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BANK CONTROL OF TITLE INSURANCE COMPANIES: PERILS TO THE PUBLIC THAT BANK REGULATORS HAVE IGNORED*

by
Joyce D. Palomar**

I. INTRODUCTION

OVER the past several decades, banks and bank holding companies have sought to expand their profit-making bases by moving increasingly into non-traditional activities. Recently, some of these entities have focused on the acquisition of title insurance companies, foreseeing an opportunity to capture in title insurance subsidiaries the millions of dollars of business banks currently refer to independent title insurance underwriters and agencies.

In 1987 Citibank, a national bank, applied to the Office of the Comptroller of the Currency ("OCC") for permission to form a subsidiary which would engage in title insurance underwriting.¹ Citibank intended for this subsidiary to issue title policies insuring Citibank's mortgage customers, Citibank's own mortgage liens, and the mortgage liens of its bank subsidiaries and sister companies.² Because of related litigation against the OCC,³ Citibank's application was still pending as 1990 dawned. On January 23, 1990, Citibank withdrew its 1987 application; however, Citibank advised the OCC that it contemplates re-submitting a similar application in the future.⁴

In 1988 First Wisconsin Corporation,⁵ a bank holding company, sought authorization from the Board of Governors of the Federal Reserve System ("Board") to acquire an existing title insurance agency, Milwaukee Title Insurance Services, Incorporated.⁶ The Board granted approval in the same

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1. Letter from Louise Firestone, manager of Citibank, N.A. to Emory W. Rushton, Deputy Comptroller of the Office of the Comptroller of the Currency (Oct. 19, 1987) [hereinafter *Firestone Letter*].

2. *Id.*

3. See *infra* notes 17-19 and accompanying text.

4. *Firestone Letter, supra*, note 1.

5. Effective January 1, 1989, First Wisconsin Corporation changed its name to Firststar Corporation.

6. 53 FED. REG. 21,525 (1988).

year.⁷

In 1989 The Chase Manhattan Bank, N.A. applied to the OCC for permission to establish two new subsidiaries to engage in the title insurance agency business. Chase Manhattan proposed that one subsidiary would act as title insurance agent in connection with residential mortgage loans originated by itself and its affiliates. The second subsidiary would act as agent in connection with commercial mortgage loans originated by Chase Manhattan's Real Estate Finance Sector.⁸ The OCC approved Chase Manhattan's application in the same year.⁹

Most recently, in May, 1990, the Association of Bank Holding Companies ("ABHC")¹⁰ petitioned the Board to add title insurance underwriting and sales to the list of permissible activities for bank holding companies in Regulation Y¹¹ of the Bank Holding Company Act.¹² ABHC requested that the Board commence a rulemaking pursuant to the Administrative Procedures Act to act on the petition as soon as possible.¹³ The Board has taken no public action at the time of this writing.

A vigorous, but largely ignored, challenge to these banking entities' entry into the title insurance business has come from the American Land Title Association ("ALTA"),¹⁴ the national trade association for title insurers¹⁵ and abstractors.¹⁶ In 1987 ALTA and the Texas Land Title Association

7. *First Wisconsin Corporation*, 75 FED. RES. BULL. 31 (1989) (Order Approving Acquisition of a Company Engaged in Title Insurance Agency Activities by William W. Wiles, Secretary of the Board of Governors of the Federal Reserve System (Nov. 17, 1988)) [hereinafter *First Wisconsin*].

8. Letter to Richard T. Erb, Domestic Licensing Manager, OCC from Thomas C. Lynch, Exec. Vice President, The Chase Manhattan Bank, N.A. (March 3, 1989) (copy attached to Plaintiff's Complaint for Declaratory and Injunctive Relief, *American Land Title Ass'n & NYSLTA v. Clarke*, 89 CIV 6939 (MJL) (S.D.N.Y. filed Oct. 18, 1989)).

9. Letter to Thomas C. Lynch, Exec. Vice Pres., Chase Manhattan Bank, N.A., from J. Michael Shepherd, Sr. Deputy Comptroller for Corporate and Economic Programs, OCC (dated June 20, 1989) (copy attached as Exhibit A to Memorandum in Support of Plaintiff's Motion for Summary Judgment and in Opposition to Defendant's Motion to Dismiss, in *American Land Title Ass'n & NYSLTA v. Clarke*, 89 Civ. 6939 (MJL) (S.D.N.Y. filed Mar. 12, 1990)).

10. ABHC represents over one hundred bank holding company members.

11. 12 C.F.R. § 225.25 (1989).

12. Petition for Rulemaking, to Board of Governors of the Federal Reserve System from Association of Bank Holding Companies, at 10 (May 9, 1990) (copy available from Board; cleared for public inspection and copying May 11, 1990).

ABHC does not seem to be seeking permission for bank holding companies to underwrite title insurance; however, the petition is unclear in this respect. ABHC's recommendation is for the Board to expand Regulation Y's list of permissible "activities" to include "title insurance;" ABHC's discussion then notes that a former Senate Banking Committee Chair recommended title insurance underwriting as an appropriate activity for bank holding companies. *Id.*

13. *Id.* at 4, 12.

14. ALTA has approximately 2,300 members, including title insurance underwriters, local title insurance agencies, abstractors and associate members.

15. The phrase "title insurers" used in this article refers collectively to title insurance underwriters and the local title insurance companies that act as their agents. When the law affects title insurance underwriters and local title insurance agencies differently, they will be referred to individually.

16. Four types of entities may be involved in the sale of title insurance: (1) national title insurance corporations which underwrite title insurance policies for local subsidiaries, for bar-related title assuring organizations, and for independent local title companies and abstractor

sued for a declaratory judgment that two Interpretive Letters issued by the OCC were not in accordance with the law.¹⁷ The Comptroller's Interpretive Letters No. 368 and 377, issued in 1986 and 1987 respectively, purportedly authorized national banks and their nonbank subsidiaries to act as title insurance underwriters or agents. The plaintiffs also sought a permanent injunction against future OCC authorization of title insurance activities for national banks or their nonbank subsidiaries.¹⁸ However, in late 1989, the United States District Court for the Western District of Texas dismissed ALTA's suit, finding that the Interpretive Letters constituted advisory opinions only and thus did not represent final agency action ripe for adjudication.¹⁹

In 1988 ALTA contested the Board's authorization of First Wisconsin Corporation's²⁰ purchase of Milwaukee Title Insurance Services by filing suit in the United States Court of Appeals for the District of Columbia Circuit.²¹ ALTA asserted, first, that the Board had incorrectly interpreted Exemption (G) of the Bank Holding Company Act to permit bank holding company acquisition of a title insurance agency. Second, ALTA complained that the Board had erroneously determined that the benefits to the public would outweigh the adverse effects from First Wisconsin's acquisition of a title insurance agency.²² On December 19, 1989, the court ruled that the Board's interpretation of the Bank Holding Company Act was not unreasonable, and that the Board's public benefit analysis, although "terse," was adequate considering the deference due the Board as administrator of the Bank Holding Company Act.²³

In 1989, ALTA joined with the New York State Land Title Association to sue for a declaratory judgment that the OCC's approval of Chase Manhattan's new title insurance agency subsidiaries was in excess of the OCC's authority and void. The plaintiffs also sought a permanent injunction requiring the OCC to (1) withdraw the ruling in Interpretive Letter No. 368 which serves as the basis for the OCC's approval of Chase Manhattan's application, and (2) refrain from facilitating further the entry of national banks and their

and attorney agents, referred to herein as "title insurance underwriters;" (2) local title insurance companies which own title plants and perform the title search and examination as agents for the underwriter, referred to in the industry as "local title companies;" but in most of the federal and state law relevant to this article as "title insurance agencies;" (3) approved attorneys and abstractors who work as agents for national title insurance underwriters and local title companies in areas where no company has established an office; and (4) bar-related title assuring organizations which most often underwrite their own policies, relying on the searches and examinations of their attorney members.

17. American Land Title Ass'n & Texas Land Title Ass'n v. Clarke, No. A-87-CA-408 (W.D. Tex. July 2, 1987) (challenging Office of the Comptroller of the Currency, Interpretive Letters No. 368 (July 11, 1986) and No. 377 (Feb. 6, 1987)).

18. *Id.*

19. The court's decision was not published. However, a copy may be found attached to defendant, OCC's, Memorandum of Law in Support of Motion to Dismiss, in ALTA & NYSLTA v. Clarke, 89 Civ. 6939 (MJL) (S.D.N.Y. Jan. 2, 1990).

20. Currently known as Firststar.

21. ALTA v. Federal Reserve Sys., 892 F.2d 1059 (D.C. Cir. 1989).

22. *Id.*

23. ALTA v. Federal Reserve Sys., 892 F.2d at 1065.

subsidiaries into the title insurance business. The suit is currently pending in the United States District Court for the Southern District of New York.²⁴

It is, of course, the economic well-being of its own members that has motivated ALTA to challenge whether banks and bank holding companies should be permitted to acquire majority shares in title insurance companies or sell title insurance themselves. Perhaps it is for this reason that bank regulators have so summarily dismissed ALTA's complaints — seeing them as mere whinings from disgruntled competitors. Clearly, this is how bank regulators have responded to complaints made by members of the general insurance industry since banks and bank holding companies began to move into the general insurance business three decades ago.²⁵

In dealing with title insurance, however, bank regulators have disserved the public interest. They have failed to make any distinction between the appropriateness of lenders controlling general insurers and title insurers. Bank regulators have failed to recognize that lender control of title insurers may create conflicts of interest which also negatively impact upon purchasers of real property, including homebuyers, and upon investors in our nation's secondary mortgage market. Bank regulators have further failed to consider the threat which lender control of title insurers poses to the quality of title insurance underwriting in the United States, the security of our nation's real property records, and the overall availability of money for real property investment and development.

This article will briefly examine the laws and regulations which apply to various banking entities' ability to acquire or become title insurers. It will then discuss the more compelling public policy considerations which bank regulators have overlooked. Finally, this article proposes that, since bank regulators have ignored the public interest when applying existing laws, lawmakers should amend the National Bank Act, the Bank Holding Com-

24. American Land Title Ass'n & New York State Land Title Ass'n v. Clarke, 89 Civ. 6939 (MJL) (S.D.N.Y. filed Oct. 18, 1989).

25. See Independent Ins. Agents of America v. Board of Governors, American Ins. Ass'n v. Clarke, 865 F.2d 278 (D.C. Cir. 1989); Saxon v. Georgia Ass'n of Independent Ins. Agents, 399 F.2d 1010 (5th Cir. 1968); see also Abbot, Scott & Barrett, *Banks and Insurance: An Update*, 43 BUS. LAW. 1005 (May 1988); Fogelson, *The Changing Environment for Financial Services and Products*, 38 BUS. LAW. 667 (Feb. 1983); Hemmer, *Insurance Underwriting Activities of Bank Holding Companies*, 100 BANKING L.J. 700 (Oct. 1983); Hinkle, *Insurance Activities of National Banks and Bank Holding Companies*, 105 BANKING L. J. 137 (Mar.-Apr. 1988); Huber, *Insurance Powers of Banking Organizations*, 8 ANN. REV. BANKING L. 147 (1989); Lange, *The Merger of Banking and Insurance: Will Congress Close The South Dakota Loophole?* 60 NOTRE DAME L. REV. 762 (1985); Ohrenstein, *Should Banks and Insurance Companies Be Allowed to Diversify Into Each Other's Activities?* 56 N.Y. ST. B.J. 7 (Dec. 1984); Saulsbury, *State Banking Powers: Where Are We Now?* FDIC REG. REV. (Mar.-Apr. 1987); Schweiker, *Bank Entry Into Life Insurance: The Insurance Industry Viewpoint*, 58 N.Y. ST. B.J. 8 (Nov. 1986); Wilson, *Separation Between Banking and Commerce Under The Bank Holding Company Act*, 33 CATH. U.L. REV. 163 (1983); Comment, *Operating Subsidiaries Under the Bank Holding Company Act: The Decision In American Insurance Association v. Clarke (AMBAC)*, 11 GEO. MASON U.L. REV. 189 (1989); Comment, *Permitting Sale of Insurance by Bank Holding Company Subsidiaries: A Revised Analytical Framework*, 32 U. MIAMI L. REV. 552 (1978).

pany Act, and state statutes to specifically curtail mortgage lenders' ability to own, control, or act as title insurance underwriters and agents.

II. LAWS APPLICABLE TO NATIONAL AND STATE BANKING INSTITUTIONS' SALE OF TITLE INSURANCE

A. *The National Bank Act*

National banks are chartered and governed by the OCC, an agency of the Department of the Treasury.²⁶ The National Bank Act ("NBA") defines the powers of national banks.²⁷ National banks may own nonbank subsidiaries, referred to in some banking regulations as operating subsidiaries²⁸. Nonbank subsidiaries of national banks may engage only in activities which the NBA permits for the national banks themselves.²⁹

The NBA does not expressly authorize national banks or their subsidiaries to sell or underwrite title insurance.³⁰ Yet, in three Interpretive Letters³¹ the OCC has announced that national banks have the power to underwrite or sell title insurance, directly or through their nonbank subsidiaries, pursuant to the incidental powers clause of the NBA.³² The incidental powers clause permits national banks to exercise, in addition to powers expressly granted by the NBA, "all such incidental powers as shall be necessary to carry on the business of banking."³³

26. 12 U.S.C. §§ 1, 21 (1988).

27. 12 U.S.C. § 24 (Supp. 1989).

28. 12 C.F.R. § 5.34(c).

29. *Id.*

30. *See* 12 U.S.C. § 24 et seq. (Supp. 1989).

31. *See infra* note 32 and accompanying text.

32. Responding to a national bank's inquiry whether the bank or its nonbank subsidiary could act as "agent in the sale of title insurance," William B. Glidden, Assistant Director of the Legal Advisory Services Division of the OCC, wrote Interpretive Letter No. 368 (July 11, 1986). Glidden stated that the OCC had determined that a national bank or its operating subsidiary "may act as agent in the sale of title insurance incidental to its express authority to make loans secured by real property." [1985-1987 Transfer Binder] FED. BANKING L. REP. (CCH) 85,538 (July 11, 1986).

On February 6, 1987, Richard V. Fitzgerald, Chief Counsel for the OCC, wrote Interpretive Letter No. 377 in response to a letter and memorandum from counsel for a nonbank subsidiary of a national bank. The memorandum proposed that the nonbank subsidiary act as an agent of a national title insurance underwriter and/or form its own title insurance underwriter. Interpretive Letter No. 377 concluded (1) that the national bank's nonbank subsidiary could operate as a title insurance agent and sell title insurance policies to the national bank's borrowers, and (2) that the nonbank subsidiary could form a title insurance underwriter to issue policies to borrowers of the national bank. [Current Binder] FED. BANKING L. REP. (CCH) 85,601 (Feb. 6, 1987). *See* Plaintiff's Complaint for Declaratory and Injunctive Relief at 8-9, *American Land Title Ass'n v. Clarke*, No. A-87-CA-408 (W.D. Tex. filed July 2, 1987).

In OCC Interpretive Letter No. 450 (October 1988), the OCC discussed whether a national bank could act as agent in the sale of title insurance, perform title searches, arrive at legal title opinions, and perform surveying work in conjunction with real estate loans. William Glidden again opined that the proposed activities were permissible for national banks as being incidental to their express authority to "make, arrange, purchase or sell loans or extensions of credit secured by liens or interests in real estate."

33. *See* 12 U.S.C. § 24(7). For a discussion of various insurance activities for which national banks have been approved see Huber, *supra* note 25, at 147; Hinkle, *supra* note 25, at 137.

The OCC's Interpretive Letters 368, 377 and 450 provided the following reasons for the OCC's determination that the issuance of title insurance is incidental to banking: (1) banks must buy title insurance to ensure the validity of their mortgage liens and may do so more easily if they own title insurers; (2) banks must insure their mortgage liens to compete in the secondary mortgage market and could do so more easily with their own title insurers; (3) borrowers could purchase owners' title insurance concurrently with negotiating their mortgage loans; (4) banks would benefit financially from collecting commissions for title insurance; (5) savings and loan institutions have been authorized to act as title insurance agencies;³⁴ and (6) title insurance companies were divisions of banks from the 1870s until the Depression of the 1930s.³⁵

Certainly, room exists to dispute the OCC's expansive interpretation of the incidental powers clause of the NBA as authorizing national banks to own or act as title insurers. First, the OCC apparently has not considered the purpose of section 92 of the NBA. Section 92 authorizes a national bank located in a town with a population of five thousand or less to engage in insurance agency activities.³⁶ The Fifth Circuit has held that since Congress found it necessary to expressly authorize insurance agency activities in small towns, Congress must believe that neither the incidental powers clause nor any other clause of the NBA permits insurance activities by national banks.³⁷ Thus, according to the Fifth Circuit, the OCC lacks the power to authorize national banks to engage in title insurance activities under the "incidental to banking" clause.³⁸

Second, in authorizing national banks to sell title insurance services and own title insurers, the OCC has looked only at financial benefits and convenience to the applicant banks. The OCC has not considered potential negative effects upon banks which do not control title insurers, upon the land title industry, upon members of the homebuying public, or upon investors in real property and in the secondary mortgage market.³⁹

B. State Banking and Title Insurance Codes

State law determines the substantive powers of state-banks. State banks are chartered and regulated by the several state banking departments.⁴⁰

34. See 12 C.F.R. § 545.74(c)(5)(ii) (1989).

35. See *supra* note 32. See also *infra* notes 251-52 and accompanying text (discussing the fallaciousness of sixth point of OCC's rationale).

36. 12 U.S.C. § 92 (1989). A federal judge on May 8 1990 upheld a 1986 ruling by the OCC that allowed banks selling insurance in small towns pursuant to section 92 to also sell insurance anywhere in the country. *Independent Ins. Agents of America v. Clarke*, slip op. No. 86-3045 (May 8, 1990); *National Ass'n of Life Underwriters v. Clarke*, slip op. No. 86-3042 (May 8, 1990). The decision confirms the OCC's ruling that there are virtually no geographic limitations on the insurance activities of small-town banks.

37. *Saxon v. Georgia Ass'n of Independent Ins. Agents*, 399 F.2d 1010 (5th Cir. 1968).

38. *Id.*

39. These concerns are discussed *infra* notes 209-52 and accompanying text.

40. Huber, *supra* note 25, at 162.

State law also defines the activities permitted to state bank subsidiaries.⁴¹ Some states restrict nonbank subsidiaries to those activities permitted to the state banks themselves.⁴² Others allow nonbank subsidiaries to engage in activities that are not permitted to their state bank parents.⁴³

Most state's statutes simply do not mention title insurance when identifying the activities permitted to state banks and their subsidiaries.⁴⁴ Presumably, title insurance underwriting or agency activities would be beyond the powers of state banks in those states. Where statutes also restrict state banks' nonbank subsidiaries to the activities permitted to the parent bank, state banks will not be able to own title insurance underwriters or agencies. Where states do not restrict state banks' nonbank subsidiaries to those activities permitted to their parent banks, however, the possibility exists for state banks to own title insurance underwriters or agencies as subsidiaries.

Delaware statutes have expressly prohibited state banks from engaging in title insurance activities for years;⁴⁵ a recent statutory revision reaffirmed that prohibition and deserves mention.⁴⁶ In 1989 and 1990, the Delaware Legislature re-assessed whether state banks should be allowed to conduct any insurance activities.⁴⁷ In a surprising turn-around from its former position, the legislature in 1990 finalized a new statutory scheme which permits

41. See *infra* notes 42-44.

42. E.g., Tex. Rev. Civ. Stat. Ann art. 342-913 (Vernon Supp. 1990).

43. E.g., N.Y. BANKING LAW art. XII (McKinney Supp. 1990)

44. In most states, neither the state banking code nor statutes pertaining to title insurance mention banks or bank holding companies as providers of title insurance. See ALA. CODE § 5-5A-18 and § 27-25-1(1986); ALASKA STAT. § 06.05.005, § 06.10.020, and § 21.66.010 (1984); ARIZ. REV. STAT. ANN. § 6-184 and § 20-1561 (1975); ARK. STAT. ANN. § 23-32-701 and § 23-62-108 (1987); D.C. CODE ANN. §§ 26-401 (1981); FLA. STAT. ANN. tit. 37 § 626.988(2) and 37 § 627.7711 (West 1988). HAW. REV. STAT. §§ 403.47 - 403.47.1 and § 432-1 (1985); IDAHO CODE § 26-102 and § 41-2701. (1977); ILL. REV. STAT. ch. 17, para. 311 and ch. 73, para. 478-612 (1965); KAN. STAT. ANN. § 9-1101 and § 40-1102. (1986); KY. REV. STAT. § 287.190 and § 304.22-030 (1988); ME. REV. STAT. ANN. tit. 9-B, § 241 and tit. 24-A, §§ 406, 3201 (1974); MD. ANN. CODE art. 3, § 206, art. 4, § 206, art. 12, § 410(a), art. 48A, §§ 48, 70-80, 242 (1983); MASS. GEN. LAWS ANN. ch. 167, § D:2, § E:1A and § F:2; and ch. 175, §§ 114-116A & 174 (West 1987); MICH. COMP. LAWS ANN. § 487.311b and § 500.7304 (West 1983); MINN. STAT. § 47-20(1)(2) and § 68A.01 (1986); MO. REV. STAT. §§ 362.105 - 362.106 and § 381.030 (Vernon 1968); MONT. CODE ANN. §§ 32-1-102 - 32-1-108 and §§ 33-15-102 (1978); NEB. REV. STAT. §§ 8-101 to 8-1139 and §§ 44-304, 44-1901 (1988); NEV. REV. STAT. § 683A.110 and § 692A.011 (1987). N.H. REV. STAT. ANN. §§ 383 and 416.A:1 (1983); N.Y. INS. LAW § 2501 (McKinney 1985) (no insurance agent licensed to sell general insurance and owned or controlled, directly or indirectly, by a bank shall sell a policy of insurance covering real property which is the security for a loan made by the bank or by any other bank owned or controlled by such bank; New York law does not prevent banks from owning title insurers but appears only to prevent general insurers owned by banks from also transacting title insurance); N.C. GEN. STAT. §§ 53-43 and 58-132 (1982); N.D. CENT. CODE §§ 6-03-02 and 26-32-01 (1978); OKLA. STAT. tit. 6, § 204(A)(8) and § 402; tit. 36, § 5001 (1976); UTAH CODE ANN. § 7-3-10 and § 31A-23-211 (1986); VT. STAT. ANN. tit. 8, §§ 603 & 605 and 3301(9) (1984); WASH. REV. CODE § 30.08.140 and § 48.29.010 (1984); W. VA. CODE § 31A-3-2, § 31A-4-13 and § 33-1-10 (1988); WIS. STAT. § 221.04 and § 3.32 (1980); WYO. STAT. § 13-2-101 and § 26-23-301 (1977).

45. DEL. CODE ANN. tit. 18, § 767 (1974).

46. DEL. CODE ANN. tit. 5, § 761(a)(14) (1990).

47. See *Id.* See also House Bill No. 193, House of Representatives, 135th General Assembly (1989) and Senate Bill No. 415, Del. State Senate, 135th General Assembly (1990).

Delaware-chartered banks to both underwrite and sell general insurance.⁴⁸ The new Delaware law has been described as the most expansive in the nation as it allows banks to engage in all aspects of the insurance business.⁴⁹ Yet, despite the degree to which the Delaware Legislature was willing to expand state banks' general insurance powers, the legislature continues to believe that title insurance underwriting and sales are inappropriate for banks. The new statute expressly excepts from banks' far-reaching new insurance powers, the power to act as a title insurer or transact title insurance business.⁵⁰

Eleven other states expressly prohibit state banks from either selling title insurance, engaging in title insurance agency activities, or participating in insurance activities generally.⁵¹ In some of these states, however, state banks might still be involved in the sale of title insurance in one of two ways. First, a few of these statutes include clauses grandfathering banks which were engaged in a general insurance or title insurance business prior to the statute's enactment.⁵² Second, while all eleven state's statutes prohibit state banks from directly engaging in insurance sales or activities, only three explicitly prohibit state banks from owning title insurance subsidiaries.⁵³ In the remaining eight states, arguably, state banks are only prevented from direct title insurance sales or agency activities, and not from owning subsidiaries that are title insurance agents or underwriters.⁵⁴

48. See DEL. CODE ANN. tit. 5, § 761(a)(14) (1990).

49. *Wall Street Journal*, June 13, 1990, at A2. See generally, In re Citicorp, Petition for Enforcement of BHCA § 1843(c)(8) to Board of Governors of the Federal Reserve System, from Indep. Ins. Agents of America, Inc., et al, (May 30, 1990).

50. DEL. CODE ANN. tit. 5, § 761(a)(14) (1990).

51. CONN. GEN. STAT. ANN. § 36-60 (West 1987) (no bank or trust company shall engage in the business of title insurance, except for any corporation actually engaged in the business of a title insurance and guarantee company on Jan. 1, 1907); LA. REV. STAT. ANN. § 6:242 (West 1978) (banks may act as credit insurance agents only, except those engaged as general insurance agents on Jan. 1, 1984 may continue to be so engaged); NEV. REV. STAT. § 683A.110 and § 692A.011 (1987) (banks may only sell credit insurance); N.J. REV. STAT. § 17:46B-6 (1984) (no bank shall act as agent for a title insurance company); OHIO REV. CODE ANN. § 3953.21 (Anderson 1971) (no bank shall act as agent for title insurance company); OR. REV. STAT. § 715.075, § 744.114(m), § 744.025 and § 707.310 (1987) (omits title insurance from classes of insurance agents bank holding companies may acquire and for which banks may be licensed); R.I. GEN. LAWS § 27-3-46 and § 19-10-9 (1982) (no financial institution shall act as insurance agent, except for credit life, health and accident insurance); S.C. CODE ANN. §§ 34-3-210, 34-29-160, & 38-75-910 (Law Co-op. 1989) (banks may sell only accident and life insurance); TENN. CODE ANN. § 56-6-201 and § 56-35-101 (1989) (banks may only sell credit, life, accident, and health insurance and insurance against physical damage to vehicles and homes); TEX. INS. CODE ANN. § 21.07-3(h) and § 9.01 (Vernon 1981) (no state bank or bank holding company shall own, directly or indirectly, a licensed insurance agent, except one so owned on June 1, 1981); VA. CODE ANN. § 38.2-205 and § 38.2-4600 (1986) (no lending institution shall directly or indirectly sell insurance if located in locality with population exceeding 5000 persons; no lending institution shall own any insurance agency).

Two states, Missouri and Texas, recently considered approving title insurance activities for state banks. In Missouri, the state legislature rescinded regulations issued by the state banking department which had authorized title insurance agency activities for banks. Hochberg, *Banks, Bank Holding Companies and Title Insurance*, 68 *Title News* 14, 18 (July-Aug. 1989). The Texas banking department withdrew a similar proposal.*Id.*

52. See *supra* note 51.

53. *Id.*

54. *Id.*

Conversely, seven states explicitly empower state banks to act as insurance agents,⁵⁵ though four restrict permission to banks operating in small towns,⁵⁶ and two do not allow an entity transacting any other class of insurance to transact title insurance.⁵⁷ In those states, state banks meeting the criteria can directly sell title insurance or own a subsidiary which sells title insurance. These state banks do not appear to be authorized to underwrite title insurance, yet they might own a title insurance underwriter in those states where state banks' nonbank subsidiaries are not limited to the activities permitted to their parent banks.

Georgia has unique statutory restrictions on the ability of lending institutions to underwrite and sell title insurance.⁵⁸ First, the relevant statute explicitly prohibits bank holding companies and other lending institutions from underwriting any form of insurance other than credit life, accident and sickness insurance.⁵⁹ The statute then lists a few types of insurance which the state will permit officers or employees of lending institutions, bank holding companies and their subsidiaries to be licensed to sell as agents, including "mortgagee title insurance," but not owners title insurance.⁶⁰ Georgia's decision to permit banks and bank holding companies to sell title insurance for mortgagees, but not for purchasers of real property, seems to be one response to the concern that banks could unfairly influence homebuyers to buy title insurance from the lender to whom they have applied for a mortgage loan.⁶¹

55. See CAL. COM. CODE § 1208 (West 1988); COLO. REV. STAT. §§ 10-2-211(2)(b), 11-6-101(2)(1987); IND. CODE ANN. § 28-1-11-2 (Burns 1986); MISS. CODE ANN. § 83-17-229 (1972); N.M. STAT. ANN. § 59A-12-10 (1978); PA. STAT. ANN. tit. 40, §§ 281, 910-24 (Purdon 1971); S.D. CODIFIED LAWS ANN. § 51-18-1.3.

56. See CAL. COM. CODE § 1208 (West 1988) (commercial banks located in places with populations less than 5000 may act as insurance agents if so engaged on October 1, 1949); COLO. REV. STAT. §§ 10-2-221(2)(b), 11-6-101(2) (1987) (bank or bank holding company may not be licensed as insurer or act as agent except in municipality where population does not exceed 5000); MISS. CODE ANN. § 83-17-229 (1972) (lending institution prohibited from selling insurance in a municipality with population over 7000); N.M. STAT. ANN. § 59A-12-10 (1978) (lending institution prohibited from directly or indirectly selling insurance in municipality where population exceeds 5000).

57. See CAL. INS. CODE § 12360 (West 1988) (insurer transacting any other class of insurance prohibited from transacting title insurance); COLO. REV. STAT. § 10-11-108 (1987) (title insurance company prohibited from underwriting or issuing any other kind of insurance).

New York was included *supra* note 44 among the states which do not mention title insurance when identifying activities permitted to state banks and their subsidiaries. N.Y. Ins. Law § 2501 (McKinney 1985). New York law does, however, bear some similarity to the California and Colorado laws by prohibiting bank-owned general insurers from negotiating insurance policies "covering real property which is the security for a loan made by the bank." *Id.* This statutory language appears to encompass title insurance. See *supra* notes 44, 56. See generally, Lange, *supra* note 25 at 762 (discussing South Dakota law regarding bank participation in insurance industry); Stromman, *Paving the Way in the Financial Services Industry: South Dakota Opens the Insurance Industry to Banks*, 29 S.D.L. REV. 172 (Winter 1983) (discussing South Dakota law regarding banks providing insurance).

58. GA. CODE ANN. § 33-3-23 (Supp. 1983).

59. *Id.*

60. *Id.*

61. See *infra* notes 209-28 and accompanying text for a discussion of the potential negative effects from lenders' implicit tie-ins of mortgage loans with title insurance sales.

C. *The Bank Holding Company Act*

A major dispute between bank regulators and the title insurance industry concerns whether additional restrictions apply to national and state bank control of title insurers when the controlling bank is part of a bank holding company system. Today bank holding companies own almost all national and state banks.⁶² Frequently, bank holding companies own nonbank subsidiaries as well.⁶³

Bank holding companies are supervised by the Board⁶⁴ and regulated by the Bank Holding Company Act ("BHCA").⁶⁵ Congress enacted the BHCA in 1956 in order to limit the activities of bank holding companies and their subsidiaries to those "closely related to banking"⁶⁶ and to prevent their uncontrolled expansion into the realm of commerce.⁶⁷

Specifically, sections 1843(a)(1) and (2) provide that, unless an exception applies, no bank holding company shall:

- (1) . . . acquire *direct or indirect* ownership or control of any voting shares of any company which is not a bank, or
- (2) . . . retain *direct or indirect* ownership or control of any voting shares of any company which is not a bank or bank holding company or engage in any activities other than (A) those of banking or of managing or controlling banks and other subsidiaries authorized under this Act or of furnishing services to or performing services for its subsidiaries, and (B) those permitted under paragraph (8) of subsection (c) of this section . . .⁶⁸

The additional activities permitted to bank holding companies under paragraph (8) of section 1843(c) are those "so closely related to banking or managing or controlling banks as to be a proper incident thereto."⁶⁹ In 1982 Congress amended the BHCA to specifically express that the underwriting and sale of insurance would not be deemed "closely related to banking."⁷⁰ In 1986 the Board concluded that title insurance is included within Congress' 1982 prohibition against insurance activities.⁷¹

Congress did provide for exemptions from the BHCA's insurance prohibi-

62. A bank holding company is a state-chartered corporation organized for the purpose of owning and operating one or more banks as subsidiaries of the company. See P. HELLER, FEDERAL BANK HOLDING COMPANY LAW §§ 4-24, 5.01[8]-[9] (1986).

63. *Id.*

64. 12 U.S.C. § 1844 (Supp. 1986).

65. 12 U.S.C. § 1841 et seq. (Supp. 1986).

66. 12 U.S.C. § 1843(c)(8) (Supp. 1986).

67. See Wilson, *supra* note 58, at 163; Comment, *supra* note 58, at 552.

68. *Id.* (emphasis added).

69. 12 U.S.C. § 1843 (c)(8) (Supp. 1986).

70. Title VI of the Garn-St Germain Depository Institutions Act. See also Regulation Y, 12 C.F.R. § 225.25(b)(8). See generally, Wilson, *Separation Between Banking and Commerce Under the Bank Holding Company Act*, 33 CATH. U.L. REV. 163 (1983) (discussing BHCA); Comment, *Permitting Sale of Insurance by Bank Holding Company Subsidiaries: A Revised Analytical Framework*, 32 U. MIAMI L. REV. 552 (1978) (discussing BHCA subsidiaries and sale of insurance).

71. First Wisconsin Corp., 75 Fed. Res. Bull. 31, 32 n.6 (1989), *aff'd*, ALTA v. Federal Reserve System, 892 F.2d 1059, 1064 (2d Cir. 1989). See also Hinkle, *supra* note 25, at 141-42.

tion in seven situations.⁷² Three of these exemptions arguably permit certain bank holding companies to act as or own title insurance agencies. A bank holding company proposing to sell title insurance or acquire a title insurance agency under one of these exemptions must prove to the Board, first, that an exemption applies, and second, that the public benefits from the particular insurance operation will outweigh any detrimental effects.⁷³

Exemptions (C) and (F), respectively, cover bank holding companies with operations in small towns and small bank holding companies.⁷⁴ Exemption (C) allows bank holding companies or their subsidiaries in towns with populations less than 5000 "or in places that have inadequate insurance agency facilities" to operate insurance agencies.⁷⁵ Exemption (F) allows a bank holding company with total assets of \$50 million or less to engage in insurance agency activities.⁷⁶ These statutory exemptions appear to allow bank holding companies to operate or own local title insurance agencies.

Two exemptions to the BHCA's insurance activity prohibition are grandfather clauses.⁷⁷ Exemption (D) allows bank holding company subsidiaries which operated as insurance agencies as of May 1, 1982, to continue those activities.⁷⁸ A grandfathered subsidiary may sell the type of insurance it sold prior to May 1, 1982, but may not sell new types of insurance unless they first became available after May 1, 1982 and cover "the same types of risks as, or are otherwise functionally equivalent to" the types of insurance the subsidiary sold on May 1, 1982.⁷⁹

There is no record of the Board approving a bank holding company's application to sell title insurance or acquire a title insurance agency prior to 1982.⁸⁰ Additionally, title insurance is not a new form of insurance that became available after May 1, 1982, nor does it insure against the same types of risks as the credit, life, homeowner's or automobile insurance that a few bank holding companies were permitted to sell prior to 1982.⁸¹ Since Exemption (D) strictly prohibits product line expansion, bank holding compa-

72. See 12 U.S.C. § 1843(c)(8)(A)-(G) (Supp. 1986).

73. *Id.* § 1843(c)(8) (Supp. 1986).

74. *Id.* § 1843(c)(8)(C) & (F) (Supp. 1986).

75. *Id.* § 1843(c)(8)(C) (Supp. 1986).

76. *Id.* § 1843(c)(8)(F) (Supp. 1986).

77. *Id.* § 1843(c)(8)(D),(G).

78. 12 U.S.C. § 1843(c)(8)(D) (Supp. 1986) allows the specific subsidiary which was acting as an insurance agency to continue to do so in any state where it was approved to act as an insurance agency on May 1, 1982, prior to the passage of the Garn-St Germain Act amendments to the BHCA.

79. *Id.*

80. See *ALTA v. Federal Reserve Syst.*, 892 F.2d 1059, 1062 (D.C. Cir. 1989).

81. To depict how narrowly Exemption (D) should be construed, both Senate and House Committees gave the example of a bank holding company subsidiary selling homeowner's insurance on May 1, 1982, expanding that coverage to protect homeowners from loss caused by volcanos if such insurance coverage became available after that date. See *Report of the Senate Committee on Banking, Housing & Urban Affairs on the Garn-St Germain Act* (S. Rep. No. 97-536, 97th Cong., 2d Sess. (1982), reprinted in 1982 U.S. Code Cong. & Admin. News 3093-95. See also, FED. REG. 36207-09 (Oct. 9, 1986) for the Board's description of the grandfather rights under Exemption (D) as "limited to the precise activities (or their functional equivalent) engaged in prior to May 1, 1982.)"

nies should not be able to sell title insurance or acquire title insurance agencies under Exemption (D).

Exemption (G), on the other hand, is the exemption under which First Wisconsin (Firststar) Corporation has claimed the right to acquire Milwaukee Title Services, Inc.⁸² Exemption (G) grandfathers bank holding companies that were authorized to engage in insurance agency activities prior to 1971 and permits them to continue to act as or own insurance agencies anywhere in the United States.⁸³ First Wisconsin (Firststar) is one of the approximately sixteen active bank holding companies with grandfather rights under Exemption (G).⁸⁴

In 1989 ALTA appealed to the United States Court of Appeals for the D.C. Circuit the question whether Congress intended Exemption (G) to permit First Wisconsin, which sold credit life insurance prior to 1971, thereafter to acquire a title insurance agency.⁸⁵ First Wisconsin contended that, unlike Exemption (D), Exemption (G) does not limit a grandfathered bank holding company to selling only the specific type of insurance it sold prior to 1971.⁸⁶ ALTA countered that Exemption (G) should be construed to grandfather only the insurance activities that the Board had approved prior to 1971.⁸⁷

ALTA emphasized the concept of grandfathering and pointed to legislative history which states that Exemption (G) was intended to "*grandfather the insurance activities of a bank holding company registered with the Federal Reserve Board which, prior to January 1, 1971, was engaged, directly or indirectly, in insurance agency activities as a consequence of approval by the Board prior to January 1, 1971.*"⁸⁸ ALTA further asserted that even if Congress intended for grandfathered bank holding companies to expand from one type of insurance agency activity into other insurance classes, Congress could only have intended those which had been approved for bank holding companies in 1971 — such as life, auto, and property insurance.⁸⁹ ALTA argued that Congress could not have meant to include title insurance

82. See *ALTA v. Federal Reserve System*, 892 F.2d 1059 (D.C. Cir. 1989).

83. 12 U.S.C. § 1843(c)(8)(G) (Supp. 1986). Exemption (G) provides an exception from Congress' determination that providing insurance as a principal, agent, or broker is not closely related to banking:

(G) where the activity is performed, or shares of the company involved are owned, directly or indirectly, by a bank holding company which is registered with the Board of Governors of the Federal Reserve System and which, prior to January 1, 1971, was engaged in insurance agency activities as a consequence of approval by the Board prior to January 1, 1971.

84. *First Wisconsin Corporation*, 75 FED. RES. BULL. 31 (1989) (Order Approving Acquisition of a Company Engaged in Title Insurance Agency Activities).

85. *ALTA v. Federal Reserve System*, 892 F.2d 1059 (D.C. Cir. 1989).

86. Brief of Respondent, at 14-22; *ALTA v. Federal Reserve Sys.*, 892 F.2d 1059 (D.C. Cir. 1989).

87. Brief of Petitioner, at 10; *ALTA v. Federal Reserve Sys.*, 892 F.2d 1059 (D.C. Cir. 1989).

88. Brief of Petitioner, at 10; *ALTA v. Federal Reserve Sys.*, 892 F.2d 1059 (D.C. Cir. 1989) (citing S. Conf. Rep. No. 97-641, 97th Cong., 2d Sess. 91, (emphasis added by petitioner) reprinted in 1982 U.S. Code Cong. & Admin. News 3128, 3134; H.R. Conf. Rep. No. 97-899, 97th Cong., 2d Sess. 91 (1982)).

89. *Id.* at 11-14.

within the grandfathered insurance agency activities because the Board had not approved title insurance agency activities for any bank holding company in 1971. The Board adopted First Wisconsin's interpretation of Exemption (G).⁹⁰ In approving First Wisconsin's application to acquire Milwaukee Title on November 17, 1988, the Board concluded that Exemption (G) allows grandfathered bank holding companies to conduct any insurance agency activities, including title insurance activities.⁹¹

In *ALTA v. Federal Reserve System*⁹² the D.C. Circuit supported the Board's construction of Exemption (G).⁹³ The court held that, if title insurance activities are deemed to be among those prohibited by section 1843(c)(8), they also must be among those permitted by Exemption (G) to that section.⁹⁴ The court construed the legislative history cited by ALTA as showing Congressional intent to grandfather holding companies engaged in insurance agency activities prior to 1971 and not just the insurance activities in which they engaged.⁹⁵ Additionally, the court found that the Board's ruling met the purpose of Exemption (G) since it permitted a grandfathered holding company to engage in a general insurance agency activity.⁹⁶ The court accepted without discussion the Board's conclusion that title insurance is a general insurance agency activity. In addition, the court stressed that it must defer to any reasonable construction by the agency where the statute is ambiguous and held that the Board's construction was reasonable.⁹⁷

The language of Exemption (G) supports the interpretation given the statute by the Board and the D.C. Circuit Court.⁹⁸ Since section 1843(c)(8)'s general prohibition against insurance activities undisputedly embraces title insurance,⁹⁹ it appears that section 1843(c)(8)(G)'s general exemption from that prohibition must also encompass title insurance agency activities.

To approve a bank holding company's owning or operating an insurance agency under any of the preceding exemptions, however, section 1843(c)(8) also requires the Board to find that the benefits to the public will outweigh any possible adverse effects from the applicant performing the particular insurance activity.¹⁰⁰ The Board fell far short of fully assessing all possible adverse effects in determining that First Wisconsin's acquisition of Milwau-

90. *First Wisconsin*, *supra* note 7.

91. *Id.*

92. 892 F.2d 1059 (D.C. Cir 1989).

93. *Id.*

94. *Id.* at 1063.

95. *Id.*

96. *Id.*

97. *Id.* at 1064.

98. See 12 U.S.C. § 1834(c)(8)(G) (Supp. 1986).

99. See *infra* note 71 and accompanying text.

100. "In determining whether a particular activity is a proper incident to banking or controlling or managing banks" under 12 U.S.C. § 1843(c)(8), the Board must consider whether the activity performed by a bank holding company or its subsidiary "can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices." 12 U.S.C. § 1843(c)(8) (Supp. 1986). A full assessment of the potential detrimental effects to

kee Title would produce a net public benefit because (1) borrowers could conveniently discuss title insurance when applying for mortgage loans at First Wisconsin, and (2) no proof existed that adverse effects on competition, conflicts of interest, or tie-ins of loan approvals to title insurance purchases would occur.¹⁰¹ While the Board spent four and a half pages in its Order parsing the language of Exemption (G), the Board responded to Congress' mandate to weigh public benefits and adverse effects with a mere three sentences.¹⁰² Additionally, the public benefit on which the Board based its approval of the bank holding company's acquisition of a title insurance agency is spurious, since borrowers already may apply for title insurance from independent title insurers when making their loan applications. In fact, the loan officer, attorney, or real estate agent handling the rest of the real estate transaction makes the great majority of title insurance applications for borrowers.

Countering this illusory benefit are the numerous potentially detrimental effects discussed in the remainder of this article.¹⁰³ However, the Board both ignored the concerns expressed by ALTA and failed to consider any possible adverse effects upon home purchasers, investors in real property, or investors in the secondary mortgage market.¹⁰⁴ Nor did the D.C. Circuit take seriously Congress' dictate to assess possible detrimental effects when reviewing the Board's decision in *ALTA v. Federal Reserve Board*.¹⁰⁵ The court merely recited the rule that courts must defer to the reasoned judgments of agencies, and concluded that "although the Board's order may have approached the outer boundary of tolerably terse, [citations omitted], it was explained in sufficient detail for us to conclude that it was, in fact, supported by substantial evidence."¹⁰⁶

The D.C. Circuit should not have felt obliged to defer to the Board's conclusion when the Board clearly fell so short of fulfilling the congressional mandate. Instead, any Board approval of title insurance activities by bank holding companies should be considered erroneous unless the Board gives

the public from bank holding companies owning and acting as title insurers should include all points discussed *infra* notes 173-215 and accompanying text.

See, Wilson, *supra* note 70, at 163; Comment, *supra* note 70, at 552.

101. See *First Wisconsin*, *supra* note 7, at 32; *ALTA v. Federal Reserve Board*, 892 F.2d at 1065-66.

102. The Board addressed the balancing issue as follows:

There is no evidence in the record indicating that consummation of First Wisconsin's proposal would result in any undue concentration of resources, adverse effects on competition, conflicts of interests, unsound banking practices, or any other adverse effects. First Wisconsin will provide an additional source for insurance that is particularly convenient for its customers. It has indicated that it will act affirmatively to ensure compliance with all laws and regulations prohibiting tie-ins by advising borrowers that they can obtain title insurance from any source they choose. Accordingly, the Board has determined that the balance of the public interest factors the Board is required to consider under section 4(c)(8) of the BHC Act is favorable.

First Wisconsin, *supra* note 7, at 32.

103. See *infra* notes 209-52 and accompanying text.

104. See *First Wisconsin*, *supra* note 7, at 32.

105. 892 F.2d at 1065.

106. *Id.*

more than the token consideration it gave in First Wisconsin's application to the balance of public interest factors which Congress set forth in section 1843(c)(8).¹⁰⁷

From the preceding it is clear that a bank holding company cannot directly own or control a title insurance company or engage in title insurance activities unless, in a rare case, one of the aforementioned exemptions applies and the public benefit is legitimately found to outweigh all possible adverse effects.¹⁰⁸ What is more, sections 1843(a)(1) and (2) expressly prohibit bank holding companies from "indirectly owning or controlling" a title insurance company unless an exemption applies.¹⁰⁹ This seems to mean that a bank holding company subsidiary cannot own or control a title insurance company, since it would be indirectly owned by the holding company. Neither sections 1843(a)(1) and (2) nor section 1843(c)(8) appear to make an exception when the bank holding company subsidiary is a national or state bank.¹¹⁰

As discussed above, bank holding companies own most national and state banks.¹¹¹ Therefore, the BHCA would seem to preclude ownership of title insurance underwriters and non-exempt agencies by bank holding companies and most national and state banks. However, various banks have succeeded in convincing the OCC and the Board to alter this policy.¹¹²

1. *Applicability of BHCA to Holding Company-Owned National Banks*

In Citibank's recent notification to the OCC of its intent to establish a subsidiary to underwrite title insurance, Citibank failed to address the fact that it is a subsidiary of a bank holding company, Citicorp.¹¹³ In a previous attempt to acquire a municipal bond insurance company, Citibank contended that the BHCA's prohibition against bank holding companies' subsidiaries owning insurance companies does not apply to the national bank subsidiaries of bank holding companies.¹¹⁴ Citibank asserted that only the National Bank Act regulates national banks' activities, regardless of whether

107. See 12 U.S.C. § 1843(c)(8) (Supp. 1986).

108. *Id.*

109. *Id.* §§ 1843(a)(1),(2) (Supp. 1986).

110. See 12 U.S.C. §§ 1843(a)(1),(2), 1843(c)(8) (Supp. 1986).

111. See *supra* note 62 and accompanying text.

112. See *infra* notes 115-22 and accompanying text.

113. See Letter to Emory W. Rushton, Deputy Comptroller of the Currency from Louise Firestone, Manager of Citibank (October 19, 1987).

114. The American Insurance Association challenged the OCC's approval of Citibank's acquisition of the American Municipal Bond Assurance Company, asserting that the OCC could not approve the acquisition of an insurance business by a bank holding company-owned national bank unless the acquisition was permissible under an exemption from the BHCA's prohibition against insurance activities. The U.S. Court of Appeals for the District of Columbia Circuit agreed in a 1988 ruling that, because Citibank was a subsidiary of a bank holding company, Citibank could not acquire a subsidiary whose activities might be deemed the business of insurance without first obtaining the approval of the Board of Governors of the Federal Reserve System under BHCA § 1843(c)(8). In 1989, however, the court vacated that portion of its opinion, ruling that the issue had not been properly before the court. *American Ins. Ass'n v. Clarke*, 865 F.2d 278 (D.C. Cir. 1989).

national banks are owned by bank holding companies.¹¹⁵

The OCC also posits that the BHCA's prohibition of indirect insurance activities by bank holding companies does not affect national banks, despite the fact that most national banks are subsidiaries of bank holding companies, and national banks' subsidiaries are indirect subsidiaries of bank holding companies.¹¹⁶ The OCC reasons that Congress intended the BHCA to correct gaps in the regulation of bank holding companies, not to govern their national or state bank subsidiaries, which are sufficiently regulated by the NBA and state law.¹¹⁷ Under this rationale and the OCC's interpretation of the National Bank Act discussed above, national banks owned by holding companies are free to engage in title insurance activities or own title insurance subsidiaries.¹¹⁸

The Board agrees with the OCC that the BHCA's insurance prohibition does not control the direct activities of the national or state banks owned by holding companies.¹¹⁹ However, in its recent orders and in litigation, the Board has maintained that the BHCA's restrictions do prevent bank holding company-owned national and state banks from owning insurance subsidiaries, since they would be indirect nonbank subsidiaries of the holding company.¹²⁰

The Board's interpretation comes from parsing section 1843(a)(2), quoted above,¹²¹ into one clause limiting the types of companies a bank holding company may own to banks and bank holding companies and a second clause limiting the bank holding company's activities to (1) banking, (2) managing and controlling banks and authorized nonbank companies, and (3) activities closely related to banking.¹²² The Board, thus, concludes that sec-

115. See *supra* note 113.

116. *Clarke*, 865 F.2d at 280. See Letter to Mr. William W. Wiles, Secretary of the Board of Governors of the Federal Reserve System from C.T. Conover, Comptroller of the Currency (March 19, 1985).

117. *Id.*

118. *Id.*

119. On March 3, 1989 the Board granted the request of a bank holding company, Merchants National Corporation, to permit two of its subsidiary state banks to engage in direct sales of property and casualty insurance. The Board did so on the grounds that "the nonbanking provisions of the Bank Holding Company Act do not apply to the direct activities of holding company banks." See *Merchants Nat'l Corp.*, 73 FED. RES. BULL. 876 (1987); *Merchants Nat'l Corp.*, 75 FED. RES. BULL. 388 (1989).

The Independent Insurance Agents of America challenged the Board's order. The court stayed the order pending a final review in the U.S. Court of Appeals for the Second Circuit. *Independent Ins. Agents of America v. Board of Governors*, 890 F.2d 1275 (2d Cir. 1989). Applying the standard of whether the agency's decision was based on a permissible construction of the statute, the court held that the Board had made a reasonable interpretation in concluding that the BHCA did not restrict bank subsidiaries of a bank holding company from selling insurance. *Id.* at 1280. The Independent Insurance Agents reportedly plan to file a petition for certiorari to the United States Supreme Court.

120. See *Independent Ins. Agents v. Board of Governors*, 890 F.2d 1275, 1280-82 (2d Cir. 1989) (citing the Board's Orders in *Merchants Nat'l Corp.*, 73 FED. RES. BULL. 876 (1987) and *Merchants Nat'l Corp.*, 75 FED. RES. BULL. 388 (1989)).

121. 12 U.S.C. § 1843(a)(2) (Supp. 1986). See *supra* text accompanying note 68.

122. The statute's language reads as follows:

no bank holding company shall . . . retain direct or indirect ownership . . . of any
 . . . company which is not a bank or bank holding company or engage in any

tion 1843(a)(2) only requires bank holding companies, not their banking subsidiaries, to engage solely in activities closely related to banking.¹²³ The Board sees nothing in section 1843 to prevent an allowed bank subsidiary from directly engaging in any activities permitted by its regulatory agency.¹²⁴ Nevertheless, bank holding company-owned national and state banks could not own unauthorized subsidiaries because the holding company would indirectly own them in violation of the BHCA.¹²⁵

Interestingly, the Board's recent interpretation is partially inconsistent with two of the Board's own regulations.¹²⁶ One Board regulation purports to allow holding company-owned national banks to own shares of subsidiaries of the same kinds and amounts permitted for national banks under the National Bank Act.¹²⁷ Similarly, another Board regulation purports to permit holding company-owned state banks to own shares of subsidiaries as permitted by state law.¹²⁸ Recognizing the inconsistency, the Board has initiated a rulemaking proceeding to rescind the latter regulation regarding subsidiaries of state banks.¹²⁹ Whether the Board will attempt to rescind its conflicting regulation regarding national banks' subsidiaries remains to be seen.¹³⁰

ALTA presents a third opinion regarding the applicability of the BHCA's insurance prohibition to bank holding company owned-national banks. ALTA interprets section 1843(a)(2) to prohibit holding companies from directly or indirectly owning nonbanking entities and from directly or indirectly engaging in activities other than those closely related to banking.¹³¹ Under this reading, any activities of bank subsidiaries would be indirect activities of the bank holding company. Thus, a holding company-owned national bank could not own a nonbank subsidiary or engage in any activities not authorized for the bank holding company.¹³²

activities other than (A) those of banking or of managing or controlling banks and other subsidiaries authorized under this Act . . . , and (B) activities so closely related to banking as to be incidental thereto.

12 U.S.C. § 1843(a)(2) (Supp. 1986). See *supra* text accompanying note 68.

123. See *supra* note 120 and accompanying text.

124. *Id.*

125. 12 U.S.C. § 1843 (Supp. 1986).

126. See 12 C.F.R. § 225.22(d)(1),(2) (1989).

127. 12 C.F.R. § 225.22(d)(1) (1989).

128. 12 C.F.R. § 225.22(d)(2) (1989).

129. Notice of Proposed Rulemaking, 53 FED. REG. 48915, 48921 - 24 (Dec. 5, 1988).

130. See 12 C.F.R. § 225.22(d)(1) (1989).

131. Brief for Petitioner at 8, *ALTA v. Federal Reserve System*, 892 F.2d 1059 (D.C. Cir. 1989); Letter to Robert Clarke, Comptroller of the Currency from Sheldon E. Hochberg, Counsel to the ALTA regarding Citibank's application to establish a subsidiary to engage in title insurance underwriting at 3, 4 n.2 (Jan. 31, 1989).

ALTA bases its interpretation, in part, on language in the Senate Conference Report on Title VI of the Garn-St Germain Act, S. Rep. No. 97-641, 97th Cong. 2d Sess. 91 (1982), which states that Title VI prohibits "bank holding companies and their subsidiaries" from selling and underwriting insurance. The Senate did not say only nonbank subsidiaries were precluded from insurance activities.

132. The Second Circuit described this interpretation, asserted by the general insurance agency, as having "the virtue of consistency." *Independent Ins. Agents v. Board of Governors*, 890 F.2d 1275, 1282 (1989).

2. *Applicability of BHCA to Holding Company-Owned State Banks*

Consistent with its view that the BHCA does not prevent holding company-owned national banks from direct insurance sales, the Board also has taken the position that the BHCA does not prohibit holding company-owned state banks from selling insurance.¹³³ According to this theory, state banks owned by bank holding companies may directly underwrite or sell title insurance if state law permits.¹³⁴ The Board, however, again maintains that holding company-owned state banks are prohibited from owning title insurance companies, since the title insurance company would be an indirect subsidiary of the bank holding company and thus unauthorized under section 1843(a)(2).¹³⁵

The Board's conclusion that the BHCA does not prohibit direct insurance sales by holding company-owned state banks recently survived a challenge by the general insurance industry.¹³⁶ In March of 1989, the Independent Insurance Agents of America ("IIAA") sued to overturn Board approval of direct property and casualty insurance sales by two Indiana state banks owned by a bank holding company, Merchants National Corporation.¹³⁷ IIAA contended that sections 1843(a)(2) and 1843(c)(8) prohibit bank holding companies and *all* of their direct and indirect subsidiaries from engaging in the insurance business.¹³⁸ IIAA argued that any other rule would permit bank holding companies to evade the BHCA merely by merging a prohibited nonbank subsidiary into a bank subsidiary which could then operate the nonbank activity itself. This precise scenario had occurred in the case before the court.¹³⁹

The Second Circuit acknowledged that the insurance industry's position had "the virtue of consistency."¹⁴⁰ The court stated that unless the BHCA unambiguously expressed Congress' intent, the court was limited to determining whether the Board's construction of the BHCA was permissible.¹⁴¹ The court then held that the BHCA is ambiguous on the question and up-

133. See *supra* note 125.

The Board's position on this issue seems to have fluctuated dramatically over the years. On January 5, 1984, the Board announced its tentative judgment that it could not approve the applications of three major bank holding companies (Citicorp of New York, BankAmerica Corp. and First Interstate Bancorp of California) to acquire state banks in South Dakota, a state which permitted banks to conduct insurance activities. The Board opined that bank holding companies could not use state bank subsidiaries to perform activities prohibited by the BHCA. The Board stated that only Congress and not state legislatures may enlarge the powers of bank holding companies. See Wilson, *supra* note 70, at 184-85. See also, Huber, note 25, at 163, for the view that the Board's opinion on this issue has never changed; the Board denied the preceding applications solely because the banks were designed to serve primarily as vehicles for conducting insurance activities and would conduct only minimal banking activities.

134. See *supra* note 119.

135. See *supra* notes 120-25 and accompanying text.

136. See *Independent Ins. Agents of America v. Board of Governors*, 890 F.2d 1275 (2d Cir. 1989).

137. *Id.*

138. *Id.* at 1282.

139. *Id.*

140. *Id.*

141. *Id.*

held the Board's interpretation as a reasonable construction that must stand until Congress enacts suitable legislation.¹⁴² The court did note a perplexing inconsistency in the Board's ruling that activities of holding company-owned banks are not subject to the BHCA's insurance prohibitions, yet activities of such banks' nonbank subsidiaries are subject thereto.¹⁴³ The court declined to resolve this issue since the facts did not involve nonbank subsidiaries of holding company-owned state banks.¹⁴⁴

The Board itself has taken steps to clarify the latter issue.¹⁴⁵ As discussed, the Board's position in its recent rulings¹⁴⁶ has been that, although the 1982 amendments to sections 1843(a) and 1843(c)(8) of the BHCA do not prevent bank subsidiaries of holding companies from directly selling insurance, the amendments do prevent holding company-owned banks from owning insurance company subsidiaries.¹⁴⁷ However, the Code of Federal Regulations still contains a regulation promulgated in 1971 which permits holding company-owned state banks to own any subsidiaries allowed by state law.¹⁴⁸ In December of 1988, the Board published a notice of proposed rulemaking to bring the regulation into conformity with the Board's current view.¹⁴⁹

In response to the Board's proposed revision of the regulation,¹⁵⁰ ALTA again has asserted that the 1982 amendments to sections 1843(a)(2) and 1843(c)(8) of the BHCA prohibit holding company-owned state banks' from owning title insurance subsidiaries.¹⁵¹ ALTA contends that the passage of the Garn-St Germain Act voided regulation 225.22(d)(2)(ii) insofar as it appears to authorize any insurance activities by holding company-owned state bank subsidiaries.¹⁵²

The banking industry's primary counter-argument is that Congress never intended the BHCA to give the Board jurisdiction over the activities of state banks or their subsidiaries.¹⁵³ The banking industry asserts that to give the Board this sort of control over state banks and their subsidiaries is contrary to the dual federal and state bank regulatory systems and violates states' rights.¹⁵⁴

142. *Id.* at 1280-81, 1284.

143. *Id.* at 1282.

144. *Id.* at 1282-83.

145. *See supra* notes 126-30 and accompanying text.

146. *See supra* note 120 and accompanying text.

147. *Id.*

148. 12 C.F.R. § 225.22(d)(2)(ii) (1989).

149. 53 FED. REG. 48915 (Dec. 5, 1988).

150. 12 C.F.R. § 225.22(d)(2)(ii) (1989).

151. Comments of the American Land Title Ass'n, In the Matter of Board of Governors of the Federal Reserve System, No. R-0652 (filed with the Board of Governors on Feb. 13, 1989).

152. ALTA also asserts that the Board cannot grandfather any title insurance activities that state banks' subsidiaries may have undertaken pursuant to the former regulation, since the regulation was contrary to law. *Id.* at 6.

153. *See infra* note 154 and accompanying text.

154. Letter to William W. Wiles, Secretary of the Board of Governors of the Federal Reserve System from Donald G. Ogilvie, Executive Vice President of American Bankers Ass'n regarding Proposed Amendment to Federal Reserve Board Regulation Y As It Applies to Subsidiaries of State Banks Owned By Bank Holding Companies (Dec. 2, 1988); Letter to William W. Wiles, Secretary of the Board of Governors of the Federal Reserve System from

Legislation is clearly required to clarify Congressional intent on these issues. Certainly, the answer to whether holding company-owned national and state banks should be permitted to sell title insurance or own title insurers cannot be deduced merely from construing the language of section 1843(a)(2).¹⁵⁵ Each of the preceding interpretations of the BHCA's insurance prohibitions upon national and state banks' selling insurance and owning insurance subsidiaries possesses merit.¹⁵⁶ Additionally, a judicial construction of section 1843(a)(2) alone will not permit the distinction which Congress needs to make between the appropriateness of banks conducting general insurance activities and conducting title insurance activities.

D. *Applicability of the FDIC Act*

Since 1946, FDIC regulations have prohibited FDIC-insured state banks, which are not owned by bank holding companies, from "insuring, guaranteeing or certifying titles to real estate."¹⁵⁷ The FDIC's regulation does not apply to FDIC-insured national banks or to insured state banks belonging to bank holding company systems, presumably because the National Bank Act regulates the former and the Board the latter.

Additionally, in 1984, the FDIC published for public comment an amendment to its regulations which would prohibit all insured banks from engaging in insurance underwriting activities, including title insurance underwriting, regardless of whether they are national banks, state banks

Richard M. Whiting, General Counsel & Secretary to the Association of Bank Holding Companies regarding rescission of § 225.22(d)(ii) of the Board's Reg Y (dated Dec. 8, 1988); and Letter to William W. Wiles, Secretary of the Board of Governors of the Federal Reserve System from Donald G. Ogilvie, American Bankers Ass'n; Thomas L. Ashley, Association of Bank Holding Companies; Gerard F. Milano, California Bankers Clearinghouse Ass'n; Mark J. Riedy, National Council of Savings Institutions; Richard L. DeCair, Bank Capital Markets Ass'n; Lawrence E. Kreider, Conference of State Bank Supervisors; John Belew, Consumer Bankers Ass'n; Kenneth W. Guenther, Independent Bankers Ass'n of America; John F. Lee, The New York Clearing House Ass'n; and Anthony T. Cluff, Association of Reserve City Bankers regarding Docket No. R-0652, Proposed Amendment to Federal Reserve Board Regulation Y As It Applies to Subsidiaries of State Banks Owned By Bank Holding Companies (Dec. 22, 1988) (the individuals formally filed these letters with the Federal Reserve Board in response to the Board's request for public comment on its proposed rescission of 12 C.F.R. § 225.22(d)(ii)).

155. See 12 U.S.C. § 1843(a)(2) (Supp. 1986).

156. See *Independent Ins. Agents of America v. Board of Governors*, 890 F.2d 1275 (1989), in which the Second Circuit repeatedly pointed to the ambiguity of the BHCA on these questions:

... we cannot say that the provisions of the Act reveal an unambiguous congressional intent concerning the precise question *Id.* at 1281; Both sides claim that the text of the Act supports their interpretations, and each can find some, but not overwhelming, support in various words and phrases. . . . *Id.*; . . . use of these phrases . . . might imply a deliberate congressional choice not to restrict the activities of bank subsidiaries . . . but might also result from drafting different clauses at different times and assembling them without intending differences in phrasing to have significance. *Id.*

However, the court found that so long as regulatory agency interpretations of the BHCA are reasonable, only Congress has the power to change them, through legislation. *Id.* at 1284. See *supra* notes 137-44 and accompanying text.

157. 12 C.F.R. § 332.1 (1989) (Powers Inconsistent With Purposes of Federal Deposit Insurance Law).

owned by bank holding companies, or independent state banks.¹⁵⁸ However, because of objections from the OCC and the Board, the FDIC aborted the proposed rulemaking in 1987.¹⁵⁹ Since 1987, the FDIC has reportedly continued to work with the OCC and the Board to develop regulations to prohibit all types of insurance underwriting by all FDIC-insured national and state banks.¹⁶⁰ The FDIC purportedly has concluded that the risks to the safety and solvency of the federal deposit insurance fund from banks' underwriting and marketing insurance outweigh any benefits obtained from allowing banks to provide insurance for their customers.¹⁶¹

E. Congressional Activity, 1988 - 1990

All that is apparent from the preceding examination of statutes and regulations is their inconsistency and the impossibility of stating that one interpretation is clearly correct or incorrect.¹⁶² Certainly the opinions of the various bank regulators regarding the permissibility of title insurance activities for banks, bank holding companies, and their subsidiaries are in disarray. Commentators writing on the question of whether banking entities are permitted to sell general insurance have similarly disagreed on how Congress intended the various relevant statutes and regulations to be reconciled.¹⁶³

In fact, because of the controversies, in each of the past two years, bills have been introduced in Congress to resolve at least some of the issues. In 1988, the Financial Modernization Act was introduced in the United States Senate, as an amendment to the Glass-Steagall Act.¹⁶⁴ The bill proposed to permit national banks to expand into securities and insurance sales.¹⁶⁵ Senator Cranston of California attached an amendment to the bill which specified that title insurance is included within the insurance activities the BHCA prohibits for direct and indirect subsidiaries of bank holding companies.¹⁶⁶ The Senate passed the bill in this form; however, the House of Representatives did not approve it before Congress recessed for the year.¹⁶⁷

In April of 1989, Congressman Carper of Delaware introduced an amend-

158. 50 FED. REG. 23963; Hochberg, *Banks, Bank Holding Companies and Title Insurance*, 68 TITLE NEWS 14, 33 (July - Aug. 1989).

159. 52 FED. REG. 48447 (1987) (FDIC withdrawal of rule proposed Nov. 26, 1984). See also Huber, *supra* note 25, at 162. Huber asserted that the FDIC "used to" prohibit state banks from insuring, guaranteeing, or certifying titles to real estate, but that "the FDIC now permits ['stand-alone'] insured state banks to undertake these activities." *Id.* For this proposition, Huber cites the FDIC's 1987 withdrawal of the rule it had proposed in 1984. *Id.* The withdrawal of that proposed rule, however, merely eliminated the possibility of additional restrictions on the ability of all banks to sell title insurance; the FDIC did not repeal 12 C.F.R. § 332.1 (1989).

160. Hochberg, *supra* note 158, at 33-34.

161. *Id.*

162. See *supra* notes 26-161 and accompanying text.

163. See generally *supra* note 25 (citing commentators discussing Congressional edicts regarding sale of general insurance by banking entities).

164. ALTA, Capital Comment, 1-2 (April 1988).

165. *Id.*

166. *Id.*

167. *Id.*

ment to the BHCA in the House.¹⁶⁸ The proposed amendment specifically exempted bank subsidiaries which conduct activities permissible under state law from any activity restrictions of the BHCA.¹⁶⁹ At this writing, Bill No. 1723 has not left the House Banking, Finance and Urban Affairs Committee,¹⁷⁰ nor is it expected to before Congress adjourns for the year. If passed, the bill would resolve few of the issues discussed herein. Essentially, the bill would permit bank holding company-owned state banks to own insurance subsidiaries, including title insurance subsidiaries, in the few states where state law permits.¹⁷¹ The bill does not address the issues of national bank ownership of title insurance subsidiaries or national or state bank direct title insurance sales.¹⁷² Additionally, the bill fails to answer questions regarding subsidiaries of national and state banks which are not owned by bank holding companies.¹⁷³

III. PUBLIC POLICY CONCERNS

Any new legislation or amendment of existing law will continue to be problematic unless Congress stops treating general insurance and title insurance as one. For years the general insurance industry has unsuccessfully sought legislation to keep banks and bank holding companies out of the general insurance business.¹⁷⁴ Congress has not been convinced of significant adverse effects upon the public from lender control of general insurers and lender sale of general classes of insurance. Despite the rhetoric about the intent behind the NBA and the language of the BHCA, the majority of lawmakers have seen the dispute between banking regulators and the general insurance industry as purely economic — with the bank regulators generally supporting banks extending their profit-making activities, and the insurance industry attempting to eliminate a source of competition.

Many of ALTA's arguments regarding the proper interpretation of the NBA and the BHCA echo those previously asserted by the general insurance industry. Of course, ALTA is motivated by the same economic interest as the general insurance industry, *i.e.*, concern for the effects of competition

168. H.R. 1723, 101st Congr, 1st Sess. (April 6, 1989).

169. *Id.* § 2.

170. Congressional Index (CCH) 26,157 - 16,158 (1990).

171. See H.R. 1723 § 2, 101st Congr., 1st Sess. (April 6, 1989).

172. *Id.*

173. *Id.*

174. See *supra* note 163. As Huber aptly noted,

The banking and insurance industries are engaged in a protracted war over the extent to which banks and bank holding companies . . . may sell and underwrite insurance. This war is now over three decades old, and no end is in sight. Battles have been fought in congress, state legislatures, the courts, and the media. The insurance industry regards the sale and underwriting of insurance as not incidental or closely related to banking, antithetical to the public interest, and perhaps even a threat to the survival of the present industry structure. Banks view many insurance activities as intimately related to the business of banking and see the insurance industry as obstructing rational organization of economic activity, simply because it fears competition.

Huber, *supra* note 25, at 147-48.

from a new source of title insurance upon existing title insurers. For this reason, it has been easy for banking regulators, courts and legislators to dismiss ALTA's complaints, as they have formerly dismissed those of the general insurance industry.

What regulators and legislators have overlooked is the uniqueness of title insurance among classes of insurance. Its special role as both indemnifier and eliminator of risks in real estate transactions deserves separate consideration. Scrutiny into the distinctive nature of title insurance reveals that the policies against title insurance activities are much more compelling than the policies against general insurance activities by banks and bank holding companies.¹⁷⁵ These differences between title insurance and other types of insurance warrant legislation specifically to prohibit bank holding companies, national and state banks, and their subsidiaries from underwriting and selling title insurance.

A. *Special Roles of Title Insurance*

While title insurance has similarities to other general insurance forms, its origin in the context of real property transactions and the financing thereof has given title insurance several unique characteristics.¹⁷⁶ Today title insurance is the preferred method of protecting purchasers and lenders in the United States against loss from unexpected encumbrances and undiscovered claims to real property.¹⁷⁷ In many states the purchase of title insurance has all but displaced attorney's title opinions and abstracts, the traditional means of title assurance, as the way to ensure that investments in real property will not turn out to be losses.¹⁷⁸

The development of title insurance and the growth of the industry was a reaction to the inability of abstracts and attorney's title opinions to adequately protect land purchasers.¹⁷⁹ Under the attorney opinion method of title assurance, a potential buyer or mortgagee of real property retains an attorney to search the public records, weigh the facts shown, and provide a written opinion as to the condition of title.¹⁸⁰ The attorney's opinion also sets forth any actions to remove encumbrances or cure title defects which the purchaser or lender should take prior to closing the transaction in order to acquire a marketable title. The attorney might perform the title search personally or hire an abstractor to perform the search at the various record offices and supply the attorney with an abstract of all documents on rec-

175. The author has read the briefs of ALTA & NYLTA and ALTA & TLTA, the OCC, and the Board which were filed in cases cited *supra* notes 17-24. Some of the concerns raised *infra* in text accompanying notes 176-267 were asserted or refuted in these briefs.

176. J. Palomar, *Liability of Title Insurers*, in B. Dunaway, *THE LAW OF DISTRESSED REAL ESTATE*, 27B-3 (2d ed. 1989).

177. Palomar, *Title Insurance Companies' Liability for Failure to Search Title and Disclose Record Title*, 20 CREIGHTON L. REV. 455, 457 (1986-87).

178. Palomar, *supra* note 176, at 457. See Whitman, *Optimizing Land Title Assurance Systems*, 42 GEO. WASH. L. REV. 40, 47-49 (1973); Note, *Washington Title Insurers' Duty to Search and Disclose*, 4 U. PUGET SOUND L. REV. 212 (1980).

179. Palomar, *supra* note 177, at 458.

180. *Id.* Comment, *Title Insurance: The Duty to Search*, 71 YALE L.J. 1161, 1163 (1962).

ord.¹⁸¹ The attorney and abstractor are each charged with a duty to exercise reasonable care in conducting the title search and preparing the abstract and title opinion.¹⁸² If a client suffers a loss because of a title defect, which was discoverable from the record, the client has a potential claim against either the attorney or the abstractor for negligence.¹⁸³ However, neither the attorney nor the abstractor will be liable for failure to discover or disclose defects that a member of the profession, exercising reasonable care, would not find or disclose.¹⁸⁴

The real property purchaser or mortgagee who relies on an abstract and attorney's opinion, thus, will not be protected against losses resulting from any one of the multiple title defects which cannot be detected from a reasonable search of the public records.¹⁸⁵ Inherent weaknesses in the grantor/grantee recording system utilized by most county recording offices in the United States,¹⁸⁶ make these uncompensable losses far too common.¹⁸⁷ For example, neither abstractor nor attorney is liable for failing to find an instrument erroneously recorded outside the chain of title being searched.¹⁸⁸ Additionally, misspellings of names, name changes, fraud, forgery or duress in the execution of instruments, apparent deeds which are actually mortgages, executions of documents by minors or incompetents, improper notice in judicial proceedings, undisclosed marriages and divorces, and pretermitted heirs all may cause title defects which are not discoverable through a reasonable search of public records. That local custom may limit attorneys and abstractors' title searches to only a few public offices increases the problem of uncompensable losses. In fact, records affecting interests in land may be found in the offices of the register of deeds, probate court, county court, city council, secretary of state, county auditor, tax assessor, tax collector, and even the federal register.¹⁸⁹ Further, when an attorney or abstractor discovers an encumbrance or title defect, but fails to require that it be cleared before the client takes title or disburses loan funds, the injured client has no recourse as long as the attorney or abstractor exercised reasonable care. Even in the event of blatant negligence, whether the client actually recovers depends entirely upon the solvency of the individual lawyer or abstractor.¹⁹⁰

The inability of abstracts and attorneys' opinions to offer protection against so many potential title defects prompted the development of title insurance.¹⁹¹ Title insurance supplemented the former method of title assur-

181. Whitman, *supra* note 178, at 47-48.

182. Palomar, *supra* note 177, at 458.

183. Comment, *supra* note 180, at 1164.

184. *Id.* at 1164.

185. Palomar, *supra* note 177, at 458 (citing Savings Bank v. Ward, 100 U.S. 195, 195-96 (1979); Watson v. Muirhead, 57 Pa. 161, 168 (1868)).

186. See Palomar, *supra* note 171, at 458 n.21 for a discussion of the weaknesses in grantor/grantee recording system.

187. *Id.* at 458.

188. Comment, *supra* note 180, at 1163-64.

189. In one instance, a company reported examining seventy-six sources of information in sixteen public offices. Comment, *supra* note 168, at 1164 n. 25.

190. Palomar, *supra* note 177, at 458.

191. The first title insurance company is said to have formed in reaction to a Pennsylvania

ance by indemnifying for losses caused by encumbrances and title defects which are undiscoverable even with the exercise of reasonable care.¹⁹² Title insurance retains from attorney's title opinions the important features of preliminary title search and disclosure to the applicant of all discovered encumbrances and title defects prior to the closing of the real estate transaction.

Thus, title insurance contrasts with virtually all other insurance forms because it is structured on the concept of risk elimination, not solely on risk assumption and distribution of loss.¹⁹³ Prior to the issuance of the policy, a title insurance company employee, or an attorney or abstractor acting as the title insurer's agent, searches the real property records pertaining to the property interest to be insured.¹⁹⁴ When the search uncovers encumbrances or title defects, the title insurer discloses them to the applicant before the real estate transaction closes. This disclosure provides the applicant with an opportunity to require the seller or mortgagor to cure the identified defects before completing the transaction.¹⁹⁵

The title insurer's title examination cannot be equated with any preliminary fact-gathering or analysis of loss expectancy and actuarial tables other types of insurers perform to assess the risk of insuring a particular applicant.¹⁹⁶ The title insurance company's preliminary title examination is much more. It is proffered as a substitute for both the record search and abstracting of a professional abstractor, and the opinion of an attorney as to the legal status of title. Indeed, the preliminary title examination is the main focus of title insurance, with as much as ninety percent of the title insurance premium paying for its cost.¹⁹⁷

To facilitate accurate title searching, title insurance agencies have invested large sums to build private title plants with real property records indexed by tract of land, and to index on computer probate court, tax lien, and some-

Supreme Court holding that a conveyancer was not liable for loss to his client from a judgment lien which the conveyancer reasonably believed would not be a lien upon his client's title. See *Watson v. Muirhead*, 57 Pa. 161, 168 (1868); Palomar, *supra* note 177, at 458 n. 24.

192. *Id.* at 459.

193. See *Lawyers Title Ins. Corp. v. Research Loan & Inv. Corp.*, 361 F.2d 764 (8th Cir. 1966) ("[t]itle insurance is also more than a contract of indemnity, usually the essence of the title insurance transaction is to obtain a professional title search, opinion, and guarantee"). See also Roberts, *Public Regulation of Title Insurance Companies and Abstractors*, 5 (1961) (title insurance not based on mere guesswork as fire insurance or automobile insurance; instead it is based on reports prepared by skilled technicians evaluating the risk); NIBLACK, ABSTRACTORS AND TITLE INSURANCE 157 (title insurance is not the taking of a risk on the validity of the title, rather the theory is that no known risks are taken).

194. Palomar, *supra* note 177, at 459 n. 28.

195. For a discussion of the standard form Commitment to Insure, Owner's Title Insurance Policy and Loan Policy used by most of the nation's title insurers, see J. Palomar, *Liability of Title Insurers*, in B. DUNAWAY, *THE LAW OF DISTRESSED REAL ESTATE*, 27B-5 to 27B-27 (2nd ed. 1989). For legal issues involving the title insurer's duty to search and disclose the status of record title, see Palomar, *supra* note 177, at 455-68.

196. "Title insurance is not based on mere guesswork as are fire insurance or automobile insurance. It instead is based on reports evaluating the risk which are prepared by skilled technicians." ROBERTS, *PUBLIC REGULATION OF TITLE INSURANCE COMPANIES AND ABSTRACTORS* 5 (1961).

197. See Bozarth, *Environmental Liens and Title Insurance*, 68 TITLE NEWS 8 (May - June 1989).

times zoning and planning records.¹⁹⁸ The local title insurance agencies' tract indexes trace title based on the legal description of parcels of land. Each tract of land is given a number and a place in the tract index. All transactions involving a particular tract then are recorded on a single page, or consecutive pages, under the tract number. The tract system is more efficient than the grantor/grantee index system, since the examiner needs to search only the one set of records involving the tract being insured, rather than the multiple indexes containing the name of each grantor and grantee in the chain of title.¹⁹⁹ The tract index system's efficiency also stems from the fact that it is not dependent upon the correct spelling of grantor and grantees' names.²⁰⁰ Furthermore, a tract index can reveal "wild deeds" which could not be found in a grantor/grantee index.²⁰¹

Thus, because of the tract index format for real property records, and because other relevant records gathered from various county offices are made accessible through a single computer search, title insurance companies today provide the most efficient and accurate title searches ever available.²⁰² County record offices simply have not had the money to duplicate these technologies.²⁰³ In many localities where title insurers own private plants, the public records are virtually unused except for the title insurance agency's daily take-offs and occasional inquiries for copies of specific documents. Moreover, only title insurers affirmatively assist insureds in eliminating discovered risks and avoiding losses. Title insurance applicants may request the insurer's assistance with procedures and documentation necessary for curing any encumbrances and title defects discovered.

The attention title insurers give to risk elimination and loss avoidance benefits not only the insurer, but also the insured and society as a whole because land may be invested in, developed, and improved with less danger that a superior claimant will later challenge the title.²⁰⁴ Investors need to know that property can be used for their intended purposes. Investors want assurance that the title is marketable before closing a transaction, not merely financial reimbursement if forced to defend against adverse claims, or to alter or interrupt their use of the property after having labored to develop and improve it. When title risks are reduced, investment and development of real property are naturally encouraged. Additionally, society's resources are allocated more efficiently and waste is prevented when purchasers are kept

198. Palomar, *supra* note 177, at 459. See also Taub, *Rights and Remedies Under a Title Policy*, 15 REAL PROP. PROB. & TR. J. 422, 422-23 (1980); Whitman, *supra* note 178, at 59; Comment, *supra* note 180, at 1164.

199. Palomar, *supra* note 177, at 459 n.29.

200. *Id.*

201. *Id.*

202. *Id.* at 459.

203. *Id.*

204. As one commentator explained:

If title insurance generally were written on a risk basis only, without search or examination, there would be a gradual deterioration in the certainty of titles. It is the curative action taken by owners upon receiving examination reports from insurers that maintains the high degree of record title certainty of insured titles.

Johnstone, *Title Insurance*, 66 YALE L.J. 492, 516 (1957).

from investing in land they cannot develop because of an encumbrance or title defect.

Furthermore, the risk elimination features of title insurance have been credited with increasing the availability of funds for real estate loans in the United States.²⁰⁵ Large investors such as life insurance companies and national banks have been encouraged to buy millions of dollars of first mortgage loans because the priority of their liens is insured.²⁰⁶ Title insurance has strengthened these investors' confidence in the mortgage market by providing (1) a form of title assurance that is standardized throughout the country,²⁰⁷ (2) a promise that the title insurer will negotiate or litigate any claims which arise against the collateral, and (3) a financially sound corporation to indemnify investors for any loss caused by the failure of a mortgage lien.²⁰⁸ As long as investors remain willing to buy insured mortgage loans, members of the public can count on a steady infusion of money into local banks and savings and loan institutions which will be available for loans for home purchases and real estate development.

Thus, lenders acting as or controlling title insurers raises several concerns for the public that are not raised by lender control of general insurers. These concerns include potential conflicts of interest, decline in the integrity of title insurance underwriting, retrogression of title insurance's role as eliminator of risks, degeneration of our nation's real property records, and decreased availability of mortgage money throughout the United States.

B. Conflicts of Interest

When a lender who makes loans for real property purchases also sells title insurance, owns a title insurer, or is the sister-company of a title insurer, conflicts of interest exist in at least three forms. First, a conflict may exist between the loan applicant's interest in obtaining the cheapest title insurance from the most reliable insurer and the bank's interest in capturing the applicant's title insurance business for itself or its affiliated insurer. Second, a conflict may arise between the borrower's interest in obtaining clear title and the lender-controlled title insurer's interest in approving title so that the lender may acquire the loan transaction. Third, a conflict may exist between a lender-controlled title insurance agent's duty to minimize the underwriter's exposure and its interest in approving title so that the lender may secure the loan transaction.

Regarding the first conflict of interest, it is ironic that the OCC cited the efficiency for borrowers of obtaining title insurance when negotiating the mortgage as a reason for granting national banks the authority to sell title

205. ROBERTS, PUBLIC REGULATION OF TITLE INSURANCE COMPANIES AND ABSTRACTERS, 18 (1961).

206. *Id.*

207. *Id.* Roberts asserts that the prime requisite for national companies investing in the secondary real estate mortgage market is "a freely transferable mortgage" and security behind it that is "everywhere acceptable." *Id.*

208. See Roberts, *Title Insurance: State Regulation and the Public Perspective*, 39 IND. L.J. 1, 8 n.22 (1963); Johnstone, *supra* note 204, at 503.

insurance.²⁰⁹ The Board included the same reason when granting First Wisconsin Corporation (Firststar) permission to acquire a title insurance agency.²¹⁰ The Board at least acknowledged the potential conflict of interest and specifically premised its permission on First Wisconsin's express agreement not to tie loan approvals to purchases of title insurance from its agency.²¹¹

A lender that sells title insurance or owns a title insurer has an economic incentive to tie its other services to the applicant's agreement to purchase title insurance from the lender or its title insurance subsidiary. The lender profits from direct commissions when it sells title insurance and from dividend payments when it owns a title insurer. The peril to the public is that consumers may be steered to the bank's or its subsidiary's title insurer over others that may provide greater coverage, lower rates or better service.

Recognizing the conflict of interest, in 1982 Congress enacted legislation making it a violation of the controlled business provisions of the Real Estate Settlement Procedures Act ("RESPA") for a lender to expressly tie approval of a federally-related mortgage loan to a title insurance purchase from a particular entity.²¹² To avoid penalties under RESPA, a lender must, at or prior to the time of referrals, (1) inform consumers of the existence of the controlled business arrangement, (2) provide consumers with a written estimate of the affiliated title insurance company's charges, (3) inform consumers that they are not required to use the services of the affiliated title insurer, and (4) accept nothing of value from the title insurer, other than a return on an ownership interest.²¹³ Borrowers referred in violation of RESPA may recover three times the amount they paid for the title insurance premium.²¹⁴

Even without illegal coercive tying, however, a mortgage lender can effectively refer the majority of its borrowers' title insurance applications to its preferred title insurer. Since consumers purchase title insurance only on the few occasions that they buy real property, and since the cost of title insurance is a relatively small portion of the transaction total, borrowers have little incentive to comparison-shop.²¹⁵ Borrowers are generally willing to let a loan officer or real estate broker direct them to the insurer with whom the bank or broker most often deals. Frequently, borrowers simply allow their

209. See Interpretive Letter No. 368 (July 11, 1986), Office of the Comptroller of the Currency, 1985-87 Fed. Banking L. Rep. (CCH) ¶ 85,538; see also Defendant's Memorandum in Support of Motion to Dismiss, *ALTA & NYSLTA v. Clarke*, 89 Civ. 6939 (MJL), at 10-11 (filed Jan. 2, 1990); *American Land Title Ass'n & Texas Land Title Ass'n v. Clarke*, No. A-87-CA-408 (W.D. Tex. filed July 2, 1987).

210. See *supra* note 101 and accompanying text.

211. See *First Wisconsin*, *supra* note 7. See *supra* note 71 and accompanying text.

212. 12 U.S.C. § 2607 (Supp. 1989). Section 8 of RESPA also prohibits a title insurance agency or underwriter from giving, and a mortgage lender from accepting, any thing of value — or any kickback — for the referral of title insurance business incident to a federally-related mortgage loan.

213. Congress added this list of steps through which lenders could avoid liability under the anti-kickback provisions in 1983 amendments to RESPA.

214. See 12 U.S.C. § 2607 (Supp. 1989).

215. See D. Cleasby, *Controlled Business Operations in the Title Insurance Industry*, REPORT TO THE COMMISSIONER OF INSURANCE, STATE OF WISCONSIN 5 (July 31, 1987).

loan officer or real estate broker to make the title insurance application for them.

Figures from a 1987 report to the Wisconsin Commissioner of Insurance bear this out.²¹⁶ In Montana, one title insurance company's market share increased from eleven to fifty-two percent in the first four years after a lender acquired it.²¹⁷ In Minnesota, the state's largest savings and loan acquired a majority interest in a title insurance company in 1979.²¹⁸ From April, 1979, to August, 1980, the amount of business referred to the title insurance company from the savings and loan increased from twelve percent to more than eighty-three percent. ALTA conducted a separate review of the mortgages recorded in seven counties in Minnesota in the first five months of 1988 which indicated that two savings banks, T.C.F. Savings Bank and First Minnesota Bank, had ninety-four percent and ninety-six percent of their mortgage transactions recorded by their respective captive title insurance agencies, North Star Title, Inc. and Warranty Title Company.²¹⁹

Besides the potential that consumers will be directed to a poorer quality, higher-priced title insurer, the report to the Wisconsin Insurance Commissioner predicted additional negative effects from even legal referrals by lenders to affiliated title insurers.²²⁰ First, a lender-affiliated title insurance company may inflate its prices above levels required by the market, since it is assured a steady flow of customers.²²¹ Second, lender control of title insurers may create reverse competition that drives prices up rather than down.²²² If a lender acquires a title insurance agency that begins to garner an increasing share of the market, title insurance underwriters will offer that agency greater incentives to channel business to them.²²³ These incentives must take the form of either higher commissions to the controlled title insurance agency or payment of the same commission to the agency for less work in searching, examining and clearing titles.²²⁴ Ultimately, purchasers and sellers of real estate would bear the cost through higher title insurance premiums or increased losses resulting from diminished attention to the title examination and elimination of risks.

An equally serious consequence of reverse competition is the potential failure of existing title insurance agencies which are not affiliated with banks or bank holding companies. As discussed above, the fixed costs of maintaining sophisticated title plants and training personnel to perform title searches and examinations are high. If lender-owned title insurance agencies are able

216. *Id.*

217. *Id.*

218. *Id.*

219. Letter to Michael J. O'Rourke, Board of Governors of the Federal Reserve System from Sheldon E. Hochberg, Counsel for the ALTA regarding Application of First Wisconsin Corporation to Acquire Milwaukee Title Insurance Service, Inc. at 15-16 (Aug. 19, 1988).

220. Cleasby, *supra* note 215, at 4. *Accord* G. Lawhun, *Who Changed the Relationship?*, 69 TITLE NEWS 22, 30 (July-Aug 1990).

221. *Id.*

222. *Id.*

223. *Id.*

224. Lawhun, *supra* note 220, at 30.

to monopolize a significant portion of the market, independent agencies will be forced to raise prices to cover fixed costs, forego computerization and other improvement of land title records, or close their doors.²²⁵ Title insurance agencies affiliated with lenders, on the other hand, will be insulated from competitive pressures in trying to obtain business because they can expect to receive a high percentage of referrals from the lenders.

The consequences of a lender's referring a homebuyer or auto buyer to an affiliated insurance agency for the initial policy purchase are not nearly so severe. If the insurer's service is poor or if the buyer learns later of lower-priced insurance, the buyer can cancel the policy at any time or change insurers when it is time to renew. The lender-owned homeowner's or auto insurance agent will thus have an incentive to keep prices and products competitive to earn insureds' renewal business. Furthermore, though independent insurers may have been foreclosed from obtaining the initial policy because of the lender's referral to its own insurer, they will not be foreclosed from competing for renewal business.

Conversely, independent title insurers have no renewal business for which they can compete. Instead of being based on term of coverage as are general classes of insurance, title insurance is a percentage of the value of the property interest insured, e.g., \$3.50 per thousand for an owner's policy and a smaller amount for a mortgagee's policy. The insured pays a single premium at the time the policy goes into effect. Payment of this one premium protects the insured throughout the entire time the insured owns an interest in the property, whether that period spans one month or fifty years. Thus, the only possible competition for title insurance business is at the time the mortgage loan is made and the property is purchased. As discussed above, since consumers do not expect to buy title insurance often and the price is not enough to create an incentive to shop around, they are likely to accept their lender's recommendation of a title insurer.²²⁶ Therefore, the lender-affiliated title insurer's competitive advantage and the adverse competitive consequences to independent title insurers are much greater than is the case with general insurers affiliated with banks or bank holding companies.

Several state legislatures have recognized and attempted to minimize the effects of reverse competition by limiting the amount of business a controlled title insurance agency can receive from its bank owner or sister-companies. California, Michigan, Colorado, Wyoming, Wisconsin, Utah, Nebraska, and Kansas statutorily limit the amount of business that title insurance agencies may receive from their bank owners or holding company affiliates to a small percentage of the agencies' gross operating revenues.²²⁷ The Model Title

225. Cleasby, *supra* note 215, at 5. See also Hofflander & Shulman, *The Distribution of Title Insurance: The Unregulated Intermediary*, 44 J. RISK & INS. 435, 440 (1977) for a discussion of the adverse impact of lender-controlled title insurers on the potential entry of new independent title insurance companies into the market.

226. See *supra* notes 215-19 and accompanying text.

227. California restricts controlled business to fifty percent, Michigan to fifteen percent, Colorado and Utah to thirty-three and a third percent, Wyoming to twenty-five percent, and Nebraska to 20 percent. Cleasby, *supra* note 215, at 5-6.

Insurance Code, promulgated by the National Association of Insurance Commissioners and recommended to state legislatures in 1982, contains a provision limiting a title insurance company's controlled business to no more than twenty percent of its gross operating revenues.²²⁸

The second potential conflict resulting from lenders controlling title insurers arises between the borrower's interest in obtaining clear title and the lender-controlled title insurer's interest in approving title so that the lender may acquire the loan transaction. The report to the Wisconsin Insurance Commissioner predicted that a title insurer affiliated with a lender would be influenced to approve issuance of a title policy despite the existence of a title defect, so as not to jeopardize the loan transaction.²²⁹ Some liens or encumbrances against property that do not concern mortgage lienholders may adversely affect the owner's use or enjoyment of the property. For example, as long as a lien is junior to the mortgage lien, the mortgage lender need not be concerned; however, such a lien could cause a loss to the purchaser. Similarly, a utility easement might not significantly affect the value of the lender's mortgage lien, but it would concern the property owner wishing to build a pool, garage or other improvement in that area. A lender acting as, owning, or affiliated with a title insurer may influence the insurer to issue the insurance policy upon a finding that the title is free of encumbrances and defects affecting the lender, without delaying the transaction to clear title defects that only affect the purchaser. The insurer could simply except from the policy's coverage any defects that do not affect the lender. Unsophisticated purchasers, such as many homebuyers, might rely upon a title insurance policy and close the transaction, unaware that exceptions to the policy subject them to risk.

A third potential conflict arises where a lender acts as or controls a local title insurance agency, in particular. The conflict exists between the lender-controlled title insurance agent's duty to minimize its underwriter's exposure and its interest in approving title so that the lender may secure the loan transaction. Generally, the local title insurance company, not the underwriter, owns the private title plant where the title company searches title as agent for the underwriter prior to issuance of the title insurance policy.²³⁰ Also, it is typically the local title insurance agent that examines the title chain and then determines whether to insure the title, whether to provide coverage for marketability, whether conveyance and mortgage documents are properly executed, and what liens, encumbrances and defects must be excepted from the policy's coverage. The local agency then issues the policy, according to its findings, in the underwriter's name. Thus, the title insurance agency is commonly the determiner of the risks which the underwriter assumes under each policy.²³¹

A bank holding company or bank that owns a title insurance agency may

228. *Id.*

229. *See* Cleasby, *supra* note 215, at 4.

230. *See supra* notes 198-203 and accompanying text.

231. *Id.*

be in a position to influence the agency's decisions regarding the policy coverage and exceptions. Absence of coverage for a particular type of encumbrance or title defect can result in either the real property purchaser or the mortgagee refusing to complete the underlying real estate transaction. Not uncommonly, a lender will approach the title insurance agency about eliminating a particular exception or insuring over a defect so that the bank can approve the loan and allow the deal to close. When the lender owns the title insurance agency or is a sister-company with the same bank holding company parent, the agent experiences more pressure to insure over the objectionable title defect and let the underwriter assume any risk of loss. However, a title insurance agent also owes contractual and fiduciary duties to minimize the exposure of the title insurance underwriter on whose behalf it issues policies. The agent is obligated by the agency agreement²³² to search the real property records and except from the policy's coverage any discovered defects that pose unreasonable risks to the underwriter.

The title insurance agency owned by a bank or bank holding company thus faces a conflict between its duty to limit the underwriter's exposure and its interest in giving the greatest scope of title insurance protection to the bank holding company or bank parent's mortgages and the ownership interests of their borrowers. This conflict is sharpened when a bank holding company or a bank itself acts as a title insurance agent. The mortgage lender that acts as agent for the issuance of policies insuring its own mortgage liens must choose between its own interest as an insured in obtaining the broadest possible coverage and its contractual and fiduciary obligations to minimize the risks its underwriter is exposed to under the policies issued.

These latter two conflicts do not exist when a bank holding company or bank controls an agency selling general lines of insurance. Such agencies essentially perform only a sales function and are not responsible for substantive judgments regarding the issuance of the policy and the risks the underwriter will assume.

In and of themselves, these three conflicts of interest would impact negatively upon the real estate buying public in terms of referrals to higher-priced or less service-oriented title insurers and decreased attention to clearing of title defects that do not affect the affiliated lender. However, lawmakers must also consider larger consequences, including (a) potential decline in the integrity of title insurance underwriting, (b) retrogression of title insurance's role as eliminator of risks in real estate transactions, (c) degeneration of our nation's real property records, (d) decreased availability of mortgage money throughout the United States, and (e) additions to the already huge number of failures of financial institutions which have occurred in recent years. The remainder of this article discusses these issues.

C. Decline in Integrity of Title Insurance Underwriting

As discussed above, a title insurer may find itself caught between the

232. An agency agreement is also known as an underwriting agreement.

lender's interest in completing the loan transaction with the broadest possible protection for itself, and the underwriter's interest in limiting its risks. If lender-controlled title insurers opt to resolve the conflict in favor of the lender by insuring over existing encumbrances or title defects and letting the underwriter bear the risks, the integrity of title insurance underwriting will likely decline.

In normal circumstances, a title insurance underwriter would, understandably, terminate its agency relationship with an agent that failed to maintain prudent underwriting standards. But where the title insurance agent is owned by a bank or bank holding company which has the capacity to direct a large portion of the region's title insurance business, the underwriter may reach a different conclusion; unless the underwriter is willing to forego access to a large portion of the market, it may continue to underwrite for the bank-affiliated agency. The consequent decline in the integrity of title insurance underwriting would increase the risk to title insurance underwriters and to insureds.²³³

D. *Deterioration of Title Insurance's Role as Eliminator of Risks*

Additionally, if a title insurance agent responds to a controlling lender's influence and insures over title defects, title insurance's most socially useful role as eliminator of risks in real property transactions will deteriorate.²³⁴ If indemnifying against losses from existing risks were the only role of title insurance, title insurance would be no more than casualty insurance.²³⁵ Purchasers and developers of real property require more than just indemnification from lost investments. They need to be able to obtain marketable title - a title sufficiently free from doubt and others' claims so that investors can expend time, labor and money improving and developing the property without fear of losing the property or losing the ability to resell it. Thus, title insurance must retain its role as discoverer and eliminator of encumbrances and title defects.

If it becomes common practice to insure over risks rather than to eliminate all apparent risks with each new transfer, many parcels of real property in the United States will likely become unmarketable.²³⁶ The ultimate con-

233. The insureds which would be affected by increased risk include purchasers of mortgage loans in the secondary mortgage market.

234. See *supra* note 229 and accompanying text. A lender may be satisfied with "insurable title", i.e., encumbrances or defects may exist in the title to the property which secures the lien, as long as the lender's title insurance policy covers the defects. The lender's interest is in recouping the amount loaned; whether repayment ultimately comes from the borrower, a sale of the real property collateral, or the title insurer if the lender's lien fails, is not critical.

235. *Id.*

236. See D.B. BURKE, *LAW OF TITLE INSURANCE*, 1-2 (1986) stating that:

Because of the permanent nature of land and real property, every parcel of land has a long, and perhaps even unique, history of transactions between persons who at one time held an interest in it. Each transaction may have involved a legal or equitable, possessory or nonpossessory, interest; each may have involved either the fee simple absolute to the land or some lesser interest. The possibility that any one of these types of interests might still exist at the time of the next transaction presents the danger that it might not be disclosed to the

sequence could be discouragement of home ownership and real property development.

Additionally, banks and bank holding companies might not be as willing as independent title insurance agencies have been to reinvest their profits toward improving title plant technology and training personnel for the labor-intensive task of examining titles to real property.²³⁷ Banks and bank holding companies' interest in acquiring title insurers began following real estate boom years and they seem to view title insurance companies as cash cows.²³⁸ Before bank regulators and lawmakers approve acquisitions of title insurers, they should determine whether banks and bank holding companies plan to divert returns to less-profitable subsidiaries or apply the profits as do independent title insurers to continued automation of land title records and improvement of title insurance's important risk elimination features. In particular, when banks or bank holding companies plan to enter the title insurance agency business *de novo*, rather than acquiring an existing title insurance agency, any plans to avoid large start-up costs and the difficulty of finding trained personnel by selling title insurance on a casualty basis should be disclosed. Commentators agree that issuance of title insurance on a casualty basis is not in the best interest of real property purchasers or of society as a whole.²³⁹

Unless banks and bank holding companies share independent title insurance companies' concerns with discovering and curing defects in land titles, there could be less emphasis on eliminating risks and greater willingness to insure titles on a casualty basis. Such a shift would not benefit society at large which requires stability of land titles to encourage investment in and development of real property.

E. Deterioration of Real Property Records

A significant consequence of reverse competition and any decrease in elimination of risks by lender-controlled title insurers is that some title insurers will fail. To the extent that independent title insurance companies survive, they will have to spread their high fixed costs over a revenue base

purchaser in that later transaction and that he or she might unknowingly take property that is subject to the pre-existing interest.

237. See *supra* notes 198-203 and accompanying text.

238. See generally Little, Morrow, Toft, & Wender, *Financial Services Deregulation: Title Insurance Implications*, 64 TITLE NEWS 17, 19 (Jan.-Feb. 1985).

239. See Johnstone, *supra* note 204, at 516 contending that:

If broadly applied, the typical casualty insurance approach to risk assumption could have a disastrous effect on titles. If title insurance generally were written on a risk basis only, without search or examination, there would be a gradual deterioration in the certainty of titles. It is the curative action taken by owners upon receiving examination reports from insurers that maintains the high degree of record title certainty of insured titles. Elimination of the search and examination would remove the basis for curative action, and as titles become more uncertain, losses would increase and insurance rates would go up.

In addition, Johnstone warned that "large title insurers with complete title plants are being threatened by low overhead insurers operating without title plants . . . on the casualty principle of risk assumption rather than on loss prevention." *Id.*

involving fewer transactions, thereby necessitating increased rates and/or decreased investment in the title plant technology required for reliable title searches. The danger to the public is that it will be deprived of the most efficient and accurate records on real property ownership available in their region. This danger, more than any other, supports legislation to prohibit bank and bank holding company control of title insurers.

F. Decreased Availability of Mortgage Money

Investors who purchase mortgage loans rely heavily on the validity and priority of the mortgage liens as determined by independent title insurance agents.²⁴⁰ Such investors have been willing to purchase mortgage loans on properties located outside of their primary bases of operation because of the security which a standard form of title protection provides.²⁴¹ This security comes from knowing that each mortgage lien was insured after a thorough title search and examination by professionals who reached independent conclusions about the validity of the underlying title as well as the priority and enforceability of the lien. This independence will be lost if a lender-controlled title insurer makes those determinations, since the lender possesses an interest in convincing purchasers of its loans that the mortgage liens securing them are enforceable.

Investors' confidence in the secondary mortgage market may erode with the knowledge that the lenders selling mortgage loans also control the entities that insure the mortgage's lien. Investors may have less assurance that their policies represent a true evaluation of the security provided by the insured parcel of real estate. Certainly, the conflicts of interest already discussed would undermine the objectivity and integrity of the title insurance underwriting process and the financial strength of underwriters and might generate adverse effects on the secondary mortgage market. If these conflicts cause investors to lose confidence in mortgages as an investment, the ultimate effect will be less money available for loans to the public for real estate purchases and development.

G. Bank Failures

Bank failures may both result from and cause the failure of title insurers they own. Expansion by thrift institutions into nontraditional activities without the necessary expertise recently has precipitated one of the greatest financial and regulatory disasters ever — the insolvency of a significant segment of the savings and loan industry and the bankruptcy of the Federal Savings and Loan Insurance Corporation. As banks and bank holding companies similarly seek to expand into nontraditional activities,²⁴² concern is

240. Obviously, if a lien is actually subordinate rather than primary, an investor stands a good chance of losing the investment, or a large portion thereof.

241. See *supra* notes 205-08 and accompanying text.

242. The OCC cited competitiveness with savings and loans as one of the reasons for permitting national banks to act as, or acquire, title insurance agencies. See *supra* notes 27-33 and accompanying text.

raised of potential similar disasters.

Banks and bank holding companies increase their risks by owning title insurers for several reasons. First, title insurance's profitability during real estate boom years piqued banks' interest in acquiring title insurers.²⁴³ However, the title insurance business is locked into the same cyclical swings as the real estate and mortgage lending industries.²⁴⁴ Permitting banks to sell title insurance or own title insurers only compounds the cyclical income problems experienced by banks.²⁴⁵

Second, the conflicts of interest that threaten the public, title insurance underwriters, and investors in the secondary mortgage market also threaten the banks and bank holding companies that act as or own title insurers. When the traditional independence between title insurers and the lenders they are insuring is lost, the real protection that title insurance is intended to provide is also lost. In deciding whether or not to approve loans, mortgage lenders should have independent assessments of the priority and enforceability of their mortgage liens.

Mortgage lenders also need for their loans to be acceptable to purchasers of mortgage loans in the secondary mortgage market. Mortgage lenders may be handicapped in that market when they insure their own loans. Additionally, any failures of existing title insurers because of inability to compete with lender-affiliated title insurers threatens banks and bank holding companies, since the industry presently insures billions of dollars of outstanding mortgage loans.²⁴⁶

Third, to the extent that one of a bank's primary goals in obtaining title insurance is to transfer the financial risks of title-related problems and losses to a third party, a serious question exists as to whether banks accomplish that goal when insuring their own mortgage loans with title insurance companies they own. The risk of loss may appear to be transferred as a formal matter, but the burden of loss still rests ultimately on the bank or the holding company parent.²⁴⁷ The bank does not actually obtain the financial security that title insurance is designed to provide when it does not transfer the economic consequences of the risks out of its corporate family.²⁴⁸

Banks insured by their own or affiliated title insurers could threaten the security that banks need from title insurance in a fourth way. When dealing with independent underwriters, banks continually review the quality of the underwriters' services, as well as their financial strength and stability in order to keep alert to conditions that might adversely affect the underwriters' ability to pay claims against the policies issued.²⁴⁹ When a bank owns or is

243. See *supra* note 238 and accompanying text.

244. Letter to Hoyle L. Robinson, FDIC Executive Secretary from Donald P. Kennedy, ALTA President regarding Advance Notice of Proposed Rulemaking Regarding Activities of Insured Banks, at 27 (Nov. 14, 1983) [hereinafter *Robinson Letter*].

245. *Id.*

246. *Id.*

247. R. Goshay, *Captive Insurance Companies*, in H. SNIDER, *RISK MANAGEMENT* 80, 85 (1964).

248. *Robinson Letter*, *supra* note 244, at 21-22.

249. *Id.* at 23.

affiliated with a title insurer, however, its review standards may loosen. In fact, financial difficulties of the affiliated title insurer may only strengthen the bank's incentive to refer business to the affiliate. If the bank has all or most of its mortgage liens insured with this one affiliate title insurer, the ultimate insolvency or failure of that insurer would have enormous adverse consequences on the security of the bank's mortgage loan portfolio.²⁵⁰

The risks to banks and bank-owned or operated title insurers are circular. If banks or bank holding companies do fail, for whatever reason, title insurance companies operated or owned by them also will be at risk. One of the specific reasons which the OCC gave for approving the issuance of title insurance by national banks was that title insurance companies operated as departments of banks from the 1870s until the Depression in the 1930s.²⁵¹ Ironically, the OCC admitted that it was the failure of so many banks during the Depression that prompted title insurers organizing thereafter to operate independently.²⁵² Yet, the OCC ignored the obvious concern for the public that future bank failures could again mean the failure of the underwriter that issued their title insurance policies or the unavailability of the local title insurance agency which owns the most reliable title plant in the locality. An independent title insurer's failure or the failure of a nonbanking corporation which owns a title insurer could raise the same concerns. However, few title insurance underwriters or agencies have failed since title insurers divorced themselves from bank ownership in the 1930s.

H. Conclusion

Because of title insurance companies' comparatively low loss ratios, bank holding companies and banks tend to view them as high-profit investments. The public has an interest in knowing whether banking entities are more interested in diverting those profits to less profitable subsidiaries than in applying them as do independent title insurers to continued automation of land title records and improvement of title insurance's important risk elimination features. Unless banks and bank holding companies share independent title insurance companies' concerns with curing defects in land titles, banks could place less emphasis on eliminating risks and move toward insuring titles on a casualty basis. This would not benefit society at large which requires stability of land titles to encourage investment in and development of real property.

The Board and the OCC cannot afford to overlook the fact that the use of title insurance enhances the safety and soundness of banks and bank holding companies by reducing the financial risks associated with mortgage lending activities. Yet these regulators fail to recognize that the soundness of both may be threatened when banking entities own title insurers. The quality of

250. *Id.*

251. See OCC Interpretive Letters No. 368 (July 11, 1986) and No. 377 (Feb. 6, 1987). See *supra* notes 31-33 and accompanying text.

252. *Id.*

real property records and the availability of money for home ownership and real property development in the United States is also threatened.

Since bank regulators continue to ignore public interest in applying existing laws, the nation's lawmakers must act. Congress must sever the consideration of banking institutions' involvement in the general insurance business from the transcendent issue of lenders acting as or owning title insurance underwriters and agencies. Lawmakers at all levels must appraise the possibility of (a) conflicts of interest, (b) decline in the integrity of title insurance underwriting, (c) retrogression of title insurers' role as eliminator of risks in real estate transactions, (d) deterioration of our nation's real property records, (e) decreased availability of mortgage money throughout the United States, and (f) additions to recent years' overwhelming number of financial institution failures. These potential effects of lenders acting as or owning title insurers warrant legislation to specifically and uniformly render underwriting and selling title insurance beyond the powers of bank holding companies, national and state banks, and all subsidiaries.