IN THE SUPREME COURT OF THE STATE OF OREGON

JOHN HARKNESS and SHERRI HARKNESS, Plaintiffs-Appellants, Petitioners on Review, v. JACK R. PLATTEN, Defendant-Respondent, Respondent on Review.	)	Washington County Circuit Court Case No.: C092970CV Court of Appeals No.: A147439 Supreme Court No.: S063222

BRIEF ON THE MERITS OF *AMICUS CURIAE*
OREGON TRIAL LAWYERS ASSOCIATION
IN SUPPORT OF PETITIONERS ON REVIEW

Petition for review of the decision of the Court of Appeals on appeal from a judgment of the Circuit Court for Washington County, Honorable Charles D. Bailey, Judge.

Opinion Filed: April 8, 2015

Author of Opinion: Hon. Rex Armstrong, Presiding Judge
Concurring Judges: Hon. Lynn R. Nakamoto and Hon. James C. Egan, Judges.

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I. INTRODUCTION

Amicus Oregon Trial Lawyers Association ("OTLA") files this brief on the merits in support of Petitioners on Review. The Oregon Court of Appeals concluded as a matter of law that a loan officer who represented two mortgage companies was not acting within her apparent authority when she convinced her customers to take out real estate mortgage loans and then used the proceeds to make real estate investment loans to others. *Harkness v. Platten*, 270 Or App 260, 348 P3d 1145 (2015). As discussed below, an objectively reasonable customer could readily believe that the agent, who was using her principals' offices and stationery, was acting within her apparent authority for the principal when she facilitated both sets of loan transactions.

This Court should adopt a rule by which an agent may bind a principal to a transaction when the agent sells not only the principal's clearly approved products or services to customers, but sells any closely related products or services (whether approved or not) while using the principal's name or facilities.

II. QUESTION PRESENTED AND PROPOSED RULE OF LAW

Question Presented

Whether a loan company may have liability based on its "apparent authority" when its loan officer, using the company's name and facilities, used

both legitimate company-approved mortgages and unapproved real estate loans to defraud the company's customer?

Proposed Rule of Law

When a company cloaks its agent with apparent authority to sell its products or services, the company has potential liability as a principal for its agent not only for the agent's misconduct related to the actual products or services sold by the company, but also for the sale of any reasonably related products or services sold while using the company's name or facilities. As applied here, a loan company may be held liable for the acts of its agents in selling both approved home mortgage loans as well as closely related, but unapproved, real estate investment loans.

III. STATEMENT OF THE CASE

A. Nature of the Proceeding Below

This is a legal malpractice action brought by clients who allege their former attorney committed malpractice when settling a case for them that arose out of a fraudulent investment scheme. OTLA does not express any opinion on the legal malpractice case itself. An issue in the underlying investment case that was settled (the "case within the malpractice case") is whether the plaintiffs had any claim against their real estate mortgage companies, Sunset Mortgage Company ("Sunset") and Directors Mortgage, Inc. ("Directors") for those

companies' loan officer's conduct in selling plaintiffs fraudulent real-estate investment loans and notes while using the companies' name and facilities.

The trial court granted the defendant lawyer's motion for directed verdict based on the conclusion that plaintiffs could not prove their underlying case against Sunset or Directors and, therefore, could not bring a claim against the defendant lawyer for malpractice in settling that case. The trial court concluded that no reasonable juror could find that Sunset or Directors' loan officer had the apparent authority to sell the real estate investment loans and notes that gave rise to plaintiffs' damages.

The Court of Appeals affirmed and similarly concluded as a matter of law that the Sunset and Director's loan officer only had apparent authority to broker conventional home mortgages to plaintiffs and not sell them the other related real estate investment loans.

B. Concise Statement of Facts

OTLA accepts and adopts the statement of facts that are set forth in the Court of Appeals' opinion, but disagrees with the inferences drawn by the Court of Appeals with respect to those facts.

IV. ARGUMENT

A. Agency Law Supports a Broad Rule that Protects the Public from Both a Company's Sale of Clearly Approved Products and Services and Any Other Reasonably Related Products and Services Sold While Using the Company's Name or Facilities.

In a modern economy, most transactions are not directly handled by principals, but by their agents. Companies act through employees and other agents who sell the companies' products and services. The law of agency permits companies and other principals to expand exponentially their business to potentially millions of consumers who, rather than dealing with a single principal, deal with multiple agents who sell their principal's goods and services.

Agency law has developed to support the expansion of the principal's reach. Thus, an agent can legally act for a principal in expanding the principal's sales if the agent acts with "actual authority," which can be either express or implied authority, to conduct sales for the principal. *Wiggins v. Barrett & Associates, Inc.*, 295 Or 679, 686, 669 P2d 1132 (1983). The principal also bears some risk and responsibility for an agent's acts even when those acts are outside of her actual authority. Under apparent authority,

> a principal may be held bound to a third person for an act of the agent completely outside the agent's implied (or express) authority if the principal has clothed the agent with apparent authority to act for the principal in that particular. In other words, the principal permits the agent to appear to have the authority to bind the principal.

Id. at 687. Therefore, agency law provides the principal with the benefits of expanding its reach through countless approved agents in exchange for some responsibility for an agent's acts under its apparent authority.

Agency law does not support a finding of apparent authority in every instance where a third party may believe that an agent is acting within the principal's authority. Rather,

> [a]pparent authority to do any particular act can be created only by some conduct of the principal which, *when reasonably interpreted*, causes a third party to believe that the principal consents to have the apparent agent act for him on that matter.

Jones v. Nunley, 274 Or 591, 595, 547 P2d 616 (1976) (emphasis added). *See also Eads v. Borman*, 351 Or 729, 737, 277 P3d 503 (2012) (holding that a third party's reliance on the apparent authority of an agent to act for a principal must be based on "objectively reasonable" reliance on the conduct of the principal); *Restatement of the Law (Second) Agency*, § 8 comment a ("[A]pparent authority exists only with regard to those who believe and have reason to believe that there is authority[.]").

This Court has addressed apparent authority issues in a case that similarly involved an investment-related fraud. In *Badger v. Paulson Investment Co. Inc.*, 311 Or 14, 803 P2d 1178 (1991), a securities brokerage firm ("Paulson") expressly authorized its brokers to sell securities to the public, but the brokerage firm did not authorize the sale of "unregistered" securities – ones not registered

with federal or state securities regulators. Despite the fact that Paulson "expressly forbade" its brokers from selling unregistered securities, this Court held Paulson could be liable for its brokers' conduct because the brokers acted out of Paulson's offices in selling the unregistered securities, used Paulson's stationery in promoting the sales, and took calls at Paulson's offices regarding the disputed sales. *Badger*, 311 Or at 25-27. Paulson also had not informed the investing public that its brokers were *not* authorized to sell certain securities. *Id*. This Court correctly concluded that the principal when approving its brokers' sale of securities to the public had engaged in conduct that "when reasonably interpreted" caused third parties to believe the broker had authority to sell even unapproved securities. *Id.* at 24.

B. Sunset and Directors' Agent Had Apparent Authority to Sell the Disputed Real Estate Investment Notes and Loans; or, in the Alternative, There is a Question of Fact for the Jury.

Based on *Badger* and the Oregon case law cited above, this Court could hold as a matter of law that the Sunset and Directors' loan officer had the apparent authority to sell the unapproved real-estate investment notes and loans that harmed plaintiffs. As in *Badger*, the Sunset and Directors' loan officer was clearly authorized to broker or sell certain real estate loans (home mortgages), but was apparently not expressly approved to sell other real estate related investment notes and loans. Despite this, an objectively reasonable customer could believe that the loan officer had authority to sell the unapproved real

estate investment notes or loans due to (a) the close relationship between these two different real estate loans; (b) the fact that the loan officer operated out of Sunset and Directors' offices, which were in the business of brokering real estate loans, and used their stationery; and, (c) as in *Badger*, there is no evidence that Sunset or Directors ever instructed the public that its loan officers were *not* allowed to sell particular types of real estate loans.

This Court could conclude as a matter of law that where an agent has authority to sell certain products, like home loan mortgages, it takes the risk that it has created apparent authority for its agents to sell closely related products, other real estate investment loans, when the agent uses the company's name or facilities.

At a minimum, and based on the procedural posture below, the facts here raise a triable issue of fact for the jury to consider. *See Ince v. AMEV Investors, Inc*., 122 Or App 66, 70, 857 P2d 165 (1993) (holding that the agent's use of the company business card could be found by a fact finder to be a manifestation of the agent's apparent authority). The Court of Appeals concluded that the hard money investment loans that the agent made in this case – using money the agent obtained by getting plaintiffs to take out approved home mortgages – was an entirely separate investment scheme that no reasonable person would understand to be related to the sale of home mortgages. *Harkness*, 270 Or App at 273. However, based on the facts of this particular case, the agent's sale of

the approved product (a home mortgage loan) was a necessary part of the entire fraudulent investment scheme; the agent used the money she raised from the approved real estate mortgages on the plaintiffs' property to finance the unapproved real estate investment loans that she created.

Moreover, as discussed in OTLA's amicus brief in support of the Petition for Review, the distinction between a traditional home mortgage and a real estate investment loan is not obvious even to sophisticated investors and lawyers. *See* OTLA Amicus Brief in Support of Petition for Review, pp. 7-8. As previously briefed, the Oregon Securities Laws define a *security* to include a "note * * *, bond, debenture, evidence of indebtedness * * * real estate paper sold by a broker-dealer, mortgage banker, mortgage broker or [certain other banks and financial institutions]." ORS 59.015(19)(A). It is error to conclude as a matter of law that no reasonable customer would believe that a loan officer was only authorized to sell home mortgages, but not related real estate investment loans. Oregon statutory law, itself, does not readily identify the difference.[1]

Here, the agent, acting within the principals' offices and using the principals' names and stationery, undertook one continuous real estate loan

[1] This case does not require the Court to decide the difference, if any, between a home mortgage and a security and the answer can be heavily fact dependent. However, there is sufficient uncertainty in this area that it is error to conclude as a matter of law that an everyday consumer would clearly understand the difference between an approved home mortgage and an unapproved real estate investment loan.

investment scheme. To call one an obviously approved mortgage deal, and the other a clearly unapproved real estate investment, draws too fine a distinction.

V. CONCLUSION

For the reasons stated above, this Court should reverse the Court of Appeals and trial court, and remand to the trial court for further proceedings.

DATED this 8th day of October, 2015.

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CERTIFICATE OF COMPLIANCE

I certify that (1) this brief complies with the word-count limitation in ORAP 5.05(2)(b) and (2) the word count of this brief (as described in ORAP 5.05(2)(a)) is 1,945 words.

I certify that the size of the type in this brief is not smaller than 14 point for both the text of the brief and footnotes as required in ORAP 5.05(4)(f).

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CERTIFICATE OF FILING AND SERVICE

I certify that on October 8, 2015, I filed the original of **BRIEF ON THE MERITS OF AMICUS CURIAE OREGON TRIAL LAWYERS ASSOCIATION IN SUPPORT OF PETITIONERS ON REVIEW** with the State Court Administrator in .pdf, text-searchable format using the Oregon Appellate eCourt filing system in compliance with ORAP 16, as adopted by the Supreme Court.

All participants in this case are registered eFilers and will be served via the electronic mail function of the eFiling system. If any are not current upon filing, they will be served a copy by United States mail and a courtesy electronic copy by electronic mail.

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