



BUILDING THE FUTURE TOGETHER

Title Insurance Claims — Why & How They Happen

Introduction: *Title insurance differs from other types of insurance.*

Most insurance lines are based on unknown, individual event liabilities. That is, it is not known where a claim will occur or when. No one can predict with certainty where a hurricane will hit or when and how destructive it might be; no one can predict who will get what disease and what it might cost to treat. Insurance is based on average claims in the past, projected into the future.

Title insurance is different because the liability for every insured home is known in advance of the insurance policy being written. The foundation of the American land recording system is that all “events” which affect a piece of property are publicly disclosed by means of the recordation of a document at the County Recorder’s office. The documents recorded with the County Recorder give “constructive notice” of all actions related to all properties in their counties. Changes in property ownership, liens, mortgages, notices, judgments and easements should all be recorded to provide constructive notice to the general public.

The fact that all of these recorded events are known to the insurer is what separates title insurance from other lines of insurance. What title insurance covers is not what “could” happen, but what has happened (to the property) and was either hidden or missed by the insurer. Therein lies the problem; although title insurance liability is typically known or discoverable from the beginning, claims still do arise and from various sources.

Title Errors and Title Plant Error:

Title indexing errors, quality control slippage, fraud, forgeries and lack of transparency all affect the reliability of property records and can result in title claims.

While title plant problems such as un-noticed recording mistakes and indexing errors can result in claims, the majority of claims stem from title examination errors. Forged and falsified documents, invalid deeds, unpaid liens, undisclosed easements, claims by missing heirs or ex-spouses all pose risks. Careful examination, common sense and quality review through the entire process are some of the keys to minimizing claims, though it is almost impossible to eliminate all claims in the title insurance process.

The extent of a title error will determine if a claim will be filed with the underwriter or handled in-house by the title company. When a title claim is made to the underwriter, it is usually significant and almost always far more than the deductible on the title company's errors and omissions policy.

Underwriters are considering changes in assigned responsibility for certain claims, with the result that more claims may become the responsibility of the title company. If this comes about, title agency E&O premiums will increase.

The Source of Some Types of Claims:

Missed Lien:

This may be due to an oversight on the part of the searcher or the lien may have been incorrectly posted in the title plant (e.g. an overlooked legal on a lien document having multiple legal descriptions).

Mortgage Line of Credit:

The original borrower's sign-off is required to authorize a lender to close a line of credit account. There have been instances where the title company failed to send in the authorization form to the lender to close the account and sometimes the lenders have not promptly submitted the authority to the title company. Sometimes, borrowers have taken advantage of this oversight or delay in closing the line of credit.

A line of credit is generally paid off by a new mortgage. If an unscrupulous borrower

finds out that the line of credit is still active they may borrow against it. After the collapse of the mortgage industry, some lenders found that their lien was not in first position when they attempted to foreclose on the owner: there was a prior debt from an unclosed line of credit. This has resulted in title insurance claims.

Lien(s) Attach When Tenancy is Broken:

A lien does not attach to property held as tenants by the entirety (husband and wife) if the lien is against just one of the parties. Once tenancy is broken, often due to a divorce, the lien will attach to the property.

One scenario: A title company will prepare a commitment for a sale. The title company may not be aware that the sale is due to the owners' pending divorce, and will not show the lien. During the course of the closing, the owners' divorce is finalized. The title company records the deed, unaware of the divorce and the property is transferred to the new owners with the lien attached. The lien may not be discovered until a new search is done on the property or the lien holder pursues collection.

Interest of all Owners Not Conveyed:

This is rare but happens when various owners are involved or interests are conveyed by a quitclaim deed that does not always promise good title. Probate or a quiet title action may be required. A quitclaim deed that shows up in a title chain should be a red flag to the searcher.

Lack of or No Access:

Although a property owner may have gained access to and from his property for many years by a roadway easement, the easement may be invalid if the owner was not legally granted access. This is usually discovered in a survey by the adjoining property owner attempting to sell or develop the land.

A claim to resolve this type of issue can be costly. The end result may not be favorable to the owner of the property that used the unrecorded easement, especially if it is determined that the property is landlocked without that roadway.

Encroachments:

Encroachments are usually discovered during a survey or appraisal. Depending on the type and extent of the encroachment, an agreement between the parties affected by the encroachment can remedy the issue. The terms of an encroachment agreement should be reviewed by the searcher to verify that they will carry over to the new owner. Encroachments become a problem when properties change hands and the

encroachment agreement between prior owners is no longer valid. Other problems may occur when the landowner seeks adverse possession of the land he is encroaching.

Invalid, Missing or Expired Power of Attorney:

A claim on the validity of a person signing on behalf of another, by way of a power of attorney, is infrequent. There have been instances where the power of attorney may have expired or the terms of the power of attorney were for a specific purpose and may invalidate the document that was signed if it was not for that purpose.

Hidden Hazards; Fraud; Forgeries:

These hard to detect circumstances almost always result in a claim.

The most common errors are generally detected and resolved by the title companies.

It is in the interest of the title agencies to resolve errors when they occur. The claim process itself is costly, often involving attorney and litigation. Title companies often correct the following types of problems internally, or through informal negotiations with the parties to the sale.

Incorrect Posting in the Title Plant:

Errors may be caught by the searcher and corrected before any damage is done. Document errors from an incorrectly drawn up document may reference the wrong names or lot numbers. Indexing errors could introduce the wrong parties or legal descriptions into the plant. In instances such as this, the title company will prepare a correction document to remedy the situation, whether the error came from a title company's document preparation or from an outside plant or another source. Correcting incorrect postings to the title plants has the benefit of improving the plant for future examiners, as well as improving the quality of the public record archive.

Unreleased or Improperly Released Mortgages:

The title company will attempt to obtain a proper release of an unreleased mortgage; this may require extensive work if the lender is no longer in business or the original lender has been acquired by a larger company, perhaps in another state. Some states have enacted legislation allowing the title company to prepare and record a release with an attached affidavit setting forth proof of the payoff. This has reduced the number of claims filed by owners looking to clear title to their property.

Priority of Lien:

Sometimes mortgages are recorded in the wrong order, second before first mortgage, or a lien is missed due to an erroneous date-down of property prior to recordation. The title company will attempt to obtain a subordination to change the priority of the lien. If the attempt to correct the priority is unsuccessful, a claim can result.

As you can see, even though there is theoretically no reason for claims in the title insurance industry, in reality, there are many places where claims can occur. Please contact us if we can be of assistance in providing a quality product and service for your business.