

# **Closing Protection Letters: Knowing What is and is not Covered**

**I**n the current real estate market, there is a lot of discomfort regarding title insurance. Claims on title policies are getting more difficult to move through the companies and even harder to obtain payment on those claims. Even worse, if the national underwriting offices can prove that the local agency made a mistake, they will not pay out on a claim, whether substantiated or not. One way to protect oneself from a situation like this is to obtain a closing protection letter (“CPL”) or “insured closing letter” from the local title agent.

## **BACKGROUND**

Title agents are customarily authorized, through agency agreements, to sell policies for one or more title insurance underwriters. These agency agreements normally provide that the agent is an agent solely for the purpose of issuing title insurance commitments and policies, and state that the agent is not the title company’s agent for the purpose of conducting settlements or performing escrow services. A buyer, seller or lender who also wants the title insurer to be responsible for the agent’s acts in connection with escrow closing activities and services must separately contract with the title insurer for such additional protection by entering into a CPL.

## **WHAT IS COVERED?**

CPLs specifically apply to escrow closing activities and services performed for title underwriters by approved agents or attorneys who are not employees of the title companies. As stated in the standardized CPL, an “Issuing Agent” is defined as an agent authorized to issue title insurance for the title insurance company. Similarly, an “Approved Attorney” is defined as an attorney upon whose certification of title the title insurance company issues title insurance. These letters are standardized indemnity agreements given to individually named lenders and recite the specific conditions under, and the extent to which, title insurers will accept liability for the acts or omissions of such parties.

A CPL generally applies only with respect to the particular transaction for which it is issued, although, title insurers usually issue a general or “blanket” CPL that protects a particular lender in connection with escrow closing activities and services involving a designated agent for a specified period of time. The CPL specifically provides that the title insurance company will reimburse the customer named in the letter, when the customer is purchasing the title company’s policy, for losses incurred under certain conditions and as the result of certain actions or inactions by the approved agent or attorney. The CPL further provides that the customer’s recourse against the title insurer is limited to and defined by the provisions of the letter with respect to such losses.

CPLs are intended to indemnify lenders solely against losses incurred as the result of:

- (1) fraud, dishonesty, or negligence by the Issuing Agent or Approved Attorney in handling the lender's funds or documents in connection with the specific transaction, as it relates to the status of the title to the interest in the land being insured or to the validity, enforceability, and priority of the lien of the mortgage on that interest in land; and
- (2) failure of the Issuing Agent or Approved Attorney to comply with the written closing instructions of the lender to the extent they relate to status of title to the lender's interest in the land or the validity, priority, or enforceability of the mortgage on the land, including the obtaining of documents and disbursement of funds in connection therewith (although not to the extent such instructions require a determination of the validity, enforceability, or effectiveness of any such document). Note: CPLs do not, however, provide coverage for such matters as failure of the documents to comply with applicable laws or regulations (including environmental, land use, lender regulation, and zoning) or facts and circumstances regarding the closing or the parties to the closing.

In October 2007, the American Land Title Association ("ALTA") Forms Committee adopted three new CPL forms ("2008 ALTA CPLs"). The number of ALTA CPL forms available is now limited to these three new forms, and the substantive changes are the same in each of the 2008 ALTA CPLs. Adverse claims experience may have prompted the changes made in the 2008 ALTA CPLs, as ALTA has "tightened up" the former CPL forms with respect to affirmative coverage and has included additional conditions and exclusions.

All three new 2008 ALTA CPLs specify the nature of the relationship between the issuer and the Issuing Agent or Approved Attorney and disclaim liability for the acts or knowledge of other third parties and for the economics of the transaction. Also, all three new forms include an arbitration clause that parallels the arbitration clause in the 2006 ALTA Owner's and Loan Policies. These new forms are available on the ALTA Web site: <http://www.alta.org>.

## **STATUTORY AND REGULATORY RESTRICTIONS**

Although the ALTA forms of CPLs generally are used in most states, some states restrict, limit, or prohibit their use. The rationale for prohibiting or restricting the use of CPLs by title insurance companies has been that their issuance results in the unauthorized writing of fidelity or surety coverage. The issuance of such coverage also may violate the nature and scope of the title insurer's business activities that are authorized by applicable state statutory or regulatory provisions, or the title company's charter.

Most states, however, permit the use of the approved ALTA forms. State regulators in these states generally take the position that the issuance of CPLs, which assure as to certain actions of the title insurer's own policy-issuing agent or approved attorney, do not violate the state's statute so long as a policy is being issued in connection with the subject transaction.

## **CONCLUSION**

The CPL serves to extend the liability of the large and creditworthy title insurance company, which would otherwise be limited to the title insurance policy, to cover certain “bad acts” of the company’s Issuing Agent or Approved Attorney. But this additional protection must be separately and specifically requested from the title insurer, and the scope of the coverage is defined solely by the terms and provisions of the CPL. Coverage under the CPL is also strictly limited to the parties designated therein, and generally applies only with respect to the particular transaction for which the letter is furnished. It is important for both the insured and the insurer to understand the legal and regulatory restrictions and limitations on the use of CPLs in certain jurisdictions, and the nature and scope of the agency relationships that exist between title insurance companies and their Issuing Agents and Approved Attorneys.