

Title Insurer Not Liable for Acts of Agent at Closing in Absence of Closing Protection Letter

By John C. Murray

© 2008

Introduction

Title agents are customarily authorized, through agency agreements, to sell policies for one or more title insurance underwriters. These agency agreements normally provide that the agent is an agent solely for the purpose of issuing title insurance commitments and policies, and explicitly state that the agent is not the title company's agent for the purpose of conducting settlements or performing escrow services. Authorized title agents also often act separately as the agent for the lender, buyer and/or seller, pursuant to instructions from such "principals" (that only such principals can enforce), in connection with the escrow closing of the transaction that is the subject of the title insurance. A lender who also wants the title insurer to be responsible for the agent's acts in connection with escrow closing activities and services must separately contract with the title insurer for such additional protection by entering into an "insured closing letter" or "closing protection letter" ("CPL"). CPLs have been available since the 1960s. They originally were not title-industry approved forms but, rather, were forms requested by mortgage lenders that were concerned they had no protection against unauthorized or fraudulent actions, or failure to comply with the lender's closing instructions, by the title company's approved closing agent or attorney. Lenders require CPLs because the agency-principal relationship between a title underwriter and a policy-issuing agent or approved attorney is limited to the issuance of a title-insurance policy, and such relationship does not extend to escrow or closing functions. CPLs specifically apply to escrow closing activities and services performed for title underwriters by approved attorneys or agents who are not employees of the title companies; as a general rule they are not issued on behalf of independent closers over whom the title company has no control. (An "Approved Attorney" is defined in the standard forms of CPLs as "an attorney upon whose certification of title the title insurance company issues title insurance"; an "Issuing Agent" is defined as "an agent authorized to issue title insurance for the title insurance company"). These letters are standardized indemnity agreements given to individually named lenders and recite the specific conditions under, and the extent to which, title insurers will accept liability for the acts or omissions of such parties.

The Pal Properties Case

The lack of a contractual relationship (absent a CPL) between the attorney-agent and the title underwriter regarding escrow-closing functions, and thus the lack of responsibility of the insurer with respect to such activities when conducted by the Approved Attorney or Issuing Agent, is demonstrated in a recent Michigan case. In *PAL Properties LLC v. Ticor Title Ins. Co.*, Case No. 06-073149-CK, (Oakland County, Mich. Circuit Court, June 4, 2007) (unreported), there was no closing protection letter ("CPL") issued to any party (it was a cash deal), and the issuing agent (acting in its separate capacity as an escrow closer) absconded with or diverted funds from the

closing intended for a mortgage payoff. The Circuit Court, based on the language in the title commitment and the agency contract, and the lack of a CPL, ruled in favor of the defendant title company (“Ticor”). The plaintiff-purchaser argued that it should have the benefit of a CPL, even though it was a cash transaction and no CPL was issued to any party. Reasoning that because it was not Ticor’s fault that the funds weren’t used to pay off the mortgage, and the escrow agent subsequently was cut off as an issuing agent by Ticor (and subsequently went out of business), the court rejected the buyer’s claims of breach of contract, fraud, agency liability, negligence, conversion, loss of profits, and fiduciary duty. The plaintiffs appealed the Circuit Court’s decision to the Michigan Court of Appeals. The appellant-purchaser’s brief (filed October 31, 2007) made the following highly unusual (at least to the court and to title insurers) statement, at page 14:

Ticor wants this court to believe that it had *no duty* to insure that its agent properly disbursed the funds. However, it is of paramount importance that the Court understands that the vast majority of mortgage transactions are funded by commercial lenders. This is the realm in which CPLs have developed. Lenders have vast amounts of bargaining power and have therefore demanded these letters to *remove any ambiguities* as to whose responsibility it is in the event of an underwriter’s agent failure to disburse. The real purpose of these letters is to make it *clear that underwriters, and not lenders are responsible, and thus to avoid costly litigation on these disputes*. Ticor wants this court to believe that since [the appellant-buyer] did not have a CPL, it is clear that Ticor is not responsible for this loss. This is simply not true. This issue presents a contingency that neither party contracted for, and is therefore, *subject to interpretation* as to who should bear the responsibility. The trial court committed reversible error by not addressing these issues. (Emphasis in text.)

On December 9, 2008, the Michigan Court of Appeals affirmed the trial court’s decision. *See PAL Properties LLC v. Ticor Title Ins. Co.*, 2008 WL 5158894 (Mich. App., Dec. 9, 2008). The appellate court noted that a title policy was never issued in this matter and, and held that because only a title commitment was produced by Ticor and only an actual title insurance policy provides insurance, the commitment did not serve to impose a duty upon Ticor to protect the plaintiff from Consolidated’s actions. The court noted that the contract entered into by the parties designated Ticor as principal and Consolidated as its “issuing agent,” which limited the scope of Consolidated’s agency to the purpose of issuing title insurance only. The court stated that “Plaintiff has provided no authority suggesting that conducting a closing is an inextricable or necessary part of transacting or promoting title insurance business.” *Id.* at *2. Also, according to the court:

Notably absent from the contract is any reference to Consolidated attending closings or performing any duties at closings for the benefit of Ticor. Nowhere in the document does it indicate that Ticor dictated how Consolidated was to proceed with any change.

Id. at *3. The court further noted that:

Ticor's only recourse under the contract would be to terminate the same. Ticor has no contractual right to take over Consolidated's business, to take control of the escrow account, or to force Consolidated to take any action.

Id. The appellate court also rejected the plaintiff's argument that Consolidated acted as Ticor's apparent agent for purposes of the closing, noting that Consolidated was the only entity, other than the buyer and seller, to sign the closing statement and it alone prepared the necessary closing documents (collecting a fee from the plaintiff) and conducted the closing. The appellate court also noted that the plaintiff had no contact with Ticor until several months after the closing. The court also dismissed the plaintiff's claim of negligent supervision, noting in particular that Ticor had the right, but not the responsibility, to examine Consolidated's records and that "Nothing in the title insurance contract serves to impose a duty upon Ticor to protect plaintiff from Consolidated's actions." *Id.* at *5. The court also rejected the plaintiff's claim of fraud, because the plaintiff "had not alleged that Ticor made any misrepresentation to it whatsoever, at any time, with respect to the escrow monies or whether or not the mortgages would be paid out of the escrow funds." *Id.* at *6. Finally, the appellate court dismissed the plaintiff's claim that a material dispute existed with respect to whether Ticor breached the title insurance policy, because even though one of the mortgages mentioned in the title commitment was not discharged (albeit through no fault of the plaintiff), "no title insurance policy, under which plaintiff could make a claim of loss, was issued." *Id.* at *7.

The vast majority of existing case law supports the holding in the *PAL Properties* case, but a few cases have held for the purchaser, even where no CPL had been issued. *See, e.g., Sears Mortgage Corp. v. Rose*, 134 N.J. 326, 350-52 (1993). In this case, the court held that the buyer's attorney, who acted as the closing agent and was an "approved attorney" of the title company, was controlled to at least some extent by the title company. The court found that because the attorney failed to remit funds deposited to pay off a mortgage the title insurer would be responsible to the purchaser for the loss, even though the buyer had retained the closing attorney and no CPL had been issued to either the buyer or the lender. According to the court, "the title insurer had a duty either to give [the borrower] . . . an opportunity to insure himself against the risk or, at the very least, to inform him that he was not covered against such a risk." *Id.* at 347.

See generally Joyce D. Palomar, TITLE INS. LAW 2-12 (1994) ("Underwriting and agency agreements generally . . . limit the underwriter's responsibility for agents' activities as escrowees in real estate closings"); Richard J. Landau and Kristin M. Tsangaris, *The Mortgage Fraud Epidemic*, S & P's THE REVIEW OF BANKING AND FINANCIAL SERVICES, Vol. 22 No.4, April 1, 2006 ("In the absence of an insured closing letter . . . a majority of cases hold that . . . the title insurer has no liability for fraud or other misconduct in connection with a closing").

Conclusion

The CPL serves to extend the liability of the (presumably) large and creditworthy title insurance company - which would otherwise be limited to the title insurance policy - to cover certain "bad acts" of the company's Issuing Agent or Approved Attorney. But this additional

protection, as specifically noted by the Michigan Appellate Court in the *PAL Properties* case, must be separately and specifically requested from the title insurer, and the scope of the coverage is defined solely by the contractual terms and provisions of the CPL. Coverage under the CPL is also strictly limited to the parties designated therein, and generally applies only with respect to the particular transaction for which the letter is furnished. The ALTA has attempted to meet the needs of title insurance customers by expanding the types of CPLs (the latest being the 2008 ALTA CPLs) to cover varying factual situations and comply with state statutory and regulatory restrictions. It is important for both the insured and the insurer to understand the legal (both case law and statutory) and regulatory restrictions and limitations on the use of CPLs in certain jurisdictions, and the nature and scope of the agency relationships that exist between title insurance companies and their Issuing Agents and Approved Attorneys.