Title Abstract/Title Opinions

• Historically, buyers often relied on an attorney’s legal opinion as to the quality of the Seller’s title
  – The attorney would reach this opinion based upon his/her title search or his/her review of a title abstract (p. 242; all of the recorded documents in the chain of title)

• Suppose that Buyer suffered a loss of title b/c a prior deed in the chain of title turned out to be a forgery. Could Buyer recover for this loss from an attorney who gave a legal title opinion?

  • No
    – Attorney would be liable in negligence only if the attorney failed to meet the appropriate standard of care
    – But even a prudent title searcher would not discover that a prior deed was a forgery, at least not based solely on a record title search
    – For this reason, an attorney’s title opinion is “qualified,” e.g., it states that it assumes the authenticity of signatures in deeds in the chain of title

• Thus, attorney’s opinion is not a guarantee of title quality
• By contrast, title insurance exists to indemnify against such an “undiscoverable” risk
Title Insurance

• Today, most rely on title insurance
• If the title problem is a “Covered Risk,” the title insurer must
  –(1) indemnify the insured (i.e., must pay to cover the insured’s economic loss due to the insured defect, up to the limit of coverage specified in the policy), and
  –(2) defend the insured (i.e., must pay legal costs insured would incur in defending title or in obtaining a “cure” of the defect)

Title Insurance: Owners’ Policy and Loan Policy

• There are two types of title insurance policies
  –Owner’s policy: insures the owner’s title
  –Loan policy: insures the validity and expected priority of lender’s mortgage lien on the land (required by secondary market purchasers of loans such as Fannie Mae and Freddie Mac)
• These are entirely separate policies, and are issued for entirely separate premiums (although coverage for the owner’s policy is only a relatively small “add-on” to cost of loan policy)
• X agrees to buy Blackacre from Y for price of $700,000
  – $350K using mortgage loan from Bank
  – $350K cash down payment
• X receives deed from Y, and X grants mortgage to Bank
  – Bank obtains loan policy; X doesn’t get owner’s policy
• 2 years later: O (true owner of Blackacre) successfully establishes title (deed from O to Y was forged)
  – At this time, X owes Bank $340,000
• Title insurer will pay Bank $340,000, but will not have to pay anything to X (who is not insured)

• If X wants to avoid loss of its equity in Blackacre due to a title defect, X must carry its own owner’s policy
• Also, if X doesn’t have an owner’s policy, note that X faces a risk of liability due to Insurer’s right of subrogation
  – When Insurer pays Bank’s policy claim, Insurer becomes entitled to assert Bank’s rights under the loan documents
  – Thus, Insurer’s payment to Bank doesn’t satisfy X’s debt; it just transfers that debt to Insurer, so Insurer can demand that X pay back the $340K balance of debt!
  – Insurer could not subrogate against X, if X is also an insured
Title Insurance Issuance Process

• Upon request, insurer searches title and (hopefully!) identifies all relevant 3rd party interests in the parcel
• Insurer issues a “commitment” (e.g., promise to issue title insurance policy, as indicated in the commitment, if transaction closes and insured party pays the premium)
  –Commitment will “except” (i.e., it will not insure against) all listed matters revealed by insurer’s title search and listed on Schedule B
  –Any “Covered Risk” is insured unless it is (1) excepted on Schedule B or (2) excluded under the general policy “Exclusions”

Title v. Casualty/Liability Insurance

• Casualty insurance and liability insurance products provide “term” coverage; you pay a premium for a limited “term” of coverage (e.g., 6 months or 1 year)
  –After the term expires, you must renew the coverage and pay an additional risk premium for the new term
• By contrast, title insurance has no term
  –You pay a one-time premium, and your coverage continues to protect you forever (even after you transfer the land)
Does Coverage “Run” with the Land?

• No; when I sell my land, I can’t sell my existing title insurance coverage to the Buyer [Condition ¶ 2, p. 266]
  – Buyer will have to obtain (and pay a premium for) a new title insurance policy that insures the Buyer’s interest

• In some situations, where title passes by operation of law (e.g., inheritance), owner’s policy coverage does pass with title [Condition 1(d), pages 264-265]

• Suppose I inherited land from my mom
• Can you explain why I might need a new owner’s title insurance policy, even if I was entitled to assert the one my mom had obtained when she got the property?
  – Her policy would’ve insured her title as of the day she acquired it
  – It wouldn’t cover any matters that arose while she owned the title [Exclusions 3(a), 3(d), p. 263]
Post-Transfer Protection

• However, title insurance continues to insure me, even after I sell the land to a purchaser and no longer own it [Condition 2, p. 266]
  – E.g., I sell to Bailey and deliver a warranty deed
  – Bailey later sues me because he suffers a loss due to a title defect that breached a deed warranty, and the defect was a “Covered Risk” under my title insurance policy
  – Insurer must defend Bailey’s lawsuit (assuming I give notice) and, if I lose, indemnify me against any judgment, up to the policy limit

Commitment and “Schedule B” Matters

• Commitment promises to insure title as reflected on Schedule A [p. 264], but subject to general exclusions [pp. 262-263] and specific “Schedule B” matters [p. 264]
• On Schedule B, insurer will list all liens and encumbrances that it discovered in its title search, and will also usually include a “survey” exception
  – Unless an item is removed from Schedule B prior to closing and issuance of policy, then, policy won’t insure against title matters listed on Schedule B
“Fixing” Defects Prior to Closing

- Defects can come in several types: some problems are “Schedule A” problems (e.g., proposed Seller doesn’t have record title)
  - E.g., Seller agreed to sell Blackacre to Buyer, but Seller only owns ½ share (with Seller’s sister)
- Insurer could “fix” this prior to closing in a variety of ways
  - E.g., have sister sign the contract of sale; have sister sign power of attorney; having sister agree to execute quitclaim deed to Seller
  - If Insurer can’t “fix” it, Seller’s title is unmarketable (and Buyer should refuse to close)

“Fixing” Defects Prior to Closing

- Defects can come in several types: some problems are “Schedule B” problems (e.g., Seller has record title, but it is subject to encumbrances like liens, judgments, easements or covenants)
- Some of these may not violate the contract’s title standard (and don’t need to be “fixed” prior to closing)
  - E.g., contract might specify that Seller will deliver title subject to utility easements and neighborhood CC&Rs; if so, Buyer cannot really object to Seller’s title based on presence of those matters on Schedule B
“Fixing” Defects Prior to Closing

• Defects can come in several types: some problems are “Schedule B” problems (e.g., Seller has record title, but it is subject to encumbrances like liens, judgments, easements or covenants)
• Some of these will violate the contract’s title standard (and do need to be “fixed” for Seller to have marketable title)
  – E.g., Seller’s mortgage will have to be paid off
  – E.g., judgment against Seller will have to be paid off
  – E.g., “false positives” (judgments, but against a different person with the same name)

“Fixable” Defects

• At or prior to closing, Insurer will “mark up” the commitment and remove matters from Schedule B, as they are cleared up
  – E.g., when Seller’s mortgage balance is paid off at closing, Insurer will strike out the Schedule B exception for that mortgage
  – E.g., if the Insurer concludes that a judgment is a “false positive,” Insurer will strike out exception for that judgment
  – E.g., if Insured gets a new survey showing no encroachments or visible easements, Insurer will remove “survey exception”
• After closing, Insurer will then issue final policy as reflected on the “marked up” commitment at end of closing
How Are Claims Triggered? Typical Examples

• Insured has a contract to sell insured parcel to Buyer, but Buyer refuses to close due to a claimed defect that is covered by the policy (unmarketability of Insured’s title)
• Insured gets sued in ejectment or in a suit to quiet title to some or all of land covered by policy as described on Schedule A
• Insured gets sued for injunction against a current or planned use based on an encumbrance that is covered by the policy (i.e., not excluded or excepted on Schedule B)

Title Insurance Claim Analysis

• Is the interest a “Covered Risk”? [pages 260-262]
• If so, did the Insurer “except” it from coverage by including it as an exception on Schedule B? [page 264]
• If not, did the Insurer “exclude” it from coverage under the “Exclusions from Coverage”? [pages 262-264]
• If the interest is a Covered Risk and is neither excepted nor excluded, then Insurer is liable for Insured’s loss (up to policy limit), as long as Insured complies with claims process
Problem: Adverse Possession

- Smith buys home; First Title issues Smith an owner’s policy
- Six months after closing, X (neighboring owner) sues Smith claiming title by adverse possession to 50-foot strip of Smith’s land along their common border. Is there coverage?
  - Yes, this is a covered risk [¶ 1, p. 260], unless Schedule B contained a survey exception and there was a fence or other visible evidence of Smith’s claim that would’ve been revealed by a survey

Problem: Mortgage Lien

- Smith buys home; First Title issues Smith an owner’s policy
- After closing, Bank won’t release mortgage of prior owner (Jones), who still owes $1,500 (it turns out Jones’s last monthly mortgage payment check had bounced just after the closing!)
  - Bank mortgage had been “marked off” on Schedule B at closing
- Result: mortgage lien is covered risk [¶ 2, p. 260], not excepted or excluded
  - First Title must pay off balance owed to Jones to clear Smith’s title
Problem: Mechanic’s Lien

- Smith buys home; First Title issues owner’s policy
- Two months later, Smith gets notice of $2,500 lien claim by ABC Tile, Inc. (retiling done, but not paid for, by Seller Jones)
  - No exception on Schedule B
- Result: mechanics’ lien is covered risk [¶ 2, p. 260], not excepted or excluded
  - First Title must pay off $2,500 to ABC Tile, Inc., to clear Smith’s title

Mechanics’ Lien

- Each state has a statute that allows a person who provides labor or materials for an improvement to land to file a “mechanics’ lien” if they aren’t paid
  - Mechanics’ lien attaches to land (including the improvement to the land)
  - Lien relates back to the date the work was commenced by lienor (known as the “first spade” rule)
  - If the bill isn’t paid, lienor can have land/improvements sold to satisfy the unpaid balance due
Mechanics’ lien risk is significant for Buyers, even when buying an already-existing home or building
– Seller typically has “work done” to get the land ready to sell
– If Seller didn’t pay, contractor has 4-6 month “window” period (which varies by state; 4 months in MO) in which to file notice of a lien claim
– *Once lien claim is filed, lien “relates back” to the earlier date that the contractor’s work began (i.e., it is deemed to have arisen on that date)!
– Thus, Buyer of land takes title subject to risk of latent mechanics’ lien claims held by any unpaid contractor (who could file a lien notice after closing)!

If insurer does not “except” this risk, it will have to indemnify the insured if a mechanics’ lien arises
– This means insurer will have to pay off the unpaid liens to “clear” the insured’s title

Why would title insurer take this risk?
– Insurer may do so if (1) Seller provides an affidavit identifying any contractors/suppliers that did work, (2) Insurer gets lien waivers from those contractors/suppliers, and (3) Seller agrees to indemnify Insurer from loss if affidavit turns out to be false
• Now assume Smith buys home; First Title issues owner’s policy
• Two months later, Smith receives notice of lien claim by ABC Tile, Inc. (retiling work contracted for, but not paid for, by Smith prior to sale; unpaid bill = $2,000)
• Covered?
  – No; while mechanics’ lien is ordinarily a covered risk [¶ 2, p. 260], policy’s general exclusions excludes coverage for liens “created … by the Insured Claimant” [Exclusion 3(a), p. 263]

Problem: Covenant or Condition?

• Smith buys farm; First Title issues owner’s policy
• Smith installs a wind turbine
• 2 months later, Smith is sued by Davis (a neighbor) for violating an “agricultural use only” restriction (which was listed on Schedule B)
  – Davis argues (1) restriction was a “condition,” (2) turbine breached it, and (3) breach terminated Smith’s title altogether
• Does First Title have to defend this claim?
  – No; while its a covered risk [Owner’s ¶¶ 1, 2, p. 260], coverage is excepted on Schedule B
ALTA Homeowner’s vs. Commercial Policy

- Homeowner Policy Covered Risk 13: Insurer is liable if “Your Title is lost or taken because of a violation of any covenant or restriction, which occurred before you acquired Your Title, even if the covenant, condition or restriction is excepted in Schedule B.”
- By contrast, in commercial transactions, or if policy is being issued on form in the book, form doesn’t provide this coverage, so Insured should ask to modify Schedule B exception to warrant that “Violation will not result in a forfeiture of Insured’s title”

Problem: Zoning

- Smith buys home; First Title issues owner’s policy
- Two months later, Smith is sued by City for a zoning violation (house is too close to street; no variance obtained)
  – City seeks injunction against Smith’s occupancy
- Result: Not covered by [Exclusion 1(a), p. 263], unless the City has recorded a notice of violation has been recorded in the land records by City [Covered Risk ¶ 5]
  – Rationale: these aren’t “title” matters unless they appear in real property records
Zoning Matters

• Generally, zoning matters are excluded from coverage [Exclusion 1, p. 263]
  – Existing violations of zoning are covered ONLY if the municipality has recorded a notice of the violation in the “Public Records” (land records) prior to Policy Date
• To get protection for “zoning”-related risks, Insured must get (and pay for) a zoning endorsement to the policy (which would override the Exclusion)

• Note: ALTA Homeowner’s policy form (which is available on ALTA’s website) does provide insured owner w/protection against some zoning risks
  –¶ 14(b): loss due to certain zoning violations recorded in public records, if not excepted on Schedule B
  –¶ 19: covers cost to move structures due to a zoning violation (such as a setback violation); no need for separate endorsement
  –¶ 20: covers loss b/c use as single-family residence violates applicable zoning ordinance; again, no need for separate endorsement
Note 3, Pages 271-273

• 2012: Buyer bought land for $150K, and got an owner’s policy from Chicago Title (CT) in amount of $150K
• 2020: Smith sues to eject Buyer and prevails
  –Smith’s prior deed was recorded, but CT “missed it” because its agent conducted a negligent search
  –In 2020, land’s value has increased to $300,000
• CT tenders $150K under the policy, but Buyer instead sues CT for $300,000 for negligence in conducting the search
• Should CT be liable in tort to Smith?

Does Title Insurer Have Duty of Care in Searching?

• Courts have split
  –Some states: yes, insured party may recover in tort (beyond the policy limit) if insurer conducted negligent title search [e.g., AR, KS, NE]
  –Rationale: insurer knows/should know that insured is relying upon the title commitment in deciding whether to buy (relying upon insurer’s superior expertise)
Insurer’s Liability in Missouri

• RSMo. § 381.071 provides:
  –(1) title insurer can’t issue a title insurance policy without first conducting a title search
  –(2) title insurer shall not “knowingly issue any owner’s title insurance policy or commitment to insure without showing all outstanding, enforceable recorded liens or other interests against the title which is to be insured”

Leading Missouri Cases

• Held: title company had a duty to use due care in preparing a preliminary title commitment [Evinger, 726 S.W.2d 468 (Mo. Ct. App. 1987)]
• Held: where commitment stated that the Insurer was liable for “actual loss incurred in reliance in undertaking in good faith ... to acquire ... the estate ... covered by this Commitment,” Insurer was held liable for the entire loss suffered by Insured due to negligent title search by Insurer [Rosenberg, 764 S.W.2d 684 (Mo. Ct. App. 1988)]
• Other courts have refused to allow recovery in tort beyond the policy limit, either because:
  – Some courts hold insurer has no duty of care (insurer is insuring risk, not certifying title) [e.g., TX, NJ]
  – Other courts give effect to policy language limiting the insured to recovery only in contract [e.g., IL]
    • E.g., Condition ¶ 8 of ALTA Residential Owners’ Policy: “Any claim You make against Us must be made under this Policy and is subject to its terms.”
    • Other states (NE, CA, MA) have refused to treat that clause as a valid waiver of tort liability (exculpation contrary to public policy)

• Note: sometimes, loss due to a title defect is not due to insurer’s negligence
  – Some defects (e.g., defects in execution or delivery of a deed in the chain of title) aren’t discoverable by a prudent search
  – For these defects, even in MO, Insured’s recovery is capped at policy limit + any costs of defense
• Thus, over time, Insured must be sensitive to the policy limit as time passes (and as the land appreciates in value)
Appreciation

• ALTA Homeowner’s form: each year for 5 years, policy limit increases by 10%
  – **Maximum increase = 150% of policy amount**
  – If land’s value increases by > 50% (either due to market appreciation or improvements), the insured should obtain a new policy w/increased coverage (otherwise, insured is “self-insuring” loss beyond the policy limit)
• Commercial deals: Insured can obtain “Inflation endorsement”