Title Insurance

Basics

Andrew C. DiPaola, Esq.

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Title Insurance Basics – Claims
Course Handouts

The Contract has been negotiated and signed, everyone is in agreement. The purchasers are approved for their loan without contingencies. The pest and home inspections are clear. Then the title search shows a problem. Below is an overview of role of title insurance in the settlement process, and a review of some major areas of title insurance claims in Virginia which affect a sale transaction.

A. Title Insurance

Often real estate agents, as the individuals in most personal contact with a purchaser, will be responsible for explaining the general settlement process to the new buyer. One aspect of this process is title insurance: what it is, how it functions and why it is required are basics a purchaser generally has questions about.

1. All policies cover the basics:

O = you own it

N = no liens against it not disclosed in the commitment

A = you have legal and physical access to the real estate

M = title is marketable; no reasonable purchaser would refuse to purchase due to the matters that show in the history of ownership of the real estate.

2. Two basic type of title insurance policies exist: one that protects the Owners, one that protects the Lender.

a. Lenders require a title policy for their protection, as they are unable to sell their loans in the secondary money market without them. A lender's policy ceases to exist when the loan is paid. Title underwriters are often willing to insure matters for a lender that they won't for an owner, unless additional information is provided, for example: survey coverage.

With survey coverage the theory is that if a problem arises that would have shown up on a survey the Owner will have to be in default before it becomes a title issue for the lender. If the Purchaser orders a survey prior to settlement any survey problems will be shown. The Purchaser can require the Seller to correct the problem, or to make an economic concession. Example: driveway of the subject property encroaches 8 inches onto neighbor's property; or neighbor's driveway encroaches 8 inches on to the property being sold.

a. Owners have the option of purchasing a policy for their protection. They may purchase a standard policy or an enhanced policy with numerous additional coverages. (See attached brochure for a summary.)

An Owner's policy may be effective in Virginia for a year after the owner has died, even after the real estate has been sold.

3. Since title insurance is required by the Lender, title insurance companies require a title search be performed to produce a commitment prior to settlement. The commitment outlines three basic matters.
   a. Schedule A identifies the record owner and legal description of the real estate being sold.
   b. Schedule B-1 lists the requirement, what is needed for the title company to insure the property. Title insurance is **risk elimination** insurance. Schedule B-1 lists the items that need to be handled for the risk to be eliminated and the lender to provide the loan. When the title agent identifies problems, they

are outlined in Schedule B-1. Curing the defects/solving the problems may slow the settlement process.

c. Schedule B-2 lists matters the title company will not cover. Matters here include restrictive covenants, utility easements, access easements, rights of first refusal, etc.

4. Ownership issues that are not properly identified, or if identified, are not properly eliminated prior to purchase may become a claim.

2. Claims "hot spots"

1. Home Equity Lines of Credit (HELOCS) paid but not closed and blocked. Lenders require that the Borrower(s) sign a statement requesting an Equity Line be closed before the lender will close the account. (See Va. Code § 55-66.3) Many individuals do not think of their Equity Line loan as a mortgage on their real estate. It's just their "credit line," something with checks or a debit card that they can use for whatever they wish and repay similar to a credit card. Many borrowers think of it as similar to a credit card without the "transaction fee" up front, just interest to pay.

Settlement agents collect the outstanding balance on the Equity Line loans during a sale or refinance of real estate, and pay the lender. Normally the agent will send a letter explaining the equity line is to be closed. For most lenders, without the Borrower's signed statement (and sometimes even with it) they will not close the line and release it of record. The Borrower can continue to use the checks/debit card and the HELOC loan will have priority over a refinanced deed of trust, or a DOT for a new owner.

If the current Owner/Seller is not the Borrower in question for the HELOC, and he/she has an Owner's title policy, the title company will be liable for the clearing title. However, identifying the problem and resolving it takes time, which delays closing.

2. Prior lien of record. Unreleased deeds of trust and judgment liens which may or may not be the seller (or a prior owner) are constant problems that delay settlements.

(a) Unreleased deeds of trust - One duty of a settlement agent is to follow up, to confirm that a deed of trust, paid in full by them from settlement funds, has been released in the record room by the lender. During the boom times of 2000 – 2005 settlement agents could not keep up with the volume of closings, much less devise a foolproof plan to track release payments. Part of the problem was due to varying instructions from the regulatory body that oversees non-attorney settlement agents, and no oversight at all for attorney settlement agents. Companies arose during this time to handle that single issue, release follow up, for the settlement agent, whether attorney or non-attorney. The cost is passed on to the seller, and the system works effectively.

During the early 2000's the General Assembly passed a statute that allows the settlement agent to administratively release a deed of trust, provided the settlement agent has followed the specific rules set out in the Code § 55-66.3. Many settlement agents, concerned about liability, do not use the provisions to release the deeds of trust. With the downturn in real estate transactions, many settlement agents and many lenders have gone out of business, so obtaining the release becomes a problem, inherited by the current Owner/Seller.

A similar problem relates to fraudulently recorded Certificates of Satisfaction. In some instances, Borrowers have recorded documents showing a lien is released, when the lien has not yet been paid in full.

A third release problem relates to title examiners who fail to look at the Certificate of Satisfaction. Some examiners just look at the computer (or paper) index and rely on the notes as to which property is released of record. In tandem with this problem is the problem of a release (a Certificate of Satisfaction) which is defective, fails to properly describe the lien that is being released. Most often the deed book and/or page number are incorrect, but other inaccuracies also show up. As a general rule, unless there is some additional reason to believe the release is fraudulent, if there in only one error, the release will probably be accepted by title companies for insurance purposes. If there are two errors, it depends more on the nature of the errors, and if there are more than 2 errors the release needs to be redone. It takes time to investigate the release process. If the settlement agent has sent the proper documentation, with the proper language, to the lender, the settlement agent can record a valid Certificate of Satisfaction using the authority granted in the Code section cited above.

(b) Judgment liens – A judgment recorded in the Circuit Court in Virginia is enforceable for 20 years from the date of the judgment, and can be renewed for an additional 20 years if the proper procedure is followed. In most cases once a court renders a decision in favor of a plaintiff, the plaintiff does not follow through with collection. Instead the judgment is recorded with the land records of the jurisdiction, becoming attached to any real estate the debtor owns in his/her own name, or might own in the future. Parties who own real estate as tenants by the entirety have statutory immunity from all but IRS liens, if the judgment or lien is against one of the marriage partners, but not both.

The title insurance agent determines whether or not the lien attaches, or whether it is an issue the settlement agent must clear up prior to settlement. Often the name is a common one, such as Susan Williams or Juan Garcia. Middle initials are not determinative with regard to liens. Generally, the judgment creditor has not provided enough information to easily identify the judgment debtor. Therefore, the settlement agent, in meeting the requirements of the title binder, must do the detective work necessary to establish whether it is the same person. The lower the amount of the lien and the more common the name, the less "due diligence" is needed. Often title underwriters allow the agent to accept an affidavit (sworn statement) that the Seller/Owner is NOT the person named in the judgment of record. However, some investigation is needed. The lender's credit report will list prior residences that can be checked to see if the address matches. The credit report itself may also list the debt. Today it is standard practice to Google a name to determine if any additional information can be obtained regarding prior addresses, or current locations. When the debtor is not the current owner, but a prior owner, an Owner's title policy can be invaluable. In these instances, depending on the details, the title underwriters often provide letters of indemnity between themselves to cover the matter, until the statute of limitation has expired.

Child support liens are treated as judgment liens.

(c) IRS liens – IRS liens fall in a unique category and must be paid and released of record. Tenancy by the entirety is no protection from IRS liens since 2002. The IRS will provide information as to whether or not the owner, or prior owner, and

the debtor are the same. IRS will also inform settlement agent or owner whether or not they will release the lien, and if so, how much will need to be paid to obtain a release. But obtaining the information takes time.

3. Deed (Contract/listing agreement) is not signed by all of the proper persons. A larger title insurance issue is when not all property owners sign a deed of trust. Often one owner qualifies for the loan, but two are on the deed. Real estate agents are involved with sales transactions. A defect in a deed of trust of record doesn't matter, as the lien, whether or not defective, will be paid and released of record.

(a) Missed life estate. These claims are becoming more frequent. Mom and Dad decide to give/sell their real estate to one or more of their children, for a variety of reasons (often not well thought out). However, Mom and Dad want to continue to live in the property as long as they are able, so they retain that right in the deed in the form of a life estate. The language in the deed makes it clear they have a right to possession for the remainder of their life (unless the deed has other limiting language for automatic termination when the last of them is a resident of a nursing home or health care facility for more than *x* days.) When the real estate is sold, Mom and Dad have to sign the deed, releasing their right to possession for their lifetime.

Title agents and examiners must review the whole deed, not just the introductory paragraph identifying the Grantor and Grantee.

(b) Restrictions of record. This is another claim that is becoming more frequent. In the foregone era of easy access to financing, community development agencies, state agencies, and others lent money to low-income borrowers on a subsidized basis. Often, the subsidies came with restrictions on the borrower's ability to reconvey or otherwise re-encumber the property. These restrictions are of public record, and can do such things as place lien caps (maximum lien limits), provide for a sub-market value repurchase by the subsidizing entity, or provide for a premium if the payoff comes before a pre-determined deadline (e.g., no payoff or refinance within the first 5 years). If a later transaction fails to comply with the restrictions, at best, it is subject to the restrictions, and at worst, it is void.

(c) Transfer on Death deed. Effective July 1, 2013 Virginia adopted the Transfer on Death deed statute, VA Code § 64.2-635 to allow owners of real estate to pass title upon their death without probate, as already occurs for tangible and intangible personal property. Heirs may be unaware the deed exists until a title search is done.

4. Incorrect legal description. Current custom in a large part of Virginia is for purchasers not to obtain a survey when buying real estate. In some instances, the survey is not ordered until the loan is completely approved, so that the survey cannot be completed prior to settlement. The purpose of surveys is primarily to identify the boundary lines and the location of any improvements on the real estate being conveyed. The practical purpose is to identify any problem (encroachments, overlaps, etc.) so that the Seller may address (i.e., fix/pay for fixing) the problem, rather than the purchaser buying an unknown issue that may need to be addressed in the future.

A survey may also identify a problem in the legal description in the deeds. Depending on where the property is located, the problem with legal descriptions may be as simple as a typographical error that can be corrected with a statement in the current deed ("erroneously referred to in prior deed as Lot 80C instead of 8-C") or it may be a problem where a metes and bounds description does not complete an enclosure, where there is an overlap of adjacent parcels, where multiple parcels were intended to be conveyed, but some were omitted in the current deed, etc.

How a problem regarding legal description is remedied, depends on the specific details of the problem in question. A worst-case scenario would be to require the courts to establish the boundary lines for a particular parcel before it could be conveyed to a new

5. Mechanic's liens. With Virginia granting mechanic's liens superiority, it is critical that mechanic's lien waivers or releases are obtained from interested parties. Often, agents will merely obtain a borrower-signed indemnity, but these are nearly impossible to recover under. This is a potential problem best addressed up front, not one to pursue after the fact.

C. What can a real estate agent do to address these potential problems that delay settlement?

1.When first meeting with a seller inform them you will need a copy of their title insurance policy once you have a ratified contract. This gives the owner time to find the policy

   a. Make sure the Owner keeps the original (it may protect them and their heirs after they sell the property.) Provide a copy to the settlement agent, who should forward it to the title insurance agent.

2. After you have the listing agreement ask for copies of all current loan statements, so payoffs may be obtained. Asking for this up front has the advantage of allowing you to determine if the loan is in arrears. If so, you need to work with the seller to make sure there is a quick sale, before foreclosure.
3. Ask about recent construction, so mechanic's liens don't pop up to cause a delay.
4. If an estate is involved, have your title and settlement agent do a current owner search to determine that the decedent didn't execute a transfer on death deed. If there is none, inquire about a will. The will may need to be probated. If the owner died without a will, a real estate affidavit will need to be recorded. Talk to your title professional.