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Title insurers are adapting to the changing landscape

March 21, 2011 - Financial Digest

Every corner of the real estate industry was affected by the economic meltdown of 2008/2009. The title insurance sector was no exception. Yet despite the negative economic factors prevailing during that period, the industry's credibility, trustworthiness and surety survived.

More harmful was the party thrown by regulators, financial institutions, appraisers and ratings agencies. That left a hangover that everyone connected with real estate shared. The title insurance industry endured two years of consolidation, streamlining and downsizing, with the attendant loss of volume, earnings and jobs.

The changes endured and trends emerging in the industry today include:

According to the American Land Title Association (ALTA), total title industry claims rose almost 92% from 2003 to 2008 hitting a peak of just over $1billion before declining in subsequent years. As things turned south, premiums rose, real estate values plunged and fraud increased. In response, especially during 2009, the industry tightened underwriting standards and dropped claim-prone agents.

Until just over a year ago, ALTA and the California Land Title Association (CLTA) supported the idea of insuring against creditors' challenges that might come up in the course of bankruptcies and could also come up outside the bankruptcy context. This coverage, which was available in many but not all states or transactions, was based more on evaluations of financial risk than the legal risk that title insurers were accustomed to. Industry players came to recognize that this type of coverage, at least for certain creditors' rights risks that arise out of the insured transaction itself, was beyond the core competency of title insurance underwriters. By March of last year, the ALTA and CLTA withdrew their endorsement, quickly followed by all major insurers ceasing the coverage.

Even as the industry has drawn back from certain excesses, new approaches have emerged. In a recent example, a title insurer played a key role in breaking a log jam between a developer and lender who sued each other during the financial meltdown in 2008. The lender sought to foreclose based on breached loan covenants; the developer countersued based on lender liability. The two parties were close to a settlement but title insurance became an issue because of millions of dollars in mechanics' liens filed when the developer stopped paying its contractors and material men. After an unusual use of underwriting resources to work through the liens to determine their true nature (many were duplicative or erroneously filed) and to suggest modification to the parties' escrow and indemnity agreement, the insurer co-insured the loan modification. Such problem solving is becoming more common as title insurers respond to customers' needs.

A raft of multilevel mezzanine loans on major commercial real estate deals occurred in 2006 and 2007. Title insurers used Uniform Commercial Code (UCC) coverage to insure these transactions. As the loans are being restructured, the loan-specific coverage is being terminated and insurers are working to provide new UCC coverage for what are effectively new loans without any new money, all while facing structuring and underwriting challenges resulting from the difficulty some customers are having accounting for the whereabouts of the original equity certificates that were delivered to the secured parties at the time the mezzanine loan was originated. Insurers will be doing more of this transaction reinventing, even as they insure new mezzanine deals, which have shown signs of resurgence.

The title insurance industry emerged from the downturn perhaps chastened, certainly re-sized and definitely more focused on its traditional legal-based risk models. At the same time, its underwriting resources and skills are being applied across a range of products and services that are playing a critical role in the recovery of real estate finance and deal making.

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