

TITLE INSURANCE - GOOD THING OR A SCAM?

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Title insurance is protection against any claims or legal costs that may arise when investigating a properties' ownership chain. Kolakowski and Henneberry examine the value of title insurance.

What do Abe Lincoln and some homeowners of today have in common?

They both have lost homes due to title defects.

Gail Pradelli, CRP, GMS, for First American Relocation Advantage, Plano, TX, shared that, "Abraham Lincoln's father lost two homes because he had the wrong kind of papers. It was the anxiety and outright losses of the Lincolns and other hardworking Americans that gave birth to the title industry in the late 1800s. There is a perception in the general public that title problems hardly ever happen when, in fact, one out of every three title searches reveals a problem."

Further Exploration

Any of us who have been involved in closing a home in relocation, or have purchased a home ourselves, in all likelihood have been handed a closing statement (HUD-1) that has detailed our expenses. On page two of that statement is a line item for title insurance. Most of us have paid for it, but few of us understand what it is that we just paid for.

Title insurance is the only insurance that is *retrospective* rather than *prospective*. Title insurance assures that you, as the buyer of the home, can enjoy your newly acquired property to its full benefit without the threat that someone will come along, ring your doorbell, and say, "Sorry, I was deeded this house 10 years ago and it's mine. Please leave."

Title insurance is bought on the basis that nothing in the past can affect your right in the property. Other types of insurance, such as health, life, and homeowner's, are bought on the premise that a future event (sickness, death, or a hail-damaged roof) is going to occur and that you will file a claim to recover some portion of your losses.

Most insurance types, other than title insurance, are paid by recurring premiums. That means that you continue to pay for the "future" event even if the event never occurs and you never file a claim. How many of us have paid homeowner's insurance for years and never have filed a claim? Title insurance, on the other hand, is a one-time premium that is paid for at the time of the closing of the property. The premium covers the cost of the search, the review, and the "insurance" to cover any problems that the title company may have missed.

Title companies will do a search of the records (county and taxing authorities) and review all the information that pertains to the property. By looking at the legal description and property address, the title company can ascertain who the prior owners were and determine how the chain of title came about (who deeded to whom). Mortgages, outstanding real estate taxes, potential judgments against the prior owner's, and any other matters will be reviewed carefully by the title examiner to determine whether any "clouds" or "defects" exist on the title. With the purchase of owner's title insurance, you will only have to worry about signing the mortgage documents and making those monthly payments.

Title insurance is broken into two separate components: the owner's policy and the lender's policy. As the two types indicate, the owner's policy protects the new owner's interest and the lender's policy protects the lender's lien position. If you get a mortgage on a property, the lender will require you to pay for a lender's title policy. The lender does not require that you pay for, and obtain, an owner's policy.

If something was missed on the search, and there is a subsequent claim for the property, the lender would be protected and the owner would be out in the cold unless an owner's policy was purchased. The information in the title search as disclosed by a title commitment is considered to be provided incidental to the policy process, and not in and of itself sufficient to be relied on by the new owner. It may be a rare case that an owner actually loses his or her home due to a title claim, but are you willing to risk everything for a few dollars?

An Extreme Example

To give an extreme example, one need only look at the mess that occurred as a result of the misappropriation of funds by the Erpenbeck Company, one of the leading builders in the greater Cincinnati, OH, area.

In 2002, an investigation was launched against the Erpenbeck Company as a result of scores of homeowners being served notices that they were about to lose their homes because of liens. Bill Erpenbeck diverted millions of dollars from closing to his own accounts and did not pay contractors and mortgage companies. The end result was approximately 132 homeowners being stung with liens against their homes.

As a result of this scandal, the Cincinnati-area title agents say 20 to 50 percent of all purchases are now sold with an owner's policy. Prior to this, most homebuyers only paid for the lender's policy. In 2002, the Cincinnati Area Board of Realtors approved language changes to standard contracts. The new language stresses that the lender's title insurance does not protect homebuyers; rather, homebuyers should look at the benefits of title insurance. As a result of this change, the contracts in use now call for the buyer to initial the paragraph explaining the role of title insurance.

Although this is an extraordinary case, homebuyer's who paid for owner's title insurance were able to look to the title company to protect their interests. They avoided the costs, both emotional and in dollars, of having to defend their biggest investment.

"There is a perception that title insurance costs too much," said Pradelli, "however, title insurance has steadily declined over the last decade. Further, the one-time fee, based on the price of the home, protects the homeowner and heirs for as long as they own the home."

John C. Morreale, president of Morreale Real Estate Services, Glen Ellyn, IL, said, "Relocation is such a stressful time for the entire family. The last thing a transferee needs to hear is that there is a title problem... We have had moves delayed for 60 to 90 days due to title defects that needed clearance. The delays could have been avoided by an owner's title insurance policy."

Corporations may want to look at encouraging their employees to negotiate an owner's policy at the time of buying a home when being transferred. This serves two purposes: one, the transferee will be protected and two, should the transferee be moved in the future, the chances that a title problem will be the reason that the move is disrupted will be minimized.

Although it may be customary for a buyer to pay for the owner's policy, everything in a contract is negotiable. For the protection of its employees, even if a seller will not agree to pay for the cost, a corporation may wish to encourage its employees to purchase title insurance to protect these major assets - their homes.

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Family Crime: The Erpenbeck Saga

You should always be careful when picking your business partners, especially when you choose your own blood.

In April 2003, Bill Erpenbeck, founder and former president of the now-defunct homebuilder Erpenbeck Company, pled guilty to charges of bank fraud manifesting from an attempt to defraud lenders that funded the company's building projects - however, Erpenbeck did not realize in doing so that he was jeopardizing the actual ownership of the houses. In July 2003, Lori Erpenbeck, head of accounting for the company, also pled to bank fraud - according to brother Bill, she was the brains behind the scheme, which she vehemently denied. Father Tony Erpenbeck joined his son in pleading guilty to obstruction of justice charges stemming from trying to pressure Lori into taking the rap for the fraud. Thanksgiving dinners in that family will be awfully tense - as soon as they all get out of prison.

The Erpenbeck Company was formed in 1991 and by the end of the decade was the third-largest homebuilder in the greater Cincinnati. However, while business had nearly reached \$100 million in sales, debt was piling up faster. One day in 1999, when handed a check for nearly \$75,000 made out to Peoples Bank of Northern Kentucky, which had financed the construction of a house, an Erpenbeck Company representative took it back to headquarters, where it was deposited in a company business account. This practice became habitual.

At first, the company stole little - only three checks to lenders were pinched in 1999. However, that sprouted to 120 in 2000, and another 100 in 2001 - many of these checks were for hundreds of thousands of dollars. The missing closing checks did not go completely unnoticed - Bill Erpenbeck would check with accounting and make small payoffs whenever lenders would make noise. The scam was supposed to be a short-term fix - a bandage for ballooning costs.

However, the market downturn after the September 11, 2001, terrorist attacks made it impossible for the Erpenbeck Company to climb out of the hole. By 2002, when the company began being investigated, \$34 million had been stolen from lenders through hundreds of closing checks.

What the Erpenbeck family had not considered was that if the loans were defaulted, the banks would respond by seizing the homes built with the funds. Thus, 260 homeowners were thrown into jeopardy, along with dozens of subcontractors. The Erpenbeck Company's scam is even considered the chief reason why Peoples Bank of Northern Kentucky was sold. Two bank executives were given prison terms for assisting bank fraud as they attempted to help the Erpenbeck Company afloat.

But as the investigations mounted and the scandal came to light, the proceedings turned bizarre. Lori Erpenbeck, who pled guilty to being involved in the scheme, wore an eavesdropping device while meeting with her father, Tony, who pressured her one too many times to concede she had concocted the scam. Lori also admitted she had embezzled \$50,000 from the company. Before Tony was sentenced for obstruction of justice, the judge and his family were given a security detail after a death threat from the Tony.

In the end, all liens between the banks and homeowners were worked out - through some toil. Two hundred and eleven homeowners joined a civil class-action suit against the Erpenbeck company. Erpenbeck headlines showered the local papers for years while the scandal played out. A parody song titled, "Bye, Bye, Mr. Erpenbeck Guy," sung to the tune of "American Pie" by Don MacLean, appeared on the Internet. Lori Erpenbeck was handed a one-year jail sentence, while Tony received six years and two months. However, it was Bill who got the hard, hard time - 30 years in prison.