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10 Lawsuits You Can't Ignore

ALTA's Title Counsel Summarizes Key Cases and Explains Relevance of Decisions to Title Industry

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10 Lawsuits You Can't Ignore

ALTA's Title Counsel Summarizes Key Cases and Explains Relevance of Decisions to Title Industry

Prudent owners and managers of title operations spend time diligently reviewing production metrics to maximize profit. Many don't follow or consider the impact litigation and court decisions could have on their operations. Unfortunately for title professionals, this is an area of growing concern as litigation is on the rise. The "2016 Litigation Trends Annual Survey" from Norton Rose Fulbright reveals an upward trend in virtually all of the metrics relating to litigation. An increased volume of regulation is resulting in the threat of more regulatory disputes, resulting in the rise in expenditures to resolve issues. The 12th annual survey of 606 corporate counsels found that 24 percent believe the volume of disputes will increase in the year ahead. >>

To keep members informed of important decisions in courts across the country, members of ALTA's Title Counsel and others provided a synopsis of 10 lawsuits they believe have significant implications on the land title industry. From state supreme courts around the country and various other courts, the lawsuits dealt with a wide range of issues including date of loss, forged deeds and time limits, bad-faith claims, duty of care to third parties in recording of legal instruments, borrowers challenging wrongful foreclosures, spousal rights involving reverse mortgages, junior liens, liability to non-insured third-party beneficiaries, marketable title after tax deed sale and corporate seals on title policies extending statute of limitations.

While a decision may not be in a title professional's particular market, the case law could be used as examples for other courts.

"Knowing about these key decisions can prove helpful in protecting a company against any unexpected liabilities," said Marjorie Bardwell, chair of ALTA's Title Counsel and director of underwriting services of Fidelity National Title Group. "Decisions in these cases could indicate a trend in the interpretation of these legal issues, so it's important all title professionals understand the implications even if the rulings are not from their state or jurisdiction. Because of Title Counsel's efforts, ALTA members have access to information that a compliance officer or general counsel would consider important in identifying trends."

In no particular order, the following are summaries of the facts from the lawsuits, the court's decision and relevance to the title insurance industry.

Arizona Supreme Court Rules Against Insurer on Date of Loss Issue

Citation: *First American Title Ins. Co. v. Johnson Bank,* --- P.3d ---, 2016 WL 3247545 (Ariz. 2016)

Facts: First American Title Insurance Co. issued Loan Policies for deeds of trust on two different properties. The policies did not except certain covenants, conditions and restrictions (CCRs) recorded against the property that prevented its commercial development. The borrowers defaulted on their loan obligations. In 2010, Johnson Bank foreclosed and took title to the properties. After the foreclosure, Johnson Bank made claims under the lender's policies that the CCRs prevented the properties from being developed for commercial purposes and the CCRs were not exceptions to coverage under the policies.

The parties disagreed over the date for calculating the diminution in value as a result of the CCRs. Johnson Bank argued for using the date the loans were issued. First American contended damages should be calculated as of the date of the foreclosure, which was after the real estate market had declined precipitously.

The parties filed cross-motions for summary judgment and the trial court granted summary judgment in favor of First America. The court of appeals reversed, holding that, absent an express date in the policies, the date to measure any diminution in property value is the date of the loan, and remanded the case for entry in favor of Johnson Bank.

Holding: After analyzing the policies in light of the legislative goals, social policy and the parties' transaction, the Arizona Supreme Court found section 7(a)(iii) of the policies was ambiguous as to the date as of which diminution in value is to be calculated, and should therefore be construed against the insurer, First American. The Arizona Supreme Court rejected First American's argument that the date of foreclosure is the only reasonable date of valuation because the lender must foreclose in order to incur and claim a loss. Reviewing cases from around the country, the Arizona Supreme Court identified a line of cases that used the date of foreclosure as the date of valuation, but, those cases, it noted, involved undisclosed superior liens as the underlying title defect. The court held that, in those cases, it may well be appropriate to value the loss as of the date of foreclosure because the damage results from the insured lender not having priority, but refused to generalize that scenario to all circumstances. Instead, it adopted a case-by-case approach to identifying the date for valuing the loss.

The Arizona Supreme Court held that the policies implicitly permit the use of the date of the policy as the date for calculating damages under section 7(a)(iii), "if the title defect caused the borrowers/owners to default on Johnson Bank's loans." It vacated the appellate court opinion and remanded the matter to the trial court, however, agreeing with First American that there was no evidentiary support in the record that the title defect had caused the borrowers' default.

Justice C.J. Bales dissented, arguing that the majority, by reasoning that First American had caused the lender consequential damages by conducting a deficient search and failing to disclose the CCRs, was effectively imposing an abstractor's duty to disclose on a title insurer. Such a duty is not, according to Justice

Bales, authorized by the policies, which contemplate an actual loss that cannot be incurred by a lender until foreclosure.

Importance to the Industry: The Arizona Supreme Court's opinion appears to revise the reasonable assumptions of the parties evident in and underlying title insurance policies in order to construe those policies against title insurers and hold them liable for market declines. Moreover, the opinion creates another unnecessary problem, as it remains unclear how a title defect can cause a borrower to default or what evidence would be required in order to show this. None of this is addressed in the opinion or the Loan Policy and trial courts will in effect have to make it up after the fact. Thus, this opinion, as the dissent points out, threatens to impose an extra-contractual liability on title insurers for a loss that the lender is in the best position to evaluate at the time of the loan. While the 2006 ALTA Loan Policy addresses this issue, giving the insured lender the option of having the loss valued as of either (i) the date the claim is made or (ii) the date the claim is settled and paid, the Arizona Supreme Court's opinion will nevertheless still have a significant impact.

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New York Court Holds Forged Deed Claims Not Subject to Time Limits

Citation: *Faison v. Lewis, et al, 25 N.Y.3d 220, rearg. denied,* 26 N.Y.3d 946 (2015)

Facts: Faison and Lewis are first cousins. Faison's father and Lewis's mother had each owned a one-half interest in a property. Lewis's mother conveyed her half-interest to Lewis by a deed duly recorded in July 2000. In February 2001, a "correction deed" was recorded by which the grantor in the first deed was changed from just "Lewis's Mother" to "Lewis's Mother and Faison's Father" and purported to convey the entire ownership to Lewis. Faison's father passed away soon thereafter.

In 2002, Faison filed an action pro se to void the correction deed based on forgery. The action was dismissed because Faison was not the administrator of her father's estate. She alerted the attorney for the administrator, who assured her he would pursue the claim. He did not do so.

In 2009, Lewis borrowed $269,000 from Bank of America, securing the loan with a mortgage on the property. In July 2010, Faison was appointed successor administrator of her father's estate. She commenced a new action to void the correction deed soon thereafter. Bank of America moved to dismiss because the statute of limitations had expired.

Holding: Both the trial court and the intermediate appellate court adhered to long-standing precedent that the six-year statute of limitations for fraud applied to forgery claims. Even under the most liberal application of the discovery rule, Faison commenced the second action more than six years after discovery of the fraud.

In a 4-3 ruling, the Court of Appeals declared that "a claim against a forged deed is not subject to a statute of limitations defense." Despite an impassioned dissent by the chief judge, the majority swept away more than a century of black letter law. The majority clearly believed its intervention was required "to ferret out forged deeds and purge them from our real property system." It determined "there is no reason to impose barriers to those who seek to vacate such deed[s] as null and void" in part because forgeries "undermine the integrity of our real property system…."

Importance to the Title Industry: This ruling is a dramatic departure from established New York precedent. It is contrary to the plain language of New York's exhaustive statutory provisions concerning statutes of limitation, as well as the overwhelming weight of authority from other U.S. jurisdictions. Most important, it exposes New York title insurers to expanded defense liability on the mere allegation of forgery, and expanded indemnification liability on stale claims, with no possibility of repose. Widespread adoption of this approach could signal a dramatic expansion of risk for the title insurance industry.

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Hawaii Supreme Court Addresses Bad-faith Claim

Citation: *Anastasi v. Fid. Nat. Title Ins. Co., 366 P.3d 160* (Haw. 2016).

Facts: The insurer issued a policy insuring a $2.4 million mortgage. Five months later, the previous owner of the mortgaged property filed a lawsuit claiming his signature on the deed to the borrower had been forged. The insured sought coverage, which the insurer agreed to provide under a reservation of rights. Within a month, the insurer's analysis revealed that the

signature on the allegedly forged deed was "very different" from the seller's actual signature, and that the driver's license information recorded by the notary at the closing didn't match the seller's actual driver's license.

The insurer, however, believed the real owner of the property may have conspired with the purchaser to defraud the lender out of $2.4 million. Thus, counsel pursued the litigation on behalf of the insured, but the insured eventually lost on summary judgment. Retained counsel filed an unsuccessful motion for reconsideration and, at the insurer's recommendation, an appeal. The parties settled while the appeal was pending, and the insured filed this action against the insurer in which it alleged the insurer acted in bad faith by litigating when it had no reasonable basis for doing so. During the action, the insured filed a motion to compel the production of certain documents generated by the insurer's in-house claims counsel, which the trial court denied because it found that they were privileged. The trial court then granted the insurer's motion for summary judgment, finding the insurer had not acted in bad faith in litigating the matter. It also found no evidence that the insurer controlled the retained counsel's handling of the litigation, and that any alleged delay by retained counsel therefore was imputed to the insured. On appeal, the appellate court reversed the trial court on the motion to compel, holding that there was a presumption that any documents produced before the insurer made a coverage determination were not privileged. The appellate court further reversed the summary judgment decision and found that there were issues of fact as to whether the insurer acted in bad faith. Specifically, under Hawaii law, an insurer who defends an insured under a reservation of rights is held to an enhanced standard of good faith, which includes "refrain[ing] from engaging in any action which would demonstrate a greater concern for the insurer's monetary interest than for the insured's financial risk." Finally, the court affirmed the insurer did not control the retained counsel's defense in the action.

Holding: On appeal, the Hawaii Supreme Court affirmed the appellate court's decision in part and vacated it in part. First, although it disagreed with the appellate court's holding that any documents produced before a coverage determination are presumptively not privileged, it held that the trial court needed to determine whether the documents were produced "because of the prospect of litigation" in order to determine if they are privileged. Second, the Supreme Court affirmed the appellate court's decision that there were issues of fact as to whether the insurer had acted in good faith, holding that "[i]nsurance companies must act reasonably even when exercising contractual rights," specifically "the right to so prosecute or provide defense in the action or proceeding, and all appeals therein[.]" Finally, the Supreme Court vacated the appellate court's decision that the insurer did not control the retained counsel's decision-making, noting emails between retained counsel and the insurer that raised disputed facts as to whether counsel was deferring to the insurer on whether to appeal.

Importance to the Title Industry: First, claims counsel must be aware that documents generated from a claims investigation are not privileged without the anticipation of litigation, which likely is unknown until the claims analysis is completed. Second, even when an insurer is exercising its contractual rights to defend title, it must ensure the defenses it raises can support and document the defense of title. In Anastasi, the court's concern was that the insurer could delay a title resolution in an attempt to recoup money from third parties, even though it knew it could not establish title. Finally, with regard to litigation, insurers must be careful in their correspondence with retained counsel so as not to give the impression that the insurer is controlling the litigation.

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Do Title Companies Owe Duty of Care to Third Parties in Recording of Legal Instruments?

Citation: *Centurion Properties III, LLC v. Chicago Title Ins. Co., 375 P.3d 651* (Wash. 2016)

Facts: Chicago Title handled a transaction in which the borrower gave a deed of trust to General Electric (GE). Chicago Title also was the trustee under this deed of trust. The deed of trust prohibited the borrower from creating any further liens or encumbrances on the property without permission from GE. Later, Chicago Title recorded four liens on behalf of other lenders. These liens were not authorized by GE, and constituted an event of default under the GE deed of trust. The resulting foreclosure by GE resulted in the borrower filing bankruptcy. The borrower and its principals then sued Chicago Title, alleging that Chicago Title knew the GE deed of trust prohibited subsequent liens and was

therefore negligent in recording the liens.

Holding: Although the litigation was in federal court, the Ninth Circuit certified a question to the Supreme Court of Washington, asking if a title company owed a duty of care to third parties in the recording of instruments. The court answered no, noting that title companies search the public records for their own benefit, not for the benefit of their insured or any other party. A title company has no duty to disclose title defects even to their insured (in this case, the subsequent lenders), let alone a third party like the borrower. The court rejected the argument that title companies owe a general duty of care based on their role as a professional institution fulfilling a public trust, and further rejected the argument that the borrower was a third-party beneficiary to the transactions for the recording and title insurance for the subsequent lenders.

Importance to the Title Industry: This ruling is an important victory for the title industry. It affirms the general rule that any searching or examination of documents performed by a title insurer is done solely for its own benefit in issuing a title insurance policy, and that an insurer's liability is established by the terms of such policy. A contrary ruling could have made title companies responsible for interpreting, and even enforcing, contractual provisions and other documents, greatly expanding both a company's role in the transaction as well as exposure to unintended liability.

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California Supreme Court Lets Borrowers Challenge Wrongful Foreclosures

Citation: *Yvanova v. New Century Mortg. Corp.,* 62 Cal.4th 919 (2016)

Facts: In a potentially far-reaching decision, the California Supreme Court held that a borrower has standing to sue for wrongful foreclosure based on allegations that the assignment of the mortgage was void.

In *Yvanova* (and several companion cases), the mortgage loan had been assigned to a securitized trust (consisting of a pool of mortgage loans) through a pooling and servicing agreement. In each case, the borrower challenged the assignments to the investor trust and argued that the foreclosing entity lacked standing to pursue the foreclosure.

The facts in *Yvanova* were fairly typical. The plaintiff obtained a residential mortgage loan from New Century Mortgage Corp. in 2006. In 2007, the deed of trust was assigned by means of a Pooling and Servicing Agreement to a securitized trust. In 2008, the borrower was served with an initial notice of default. In 2012, the borrower was served with second notice of default; the trustee conducted a non-judicial trustee's sale and the property was sold. The plaintiff continued to live in the property through the appeal.

Holding: Prior to *Yvanova,* the California courts mostly held that the borrower lacked standing to challenge the validity of the assignment into a securitized trust. In granting review, the California Supreme Court framed the issue as follows: "In an action for wrongful foreclosure on a deed of trust securing a home loan, does the borrower have standing to challenge an assignment of the note and deed of trust on the basis of defects allegedly rendering the assignment void?"

After repeatedly emphasizing the narrowness of its ruling, the California Supreme Court concluded that the borrower had standing, in post-foreclosure litigation, to challenge the assignment as being void (as opposed to merely voidable). The court reasoned that a borrower could assert a claim for wrongful foreclosure if, in fact, the wrong lender/trustee had foreclosed on the borrower's property. "The borrower owes money not to the world at large but to a particular person or institution, and only the person or institution entitled to payment may enforce the debt by foreclosing on the security."

Importance to the title industry: Prior to *Yvanova,* California courts had routinely rejected borrowers' attempts to challenge the lender's assignment of the deed of trust, and those cases created more certainty for the purchasers and the title insurers in subsequent transactions. The *Yvanova* decision creates more uncertainty and the opportunity for borrowers to file post-foreclosure litigation seeking to challenge the validity of the trustee's sale, potentially creating a cloud on title that could remain for several years of litigation. On the other hand, the *Yvanova* court expressly noted the narrowness of its decision (which reversed a demurrer/motion to dismiss and upheld the technical question of standing), and thus the ultimate effect of *Yvanova* on residential lending, foreclosures and subsequently insured transactions may be minimal.

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Florida Appeals Court Addresses Spousal Rights Involving Reverse Mortgage

Citation: *Edwards v. Reverse Mortg. Solutions, Inc., 2016 Fla. App. LEXIS 3064* (Fla. Dist. Ct. App. 3d Dist. 2016).

Facts: A HECM reverse mortgage was placed on a Florida marital residence in 2006. Prior to the husband's application for the reverse mortgage, title to their homestead, which had been vested in both the husband and wife's name, was properly transferred into just the husband's name. The reverse mortgage transaction closed and funded. The husband alone executed the promissory note, while both spouses executed the reverse mortgage. When the husband died in 2008, the lender accelerated the debt based upon the mortgage provision permitting acceleration upon the death of the borrower. When the widow did not pay off the debt, and despite the fact that the widow continued to reside in the home, the lender instituted a judicial foreclosure. The trial judge ruled in favor of the lender and entered a final judgment of foreclosure. The widow appealed. The appellate court reversed the trial court, remanding the case with directions to enter a final judgment in favor of the widow.

Holding: The appellate court held that even though the widow was not a maker of the promissory note, her joinder in the reverse mortgage (which joinder was required under Florida law in order to have validly encumbered the marital homestead property) relegated her to the status of a co-borrower under the reverse mortgage. As a result of that co-borrower status, the condition precedent upon which the lender had relied to accelerate the debt and institute foreclosure proceedings had not occurred. Acceleration and foreclosure were premature.

Importance to the Title Industry: For the reverse mortgage industry, this decision and others like it (*Smith v. Reverse Mortg. Solutions, Inc.*) call into question the financing technique used here. To maximize the reverse mortgage loan amount available to a borrower, a property owner might be advised to transfer title into the name of the borrower most likely to die, based on actuarial data. Beyond obvious implications for the reverse mortgage industry, this decision more broadly illuminates the potential perils and pitfalls of the routine practice of requiring an out-of-title spouse to "join" in the execution of a mortgage in order to validly encumber a marital property even though the only obligor under the promissory note is the in-title spouse. Review of the terms and conditions of the loan documents is needed whenever there is not a complete identity of interests between the makers of the promissory note and the parties to the mortgage it secures.

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First Mortgage Precludes Junior Lender from Incurring Any Actual Loss

Citation: *Twin Cities Metro-Certified Dev. Co. v. Stewart Title Guaranty Co., 2015 WL 4715064* (Minn. App., 2015)

Facts: In 2007, Prime Security Bank loaned Red Wing Lodging $3.8 million to develop a hotel. The loan was a part of a program run by the Small Business Administration and was secured by a mortgage. In 2008, Twin Cities Metro-Certified Development Company (TCM), as loan servicer for the SBA, lent Red Wing $1.5 million.

This loan was also secured by a mortgage and TCM purchased a title insurance policy from Stewart Title Guaranty. In 2009, a construction contractor filed an action to foreclose on its mechanic's lien. Three other contractors joined the action. Prime Security defended against the action but TCM was not a party. The court determined the liens were valid and had priority over both mortgages. The mechanics' liens judgments totaled $252,927.07. In June 2011, Prime Security foreclosed and bought the property for $2,462,048.54. In December 2011, TCM redeemed the property for $2,391,551.51 and immediately sold it for $3,505,175.62. Over $1.4 million was still owed on TCMs loan and it was required to pay the mechanics' lien judgments. TCM claimed it lost a total of $576,510.01.

As a result, in 2012, it filed an indemnification claim with Stewart for reimbursement of the mechanics' lien judgments, plus interest and attorney fees. Stewart denied the claim. In January 2014, TCM sued Stewart claiming it breached its policy by failing to indemnify TCM for the mechanics' liens. The district court granted partial summary judgment in favor of TCM. It concluded TCM had suffered a covered loss under the title insurance policy as a consequence of the liability resulting from the mechanics liens. The district court entered a judgment in the amount of $360,833.22 for the mechanics'

liens plus interest and attorney fees. Stewart appealed.

Holding: The appellate court interprets insurance contracts *de novo*, and addressed the issue as to whether or not the language in the policy was ambiguous. The language is ambiguous when it is "reasonably subject to more than one interpretation" and unambiguous language is interpreted "in accordance with its plain and ordinary meaning." If there are any ambiguities, they are construed in favor of the insured.

The district court determined that, because the mechanics' liens had priority over the insured mortgages, they were a risk covered by the policy. That being said, title insurance "does not guarantee that the covered conditions does not exist" but indemnifies the insured if it suffers damages due to the condition. As a result, to succeed in its claim, TCM must have incurred an actual loss. The policy limits the actual loss to "the least of (1) the amount of insurance, (2) the amount of debt secured by the mortgage, or (3) the difference in value of the Title as insured and the value of the Title subject to the risk insured against by this policy."

TCM's argument was based upon the definition of actual loss in an *owner's* policy, not a loan policy. In an owner's policy, the actual loss of the insured is simply the difference in value of the property as insured and its value without the defect in title. This formula doesn't apply in this situation because TCM is a mortgagee insured under a lender's title insurance policy, not an owner. A mortgagee suffers actual loss only to the extent to which the insured debt is not repaid because the value of the secured property is diminished by outstanding liens or title defects. Therefore, TCM needed to show that the loss of value actually reduced the equity that TCM was able to recover from the property in satisfaction of its mortgage.

TCM was the lender in a second position, and Prime Security's mortgage exhausted all of the equity in the property. Therefore, in order for a junior mortgage to sustain an actual loss under a lender's policy, the junior mortgagee must retain equity in the property notwithstanding any defects in title covered by the policy. If there is no more equity in the property because of a senior mortgagee or senior lienholder, whose interest is excluded on the policy, the junior mortgagee does not suffer an actual loss when a covered title defect further reduces the property's value.

The appellate court ruled as a matter of first impression, the first mortgage precluded the lender from incurring any actual loss due to liens. The appellate court reversed and remanded because the district court misconstrued the definition of actual loss under the policy.

Importance to the Title Industry: The Minnesota Appellate Court provided a skillful analysis of the differences between an owner's policy and a lender's policy and the definition of actual loss. This is a good case for the industry as it clarifies the position held by other courts that if a lender chooses to take a risk and be in a junior position, that is their risk and if there is no equity after payment to the first lender/lienholder, there is not an actual loss under the policy.

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Utah Court Addresses Insurer Liability to Non-insured Third-party Beneficiary

Citation: *Orlando Millenia, LC v. United Title Servs. of Utah, Inc., 355 P. 3d 965* (Utah 2015)

Facts: Orlando Millenia LC financed a $1 million down-payment for property purchased by IDR Investments LLC from Paydirt LP. Paydirt had previously purchased the property at auction from SITLA. United Title Services of Utah Inc. acted as the title and escrow agent for the transaction. United Title issued a Stewart Title Guaranty Company title commitment to IDR, with Stewart's authorization, but also issued an unauthorized First American Title Insurance Company title commitment to IDR.

Orlando drafted escrow instructions which incorporated the terms of the real estate closing contract and conditioned disbursement of the $1 million down payment upon Orlando and IDR's receipt of certain documents. The escrow instructions were signed by IDR and Orlando. Orlando did not attend the closing, but rather gave IDR verbal instructions to protect Orlando's interest at closing. At closing, IDR insisted that it must receive a warranty deed as required by the real estate closing contract. IDR was confused by the length and complexity of the closing documents, but signed upon assurance from United Title that it would receive its warranty deed to the property.

United Title released the $1 million escrowed funds to Paydirt, without permission from Orlando even though IDR had not received its warranty deed. Orlando subsequently learned that Paydirt did not own the property

and would not get a deed until SITLA was paid in full for the property. Demand letters from Orlando to United Title for the return of the $1 million and resolution of the title to the property went unresolved. IDR declared bankruptcy. Orlando filed suit, asserting (1) breach of fiduciary duty against United Title for releasing escrowed funds without fulfilling the terms of the escrow agreement, and (2) vicarious liability against Stewart and First American pursuant to a vaguely worded Utah statute, Utah Code section 31A-23a-407 (2003), which makes a title insurer liable "to others" for escrow funds where a title commitment has been issued. Both title insurers moved for summary judgment arguing that they were not vicariously liable for United Title's actions as an escrow agent under §407. United Title also moved for summary judgment arguing that §407 did, indeed, impute liability to Stewart and First America. The trial court, without a written opinion, found in favor of Stewart and First American and against Orlando. In painstaking detail and with obvious concern for the lack of clarity, uncertainty, and breadth of coverage, it attributed to § 407, the Utah Supreme Court reversed.

Holding: The court held: (1) Orlando asserted a viable claim against United Title arising from its alleged breach of fiduciary duty and genuine issues of material fact precluded entry of summary judgment against it; and (2) Orlando asserted a claim for vicarious liability against Stewart and First American under Utah Code section 31A-23a-407 (2003). In so holding, the court noted that Stewart and First American's statutory liability was fully contingent upon Orlando's success with its fiduciary duty claim. The court also, with great deference to Utah's legislative branch, urged amendment of the statute.

Relevance to the Title Industry: Depending on the facts of each individual case, this action could have impacted and significantly increased a title insurer's liability in Utah to non-insured third-party beneficiaries of an escrow agreement, where the third party uses the escrow services of the insurer's agent and the agent improperly disburses escrow funds. However, as a result of the amendment of §407, liability for insurers in Utah is now more clearly defined. It is unlikely that the broad liability imposed by the earlier version of the statute can be incurred. For instance, under amended §407, First American most likely cannot be found liable under the facts of this case. Furthermore, under the amended statute a title insurer may have contractual recourse in the event the agent breaches escrow arrangements. Lastly, monetary damages are limited under amended §407 to the amount of money disbursed, plus 10 percent, up to the amount of title insurance. Title insurers should be cautioned that they may still be liable to "third parties" under amended $407.

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Tennessee Supreme Court Ruling in MERS Case Muddles Marketable, Insurable Title After Tax Deed Sale

Citation: *Mortgage Electronic Registration Systems, Inc. v. Carlton J. Ditto, Case No. E2012-02292-SC-R11-CV* (Tenn. December 11, 2015).

Facts: Hamilton County conducted a tax sale as to property that was subject to a deed of trust (DOT). The DOT identified the original lender and Mortgage Electronic Registration Systems Inc. (MERS) as nominee for the original lender. Although the county gave notice to the original lender, it did not attempt to give notice to MERS. The property went to tax sale, and Carlton J. Ditto purchased it for $10,000. A year and a half later, MERS filed a petition to set aside the sale as *void ab initio* due to the failure to give MERS notice. MERS claimed, *inter alia*, that it was entitled to notice because it was named in the DOT and had a constitutionally protected right in the property. Ditto argued MERS lacked standing to challenge the sale because the DOT did not grant MERS a legal protected interest in the property and thus MERS was not entitled to notice of the tax sale. The county joined in Ditto's argument. The trial court granted Ditto's motion for judgment on the pleadings. The Tennessee appellate court affirmed, ruling that MERS lacked standing to file an action to set aside a tax sale because it was never granted an independent interest in the property. MERS appealed to the Tennessee Supreme Court.

Holding: The Tennessee Supreme Court affirmed the trial court's grant of judgment on the pleadings to Ditto. In a detailed 35-page opinion, the Tennessee Supreme Court outlined the role of MERS in the mortgage industry and its system of registering and tracking mortgages designed to address the problems arising out of mortgage securitization. It discussed the United State Supreme Court's prior ruling in *Mennonite*

noting that a mortgage lender has a legally protected property interest and is entitled to notice of a tax sale. It also reviewed a number of varying opinions on the meaning of MERS' involvement as a beneficiary "solely as nominee" for the lender.

Turning to the language of the DOT itself, the Tennessee Supreme Court confessed its perplexity at the "mishmash of descriptive terms and qualifiers in the DOT regarding MERS." In the end, the Tennessee Supreme Court concluded that, while it did not question MERS' authority as agent for the lender or its successors, MERS was not a true "beneficiary" of the DOT. Not even the notice provision of the DOT itself, the court observed, called for notice to MERS and the rights and obligations outlined in the DOT belong exclusively to the lender and not to MERS. The Tennessee Supreme Court thus held that, despite the language of the DOT designating MERS as "beneficiary solely as nominee for the lender and its assigns" and stating that MERS had "legal title" to the property, the DOT did not grant MERS any independent, protected property rights. As a result, the court determined the sale of the property without notice to MERS did not violate its due process rights.

Importance to the Title Industry: By ruling that MERS had no constitutionally protected property right and was not due notice of a pending tax sale, the Tennessee Supreme Court's opinion may result in many properties being sold without any effective notice to the current lenders. Given the prevalence of the use of MERS as a lender's nominee, this opinion raises unsettling questions about whether lenders are due any real or effective notice of a tax sale. By raising such questions, the opinion may open the door to other litigants who may seek to effect notice of tax sales and perhaps foreclosures without any notice to MERS and thus without notice to the current owners of the security instruments encumbering real property. This will almost certainly lead to an increase in disputes and litigation as to the marketability and insurability of title in Tennessee.

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Corporate Seal on Title Policy Extends Statute of Limitations

Citation: *Lyons v. Fidelity National Title Insurance Company, Case No. 2013–002137,* (S. C. App., December 2, 2015).

Facts: Security Title issued a fee policy to Lyons in 2005. In 2006, Lyons learned the federal government claimed an easement over their property. The easement was not excepted in policy Schedule B, but Lyons did not submit a claim until 2011. Security Title rejected the claim. In 2012, Lyons filed an action for breach of contract and bad faith failure to pay. Security defended on the merits, as well as pleading South Carolina's three-year statute of limitations for contract actions. The trial court determined the policy was a "sealed instrument" subject to the 20-year statute of limitations applicable to "an action upon a sealed instrument." The basis for this determination was the pro forma Security Title corporate seal on the face of the policy. Security Title appealed.

Holding: The Court of Appeals of South Carolina upheld the trial court's determination. Security Title had cited South Carolina case law explaining that the seal of corporation is not, in itself, conclusive of intent to create a "sealed instrument." The court brushed this aside. Referring to "the unique circumstances of this case," the court observed "there is no statutory requirement that a title insurance company place its corporate seal … on a policy." Due to "the rules of contract construction requiring that insurance policies be construed against the drafter and in favor of coverage … we find the presence of the seal on the face of the policy, next to the president's signature, evidences an intent to create a sealed instrument." Just like that, the court extended sevenfold the statute of limitations on any title insurance policy bearing a corporate seal. The court went on to rationalize this result with the observation that "a twenty-year statute of limitations allows policyholders to carefully monitor situations as they unfold, ultimately preventing the bringing of unnecessary claims or litigation."

Importance to the Title Industry: This decision dramatically increases exposure in South Carolina for title insurers that include their corporate seal on the face of their policies. Most states adhere to the basic rule that the mere affixation of a corporate seal to a contract, by itself, is insufficient to create a "sealed instrument." Unless this holding is overturned by the South Carolina Supreme Court, however, the pro-consumer policy rationale may begin to influence other courts around the country.

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