CHAPTER ONE

WHAT IS TITLE INSURANCE?

Title insurance can insure any right of use or ownership in land or personal property. It can insure against past events and future events. Although it primarily insures title to property it can offer protection for some physical conditions.

CHAPTER ONE IN A NUTSHELL

Title insurance does each of the following things:

- Title insurance protects the insured, who is a lender or an owner of the land, against actual monetary loss.
- Title insurance protects against third-party rights or claims that may or may not be recorded in the local land records.
- Title insurance primarily insures against third-party rights or claims that exist before the title insurance policy is issued.
- Title insurance agrees to hire an attorney to protect the insured if a third-party claims a right or claim to the land.
- Title insurance insures other matters, such as execution of promissory notes and security interests in personal property, in some states.

I. WHAT RIGHTS ARE INSURED?

A. Rights in Real Property

Title insurance insures with respect to the title to real property. Such insurance may insure various rights in and uses of the land, such as fee simple, easement, profit a prendre, some licenses, surface rights, air rights, subsurface rights, mineral rights, covenants running with the land, and liens.

B. Jurisdictions Where Available

Title insurers may operate within all jurisdictions of the United States except in Iowa (but title insurers may insure title to land in Iowa from other locations), Guam, Northern Mariana Islands, Puerto Rico, U.S. Virgin Islands, and numerous foreign countries (either by doing business in the foreign countries or by issuing title policies in the United States).

C. Standard Title Policy

The standard title insurance policy insures against

- defects in the title;
- liens and encumbrances on the title;
- adverse ownership of or rights in the title;
- lack of legal right of access to the land;
- unmarketability of title;
- validity of the lender's insured mortgage; and
- priority of the lender's insured mortgage.

Title insurance agrees to provide defense as to insured matters, and this may constitute thirty percent to forty percent of the aggregate claims-related expenses of the title insurer.

D. Personal Property

Title insurance also may insure with respect to the security interests and other rights in the personal property in about half of the states, including Arkansas, California, Delaware, Florida, Illinois, Indiana, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Mississippi, Missouri, Nebraska, Nevada, New York, North Carolina, North Dakota, Oklahoma, South Carolina, South Dakota, Texas, Utah, Vermont, Virginia, Washington, West Virginia, and Wisconsin, and also in Puerto Rico. Uniform Commercial Code (UCC) insurance as a casualty product may be available for issuance in some other jurisdictions.

E. Physical Condition of the Land

Title insurance insures the title to the land, and generally does not insure as to the physical condition of the land. There are widespread exceptions to this generalization; in some cases, title insurance does insure with respect to the physical condition of the land, such as the types of improvements located on the land (the American Land Title Association (ALTA) 22 Series endorsements), the location of improvements (the ALTA 9 Series endorsements (Covenants, Conditions, and Restrictions; Encroachments; and Minerals) and the ALTA 28 Series endorsements (Encroachments, Boundaries, and Easements), as well as the nature of physical access (the ALTA 17 Series endorsements). Each of these types of coverage is facilitated by a survey or inspection of the land. In a similar fashion, title insurance may insure as to the physical occupancy of the land by deleting any exception for the rights of the parties in possession or the rights that would be discovered by an inspection or survey of the land.

F. Statutory Definitions

The following are examples of the definitions of "title insurance business" and "title insurance policy" in § 44-1981 of the Nebraska Revised Statutes that were derived from the National Association of Insurance Commissioners (NAIC) Title Insurers Model Act:

> Title insurance business or business of title insurance means:
>
> (a) Issuing as a title insurer or offering to issue as a title insurer a title insurance policy;
>
> (b) Transacting or proposing to transact by a title insurer any of the following activities when conducted or performed in contemplation of or in conjunction with the issuance of a title insurance policy:
>
> (i) Soliciting or negotiating the issuance of a title insurance policy;
>
> (ii) Guaranteeing, warranting, or otherwise insuring the correctness of title searches for all instruments affecting titles to real property, any interest in real property, cooperative units, and proprietary leases and for all liens or charges affecting the same;
>
> (iii) Handling of escrows, settlements, or closings;
>
> (iv) Executing title insurance policies;
>
> (v) Effecting contracts of reinsurance; or
>
> (vi) Searching or examining titles;
>
> (c) Guaranteeing, warranting, or insuring searches or examinations of title to real property or any interest in real property;
>
> (d) Guaranteeing or warranting the status of title as to ownership of or liens on real property by any person other than the principals to the transaction; or
>
> (e) Transacting or proposing to transact any business substantially equivalent to any of the activities listed in this subdivision in a manner designed to evade the provisions of the Title Insurers Act; . . .
>
> Title insurance policy means a contract insuring or indemnifying owners of, or other persons lawfully interested in, real property or any interest in real property, against loss or damage arising from any or all of the following conditions existing on or before the policy date and not excepted or excluded:

(a) Defects in or liens or encumbrances on the insured title;
(b) Unmarketability of the insured title;
(c) Invalidity, lack of priority, or unenforceability of liens or encumbrances on the stated property;
(d) Lack of legal right of access to the land; or
(e) Unenforceability of rights in title to the land.

The Nebraska definition is consistent with the prevailing understanding of title insurance, which is that a guarantee of a search constitutes title insurance; a warranty of a search is title insurance; and the insurance of other rights in the title to the land, such as the rights arising out of the zoning or building permits, is title insurance.

Another example of a law authorizing the insurance of a broad set of rights relating to real property is § 500.7301 of Michigan Compiled Laws, which authorizes the insurance against matters "adversely affecting the rights of use, enjoyment, or disposition of the real estate."

G. Post-policy Matters

Most state laws, such as in California,[1] Florida,[2] and Texas,[3] clearly allow "post-policy" coverage of matters such as gap coverage, mechanic's lien coverage to the lender, street assessment coverage to the lender, future advances and numerous other endorsements, and several Covered Risks in the ALTA Homeowner's Policy and the ALTA Expanded Coverage Residential Loan Policy. Even in those few states, such as Alabama, Connecticut, Hawaii, Kansas, Nebraska, and Oklahoma, that authorize an insurance policy to insure as to "conditions existing on or before the policy date" or similar language, the statutes do not appear to prohibit post-policy coverage so long as the insurance provided is substantially equivalent.

H. Access

Some states, such as Alabama,[4] do not explicitly address the rights of access to the lands, but this coverage of access is well within the general scope of any definition of title insurance, given that the lack of access might result in an unmarketable title and that access insurance may entail insurance of an easement or other right.

[1] Cal. Ins. Code § 12340.1.
[2] Fla. Stat. § 624.608.
[3] Tex. Ins. Code Ann. § 2501.003.
[4] Ala. Code § 27-25-3.

I. Closing Protection Letters

Many states, such as South Carolina,[5] statutorily authorize closing protection letters, and only one state, New York,[6] prohibits closing protection letters.

J. Statutory Escrow Liability

A few states, including California, Florida, Nebraska, and Utah, impose liability on the title insurers in some cases for certain escrow defalcations by their title insurance agents. An example of such a statute is California Insurance Code § 12376:

> (a) If an underwritten title company is placed into bankruptcy, receivership, or conservation by the commissioner, each title insurer operating under an underwriting agreement with the underwritten title company during the six months prior to the earliest of the conservation, bankruptcy, or receivership shall be liable for its proportionate share of the commissioner's costs and any escrow and sub-escrow account shortages as determined by the calculations set forth in subdivisions (b) and (c).
>
> (b) If, during the six months prior to the earliest of the establishment of a conservation, bankruptcy, or receivership under subdivision (a), the underwritten title company was authorized by underwriting agreements to issue title policies for more than one title insurer, the liability of each title insurer is determined by multiplying the amount of the total escrow and sub-escrow shortages, as well as the costs, and expenses, as set forth in subdivision (c), by that title insurer's percentage of the underwritten title company's net premiums for policies issued by each title insurer during the 12-month period preceding the earliest of the establishment of the conservation, bankruptcy, or receivership, with each title insurer's liability pursuant to this subdivision to be referred to as its proportionate share.

K. Insurance of Promissory Notes

Some states, such as California, Hawaii, Idaho, Vermont, and Wyoming, authorize insurance with respect to promissory notes, such as what appears in California Insurance Code § 12390:

> Every domestic title insurer may issue title policies and may also insure:
>
> (a) The identity, due execution, and validity of any note or bond secured by mortgage.
>
> (b) The identity, due execution, validity, and recording of any such mortgage.

[5] S.C. Code Ann. § 38-75-1010.

[6] N.Y. State Ins. Dep't, Circular Letter No. 18 (Dec. 14, 1992) (on file with author).

(c) The identity, due execution and validity of evidences of indebtedness issued by this State, or by any political subdivision or district therein, or by any private or public corporation.

L. Guarantee of Debts (Mortgage Guarantee)

A majority of states prohibit the title insurer from guaranteeing debts, such as is set forth in Ohio Revised Code § 3953.09 and in Pennsylvania Statutes title 40, § 910-9.

M. Special Prohibitions

A few states do not allow issuance of usury endorsements (Alaska, Idaho[7], Kansas, and Missouri), and such endorsement is not approved in Delaware, Florida, New Jersey, New Mexico, New York, Oregon, Pennsylvania, Texas, and Vermont), zoning endorsements (for example, New York), or insuring around outstanding enforceable liens (for example, Idaho[8] and Texas[9]). Texas Procedural Rule P-8 also requires the following promulgated mechanic's lien exception in policies insuring construction loan mortgages:

> "Any and all liens arising by reason of unpaid bills or claims for work performed or materials furnished in connection with improvements placed, or to be placed, upon the subject land. However, the Company does insure the Insured against loss, if any, sustained by the Insured under this Policy if such liens have been filed with the County Clerk of _______________ County, Texas, prior to the date hereof."
>
> AND THE FOLLOWING "PENDING DISBURSEMENT" PARAGRAPH:
>
> "Pending disbursement of the full proceeds of the loan secured by the lien instrument set forth under Schedule A hereof, this policy insures only to the extent of the amount actually disbursed, but increases as each disbursement is made in good faith and without knowledge of any defects in, or objections to, the title up to the face amount of the policy. Nothing contained in this paragraph shall be construed as limiting any exception under Schedule B, or any printed provision of this policy."

II. MONOLINE RESTRICTIONS

An understanding of title insurance requires the recognition that title insurers are monoline insurers and may not engage in other lines of insurance. A majority of states have a monoline restriction, as does the NAIC Title Insurers Model Act. Those states include Alabama,

[7] Idaho Admin. Code r. 18.01.25.005.

[8] Idaho Admin. Code r. 18.01.25.005.

[9] Tex. Procedural Rule P-11; Tex. Ins. Code § 2502.003.

Alaska, Arizona, Arkansas, California (expressly extraterritorial), Colorado, Connecticut, the District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Kentucky, Louisiana, Maine, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New York (expressly extraterritorial), Ohio, Oklahoma, Oregon (in Oregon only), Pennsylvania, South Dakota, Tennessee, Texas, Utah (if order, applicable outside of state), Virginia, Washington, Wisconsin (possible extraterritorial application), and Wyoming.

The monoline approach is prevalent in much of the United States, in contrast with the multiline insurance practiced in the United Kingdom and the remainder of Europe.

The reasoning of the monoline restriction is that

1. some lines of insurance require specialized expertise, and these will be maintained best by separate lines of insurance;
2. some lines are higher or lower risks, and it is best to maintain the separateness of the risks; and
3. given varied risks, the reserves can best be maintained by retaining separate lines for the different types of risk.

Typifying the monoline statute is the Louisiana Code,[10] which states that an insurer transacting any kind of insurance other than title insurance shall not be eligible to transact the business of title insurance in Louisiana.

California Insurance Code § 12360 acts as a multistate monoline restriction and prohibits the title insurer from violating its limitations by engaging in any other lines of insurance anywhere in the United States.

New York's monoline law requires that insurers doing business in New York comply with the monoline requirements for all business nationally (named the "Appleton Rule" because the rule was adopted when Henry Appleton was deputy superintendent) set forth in New York Consolidated Insurance Laws § 1106.

This application of an extraterritorial monoline restriction actually seems to be inherent in most monoline limits, unless specifically addressed by the law. Otherwise, a multiline insurer, engaged in practices in other states that would be considered extrahazardous if conducted in the host state, may undertake those practices, such as mortgage guaranty, in other locations and incur the same risk profile as a multiline insurer in the host state.

[10] La. Rev. Stat. § 22:515.

III. APPLICATION OF MONOLINE RESTRICTIONS TO PROHIBIT OTHER TYPES OF INSURANCE

A. Warranties

Title insurance has always competed against warranties of title, title searches, and title examinations, with or without abstracts of title. The advantage of title insurance over these alternatives has long been argued: a title insurer's deep pocket generally exists to pay a title insurance claim, but a deep pocket does not necessarily exist in a claim against the warrantor, searcher, or examiner, although the warrantor may be financially strong, or the searcher or examiner may have malpractice or errors or omissions insurance, subject to deductibles, maximum liability, and term of coverage.

Warranties, with agreed-upon limits of liability, may be structured on the basis of (1) a standup examination of public records; (2) an examination of an abstract of title, which may be limited in the time or nature of the search, and which is inherently based solely upon information in the real property records; (3) a credit report; or (4) a combination of these alternatives. In some jurisdictions, to qualify as an abstract, however, the list may be required to include all recorded documents in the chain of title. The warranty may be backed by an errors and omission policy or other property and casualty policy that may inure only to the warrantor.

However, some warranties will be viewed as a type of illegal title insurance. Donald Bryan, Acting Commissioner of Bank and Insurance New Jersey, stated in Bulletin No. 05-05 that the fact that an insurance product is labeled as a warranty does not prevent it from being considered title insurance.[11] Paula A. Flowers, Tennessee Department of Commerce and Insurance Commissioner, also concluded in a bulletin that mortgage impairment products covering second and third mortgages were title insurance because they insured against loss by reason of defective titles or incorrect searches.[12]

B. Other Recent Products

In the most recent decades, three additional products have been offered that have competed with title insurance: Title Option Plus (TOP), Radian Lien Protection (RLP), and Mortgage Impairment Insurance (MII). The essence of the last two has been to require that a legal description (such as through the last deed, as one alternative) be secured, an affidavit of the borrower be used, an exception be made to liens on the credit report, and the parameters of the loan programs be acceptable (such as the loan-to-value ratio (LTV),

[11] N. J. Dep't. of Banking and Ins. Notices and Bulletins, Bulletin No. 05-05 (Mar. 9, 2005), *available at* http://www.state.nj.us/dobi/bulletins/blt05_05.pdf.

[12] Tenn. Dep't of Commerce and Ins. Notices and Bulletins (Apr. 8, 2004), *available at* https://www.tn.gov/insurance/documents/4-8-04.pdf.

the FICO® credit score, the limitations on late payments within the last 12 months, the type of residential property, and the existing ownership only). The crux of RLP and MII is to insure against liens that are not shown on the credit report. The TOP program is based on a warranty.

C. Title Option Plus

The TOP program consisted of three related contracts: the first agreement was the master agreement, which was a "warranty" by NMI (the lender, Norwest Mortgage, Inc.) to Freddie Mac and Fannie Mae that those mortgages NMI sold to Freddie Mac or Fannie Mae were secured by a first-lien. NMI protected Freddie Mac and Fannie Mae against any title claims, including non-record title matters that may affect Freddie Mac's interest. If a defect was discovered and could not be cured, NMI agreed to repurchase the loan. NMI only warranted the title and priority of the lien if the title search and title report were performed by ATI (the title insurance agent, American Land Title Company, doing business as ATI Title Company, a wholly owned subsidiary of NMI). The second agreement was a title report prepared by ATI to determine that NMI's mortgage was a first-lien. Although ATI remained liable for any defects missed in the title search, NMI assumed the risk of off-record defects. The third agreement was the guarantee agreement by Norwest (the guarantor, Norwest Corporation, the bank holding company that owned NMI) to Freddie Mac or Fannie Mae pursuant to which Norwest guaranteed NMI's title-related obligations to Freddie Mac or Fannie Mae.[13]

TOP was generally, but not universally, determined to be title insurance transacted, sold, or marketed in violation of applicable insurance laws in most, but not all, jurisdictions that administratively or judicially considered it.[14]

Numerous state insurance departments considered TOP:

STATE	TOP CONSIDERATION
Colorado	TOP is title insurance.
Connecticut	TOP is title insurance.
Idaho	The Attorney General concluded TOP is title insurance; a later ruling by a hearings officer determined that TOP is not title insurance.
Illinois	A letter from the Division of Financial Institutions concluded that TOP is title insurance.
Iowa	The Insurance Division concluded that TOP is title insurance.

[13] Norwest Corp. v. State, 571 N.W.2d 628 (Neb. 1997).

[14] *Id.* (TOP is insurance); Div. of Ins. v. Norwest Corp., 1998 SD 61, 581 N.W.2d 158 (TOP is title insurance); *cf.* Lawyers Title Ins. Corp. v. Norwest Corp., 493 S.E.2d 114 (Va. 1997) (TOP is not insurance).

STATE	TOP CONSIDERATION
Kansas	The Insurance Department and hearing determined that TOP is title insurance.
Minnesota	The Commissioner of Commerce concluded that TOP is not title insurance.
New York	The Superintendent of Insurance concluded that TOP is title insurance.
North Carolina	The Attorney General concluded that TOP is title insurance.
Oklahoma	The Insurance Commissioner concluded that TOP is title insurance.
Oregon	The Insurance Division concluded that TOP is title insurance.
Pennsylvania	The Insurance Department concluded that TOP is title insurance, and a later hearing was conducted.
Tennessee	The Department of Commerce and Insurance concluded that TOP is title insurance.
Texas	A letter from the Department of Insurance suggested that TOP is title insurance.
Utah	The Insurance Department concluded that TOP is title insurance.

D. Radian Lien Protection

The RLP was offered as mortgage pool insurance (in a mortgage pool insurance policy) for an entire mortgage pool on second mortgages, home equity mortgages, and refinances by existing owners at a fixed price of $275. The coverage for monetary liens was limited to 50 basis points (0.5 percent of the initial principal) on the mortgage pool. At one time, the program required that loans must be made to borrowers with a FICO® credit score of 570 or greater, the loan amounts were not to exceed $650,000, and the maximum LTV/CLTV (combined loan-to-value ratio) could not exceed 100 percent on loans up to $650,000. The RLP, like some guarantees and limited-coverage home equity policies, did not cover all of the defects in the title (nor have a number of other home-equity products) and did not provide for defense. Standard & Poor's concluded that the RLP was an acceptable substitute on the loans it rated.

The RLP was a limited-coverage policy and thus did not include many of the provisions that normally appeared in an ALTA policy. These differences from the ALTA policies and endorsements were not unique to the RLP; the RLP was similar to some of the other home-equity products used by title insurers. Some of the limitations to the coverage under the RLP included the following:

- The RLP did not insure
    - that the borrower owns the land.
    - against an invalid mortgage because of the failure of the borrower's spouse (or partner in civil union) to join in the mortgage.

  - against liens recorded after the mortgage.
  - the location of a house with the address on the land.
  - the priority over later filed environmental protection liens.
  - against survey matters, such as boundary conflicts and encroachments.
  - against lis pendens or pending suits claiming title.
  - the access to the land.
  - against damage due to the use of the surface for mineral development.
  - the mortgage was valid.
  - against defective recording of mortgage.
  - against forgery or impersonation causing the mortgage or title to be invalid.
  - mortgages, unless the mortgages were duly recorded within 48 hours after the funds were advanced.
- The RLP required the lender to
  - advance money to pay taxes.
  - restore any damaged property.
- The RLP did not promise to hire a lawyer as to the insured matters.
- The RLP had various parameters, such as credit scoring, no purchase money loans, and aggregate loss limits. Aggregate loss limits were not applicable to title insurance home equity products.
- The RLP protected only the named insured.

States considering the RLP to be title insurance included Alabama, Connecticut, Florida, New Mexico, North Carolina, Pennsylvania, and Texas. Illinois, however, concluded that Radian Guaranty, Inc., could sell its RLP if it did not market the product as title insurance, if the claims would be made only if there was a deficiency balance, and if Radian Guaranty, Inc., did not sell other mortgage pool products.

The California Insurance Commissioner subsequently issued a cease-and-desist order that prevented Radian Guaranty, Inc., Amerin Guaranty Corporation, and RadianExpress.com, Inc., from marketing, soliciting, negotiating, and selling the RLP program, which the Insurance Commissioner found to be title insurance under California law and to be an improper combination of mortgage guaranty and title insurance, both of which are subject to extraterritorial monoline limitations. The court of appeal upheld the cease-and-desist order.[15]

E. Mortgage Impairment Insurance

Some polices may insure against loss resulting from

[15] Radian Guar., Inc. v. Garamendi, 127 Cal. App. 4th 1280, 26 Cal. Rptr. 3d 464 (2005).

1. failure to pay real estate taxes;
2. error, neglect, omission, or breach of duty in actual performance or failure to perform activities, including obtaining a tax bill showing ownership, review of credit bureau report showing liens and property address, or owner's affidavit relating to title or impairment by discovery of a previously unknown property interest in the collateral;
3. perfection of a second lien mortgage that could not be obtained despite timely filing of the mortgage;
4. loss by reason of defective title, if the insured required title insurance; and
5. impairment of lien, due to an unknown interest, if the lender required a tax bill showing ownership, a credit report showing liens and property address, and/or an owner's affidavit of title, and presented the (second) mortgage for recording.

Typically, this type of insurance has been offered on junior home equity loans, but it is equally adapted to first lien refinances. It is sometimes offered on a surplus-line basis. Some of the policies are written as master policies with a stated maximum limit of liability. Some policies are called equity or lending-activities policies. The terms used in such a policy often include "lien priority," "lending activities," "mortgage impairment," and "undisclosed liens." This coverage should be contrasted with collateral protection insurance, which provides insurance because of the consumer's failure to provide evidence of insurance and excludes title insurance.[16]

Often, the language used in mortgage impairment policies is rather obviously title insurance. Examples include the following:

- "guarantees the lender's second lien position"
- "Coverage is extended . . . to loss incurred by the Assured . . . due to impairment to the Assured's Second Position Mortgage Interest. . . . The mortgage interest must have been impaired due to previously unknown Mortgage interest or lien held by one who is not liable on the Assured's Second Position Mortgage."
- "your inability to enforce your rights under a second mortgage loan, due to the existence of a superior lien of which you were unaware; solely as a result of you not performing a standard title search prior to recording your lien or encumbrance on property against which you hold a second mortgage interest"
- "guarantees the lender's second mortgage position"
- "indemnifying the Named Insured against loss . . . caused or occasioned by an act or omission of the Borrower, whether fraudulently or not, or a servicer, including a failure to disclose a lien or mortgage position secured by Borrower's property"

[16] *See, e.g.*, 815 Ill. Comp. Stat. Ann. 180/5; N.J. Stat. Ann. § 17:16V-2; W. Va. Code § 46A-3-109a.

- "insures your mortgagor's representations regarding the nonexistence of mortgages, liens, or Judgments, which would impair your intended second mortgage position."
- "Loss means the amount of your second mortgage interest, after foreclosure and sale of the property, you are unable to recover from the proceeds of said sale because of the existence of an encumbrance not known or disclosed to you as required by your loan application and Property Owner Affidavit."
- "WE will pay YOU for Loss, in excess of the deductible amount . . . that is the result of a Foreclosure provided . . . the Superior Lien was recorded before the closing of the Second Mortgage Loan; and . . . YOU had no knowledge of the Superior Lien at the time of the closing of the Second Mortgage Loan because YOU made an intentional decision not to perform a standard title search prior to closing the Second Mortgage Loan."

A number of states have rejected mortgage impairment products because they were construed as title insurance. Those states include Alabama, California, Connecticut, Florida, Illinois, Kansas, New Mexico, North Carolina, Oklahoma, Oregon, Pennsylvania, and Texas.

The ALTA filed a complaint in the U.S. District Court for the Northern District of California on October 26, 2005, in connection with the issuance of "mortgage impairment" insurance and sought a determination that the mortgage impairment/lien priority insurance of the defendants constituted title insurance or illegal bundling of title insurance risks that is prohibited because the defendants are not licensed as title insurers and also sought injunctive relief.[17] It alleged that

> [a]n insurance company that is not a licensed title insurer cannot issue title insurance and cannot provide insurance coverage for a title insurance risk. Indeed, in California, as in the majority of states, title insurance is legislatively mandated to be mono-line, meaning that a licensed title insurer cannot be licensed to issue any other class or line of insurance . . . The risk of loss arising out of undisclosed liens or encumbrances senior to the insured mortgage is commonly referred to in the title insurance industry as lien priority insurance and has always been categorized as title insurance.[18]

The complaint joined as defendants

[17] Am. Land Title Ass'n v. Great Am. Ins. Co., No. C 05-4365 PJH, 2006 U.S. Dist. LEXIS 32771 (N.D. Cal. May 16, 2006).

[18] *Id.*

- Great American Insurance Company, Great American Assurance Company, and Agricultural Insurance Company;
- Group 9, Inc.;
- Seattle Specialty Insurance Services, Inc.;
- Zurich North American and Zurich American Insurance Company;
- Fidelity & Deposit Company of Maryland;
- Colonial American Casualty and Surety Company;
- Empire Indemnity Insurance Company;
- Travelers Indemnity Company of America;
- Guaranty National Insurance Company;
- Deerfield Insurance Company;
- Safeco Insurance Company and Safeco Financial Institution Solutions, Inc.;
- North American Capacity Insurance Company;
- BancInsure, Inc.; and
- Matterhorn Financial Services, Inc.

The ALTA complaint was subsequently dismissed, and the court also declined to exercise jurisdiction under the Declaratory Judgment Act because insurance regulation is left to the states and courts in fewer than half the states had ruled on whether the "lien protection" policy is a policy of title insurance. The court concluded that each individual state must decide who can be licensed to sell title insurance policies.[19]

F. Competitive Title Insurance Products by Title Insurers

Title insurers also developed products that in some respects were modeled on the mortgage impairment products but were issued as title insurance policies. These products entailed a limited public record search to conform to state requirements in some jurisdictions for the examination of title. The products were often conditioned on the review of the loan programs, which inherently included the LTV and FICO® credit score parameters. Often, the policy was a master policy that was issued at a substantially reduced charge on existing owner residential finances of up to $250,000 and insured (similar to the junior loan policy) that the mortgagor was the grantee in the last recorded deed, that there were no recorded monetary liens except those shown in Schedule B, and that there were no taxes due and payable. Other matters covered may have included the priority of future advances and variable rate provisions. The cost was generally significantly less than $100 (often less than $50) for loans of less than $250,000, and the core of some of the programs was reliance on the credit reports for monetary lien information, together with whatever risk

[19] *Id.*

reduction was inherent in the loan program requirements. These title insurance forms avoided errors and delays in the production; however, the logic of the coverage was reliance on the creditworthiness of the borrower, given the lack of complete reliability of the credit reports and the variations in the coverage given.

Examples of these inexpensive products for junior residential loans included the following:

- Fact Master Loan Policy for Residential Junior Mortgages (issued by First American Title Insurance Company)
- Stewart Master Residential Junior Loan Policy, EQUICK Policy, and Master Residential Loan Policy (issued by Stewart Title Guaranty Company)
- Mortgage Impairment Protection Insurance Policy (issued by Old Republic National Title Insurance Company)
- Master Equity Line Loan Policy (issued by LandAmerica)
- Master Lien Protection Loan Policy (issued by Fidelity National Title Insurance Company, Chicago Title Insurance Company, Ticor Title Insurance Company, and Security Union Title Insurance Company)

Typical exceptions included taxes and assessments not yet due and payable; covenants, conditions, and restrictions, whether or not appearing in the public records; easements and servitudes, whether or not appearing in the public records; minerals and mineral rights, whether or not appearing in the public records; liens or rights to liens for services, labor, or material hereafter furnished; survey matters; and any mortgage, judgment, or other lien or encumbrance, whether or not appearing in the public records, that would be (1) disclosed by a borrower's affidavit, (2) shown on a tri-merged credit report, (3) excepted in any prior title policy to the insured or an affiliate, or (4) agreed to or known by the insured. Such policy would be conditioned on a borrower's affidavit and tri-merged credit report, the report reflecting a prior mortgage, recordation within a stated time after funding, and use of the same description shown on the last deed pulled, and it might be subject to a separate service agreement that entailed additional services, including securing a legal description from the last recorded deed. The lender's program might require a minimum 625–650 FICO® credit score and a maximum LTV/CLTV of 100 percent.

With the Great Recession and the large number of loan defaults, reduced home values, and fraud, these title insurance products culminated in significant losses in the industry.

G. Environmental Superlien Coverage

The Connecticut Insurance Department determined that a form of title insurance coverage for environmental liens (unlike the ALTA 8.1-06 and ALTA 8.2-06) was casualty insurance. The Connecticut Insurance Department ruled on a request by Lawyers Title for determination that a title insurer violates the monoline or single-line restrictions on title insurers imposed by Conn. Gen. Stat. § 38-29 of the Connecticut General Statutes if the title insurer insures in a title insurance policy against loss or damage because of loss of priority of the insured mortgage or loss of title to the land because of a statutory lien for the cost of cleanup of a hazardous waste spill imposed by § 22a-452a of the Connecticut General Statutes.[20] The Department concluded that providing coverage in a title insurance policy against this risk would be an impermissible assumption of a casualty risk that is outside the awful business of title insurance.

H. Creditors' Rights Coverage

Creditors' rights coverage insured against stated loss because of (1) insolvency of the seller or mortgagor, (2) unreasonably small capital of the seller or mortgagor, and (3) belief or intent of the seller or mortgagor to incur debts beyond its ability to pay. All of these matters can trigger an avoidance of the transfer or a judgment for money, for example, if the consideration for the loan is given an affiliate or corporate parent of the mortgagor or seller, and not to the mortgagor or seller. Such creditors' rights coverage relating to the current transaction had frequently been provided in many states by all of the major title insurers, principally to lenders.

Creditors' rights coverage could have potentially resulted in catastrophic loss to title insurers when provided on a Loan Policy or an Owner's Policy. For example, in *Official Committee of Unsecured Creditors of Tousa, Inc.* (*In re Tousa, Inc.*), the bankruptcy court invalidated mortgages securing $200 million and $300 million with Wells Fargo as administrative agent and awarded additional damages against the lenders.[21] The court concluded that the subsidiaries did not receive reasonably equivalent value for mortgages granted, were insolvent before and after the transaction, and were left with unreasonably small capital to operate their businesses because of the mortgages. The court avoided the mortgages and ruled that the debtors could recover the value of the land mortgaged with interest for the benefit of the debtors' estates. Underscoring the argument that creditors' rights coverage cannot be safely evaluated, the court rejected two procedures that have been used to underwrite creditors' rights coverage: first, a solvency opinion that was determined not to be credible, and second, "savings clauses" in loan documents (for example, "[S]uch joint and several liability and each such Lien shall be valid and enforceable to the

[20] Memorandum of Decision and Declaratory Ruling Docket No. RD 86-22, Re: Lawyers Title Insurance Company Petition for Declaratory Ruling (Jan. 8, 1987) (on file with author).

[21] Official Comm. of Unsecured Creditors of Tousa, Inc. v. CitiCorp N. Am., Inc. (*In re* Tousa, Inc.), 422 B.R. 783 (U.S. 2009), *decided, quashed by, appeal dismissed by, in part, judgment entered by sub nom*, 3V Capital Master Fund Ltd. v. Official Comm. of Unsecured Creditors of Tousa, Inc. (*In re* Tousa, Inc.), 444 B.R. 613 (Bankr. S.D. Fla. 2011), *reversed and remanded by sub nom*, Senior Transeastern Lenders v. Official Comm. of Unsecured Creditors (*In re* Tousa, Inc.), 680 F.3d 1298 (11th Cir. 2012).

maximum extent that would not cause such joint and several liability or such Lien to be unenforceable under applicable law, and such joint and several liability and such Lien shall be deemed to have been automatically amended accordingly at all relevant times.")

The ALTA 21-06 (Creditors' Rights) was designed for issuance with an Owner's Policy or Loan Policy when insuring with respect to the voidability of an estate or interest or the lien of the Insured Mortgage because of the occurrence on or before the Date of Policy of a fraudulent transfer or a preference under federal bankruptcy, state insolvency, or similar creditors' rights laws, subject to the terms and provisions of the endorsement, the Exclusions from Coverage, and other terms of the policy. The revision or the decertification and withdrawal of the ALTA 21-06 were discussed with the benefit of outside antitrust counsel. The ALTA Board voted to decertify the ALTA 21-06 on February 3, 2010.

The New York State Insurance Department had previously determined that title insurance is not designed to provide creditors' rights coverage. The New York State Insurance Department, in reviewing title insurance policies filed with the Department, stated that

> [i]n view of testimony received and contemporary complexity of corporate deals such as leveraged buy-outs, mergers and acquisitions, and tender offers—often involving and impacting real estate transactions—the Insurance Department has determined that *a creditors' rights exclusion is appropriate and should be included in title insurance policies. Title Insurance was never intended to cover these phenomena. Unrequited creditors of a real estate seller or buyer should not be able to claim against title insurance*.[22]

The Florida Office of Insurance Regulation concluded by letter dated July 17, 2009, that a Creditors' Rights Endorsement (ALTA 21-06) did not provide title insurance coverage:

> *This endorsement is not title insurance* because, in insuring loss or damage sustained by the insured by reason of the avoidance, in whole or in part, or a court order providing some other remedy, based on the voidability of any estate, interest, or insured mortgage because of an occurrence on the date of policy of a fraudulent transfer or a preference under federal bankruptcy, state insolvency, or similar creditors' rights laws, the coverage is prospective. The determination of insurability cannot be based on the evaluation of a reasonable title search as is required by . . . [applicable law].[23]

Subsequently, Texas adopted § 2502.006 of the Texas Insurance Code, which prohibited a title insurer from conducting business in Texas if it provided creditors' rights coverage

[22] Title Ins. Memorandum Decision & Opinion (Nov. 19, 1991) (emphasis added), *available at* http://www.dfs.ny.gov/about/hearings/11032006_title_hear/11032006_tirsa_corr_sub.pdf.

[23] Letter from Fla. Office of Ins. Regulation (July 17, 2009) (emphasis added).

arising out of the transaction vesting title in the insured or creating the lien of the insured mortgage based on a claim of a voidable preference or fraudulent transfer.

This legislation prohibits a title insurer from doing business in Texas if it provides creditors' rights coverage arising out of the current transaction in any other state. This law applies to any title insurance policy delivered, issued for delivery, or renewed (by issuance of a new policy) on or after January 1, 2012.

IV. TITLE EXAMINATION VERSUS CASUALTY INSURANCE

It should be clear that title insurance actually is insurance. The purpose of insurance is to spread risks. *Black's Law Dictionary* defines insurance as a contract in which a person agrees, for consideration, to compensate another person for loss on a particular subject by specified perils.[24] Whether a practice is the business of insurance depends on (1) whether the practice transfers or spreads the insured's risk, (2) whether the practice is an integral part of the relationship of the parties pursuant to the policy, and (3) whether the practice is limited to insurers. For example, while title insurance is insurance, the title search, title examination, and escrow do not spread the risk and are not the business of insurance.[25]

Even though title insurance is a category of insurance, it operates on the principle of risk avoidance or minimization, but not on the principle of risk elimination. Thus, most of the premium is devoted to determining for the benefit of the title insurer, in its decision to insure, the status of title and to underwriting the title insurance policy. Title insurer loss ratios range from around 4 percent to about 9 percent of the premium, with recent averages of around 7.5 percent or less, while title insurance agent retention varies from 60 percent to 90 percent of the premium, depending on the state, regulation of remittance, and the definition of the premium and type of regional losses.

Risk avoidance is implemented by the title search, examination, and underwriting requirements, including curative work. The ALTA Research Committee on operations estimated that 25 percent of titles require curative work to remove defects, and most titles require the release of outstanding encumbrances to secure clear title.

The title insurance guidance in the NAIC *Financial Condition Examiners Handbook*[26] explained the difference between the nature of title insurance and casualty insurance. It stated that property and casualty insurance provides indemnity for events that neither the insurer nor the insured has control over, whereas title insurance engages in loss elimination or identifies and removes a risk. Title searches are made to determine that there are

[24] Black's Law Dictionary 802 (8th ed. 1990).

[25] Ticor Title Ins. Co. v. Fed. Trade Comm'n, 998 F.2d 1129 (3d Cir. 1993).

[26] Nat'l Ass'n of Ins. Comm'rs, NAIC Financial Condition Examiners Handbook (2014).

no unknown defects in title. Although in theory title insurance would have no loss if title searches were done perfectly, in reality losses will occur because of errors in title searches, closings, and off-record matters such as mechanic's liens. While much of the premium for property and casualty insurance is used to pay claims, much of title insurance premium is devoted to the costs of maintenance of title databases or title plants (where relevant), title searches, title insurance agent retention, and other administration costs. Property and casualty profitability is based on favorable loss and loss adjustment expense ratios, while title insurance profitability is more related to the volume of title business.

Title insurers are required in a majority of states to perform due diligence of the status of title before insuring, and this due diligence consists of a search and examination. States requiring title examination include Alabama, Arizona, Arkansas, Colorado, Connecticut, the District of Columbia, Florida, Georgia, Hawaii, Idaho, Indiana, Kansas, Louisiana, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, South Dakota, Tennessee, Texas, Utah, West Virginia, and Wyoming.

Colorado Revised Statutes § 10-11-106 is a typical statute mandating an examination of title by requiring a reasonable examination of the title and a determination of insurability of title in accordance with sound underwriting practices before a policy or contract of insurance is issued.

In some states, primarily in the western United States, the title insurer or its title insurance agent must also maintain a title plant. For example, Missouri Revised Statutes § 381.071 prohibits issuance of a policy unless based on a title plant of the county where the property is located, or if no title plant of the county exists, or the owner of the plant refuses to furnish title evidence, then the policy shall be based on the best title evidence available.

The definition and period of time covered by a title plant varies, but Arizona contains a typical definition of a title insurance plant in Arizona Revised Statutes Annotated § 20-1562, which requires a geographic plant including an index or indices in which notations of or references to documents describing property are posted, entered, or included according the property described and an index or indices in which all other documents are posted, entered, or otherwise included according to the names of the parties.

Consistent with the requirement that the title insurer undertake risk reduction by an examination of title, a number of states prohibit insuring around known matters. Florida succinctly addresses this issue in Florida Statute § 627.784 ("Casualty title insurance prohibited"), which states "[a] title insurance policy or guarantee of title may not be issued without regard to the possible existence of adverse matters or defects of title."

In a similar vein, Texas prohibits "insuring around" outstanding enforceable recorded liens in Texas Insurance Code § 2502.003 unless allowed by regulation.

V. TITLE INSURANCE VERSUS TITLE INFORMATION

Title insurance forms are not abstracts of title, title opinions, or title information. They are written in the form of indemnities against loss under stated circumstances, not as representations of fact. It is common to see the policy or other form indemnify against loss if certain claims or defects are asserted, but not to represent or "assure" the insured that particular facts exist relating to the ownership or use of the land. For instance, the 2006 ALTA Owner's Policy insures against loss or damage sustained by the Insured by reason of any defect in or lien or encumbrance on the Title; the policy does not represent that there is no defect in the Title.

This principle is an important distinction in understanding the damages recoverable, which usually are as stated in the policy, and should not be based on tort liability, such as negligence or negligent misrepresentation. Some courts, however, recognize a cause of action for negligence in the title company examination undertaken to evaluate the risks relating to title.

Several different results may occur when considering the issue of negligence in the search or examination for issuance of a commitment or policy:

1. Tort recovery is not allowed against the title insurer or title insurance agent. This conclusion appears to be the rule in Alabama, Arizona, California, Colorado, Delaware, District of Columbia, Idaho, Illinois, Maine, Maryland, Michigan, Mississippi, Montana, Nevada, New Jersey, New Mexico, New York, Ohio, Oregon, Rhode Island, Texas, Utah, Washington, Wisconsin, and Wyoming. This result may occur because of case law, such as *Greenberg v. Stewart Title Guaranty Co.*,[27] or because of state statutes that distinguish a title insurance form and an abstract or representation of title, such as in California. California Insurance Code § 12340.10 provides that an abstract of title is not a title policy, and § 12340.11 provides that a preliminary report, commitment, or binder is not a representation of the condition of title to real property, but it is a statement of the terms and conditions upon which the title insurer is willing to issue its title policy.

   In some cases, the law may state that the title examination is done solely for the title insurer, as in Alabama Code § 27-25-3(13), although this may not prevent recovery for alleged negligence.
2. The title insurer and/or title insurance agent may be liable for negligent misrepresentations about the title made in the preliminary commitment. This appears to be

[27] Greenberg v. Stewart Title Guar. Co., 492 N.W.2d 147 (Wis. 1992).

true in several states, including Alaska, Arkansas, Florida, Georgia, Hawaii, Indiana, Kansas, Missouri, Nebraska, New Hampshire, Oklahoma, Pennsylvania, and South Dakota.

In the case of *U.S. Bank, N.A. v. Integrity Land Title Corporation*,[28] the court expressed the view that the title commitment could be a basis for negligent misrepresentation and held:

> The precise issue presented here concerns the exception of negligent misrepresentation: whether the issuance of a title commitment and subsequently issued title insurance policy give rise in Indiana to a tort cause of action for negligent misrepresentation against a title insurer or commitment issuer, separate and apart from the contractual obligations of the title policy. Courts in our sister jurisdictions are split on the question of whether a title insurer or a commitment issuer can be exposed to liability in tort for negligent misrepresentation regarding the search of title records. Some jurisdictions have refused to impose tort liability on a title insurance company or a commitment issuer.... These courts reason that because a title insurer does not purport to act as anything other than an insurance company, no tort liability exists unless the insurer has voluntarily assumed a duty of searching title for the insured's benefit in addition to the contract to insure title. . . . Other jurisdictions have concluded that a title insurance company and the commitment issuer have duties in tort to search for and disclose all recorded title defects and base that duty on the relationship between the parties, rather than on any agreement between them. . . . "We agree with the authorities which hold that there may be tort liability for misrepresentations made in preliminary commitments for title insurance. In our view, such commitments provide an essential service to prospective buyers and lenders. They are told what transactions must take place before they can receive clear title or an effective security."

Section 552 of the *Restatement (Second) of Torts*, which is frequently cited on negligent misrepresentation, states that anyone who in the course of that person's business, profession, or employment, or in any other transaction in which the person has a pecuniary interest, provides false information is liable for pecuniary loss caused by justifiable reliance on the information if the person fails to exercise reasonable care or competence in securing or communicating the information.

[28] U.S. Bank, N.A. v. Integrity Land Title Corp., 929 N.E.2d 742, 746–749 (Ind. 2010) (citations omitted).

An example of a cause of action for negligent misrepresentation may occur when the title insurance binder, commitment, or policy states "none" after the exception provided for restrictions or for other matters.[29]

Another example involves use of "assurance" language as described in *Alliance Mortgage Company v. Rothwell*,[30] in which the title insurer assured the insured on the date of policy that there was located on the land a four-unit residence with an identified address and precise number of units. The court concluded that the assurance language could serve as a basis for negligent misrepresentation.

A disclaimer has proved effective and enforceable in some cases. The following disclaimer was recognized in *Hoffman v. Fraser*:

> "THE COMMITMENT FOR TITLE INSURANCE IS ISSUED IN CONTEMPLATION OF THE ISSUANCE OF A POLICY *** OF TITLE INSURANCE AND *** MIDLAND TITLE *** (AGENT) OR FIRST AMERICAN *** SHALL HAVE NO OBLIGATION OUTSIDE THE TERMS OF THIS COMMITMENT. SPECIFICALLY, *ANY TITLE SEARCH OR EXAMINATION CONDUCTED BY MIDLAND TITLE *** AS A BASIS FOR ISSUING THIS COMMITMENT SHALL BE FOR THE BENEFIT OF MIDLAND TITLE *** AND FIRST AMERICAN ONLY*, AND DOES NOT INURE TO THE BENEFIT OF ANY OTHER PARTY, INCLUDING ANY SELLER, PURCHASER OR LENDER. *IN THE EVENT ANY PROPOSED INSURED UNDER THIS COMMITMENT FAILS TO ACQUIRE*, OR ELECTS NOT TO ACQUIRE, *A FINAL POLICY* PRIOR TO THE EXPIRATION DATE OF THE COMMITMENT, *SAID PROPOSED INSURED SHALL HAVE NO CAUSE OF ACTION OR RECOURSE AGAINST MIDLAND TITLE *** OR FIRST AMERICAN* AND IN NO EVENT SHALL ANY PROPOSED INSURED HAVE ANY CLAIM OR CAUSE OF ACTION AGAINST MIDLAND TITLE *** OR FIRST AMERICAN BASED ON THE TITLE SEARCH OR EXAMINATION. BY ACCEPTING THE WITHIN COMMITMENT, THE PROPOSED INSURED, ALONG WITH ANY OTHER PARTIES TO THE CONTEMPLATED TRANSACTION, CONSENTS TO AND AGREES WITH THE FOREGOING." (Emphasis added.)[31]

An example of a limitation on liability appears in the ALTA Application for the Recorded Document Guarantee, which acknowledges that the Guarantee is not an abstract of title and may not be relied upon by the Applicant as a representation of title.

[29] Great Am. Mortg. Investors v. Louisville Title Ins. Co., 597 S.W.2d 425 (Tex. Civ. App. 1980, *writ refused, no reversible error*); First Title Co. v. Garrett, 860 S.W.2d 74 (Tex. 1993).

[30] Alliance Mortg. Co. v. Rothwell, 34 Cal. Rptr. 2d 700, 715, 33 Cal. App. 4th 1372 (1994), *affirmed*, 10 Cal. 4th 1226, 900 P.2d 601, 44 Cal. Rptr. 2d 352 (1995).

[31] Hoffman v. Fraser, 2011-Ohio-2200 at ¶ 33, 2011 Ohio App. LEXIS 1886 (Ct. App.).

CHAPTER ONE IN SUMMARY

- Title insurance is generally a monoline insurance, and neither property and casualty insurers nor mortgage guaranty insurers may insure title to real property.
- In most states, title insurers are required to perform an examination of title in order to issue a title policy. In some states, the title insurer may not disregard defects in title that are discovered in the title examination.
- In some states, the title insurer or title insurance agent may be sued for negligence or negligent misrepresentation for defects in title not excepted in the commitment or policy.