2. AVOIDING CLAIMS
PDF Supplement

- Claims outline
- “A Claims Perspective on Short Sales” 45 *Fund Concept* 127 (Dec. 2013)
- “Keeping Pace with P.A.C.E. Liens” 50 *Fund Concept* 102 (Oct. 2018)

AVOIDING CLAIMS

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Many title claims can be avoided by paying close attention to detail, monitoring the closing process from start to finish, and by applying common sense. The purpose of this section of New Member Training is to discuss with our new agents some of the most common sources of title insurance claims submitted to Attorneys' Title Fund Services, Inc. ("ATFS") so these claims can be avoided. Some of the examples may seem obvious, but they can be easily overlooked in a high paced or high stress closing, or by agents and their staff members with limited experience in conducting real estate closings. While these examples are not a completely comprehensive list of all the title claims we receive, they are a good representation of the claims we most commonly receive in our office.

If you happen to learn of a potential claim before the Claims Department is notified and you realize you cannot resolve the matter yourself quickly and completely, then please bring it to The Fund's attention without delay. Prompt action on your part may well result in a quicker and less expensive resolution and less chance that any critical deadlines will be missed. Please also make your contribution towards the resolution a matter of priority as you are often the person with the most knowledge of the issue at hand.

I. Claims Prevention

A. No one claim is identical to another, although their patterns do tend to repeat themselves in ways that can be broadly categorized. Florida's title insurance industry offers underwriting assistance and education so that *most* claims can be eliminated – or at least be reduced to those risks that the underwriter might willingly agree to assume up front.

B. Probably the most common type of claim we see is one that is based upon some underlying defect in execution, such as the wrong or missing legal description of the subject property, wrong name of one of the parties, or improper witnessing or notarization.

C. Successful Avoidance of Claims:

1. Training and Educating yourself and your staff
2. Closely supervising the closing process
3. Following uniform office procedures
4. Immediate recording of documents in the public records
5. Promptly sending policies to owners and lenders
6. Careful monitoring of your trust account access and reconciliation

II. Common Claims

A. The following is a list of the type of claims most commonly reported:

Bad legal descriptions	Defective instruments
Superior mortgages	Easements
Ad valorem taxes	Corporate defects
Non-joinder	Judgments
Ingress/egress and access	Foreclosure defects
Code liens and assessments	Restrictions and reservations
Breaks in chain of title	Undisclosed heirs
Survey-related	Homestead
Homeowner or condo liens	Federal tax liens
Construction liens	Probate defects

<u>B.</u> Shamefully, Broward and Miami-Dade Counties are the runaway leaders in the manufacture of statewide claims. A recent report shows that, together, Broward and Miami-Dade generate more claims *than the next 10 Florida counties combined!*

<u>C.</u> <u>Causes for the Common Claim</u>

Claims occur due to four basic reasons:

(1) *Simple Negligence:* Including human and computer error.

(2) *Gross Negligence:* Reckless indifference to closing instructions and sound underwriting principles.

(3) *Fraud & Illegality:* From misuse of notary seal, to preparation of false conveyance documents, to participation in criminal acts.

(4) *Unavoidable Risks:* Such as the gap and back chain defects.

III. <u>Common Claims</u>

<u>A.</u> Unrecorded Easements

<u>B.</u> Homestead Claims

<u>C.</u> Corporate Authority

<u>D.</u> Probate Issues

<u>E.</u> Code Violations v. Code Liens

IV. <u>Top Ten Tips to Consider to Avoid Claims</u>

<u>1. Active Involvement Are</u> *you actively involved in the closing process?* Do not simply turn everything over to paralegals. Remember, it's your name on that policy, not theirs.

a. Carefully research the background of new hires and supervise them. Sadly, young lawyers oftentimes fall prey to unscrupulous "closers" who float from one firm to another, with promises to bring a book of business in exchange for employment and a percentage of the business referred. These persons might even ingratiate themselves to the point of asking for check signing authority. History shows that unsuspecting lawyers may be victimized by persons very knowledgeable in the title business. For example, a recent claim involved a para-professional that presented her lawyer-employer bogus Title Insurance Commitments and Settlement Statements and successfully induced the lawyer to issue payoff checks to companies that the employee owned. In turn, the employee would keep the second mortgage (often a HELOC) current by making the minimum monthly payments. A best practice might mandate that the attorney insist that a copy of the Commitment issued by the underwriter go directly to the lawyer and that disbursement be made against that copy.

b. Know how to read the title search and review the exceptions. Simply ordering a title search is not enough. Reviewing it and understanding what it reveals is paramount. Sometimes, for example, the report will give a "Replat Warning." This means, in simple terms, that by virtue of a replat of the property, the legal description has changed, thereby mandating that an additional search of the "new legal description" be ordered and reviewed. Also, do not rely on the import of abbreviations and shorthand codes stated in a computerized data report. An underwriter was recently obliged to pay-out a significant sum in settlement of a title claim where the agent ignored what appeared to be an innocuous "AFF" (affidavit) in the search report. It turned out that the AFF was an Affidavit of Reinstatement recorded by a mortgagee who claimed that an earlier filed Satisfaction of Mortgage was recorded erroneously. In another case, an insurer was similarly liable on a claim submitted on a mortgagee policy where the agent similarly ignored an

"AFF" code – in that case, the Affidavit was that of the grantor to the mortgagor disclaiming and denying his signature on the deed into the mortgagor/owner. Take the time to actually review the exceptions. Do not blindly copy exceptions from a prior policy into your Title Commitment without first noting the significance of each instrument and whether the exception still applies. Understand that the exceptions may have a large impact on the property. Beware in particular any exception that references the term "reservation." Explain to your insured what has been reserved and to whom.

2. LEGAL, LEGAL, LEGAL *Have you double checked the legal description* before you send the deed/mortgage in for recording? All it takes is one erroneous keystroke to turn "Lot 12" into "Lot 22".

a. Ensure proper preparation and execution of the closing documents. This seems elementary, but the number of claims emanating from improper execution and faulty legal description is truly astounding. While you, the lawyer, may be fully cognizant of joinder issues, is your staff sensitive to the concerns? Take the time to educate your para-professionals of homestead-execution issues. Spend the few extra moments to cross-read that lengthy metes-and-bounds legal description. Confirm that if the deed is intended to read Lot 11, Block 1, that the instrument you are recording does not instead state Lot 1, Block 11.

b. Did you remember to attach the legal description as Exhibit "A" to your deed or mortgage if such an exhibit is being used? You would be amazed how often this does not happen.

c. ***Proofread Legal Descriptions***. There is simply no substitute for having two people proofing the legal description of the property before any document is sent for recording. Metes and bounds descriptions should be read against the legal description on the survey if a survey is provided. While most claims for an error in legal description are resolved by obtaining corrective instruments, the requirement may embarrass the title agent. It may also not be possible to get corrective documents executed because one of the parties is deceased or the business entity is dissolved. Two related observations. Simply rerecording the original instrument with the legal description altered is ineffective if the instrument is not re-executed and re-acknowledged. *Connelly v. Smith*, 97 So.2d 865 (Fla. 3d DCA 1957). This happens frequently and it resolves nothing. Also, if a mortgage is recorded with an error or without a legal description and the lender does not readily return the mortgage for correction, a mortgage modification signed by the mortgagor spreading the mortgage to the correct property may be effective. Do not assume separately described parcels are contiguous, carefully examine the survey.

3. <u>Who should be signing?</u>

a. ***Have you confirmed that all title holders have signed*** the deed or mortgage?

b. ***Minors?*** If one of the title holders is a minor, you may well need a court appointed guardian. Court appointed guardianship cannot convey or mortgage property without a court order, which needs to be recorded with the deed or mortgage. If the title interest is held by a minor, consult Title Note 10.04.06. If the minor's interest exceeds $15,000.00, then a formal court appointed guardian must be established, along with a separate order authorizing the guardian to execute the documents on behalf of the minor. Both the order establishing the guardianship and authorizing the subject real estate transaction must be placed of record with the deed or mortgage. If the value of the minor's interest is less than $15,000.00, the parents may act as natural guardians.

c. ***Homestead?*** Remember that even if one spouse is not on title, if you are selling or mortgaging homestead property, they have to join? No exceptions. Even if they've lived apart for the last 10 years and the divorce is pending.

d. ***Fiduciaries?*** If dealing with fiduciaries, do you have the appropriate documents or court orders ready for recording? Do you have the original power of attorney? Have you reviewed the trust to confirm selling authority? Did they sign as trustee? If the trustee is also the settlor and it is his/her homestead, they need to sign both individually and as trustee.

e. ***Business Entities?*** If someone is selling or mortgaging property on behalf of a business entity, do they have the apparent authority or do they have the appropriate resolution authorizing them to execute the documents? Also, make sure they are signing in their business capacity and not individually. If the deed or mortgage is coming from a corporation, remember that only the chief executive officer, president, and a vice-president have apparent authority to sign. **There is no apparent authority for Directors or Secretaries to sign deeds and mortgages.** Anyone other than a CEO, president, or vice-president who intends to sign a deed on behalf of a corporation requires a board resolution; and that resolution must be recorded with the deed or mortgage. If a resolution is recorded elsewhere, make certain it is recorded in the same county the property is located in and reference the recording information in the deed or mortgage. Further information on deeds and mortgages from corporations and limited liability companies (LLC's) can be found in Chapter 11 of the Title Notes.

f. ***Probate?*** Even if the probate court has entered an order authorizing the sale of real property, have you confirmed this property was not the homestead of the deceased? If it was, the order is likely meaningless for title insuring purposes. Personal representatives do not have the power to convey property from the estate if that property was the homestead of the decedent. This is true even if the probate court enters an order authorizing the sale. Homestead property is not part of the deceased's estate. Too many times the *Order Determining Homestead* is entered after the sale which does not avoid the title claim. It is worth investigating to see if the deceased was residing on this property, or was getting a homestead exemption on the property, prior to their death. If it is not homestead, does the will give the personal representative the authority to sell the property? If not, you will need an order from the probate court. Agents should familiarize themselves with Chapter 2 of the Title Notes, as there are a multitude of issues that must be dealt with regarding probate estates. Underwriting Counsel should be contacted in the event clarification on any issue is needed. Probate errors are one of the top sources of claims with title insurance companies. It is also worth noting that **Power-of-attorney?** Make certain the power to sell and convey title is included. Also, make certain the principal behind this power of attorney is still alive. It is not uncommon to see an attorney-in-fact attempting to use a power-of-attorney on behalf of someone who is deceased. If the principal is available, he or she should execute the documents instead of relying on the power-of-attorney. This will help decrease the likelihood of fraud. Make certain the power of attorney is recorded with the deed, or if it is recorded separately, include the recording information for the power-of-attorney in the deed itself. If a power-of-attorney is to be used on behalf of a trust, corporation, or other business entity, the express authority for any officer or trustee to delegate that authority must be included with the power-of-attorney and recorded. A resolution authorizing the person who is going to sign on behalf of the organization or trust will likely also be required. A call to the Underwriting Department is highly recommended before you accept a power-of-attorney in these circumstances. Powers-of-attorney are discussed in further detail in Chapter 4 of the Title Notes.

4. <u>Check the Survey</u>

Did you review the survey for specific exceptions to be included in Schedule B before you deleted the standard survey exception? If there is an encroachment identified and you make no exception, you have created instant liability under the policy. An immeasurable amount of claims occur because the title agent failed to review the survey or, having looked at it, did not understand its importance. While survey defects do affect platted residential closings, it is far more common that they will come back to haunt commercial, vacant land, and unplatted property closings.

a. All Florida title insurance underwriters offer courses in how to read surveys -- take a class or two, it's that important. If nothing else, understand that your surveyor, in rendering a boundary survey, will only pick up easements that appear on the plat. If it is not a platted easement, the surveyor will not learn of the easement's existence UNLESS YOU DELIVER A COPY OF THE TITLE COMMITMENT TO THE SURVEYOR TOGETHER WITH HARD COPIES OF THE EASEMENTS. Only then will the surveyor know to plot the easements on the boundary survey. Share the survey with the buyer early on - not at the closing table - and consider having the buyer initial by all encroachments and other survey defects. Delete the standard exception only once a valid survey is obtained and the specific survey exceptions to Schedule B of the Policy are included – this is typically the practice where a “clean” Form 9 Endorsement is being issued.

5. <u>Confirm the correct Mortgage is Being Paid Off</u>

a. ***Be sure you’re satisfying the right loan***, confirm the estoppel letter and obtain the Satisfaction of Mortgage. Where possible, do not rely on the seller (in a purchase and sale) or the owner (in a refinance) to obtain the payoff letter. It is always preferable that the agent, himself, obtain the estoppel letter. Carefully compare the legal description and/or loan number of the mortgage to the payoff letter. Do not assume that is impossible or improbable that the seller has two different loans with the same lender. The payoff letter may reflect a “mailing address” for the borrower/seller – do not assume that that address is the property address. A seller or borrower on a refinance transaction may have multiple mortgages from the same lender secured by one property or different properties. The property owner may provide the wrong loan number, either innocently or otherwise. The payoff should bear a reasonable relationship to the original mortgage amount. Follow any instructions on the lender’s payoff letter, including updating the payoff amount by a telephone call the day of closing. Due to a litigation risk, an estoppel letter should not be relied on if there is a reason to believe a mistake has been made by the lender.

b. A particularly vexing issue concerns the lender who, in essence, “disavows” its payoff letter. This typically involves a poorly prepared estoppel letter which fails to include an item, say, a prepayment penalty. After closing and remittance of the payoff check, the lender returns the payment with a letter insisting that the payoff be re-calculated to include the prepayment penalty. By this time, the seller is long gone. The lender snidely points out that it was the agent’s duty to follow its estoppel letter instructions, which upon careful examination does state that the agent cannot rely on the accuracy of the estoppel letter unless the agent "re-verifies" the payoff information by requesting an update immediately prior to closing.

To avoid this scenario, the safest practice would be to do as the lender requires and re-verify the payoff information immediately prior to the closing. Also, review the mortgage that you are satisfying. Does it mention a pre-payment penalty? If so, and assuming the payoff falls within the penalty period, does the estoppel letter likewise reflect a pre-payment penalty? If not, inquire why.

c. Lastly, follow up on obtaining the satisfaction of mortgage. Under Florida law, a lender must deliver a satisfaction or release of mortgage within 60 days of receipt of the correct payoff, and in an action to enforce deliver, fees may be awarded. Sec. 701.04, F.S. Mention or even cite the statute in your form letter enclosing the payoff check. More importantly, have a system in place reminding you to follow up for the Satisfaction. Don't just assume that the institutional lender will eventually record one. Many a title claim involves chasing after a Satisfaction. What with the failures, takeovers and mergers in the lending industry, it is often very difficult to obtain a Satisfaction for a loan that was paid-off years earlier.

d. Fund Title Note 22.05.16 also suggests recording a notice limiting future advances as provided by Sec. 697.04(1)(b).

6. <u>Reduce the Gap</u>

a. ***Narrow the gap and record promptly***. The gap is the period of time from the most recently examined public record and the time of recording the insured instrument. Public records are not posted and indexed immediately upon recording so there will always be some period of time (the gap) that remains invisible to the title examiner. A large amount of claims arise as a result of instruments that are recorded between the effective date of the title commitment and the date of the recordation of the insured deed or mortgage. Sec. 627.784, F.S., states that the standard gap exception set forth in paragraph 1 of Schedule BII of the Title Commitment is to be deleted if the title insurer or its agent "disburses settlement or closing funds." The significance of promptly recording the insured instruments cannot be over-emphasized, as Florida law protects the subsequent bona fide purchaser who has no notice, actual or constructive, of the earlier delivered instrument. Thus, for example, if the agent fails to timely record a deed from grantor to A, and the same grantor then delivers a deed to the same property to B, if the deed to A is not recorded on the day B pays value without notice, B prevails over A, *even if A subsequently records first.* Sec. 697.01, F.S.; *McCahill v. Travis Co.*, 45 So.2d 191 (Fla. 1950).

b. There are two aspects to reducing the gap.

    i. Conduct a "day of disbursement title search": update the title search just before closing; this is also referred to as "checking down" the title. This is a critical step that too many agents miss.

    ii. Record the documents immediately upon closing. Hand delivery to the recording office is best. Sending by overnight courier is second best. Merely mailing the documents is the slowest and promises to extend the gap period.

c. In addition to the obvious matters a shortened gap will protect against, judgments, competing deeds and mortgages. You may be surprised how many sellers or borrowers never disclose these pending matters to the closing agent. Avoiding recording delays are your best defense.

7. **Forgeries in the Chain** Forgeries in the chain have been described as "pure title insurance loss" because an examiner today will not have any information

about the person who executed a document a month or a year ago. There are certain documents that carry a higher risk of forgery and bear closer examination or investigation. If a document or situation seems to be suspicious, all title insurance underwriters would invite agents to consult the underwriter department for direction or assistance. The higher risk documents include the following examples.

a. Quit claim deed recorded with minimal stamps. A simple check that may reveal a significant problem is to compare the signature on the quit claim deed with signatures on prior mortgages by the grantor. Fund Title Note 10.03.09 lists the following flags that may suggest further investigation should be conducted.
    i. The deed does not appear to be for one of the traditional purposes of quitclaim deeds, such as clearing defects, deed in lieu of foreclosure, dissolution, etc.
    ii. The deed is handwritten.
    iii. The deed does not show the scrivener.
    iv. The deed shows the grantee as the scrivener.
    v. The deed is recorded several months after it was purportedly executed.
    vi. The acknowledgment is incomplete.
    vii. The property appraiser's records show an out of state address for the grantor but the deed was acknowledged in Florida.
    viii. The deed shows minimum documentary stamps.
b. ***Be suspicious of the naked Satisfaction of Mortgage***. Satisfaction of mortgage recorded with no refinance or sale. This may be a simple satisfaction or coupled with a mortgage elimination scheme. Yes, it's theoretically possible that an owner has paid off her mortgage in, say,

January, and then contracts to sell the premises in March. Having said that, in situations where the seller's mortgage is satisfied of record without a corresponding new loan, take the time to closely examine the release or satisfaction of mortgage.

8. **Code Violations and Code Liens** Title insurance policies in Florida contain an exclusion for code violations unless there is a notice of the violation or a code enforcement lien recorded. In Dade and Broward counties the code enforcement offices have started pursuing open permits dating back to Hurricane Andrew. While open permits are not a covered matter under a title insurance policy, buyers have begun to ask the attorneys who represented them at closing why such matters were not investigated.

9. **Small Lien and Cross-claim Foreclosures:**
    a. Small Lien Foreclosures. Many underwriters, including The Fund, decline to insure property that has passed through a small lien foreclosure unless certain safeguards are employed. See Fund Title Note 22.02.12. The small lien may be a condominium lien, judgment lien or tax lien. There is a very real litigation risk in insuring such property as the prior owner may seek to set aside the foreclosure, usually for lack of proper due process.
    b. ***Take extra precautions when insuring title out of small lien foreclosures***. All too many title claims involve poorly conducted foreclosures. This might mean a foreclosure where invalid or no service was obtained or a junior lienor was altogether omitted from the action. When insuring a purchaser out of foreclosure, a careful review of the foreclosure file is necessary. Determine that all appropriate persons were joined as defendants in the suit and be certain that all such defendants are shown to have been properly served. Was personal service effected? Be extra cautious of substituted

service. And, where service is by publication, does the *Affidavit of Diligent Search and Inquiry* meet the basic requirements?

c. The potential for loss in this context is staggering, particularly where the agent issues an owner's policy out of a small lien foreclosure. Bear in mind that most all trial judges will bend over backwards not to deprive an owner of his property when the lien amount is small. The risks here are so dramatic that many underwriters will require that the agent receive specific underwriting approval

d. To avoid this scenario, limit writing policies out of small lien foreclosures (e.g. HOA and condo liens, small judgments, municipal liens) to only those instances where personal service was made on the owner. Be sure to follow your underwriter's guidelines, particularly where service is by publication and defendant's whereabouts were unknown, See Fund Title Note 22.02.12. Try to stand clear of substituted service.

10. **Watch out when paying off PACE liens**. Recent reports from the field have revealed that PACE lien payoff statements may not include the current year's non-ad valorem assessment, particularly if the payoff letter is issued after June 1st. The TRIM notice will not reflect the assessment, as it's a non-appealable item. Be prepared to collect and escrow that year's assessment or add language to a Re-Proration Agreement that specifically covers the upcoming year's assessment.

V. FRAUD IN THE CLOSING PROCESS

Unfortunately, mortgage fraud is a major problem in Florida. In the past several years there have been well-publicized reports of arrests, indictments and convictions involving Florida attorneys caught up in all manner of mortgage fraud. Lawyers are targeted for arrest even where it is shown that the lawyer did not share in the illicit gains – it may be enough that the lawyer was willing to look the other way in exchange for doing the closings. Common sense and a healthy dose of skepticism (if not cynicism), will go a long way in protecting oneself.

A. ***Be suspicious of cash-out loans on vacant lots***. Fraudsters have long shown an affinity for fraudulently conveying and borrowing against vacant lots due to the ease of accomplishing the fraud. Carefully review the vesting deed and look for red flags. See Fund Title Note 10.03.09 for an exhaustive list of indicia of fraud. Scrutinize the borrower's identification.

B. ***Be suspicious of buyer-borrowers who put little or no money down and title has just come out of foreclosure.***

C. ***Be suspicious of buyer-borrowers who put little or no money down and seller is not yet in title.*** Experience teaches us to be extremely wary of these situations, particularly where there is no real estate salesperson involved in the transaction. These deals usually involve a seller looking to get in and get out quickly. Conspiracies among sellers, buyers, and mortgage brokers involve what is termed "fraud for housing." A seller may induce a sale on the promise of paying all of buyer's costs and, with the mortgage broker's assistance, will prepare and submit a bogus loan application in the "buyer's" name. The sales price is often inflated and justified by an ill-prepared appraisal. When the insured-lender foreclosures, the buyer, who hasn't invested anything and who doesn't care about her credit score, typically resists, all the while living "rent-free."

D. ***Be cautious with mail away closings***. A mail away closing refers to those occasions when a party to the transaction is unavailable to physically attend the formal closing and the paperwork is sent out of town to that party with instructions that they be signed before a local notary public. This, of course, invites notary fraud, a major problem for the title insurance industry. To minimize the inherent risks associated with entrusting that the proper parties are signing the documents before a notary public and witnesses, have the signing parties visit an office of a trusted lawyer or title agency in their town. If you don't know anyone, odds are that your underwriter does. Have the local notary complete a *Notary's Certificate*. Never allow a seller or borrower to take a document from a title agent's office to have it signed by a co-owner or spouse; there is a high incidence of fraud in the execution of such documents. An attorney, notary or branch office of a title agent's underwriter may be independently identified. Send the documents directly to the notary in that office. Any charge by an underwriter's branch office will likely be minimal.

E. ***Never assume someone's capacity; beware the caregiver*** Claims frequently arise when a closing agent does not make reasonable inquiry into the capacity of a party to sign a deed or mortgage. This issue often comes into play when a crooked "caregiver" or "friend" sees an opportunity to swindle an elderly person's real estate. The lawyer is asked by the caregiver to prepare the deed and the preparer does not make sound inquiry into the elderly person's mental capacity. Real estate attorneys are not trained mental health professionals. Remember that litigators love asking "what professional training did you receive in order to sufficiently gauge the grantor's capacity"? Do not blindly prepare a deed for an elderly or seemingly confused person, particularly where the proposed grantee is the party asking you – and paying you – to prepare the instrument. This is all the more true where the grantee refuses to leave the side of the grantor.

F. ***Be sensitive to recent changes to SunBiz filings and corporate***

documents. Underwriters have seen a rash of claims involving business identity theft, e.g. unauthorized on-line changes to managers of LLCs. Look carefully at an entity's SunBiz page and check to see if there was a recent change; is the person you are dealing with for that entity new to the company? Is he preventing you from speaking with other persons whose names were long associated with the entity, per SunBiz? Does the Operating Agreement look fishy? Are you being told there is no OA?

G. ***Beware of the Flips*** A "flip" is the resale of property in a very short time frame. The property may be resold the same day, using the proceeds of the resale to fund the first sale, or delayed up to a year. A flip may be perfectly legal as long as there has not been a misrepresentation to any party. Due to a high incidence of first payment defaults lenders are restrictive when asked to lend money to purchase a "flipped" property. Due to these restrictions, closing agents and title agents are occasionally asked to misrepresent the buyer's cash to close or a title agent is asked to misrepresent the party in title on a commitment. While these types of misrepresentations may not result in a covered claim (title is validly in the borrower at the time of the mortgage) such misrepresentations may result in liability for the individual agent. See *Beware of the Mortgage Fraud Trap* by Ted Conner, 30 *Fund Concept* 139 (Oct. 1998). *Buy Low, Sell High?: HUD Rule Attempts to Curb Land Flipping* by Connie Clark, 36 *Fund Concept* 53 (May 2004). In short, the settlement statement must accurately represent the money passing through a trust or escrow account.

V. <u>CONCLUSION</u>

As can be seen, avoiding title claims is no easy task. Attention to detail will help avoid the common claim, while a healthy dose of skepticism will go a long way in ferreting out the possibility of being ensnared in a fraud scheme. Do educate your staff what to be on the lookout for. Don’t look the other way and ignore the lender’s written instructions no matter how onerous they may appear. Do take advantage of the legal education programming and underwriting assistance made available to you. Don’t take the easy way out and hope for the best. With luck, you can avoid being a statistic … and you will undoubtedly sleep better at night.

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A Claims Perspective On Short Sales

BY SCOTT D. JACKSON, FUND CLAIMS COUNSEL

As the real estate market in Florida continues its slow, progressive recovery, closing agents are handling an increasing number of short sales, wherein the lender, often already engaged in a foreclosure action against the borrower, agrees to a sale of the property for less than the amount owed on the note. These short sales allow the property to be sold for its current market value, which is often less than the amount owed on the note, and creates an opportunity for Fund Members to increase their business volume.

However, with these opportunities come certain challenges. The Fund's Claims Department has noticed an increase in the number of title insurance claims associated with short sales, and we are finding certain recurrent themes. The purpose of this article is to assist Fund Members and their staff in avoiding these common pitfalls when handling a short sale transaction.

It is also worth noting that some of these guidelines will easily apply to any transaction handled by your office.

1. Is your closing taking place before the deadline on the lender's estoppel letter?

Often short sale estoppel letters will not contain a per diem rate that goes beyond the deadline stated in the estoppel. If the closing is going to be delayed and will occur after the deadline date on the estoppel letter, do not rely on verbal authorization from the lender as to any per diem rate or new payoff amount. Always get the new payoff or per diem in writing. There have also been circumstances wherein the lender attempts to reject the payoff due to the lender's miscalculation on the estoppel, even when the Fund Member conducted the closing and submitted the funds prior to the deadline stated on the estoppel letter. If the lender refuses or returns the payoff to the Fund Member's trust account, the member should contact The Fund's Claims Department immediately.

2. Have you submitted your estoppel request to the correct lender?

While this may seem obvious, The Fund's Claims Department has dealt with situations where the first mortgage was held by "ARG Mortgage" and the equity line mortgage was held by "ARG Bank." The Fund Member seems to have simply focused on "ARG" without realizing the bank lender and the mortgage lender were completely different business entities that do not cross-communicate with one another. The member would submit an estoppel request with both mortgage numbers on the same estoppel

(Continues on page 130)

in this issue:

Short Sales...*continued from page 127*

request to the first mortgage lender, who would then submit a short sale payoff amount. The member would miss the fact that only the first mortgage number appeared on this estoppel and that the equity line mortgage number was nowhere to be found. The member would then rely on that one estoppel and proceed with the closing; only to have the new owner face a post-closing foreclosure action filed the equity line lender. As no notice of the short sale or estoppel request was ever submitted to the equity line lender, they may not bound by the payoff terms of the mortgage lender. The only recourse is to satisfy the equity line mortgage in full and obtain a satisfaction of mortgage from them.

3. Is foreclosure counsel for the lender aware the short sale is taking place?

Communications between the lender and their foreclosure counsel can often be inconsistent, especially if both are dealing with a large volume of foreclosure actions. The Fund Member should never presume that communications with the lender are automatically being forwarded to their foreclosure counsel. If the foreclosure counsel is not properly advised of the short sale, the foreclosure can easily continue after the short sale has occurred, go through to final judgment of foreclosure, and even to sale with the issuance of a certificate of title.

To avoid this, the Fund Member closing a short sale should separately contact the foreclosure counsel to advise them of the short sale. This will allow the foreclosure counsel to confirm to the lender and the member that they will dismiss the foreclosure action with prejudice and release the lis pendens upon completion of the short sale. If the final judgment of foreclosure has already been obtained, it will allow foreclosure counsel to take the necessary steps to vacate the final judgment, cancel the sale, release the lis pendens, and dismiss the foreclosure action with prejudice. This contact will also allow the foreclosure counsel to coordinate their fee with the lender for taking these actions and avoid any post-closing attorney fee issues.

4. Have you received the necessary estoppels from all the homeowners' or condominium associations and is there a collections attorney involved?

Sometimes a homeowner or condominium unit owner can be subject to more than one association. While this is not a common occurrence, it does happen often enough that the closing agent should be aware of the possibility. One "red flag" to look for is a situation where the title search reveals two sets of covenants, conditions and restrictions, or in the case of a condominium, both a declaration of condominium and an additional set of covenants, conditions and restrictions. When in doubt, the Fund Member can usually contact the association to confirm if more than one association exists for this property.

5. Are you sure the estoppel sent by the association reflects all of the sums they are owed?

Often in short sales, not only is the mortgage is default, but also the association dues and assessments are severely in arrears. After a certain point, these amounts are often "written off the books" by the association and sometimes are turned over to an attorney for collection.

These delinquent amounts will not appear on the estoppel from the association. Instead, the Fund Member will often find a single line on the estoppel letter advising them to contact a certain law office to inquire as to any additional amounts which may be owed on the subject property. That is the member's "red flag" and the law office should be contacted immediately. The notice on the estoppel to contact the attorney is viewed as sufficient to put the Fund Member closing short sale on inquiry notice. Members should also note that the amount they are attempting to collect through counsel will often be much larger than the amount appears on the association estoppel letter.

Most of these guidelines will prove helpful to Fund Members even in a regular closing, but The Fund's Claims Department has noticed a particular association between these kinds of claims and short sales. Following these steps will help to ensure a smooth closing, without surprises, for all the parties involved.

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KEEPING PACE WITH P.A.C.E. LIENS

BY CHARLES D. NOSTRA, FUND SR. UNDERWRITING COUNSEL

As Property Assessed Clean Energy (PACE) financing agreements become more commonplace, they are increasingly showing up in title searches, and Fund Members are likely to see related requirements in title commitments.

PACE financing agreements are used to make certain qualifying energy efficiency and hurricane hardening improvements to commercial and residential properties. See "PACE Picks up in Florida," 49 *Fund Concept* 101 (Sep. 2017). As a reminder, the article further explained that, "bonds may be issued by counties, municipalities, dependent special districts under Sec. 189.012, F.S., and separate legal entities under Sec. 163.01(7), F.S., to finance the improvements. The repayment of such improvements is then secured by liens paid through non-ad valorem assessments on the property tax bills of the specific property owners who availed themselves of the program."

Qualifying requirements for PACE financing agreements are relatively simple and are based on the home's equity and tax payment history. The approval process typically takes less than an hour. However in May 2018, President Trump signed the Dodd-Frank Wall Street Reform Act that directs the Consumer Financial Protection Bureau (CFPB) to create federal oversight of, and rules for, the program. New requirements may be added, requiring residential consumers to pass an "ability-to-pay" analysis before they are approved. The additional documentation is likely to create longer approval times, and result in more applications being rejected. Florida, California, and Missouri are the only three states with PACE programs. While California has already imposed new requirements for its state program, Florida has no current plans to require a more comprehensive approval process, and the CFPB has no timetable or deadline for the creation of the new rules. For now, Florida's PACE program qualification requirements remain unchanged, and the number of PACE agreements continues to increase from year to year.

The PACE Lien and the Payoff Process

Once the property owner is approved for a PACE loan, a memorandum of financing agreement is recorded in the official records of the county where the property is located within five days of execution of the agreement by the property owner. Even though the agreement is of record, the first yearly assessment may be postponed up to eighteen months based upon the timing of the funding of the project.

Through interviews with PACE administrators and experiences related by Fund Members, it appears that the methodology by which PACE loans are released has a few unique twists, which can create some challenges pre- and post-closing. These challenges have come to light since the Sep. 2017 *Concept* article. The purpose of this article is to provide additional guidance to Fund members in light of this new information.

Disclosure of the PACE Lien and Non-Ad Valorem Assessment

Sec. 163.08(14), F.S., requires sellers to disclose, in the contract or by a separate writing, the existence of the PACE assessment prior to the execution of the contract by the buyer. The disclosure must be as set forth in the statute:

> QUALIFYING IMPROVEMENTS FOR ENERGY EFFICIENCY, RENEWABLE ENERGY, OR WIND RESISTANCE.
>
> The property being purchased is located within the jurisdiction of a local government that has placed an assessment on the property pursuant to s. 163.08, Florida Statutes. The assessment is for a qualifying improvement to the property relating to energy efficiency, renewable energy, or wind resistance, and is not based on the value of property. You are encouraged to contact the county property appraiser's office to learn more about this and other assessments that may be provided by law.

Despite the statutory requirement, it appears that most sellers, and many real estate agents, may not be aware of the disclosure obligation; therefore many buyers may not be aware of the existence of the lien until after the contract is executed and a title commitment is provided.

Underwriting Requirements

A PACE lien is a super-priority home improvement loan secured by a recorded lien, and paid through the tax bill. Even though the PACE program provides that the financing agreement is fully assumable, many lenders are unfamiliar with PACE lien agreements and require their mortgage be insured in a first lien position. Accordingly, for insuring, the FUND will require a satisfaction of the lien in commitments where financing is being obtained by a buyer. Satisfaction of the PACE lien will also be required for refinance transactions. The commitment requirement related to satisfaction of PACE liens will be similar to the following:

> *Record satisfaction of that certain "Summary Memorandum of Agreement" dated, duly recorded, in BOOK ____ PAGE ________, Public Records of ________ COUNTY______ County, Florida. Alternatively, record release of the lien of such (type of lien) as to the subject property.*

However, if the lien is to be assumed by the buyer, pursuant to the contract and without objection from the insured lender, the requirement may be removed with an exception for the lien added to Schedule B-II of the commitment. If the buyer agrees to assume the PACE lien, then only the current year's assessment should be prorated at closing.

The Payoff Request and Calculation Process

When improvement projects are funded before June 30 of the current year, the assessment will typically appear on the current year's tax bill in November. Assessments for projects funded on or after July 1 will typically not appear on the tax bill until the following year. PACE Assessments do not appear in the Truth-in-Millage Act (TRIM) notice, because PACE assessments are not subject to appeal. The PACE assessment will only show up in the November tax bill once the assessment amount is relayed to the assessor by the plan administrator.

Fund Members requesting payoff information related to the PACE lien should keep in mind that whether an estoppel letter received from the plan administrator will be for a complete payoff amount depends on when the assessment is made and when the figure is relayed to the tax assessor. Since the PACE program and its administration appear to have been set up for the agreements to be assumed by a subsequent buyer and not paid off upon sale, it may be a struggle to get a complete payoff from the administrator.

If a payoff request is made after the effective date of the agreement, but before the submission of the assessment information to the tax collector, it may be possible for the homeowner to negotiate for removal of the assessment from the planned submission to the tax collector. If the administrator has already submitted the assessment for collection by the tax collector, the process of taking it off the tax roll will likely be very difficult. The most likely scenario is that the payoff letter will have a notice that the payoff amount does not include the current year's assessment because it will be included on and paid through the tax bill.

For most transactions, Fund Members are likely to encounter a PACE lien payoff statement issued by the PACE administrator containing language indicating that the payoff amount does not include the current year's assessment in the tax bill (whether the tax bill has been issued yet or not). The Fund Member will have to review the recorded memorandum and any documents provided by the seller, as well as inquire of the administrator about what the current year's assessment will be (if not already on the tax bill from the prior year). The assessment will never be higher than the maximum amount listed in the recorded memorandum. For the payoff line on the closing disclosure, the Fund Member will use the PACE administrator's payoff amount. The full amount of the current year's assessment will be charged to seller on a separate line in the prorations section of the closing disclosure.

PACE Proration Considerations

Since the PACE lien results from financing improvements to the property, and the value of those improvements were likely factored into an increased property sale price, the PACE assessment should not be prorated, but should be charged 100 percent to the seller.

There are typically two components of the tax bill that are subject to proration, ad-valorem taxes and non-ad valorem assessments. When there is a PACE lien, the "prorating" of the tax bill requires three steps.

Step 1: The entire PACE assessment is charged to the seller;

Step 2: The ad valorem taxes are apportioned between the seller and buyer based on a calendar year in arrears; and

Step 3: The non-ad valorem assessments are apportioned between seller and buyer based on the charging entity's tax year, fiscal versus annual, and on whether it posts payments in arrears or in advance. Each charging entity's program could be different, so multiple lines on a settlement statement may be required for the proper proration of the non-ad valorem assessments.

Release of Lien and Post-Closing Considerations

Finally, correspondence from PACE administrators indicate that the final release of lien (satisfaction of the PACE Agreement) will not be recorded until the property tax payment window closes in March and taxes are confirmed as paid.

The Fund has been made aware of at least one instance where the PACE lien was paid off and the lien was satisfied, but the assessment continued to be included in the non-ad valorem assessments the next year. Fund Members should advise buyers to double check the next year's tax bill to confirm removal of the assessment.

Seller Issues

Fund Members should be prepared to explain the proration nuances to a seller who may not fully understand how the program works. Particularly, sellers may require assistance in understanding lender priority requirements and the program's "assumption of the lien by the next owner," or "the lien runs with the land" features that may have been overlooked at the time the contract was negotiated. Whether a PACE lien may be assumed is the buyer's and lender's choice to make, not the seller's. Sellers may be surprised (and upset) to learn that in most transactions the lien will have to be paid at closing, and that they may incur pre-payment penalties in doing so.

Fund Members who encounter a PACE lien in their examination should be aware that a payoff amount may not include the assessments portion being collected with the first installment under a financing agreement, and the complications that may arise when prorating the assessment on a closing statement.

UNDERWRITING APPROVAL REQUIRED FOR POLICIES OVER $1 MILLION AND FOR INSURING EXTRAORDINARY RISK

BY THE FUND'S UNDERWRITING DEPARTMENT

Transactions Requiring Underwriting Approval

Title insurance commitments and policies with an insured amount exceeding $1 million require approval by The Fund's Underwriting Department. Additionally, specific underwriting approval is required for insuring certain "extraordinary" risks. Commitments prepared by a Fund branch with an insured amount of over $1 million include the necessary approval upon delivery to the Fund Member as long as no substantive changes to the commitment's insuring provisions are made. Any substantive changes must be confirmed with Fund Underwriting Counsel.

Insuring Extraordinary Risks

Several areas present extraordinary insuring risks. If these risks are known by Fund Underwriting, they will be considered prior to delivery of a Fund branch commitment. However, sometimes these risks are discovered by the Fund Member after receipt of the commitment. In this situation, the Fund Member must seek approval from Fund Underwriting.

Extraordinary risks requiring underwriting approval regardless of policy amount include the following:

- Creditors' rights risk;
- Title to land under or formerly under navigable waters;
- Title to severed mineral or oil and gas interest;
- Title to land which derived from a swamp and overflow patent;
- Title derived from a mineral patent;
- Insurance of options to purchase;
- Title emanating from condemnation or governmental forfeiture proceedings such as tax, Internal Revenue Service, drug, and civil or criminal forfeitures, or titles otherwise derived through a sheriff's or federal marshal's deed;