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Dual Agent or Double Agent

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A recent Federal Court case highlights the risks inherent in using a title agent that is also a "settlement agent."

What is a "settlement agent?"

Settlement agents (sometimes referred to as "escrow agents") act on behalf of the lender leading up to, and at, the closing. Following instructions from the lender, they prepare documentation, calculate various fees and costs, receive and disburse funds, etc. In short, they fill a large portion of the role traditionally assumed by the "bank attorney" in a downstate transaction. In theory, at least, they do not provide "legal services."

Many companies that provide settlement services are also authorized to write title insurance policies by licensed title insurance companies. Title insurance agency agreements typically prohibit the agent from providing settlement services on behalf of the insurer. Some agency operators, but not all, form a separate entity to provide settlement services, apart from the title insurance business. Even if corporate formality is observed, both businesses are usually operated by the same individuals, out of the same location.

Widely used in other jurisdictions, as well as upstate New York, settlement agents have been an increasing presence on Long Island in recent years. Probably the most well-known local example was TitleServ, Inc., and various subsidiaries thereof, all of which ceased operations in 2011 amid allegations of embezzlement and misappropriation in connection with "settlement" activities.

The federal case

In *Fidelity National Title Insurance v. Cole Taylor Bank,* No. 11 Civ. 4497 (MGC) (U.S. Dist. Ct., S.D.N.Y., July 10, 2012), the court held that a title insurer was not liable for the defalcation and malfeasance of one of its policy-writing agents. The agent had been contacted by Illinois-based Cole Taylor Bank to perform settlement services in connection with loan refinancings in the Albany area. The case revolved around two specific instances in which the agent prepared title insurance commitments and proceeded to close each loan. The closings were carried out in accordance with detailed instructions provided by the bank and previously accepted, in writing, by the agent. At each closing, the commitments were "marked up." Post-closing, the bank discovered that prior loans had not been paid off and that the monies earmarked for that purpose had been stolen by the agent. The bank made claims against Fidelity only to learn that the agent had not remitted the policy premiums to Fidelity, the mortgages had not been recorded and the policies had never been issued.


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The bank sought to hold Fidelity liable based on apparent authority in the agent to act on behalf of Fidelity. Fidelity pointed out that its agreement with the agent explicitly prohibited the agent from providing settlement services on Fidelity's behalf. More importantly, the bank was unable to show that Fidelity had made any representations to the bank that established apparent authority. In addition, testimony by the bank's own expert witness established that customary upstate closing practice did not establish apparent authority. Indeed, the expert testified that the "closing instructions from the lender to the settlement agent have nothing to do with the title agent." And, that "when [the agent] stole the loan proceeds, it did so as a settlement agent."

The *coup de grâce* came in the court's finding that the agent was legally the bank's agent, whose conduct could be imputed to the bank. As a result, any liability that might have arisen under the marked up commitments was barred by Exclusion 3(a) of the ALTA policy, which excludes coverage for "[d]efects, liens, [and] encumbrances" that are "created, suffered, assumed, or agreed to by the Insured claimant."

Due Diligence is indispensable

All the reported New York case law on this issue appears to emanate from the First and Second Departments (*see, e.g., HSA Residential Mortgage Services Of Texas, Inc. v. Stewart Title Guaranty Co., et al.,* 7 A.D.3d 426 (1st Dept., 2004); *Forest Park Cooperative, Inc., Section 2 v. Commonwealth Land Title Insurance Company*, 2011 NY Slip Op 31352(U) (Sup. Ct., Queens County, 2011)). Because dual-agency practice is primarily an upstate phenomenon, it will be interesting to see where the Third or Fourth Departments come down on similar fact patterns in the future.

In other states, parties can protect themselves against settlement agent malfeasance by obtaining a "closing protection letter" from the insurer, but CPL's are not available in New York for this purpose (*see* N. Y. S. Ins. Dept. Circular Letter No. 18 (Dec. 14, 1992) and N. Y. S. Ins. Dept. Office of General Counsel Opinion issued Dec. 28, 2005)). Therefore, prudence dictates that any settlement agent be carefully vetted prior to being retained.

Note: Lance R. Pomerantz is a sole practitioner who provides representation, expert testimony, consultation and research in land title disputes. He is also the publisher of the widely-read land title newsletter Constructive Notice. Please visit www.LandTitleLaw.com.