

Real Estate Title Insurance & Construction Law

Title Insurance: Protection Or Unnecessary Expense

Awaiting a potential change to a title company's duty to defend

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A case first reported in the *Chicago Tribune* in August 2008 may cause you to ask yourself and your title company is it really worth having title insurance if Tigor Title Insurance Company prevails in its case against Countrywide Home Loans, Inc.

On July 18, 2008, Tigor Title Insurance Company filed a complaint for declaratory judgment against Countrywide Home Loans, Inc. in the Circuit Court of Cook County, Illinois (Case No. 08CH25938), seeking a declaration that it owes no defense to Countrywide nor does it have to indemnify Countrywide for any loss or damage with respect to a policy of title insurance issued by Tigor to Countrywide on a property located at 4578 S. Oakenwald Avenue in Chicago, Illinois.

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A title company refusing to defend an insured is not what should give you pause. It's Tigor's reasoning as to why a court should determine it has no duty to defend that is concerning and has real estate attorneys and title companies keeping an eye on the outcome of this litigation.

The facts of this case read like a made-for-television movie. In January 2007, Donald Franklin purchased the property at 4578 S. Oakenwald Avenue from Rhonda Evans. The entire purchase price was financed by Countrywide with two mortgages in the amounts of \$360,000 and \$90,000. Franklin never made one mortgage payment. Countrywide foreclosed and sold the property to Thomas Jacobs for \$93,000. Upon taking possession of the property, Thomas Jacobs discovered the body of Randy Johnson, son of Arellia Johnson (a prior owner of the property), and his deceased dog inside the house. This discovery led the Cook County Public Administrator Michael Bender to investigate the case. The investigation quickly revealed that the deed conveying title to Rhonda Evans

was a forgery since Arellia Johnson, the grantor in that deed, did not sign the deed nor did she authorize anyone to sign on her behalf. Bender moved to intervene in the foreclosure action on behalf of the Estate of Arellia Johnson, seeking to vacate the foreclosure judgment and to revest the property back to the estate.

Countrywide sought coverage from Tigor under the title insurance policy it issued on the property based upon Bender's claim that the true owner of the property is not Donald Franklin but the Estate of Arellia Johnson. Tigor denied coverage, which led to the lawsuit filed by Tigor.

In reviewing the recorded deed, there were many red flags that should have alerted even the greenest of title searchers to raise questions about its validity. The grantor's name was misspelled in the signature on the deed. The deed was notarized by Mae Evans, a relative of the grantee, Rhonda Evans. The deed was dated October 17, 1996, but not recorded until October 23, 2006, 10 years after it was allegedly executed. The deed was printed on the stationery of Eugene "Gene" Moore, the Recorder of Deeds. Eugene Moore did not take office until 1999, three years after the deed was supposed to have been executed. Any one of the above should have been cause for concern. The fact that Tigor issued a title insurance policy to Countrywide despite such issues may be considered

sufficient enough to compel Ticor to defend Countrywide.

Ticor, however, took a different approach and alleged that Countrywide is to blame and not entitled to coverage based upon its business practices and the belief that the loan to Franklin should have never gotten out of underwriting.

The pertinent facts presented by Ticor in the Complaint are that Franklin contracted to purchase the real property located at 4578 S. Oakenwald Avenue from Rhonda Evans for \$450,000.00. Franklin's agreed to pay \$500.00 as the contract deposit and the seller was to pay 5 percent of the closing costs for the transaction. Ticor notes in the complaint that "other than contracts to purchase VA or FHA-insured mortgages, it is unusual in the Chicago area for a seller to pay any part of the buyer's closing costs."

Franklin submitted an application to a mortgage broker at E&I Funding Corporation which indicated he was applying for a \$360,000 mortgage as well as \$90,000.00 subordinate financing to cover the entire contract price. The application stated Franklin was employed as an excavator for Class A Construction with an income of about \$12,000 per month. E&I Funding transferred the application to Countrywide. The complaint alleged that Countrywide's acceptance of the loan was "purportedly subject" to certain conditions. One of those conditions was verbal verification of Franklin's employment. A Countrywide checklist showed they were having difficulty obtaining that verification and it appears they verified Franklin's Social Security number through Rapid Reporting DirectChek instead.

To make matters more interesting, according to newspaper reports, E&I Funding, the mortgage company that originated Franklin's loan application, was owned by Rhonda Evans' brother, Edwin Evans, and his wife, Iva. Edwin Evans also owned Class Act Construction, the employer listed on Donald Franklin's loan application. It appears, and the Cook County Public Administrator alleged in his Motion to Intervene, that "Franklin was a fraudulent 'straw' buyer" who is now no where to be found.

In its complaint, Ticor alleges a pattern of Countrywide's "grossly negligent" and "reckless underwriting practices" and its practice in particular with respect to the Franklin mortgage. Ticor claims that "Countrywide was reckless and grossly negligent in its underwriting of the Franklin mortgage. Countrywide's failure to exercise reasonable care in the underwriting of the Franklin mortgages was the sole proximate cause of any loss suffered by Countrywide with respect to its inability to foreclose on the Subject Property." Ticor lists examples of Countrywide's alleged negligence, including but not limited to (i) its failure to require full documentation for an application for 100 percent financing for a first-time home buyer; (ii) accepting a loan based upon a sale price of \$450,000, where the buyer deposited \$500 in earnest money and where the seller agreed to pay up to 5 percent of the buyer's closing costs; and (iii) failing to obtain verification of Franklin's employment. Ticor further alleges that "Countrywide adopted corporate policies that resulted in the abandonment of proper underwriting standards as part of its effort to increase market share and, in the short term, profits." Ticor claims that because of Countrywide's lack of "any meaningful underwriting standards, fraudulent conduct like the 'straw man' scheme alleged to have occurred in this instance went undetected."

Ticor's claims may not be completely without merit. Exclusion 3(a) of the policy in question expressly excludes "Defects, liens, encumbrances, adverse claims or other matters (a) created, suffered, assumed or agreed to by the insured claimant." Therefore, if Countrywide caused or somehow contributed to the basis for the claim made, Ticor may have a legitimate case. However, in this case, the basis for the claim appears to be the fraudulent deed. If not for the fraudulent deed, Countrywide would have foreclosed on the property, taken the loss and moved on. However, because the Cook County Public Administrator made a motion to intervene in the foreclosure action based upon the discovery of the fraudulent deed, Countrywide has a claim based upon a defect in the chain of title.

The very reason one buys title

insurance is to protect against possible defects in title such as fraud. A buyer or lender want title insurance to make sure the seller actually owns the property it is selling or that the mortgagor is the rightful owner of the property it is mortgaging. If, after the policy of title insurance has been issued, someone else claims to be the owner of that property, it is the title company's obligation to defend such a claim and indemnify the insured against any loss as a result of such claim. If Exclusion 3(a), which is a common exclusion in most, if not all, title policies, is interpreted to cover the due diligence practices of lenders in making their loans, then the number of title coverage denials could increase dramatically. In essence, a title company would be able to tell a lender it's denying coverage because they don't like the way that lender conducts its business.

Countrywide may have been relaxed in its underwriting of the Franklin mortgage; however, many practitioners may believe that does not relieve Ticor of fulfilling its contractual obligations. The title insurance policy it issued was a written contract issued based upon Ticor's underwriting procedures. Ticor was expected to raise any title issues before it issued the policy. The fraudulent deed was a title issue. Ticor did not raise that issue, so anything Countrywide may or may not have done with respect to its underwriting should not be relevant.

Unfortunately for Ticor, they subcontracted the title search to Tri-Star Title which, according to news reports, is now defunct and under investigation for mortgage fraud.

If Ticor does prevail in this case, we will certainly be asking ourselves, why bother getting title insurance? As of the date we submitted this article, Countrywide has not yet filed an answer to Ticor's complaint. That answer will likely include a counterclaim demanding that Ticor be compelled to defend Countrywide and provide coverage pursuant to the terms of the loan policy.

To those lenders whose underwriting practices are impeccable and could never be called into question, this case may not be of interest to you, but for the rest of the lenders who live in the real world and the attorneys who represent them, we eagerly await the outcome. ■