

# Market Conduct of Title Insurance

## Part Two of a Two-Part Report on Title Insurance

by Joe Bieniek, CPCU, AIE, CCP, CIC, ARC, MCM, AIS, AU, AINS

In the first article, *Demystifying Title Insurance* (*The Regulator*, Summer 2011), similarities and differences between title insurance and property and casualty (“P&C”) insurance were presented. The same will be done here as we explore market conduct examinations of title companies and agencies.

Some state laws will apply to both title and P&C, such as those dealing with producer licensing and unfair trade practices (rebating and illegal inducements); there are others that will only apply to title, such as those related to escrow accounts, mono-line requirements, closing protections letters (CPL), and releasing reserves, to name just a few. In addition to differences between title and P&C lines, there are also many differences in state laws, which can result in multi-state companies and agencies struggling to maintain compliance in foreign jurisdictions.

### Market analysis

Regulators typically will begin the examination process by conducting market analysis to determine what is occurring in the marketplace, which company or agency they should examine, and what the scope of an examination should be. An examination may include applying a continuum action, conducting a risk assessment, or performing either a narrowly focused or “comprehensive” examination of the targeted company or agency. Examinations can be done on-site or remotely by an outside vendor, a state’s market conduct section, or by several states working together (known as a multi-state examination). Market analysis, along with other elements, will help regulators to determine the best approach for the examination.

Unfortunately, the basic tools for conducting market analysis (which are available for other insurance lines, including the collection of certain data) have not been available in a useful form for title insurance. The United States Government Accountability Office’s (GAO) 2007

*Report on Title Insurance: Actions Needed to Improve Oversight of the Title Industry and Better Protect Consumers* (GAO-07-401) also pointed out the need for regulators to learn more about the marketplace.

State regulators and the NAIC have recently taken several steps together to provide regulators with additional information to help with market analysis of title insurance. Beginning in 2011, companies’ annual statement filings will now include a “state page” for title insurance, which helps regulators look at annual statement elements that pertain specifically to title insurance. The last article mentioned that a “Title Agent Statistical Data Plan Implementation Guideline” was in the process of being approved by the NAIC’s Title Insurance Task Force. This guideline was approved during the 2011 Summer National Meeting; hopefully, most (if not all) states will adopt the guideline and its statistical plan. The statistical plan will give information that is more useful to state regulators about the business of title insurance in the marketplace and at the agency level.

The previous article (*Demystifying Title Insurance; The Regulator*, Summer 2011) mentioned five benefits to consumers when purchasing title insurance and obtaining a CPL. These included:

1. Providing peace of mind knowing there is clear title and, if the title is not clear, there is insurance to protect the owner against losses incurred;
2. Ensuring all payments were made to prior lienholders (CPL);
3. Providing coverage to the owners for an unlimited amount of time;
4. Paying a premium for title insurance only once (single premium); and
5. Knowing that escrow funds were set up and held in a fiduciary capacity.

Using these five elements as an example, regulators will be able to verify that a company or agency is managed and performs in a manner that ensures that



it is safe, sound, and entitled to the trust of the public. Some of these elements are reviewed by market conduct examiners and others by both market conduct and financial examiners, such as in item one listed above.

As stated earlier, conducting a market conduct examination of a title company may include looking at all of the elements (comprehensive) or may only look at one or a few of the business areas (narrowly focused or targeted examination). Regardless of the scope of the examination, the process will likely follow the suggested examination procedures as outlined by the Market Regulation Handbook.

### The Market Regulation Handbook

The NAIC Market Regulation Handbook (MRH) is the primary guide for market conduct regulators doing market conduct examinations. I learned the value of the MRH when I was still at Allstate. The MRH should be used by insurance companies to develop their own compliance self-audit programs. The MRH guides the regulator in performing market analysis and in conducting a market conduct examination. I encourage all regulators and industry compliance professionals to use the MRH.

The main guts of any examination are found in Chapter 16: General Examination Standards. Chapter 16 outlines the standards to be used in conducting an examination of any type of insurance company. The general standards include seven broad business area categories and 57 collective



standards (Business Area/Number of Standards):

1. Operations/Management (18)
2. Complaint Handling (4)
3. Marketing and Sales (3)
4. Producer Licensing (6)
5. Policyholder Service (7)
6. Underwriting and Rating (9)
7. Claims (11)

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Each standard under the seven standard categories follows a similar format and includes the stated standard, who it applies to, what the priority is (recommended or optional), what documents are suggested for review, what NAIC Model (law) the standard emanates from (references), and more detailed review procedures and criteria (how to look at the information and what to look for). Before a state can proceed with an examination, it must first reconcile the standards with its respective laws and regulations (statutes, rules, bulletins, etc.). Because the standards were developed to encompass all states and territories, they were derived primarily from the model laws. Since the model laws have not been adopted by every state and only partially by others, the process of reconciling the standards to state regulations is a very important step in the examination process.

In addition to the seven business area categories and their respective standards, there are an additional six title insurance business area categories with multiple subsequent standards found for each in Chapter 18: Conducting the Title Insurance Company and Title Insurance Agent Examination. Chapter 18, which focuses on conducting title insurance company and agency market conduct examinations, builds on Chapter 16. For instance, regarding the Operations/Management portion of an exam, the MRH in essence

says to use the 17 standards included in Chapter 16 for Operations/Management plus an additional five title insurance related standards. The Marketing and Sales portion says to use the three standards in Chapter 16 plus three additional standards. In the case of Producer Licensing, however, Chapter 18's guidance indicates that the six general standards from Chapter 16 are not applicable to a title insurance examination but provides others that may be more appropriate to the title line.

Two of the additional six business area categories for title insurance in Chapter 18 are Escrow, Settlement, Closing or Security Deposit Funds (which has three standards) and Title Insurance Producer (Agent) Licensing and Relations (which has five standards). The other four business area categories in Chapter 18 do not have specifically identified standards. The categories are Special Considerations for Title Insurance Companies and Title Insurance Agents, Example Title Letter, Example Title Interrogatory, and Sample Checklist. These additional standards are pretty intuitive to the title insurance business but it is important to reiterate that each state's title and insurance laws differ enough that the applicability of any one standard is subject to each state's respective regulations.

In total, there are 50 standards for title insurance.

### A walk-through



Before we look at the general and specific standards categories, I will explain a little more about how a state might use this information.

Essentially, a typical market conduct examination seeks to verify three things regarding the practices and procedures (or conduct) for a given company. First, an examination will verify that a company's conduct complies with state statutes. Second, it will verify that the company's conduct complies with the company's own standards (established procedures and manuals). And third, an examination will verify that the company's conduct is "in the best interest of the consumer." Now let's take a look at the general standards that

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regimes (Basel II and Solvency II). However, it is unclear how supervisory colleges will be implemented in this context.

### Conclusion

Currently, Texas, Rhode Island, and West Virginia have been reported to have enacted in some form the NAIC's amendments to the Model Act and Regulation. Many more states are expected to follow, especially if certain amendments are required for state accreditation by the NAIC. As states adopt and implement the amendments, regulators as well as stakeholders in the industry will be required to implement and address practices to ensure compliance with all applicable standards. ■

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will apply to all types (lines) of insurance companies, including title, as well as the additional standards dedicated to examining a title company or agency.

**Operations and Management:** This general category encompasses verifying how the company implements self-governance for compliance (self-audits and third-party relationships) and looks at the written policies and procedures for management oversight of systems and information. It includes looking at computer systems (access and disaster recovery); transaction and business records retention; the protection, use, and disclosure of consumer non-public information; privacy notices; anti-fraud (detection, prosecution, and prevention); and cooperation during an examination. Standards associated with title insurance include ensuring that the company acts only within the statutorily allowed scope of title insurance laws and is compliant with respect to board member affiliations, errors and omissions, business diversification requirements, and title plan management. Again, it is worth reiterating that all standards are subject to applicability within a specific jurisdiction (state or territory).

**Complaint Handling:** This category includes verifying that the company/agency is logging and maintaining proper complaint registers, maintains and advertises to policyholders about complaint handling procedures, and processes complaints as required by law (e.g., timely, accurate, and complete). There are no additional title standards.

**Marketing and Sales:** In this examination standard, the state seeks to ensure that sales and advertising materials and producer training manuals and procedures are in compliance with applicable laws. It also looks at the communications from the company that is ultimately responsible for sales and advertising material to its producers who will be using the material. The additional title-related standards include looking at Affiliated Business Arrangements (AfBA) and other controlled business and making sure that there are not any illegal inducements associated with the referral of business that is unique to the title insurance industry.

**Producer Licensing:** Because of the unique marketing of title insurance relative to other types of insurance (where it is uncommon for individual producers to act as individual producers outside of the employment of an agency), Chapter 18 has adopted its own producer licensing standards.

**Policyholder Services:** Contrary to producer licensing standards, policyholder services actually involve areas that may not be applicable to title companies. Chapter 18 indicates that the examiner should use the general standards. According to the MRH, the policyholder standards are “designed to test a regulated entity’s compliance with statutes regarding notice/billing, delays/no response, and premium refund and coverage questions.” The regulator may find some guidance from these standards but will likely adopt portions when developing state specific programs for examination.

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**Underwriting and Rating:** Many of the obvious items that you would imagine are involved are, such as ensuring that rates, forms, endorsements, etc. are compliant and filed in accordance with applicable statutes and do not unfairly discriminate, and that both the company and its appointed producers use only the approved versions. The additional title standards add elements related to simultaneous rates, re-issue and refinance credits, and collusion in setting rates. The standards also contemplate “other” charges and fees (when regulated), CPL and other indemnity practices, document recordation procedures and experience, and the coding of policies.

**Claims Handling:** The Claims Handling standard is the last examination standard, but it is by far the least. As in all examinations that include claim handling, the emphasis is on ensuring that the company

handles claims timely, accurately, and completely and without violating unfair trade practices such as forcing an insured to sue the company before they will settle a claim. The title standards for claims also includes indemnification of a proposed insured solely against the loss of settlement funds and ensuring that loss statistical coding is complete and accurate.

## Follow the money

Does the state require title agents to have a separate fiduciary trust account to hold escrow or closing monies?

Depending on the state, title agents will perform other duties, including the collection or disbursement of premiums, escrow or security deposits or other funds, and the handling of escrows, settlements, or closings. This could be sizeable! It also leads to temptation. There is not a week that goes by that I do not see some sort of impropriety whereby a title agent has misguided funds from his fiduciary responsibility into his own hands. Regulators need to follow the dollar transactions.

As mentioned in the earlier article, the HUD-1 Settlement Statement is a standard form that clearly shows all charges imposed on borrowers and sellers in connection with a settlement. Commitment letters and disbursements instructions need to be reviewed. Regulators need to verify what transactions the agent is performing and then verify that all amounts received at a closing are disbursed as they were intended.

All of this gets to the three standards mentioned earlier that are specific to title insurance in the business category standard of Escrow, Settlement, Closing or Security Deposit Funds. This also meets the second and fifth benefit mentioned above to a consumer: ensuring all payments were made to prior lienholders and knowing that escrow funds were set up and held in a fiduciary capacity. It could be the regulated entity the regulator is reviewing that is responsible for receiving and distributing those payments to lienholders and it is therefore the regulator’s responsibility to follow up in this regard. The market conduct examiner



also needs to make sure the premium was distributed and received by the title company.

### Kickbacks and rebates

The downturn in the economy beginning in the fall of 2008 has affected title insurance immensely. There are fewer agents, fewer title companies, and fewer home sales, but there is an increase in competition in the marketplace. Regulators have tried—and were successful, in many cases—to curtail any kickbacks and rebates in procuring title insurance business to the title company. Many regulators have said that the margins are so reduced that there are not as many kickbacks and rebates at this time. That does not mean to say the problem is past us. Regulators need to be vigilant.

### Advertising and referrals

Many states have very unique laws or regulations related to advertising and referrals. In some states, no amount of money or item of value is allowed; in others, the amount may be limited to \$50. Regulators

could also determine inappropriate actions by reviewing closing and escrow documents revealing any agreements between the lender and the title agent guaranteeing any prices other than the title agent's filed fees or charges were made. Regulators should also obtain a list of all disbursements pertaining to advertising, sales and marketing, and promotional activities to be certain the state laws are being met.

### At the end of the day...

A market conduct review of a title insurance company or title agent cannot be performed by a novice. An experienced person who knows what title insurance is and what the differences and similarities with P&C business are is of utmost importance in conducting an examination of a title company or title agent. If you are a company or an agency and you are looking to establish a compliance program, you are encouraged to work with your state regulators. Some states are moving towards the implementation of risk assessments that test a company's "self governance" before they conduct a market conduct examination. Part of the theory behind the

use of risk assessments is to eliminate an unnecessary use of an examination if the regulator can determine that a company is actively self-governing and can demonstrate through the assessment that there is no need to look further (transparency recommended). By working with your state regulators to set up your system, you are essentially inviting the regulator to see what you are doing even before they might initiate the assessment. That may go a long way towards giving your regulator a sense of confidence that you are successfully self governing your company for continuous compliance. ■

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## Regulatory Roundups

### *The Experiment Continues...*

#### Florida

by Travis Miller

#### **G**overnor seeks to reduce size of residual market

Florida's residual property insurance market, Citizens Property Insurance Corporation, continues to grow and poses a threat of potential deficit assessments from future hurricanes. Governor Rick Scott is seeking recommendations from Citizens and others for privatizing the residual market or significantly reducing its size. The governor has asked Citizens to present its recommendations in December.

#### **Catastrophe fund capacity under review**

The Florida Hurricane Catastrophe Fund (FHCF), which sells a low-cost form of

reinsurance to residential property insurers, says that global financial conditions create a narrow margin by which it expects to meet its obligations. The FHCF proposes to address this by gradually reducing the capacity it offers and increasing its price. However, some observers are concerned that the FHCF's proposals will increase insurance rates and be detrimental to efforts to reduce the size of Florida's residual property market. This issue will be debated in Florida's 2012 legislative session, which begins in January.

#### **New deputy commissioner named for life & health insurance**

Michelle Robleto has joined the Office of Insurance Regulation as its deputy commissioner for life and health. In this

capacity, she will oversee the life and health product review section and the life and health financial oversight section. Ms. Robleto most recently served as the director of the Division of State Group Insurance within Florida's Department of Management Services. ■

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