

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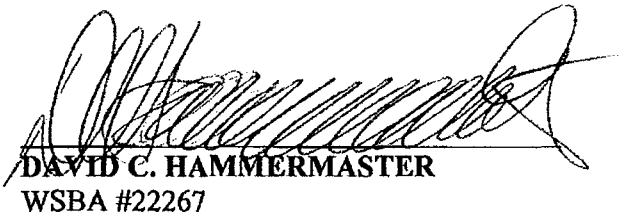
(6) It is the movant's opinion that this decision is not in conflict with any prior opinion of the Court of Appeals. It does, however, enhance and clarify previous decisions of the Court of Appeals and perhaps the Supreme Court itself.

Therefore, the movant hereby respectfully requests that this Court publish the opinion entered herein.

RESPECTFULLY SUBMITED this 19 day December, 2013.



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