

# STROOCK SPECIAL BULLETIN

## Title Insurance: Is the Sky the Limit?

*April 24, 2018*

One Billion, Six Hundred and Fifty Million (\$1,650,000,000) Dollars. This enormous sum was the purchase price for a trophy office building on Avenue of the Americas, a sale Stroock & Stroock & Lavan LLP closed in May, 2016, on behalf of one of its clients, as the 50% owner in this property. Although this sale was in the top ten single property sales nationwide, it was still only the third largest single building sale in New York City in 2016.

In 2017, the sale and purchase numbers continued to rise. The largest single property sale reported in New York City in 2017 was the sale of 245 Park Avenue, for a purchase price of \$2,210,000,000. As 2018 begins and with real estate values at these astronomical levels, with no ceiling in sight for trophy New York City assets, this is a propitious time to step back and analyze the financial capability of the major title insurance companies to provide title insurance in New York on large-liability owner and lender title policies.

### STATE REGULATION

The title insurance industry in New York is regulated by the New York State Department of Financial Services (the “DFS”). New York State Insurance Law mandates that title insurance companies limit the dollar amount of title insurance risk they insure on any single risk (the “DFS Maximum Risk”) to the “sum of its capital, surplus, statutory premium and any voluntary reserves”. The determination of the DFS Maximum Risk requires reference to the title companies’ annual financial statements (the

“Form 9”) which are filed with the DFS on a calendar year basis, and updated on a quarterly basis throughout the calendar year.

“Capital” has no statutory definition but representatives of four (4) of the New York title companies listed below advised us that in their view, “capital” refers to “Common Capital Stock” and is reported on line 25 of the “Liabilities, Surplus and Other Funds” page of the Form 9.

“Surplus” is the “Surplus as Regards Policyholders” which is reported on line 32 on the “Liabilities, Surplus and Other Funds” page of the Form 9.

“Statutory premium” is the “statutory premium reserve” reported on line 2 on the “Liabilities, Surplus and Other Funds” page of the Form 9.

The term “voluntary reserves” is not defined in the statute but in the Form 9, generally referred to as “Supplemental Reserve”. By and large, title companies operating in New York do not fund the Supplemental Reserve.

Based upon our review of the annual Form 9 statements for the year ended December 31, 2017 filed with DFS, a sampling of a number of New York title insurance companies, reveal the following DFS Maximum Risk numbers:

<u>Company</u>	<u>DFS Maximum Risk Number</u>
First American Title:	\$2,477,005,463
Chicago Title:	\$1,569,886,461
Old Republic National Title:	\$1,032,390,782
Fidelity National Title:	\$965,508,791
Commonwealth Land Title:	\$566,428,476
Stewart Title Insurance Company of New York:	\$109,927,946
AmTrust Title:	\$23,524,810

## INTERNAL COMPANY LIMITS; REINSURANCE

Notwithstanding the Insurance Law and the DFS Maximum Risk, each of the major title insurers self-impose maximum risk limits on any one transaction. These self-imposed maximum risk limits are typically based on two factors: (1) the amount of the company's "Surplus as Regards Policyholders", and (2) Reinsurance within the title company family and/or Parent Company Guarantees.

In order to enable title insurers to spread their insurance risk, and reduce their liability in the event of a title claim, title companies often enter into reinsurance agreements. A reinsurance agreement is a contract between the company that issues the policy, known as the "Ceder," and the company that agrees to indemnify the Ceder if there is a loss under the applicable title policy, known as the "Reinsurer." Often, the Ceder retains primary liability for a certain dollar amount, for which its liability is 100%, and the Reinsurer will accept secondary level liability for the remaining amount. In large liability transactions, the slicing and dicing of liability also extends to additional Reinsurers who will take on tertiary and quaternary liability, and, both the Ceder and the Reinsurers may take multiple levels of liability; for example, the Ceder may agree, in addition to its primary liability, to be liable for limited amounts of secondary and/or tertiary liability, and a Reinsurer may agree to accept designated portions of liability at the secondary, tertiary and quaternary liability levels.

Reinsurance is generally effected through three (3) methods: (1) Facultative Reinsurance treaties with

third-party reinsurers, (2) Reinsurance within a family of related title insurance companies, or with a parent title insurance company, and (3) Reinsurance through an affiliate reinsurance company.

Reinsurance through treaties with third-party reinsurers, and the amounts and splits of primary, secondary and tertiary liability is often effected by the Ceder without disclosure to the insured. An insured that is unaware of the identity of the Reinsurer and the liability splits will be unable to measure the risk of a Reinsurer failure in the event of a major title claim. Prudence and best practices dictate that in large liability transactions, real estate attorneys should be asking the primary insurers for the identity of their Reinsurers and for the liability splits in order to assess the risk involved with Reinsurance. To the extent the Reinsurer is one of the large reinsurers such as Munich Re, Swiss Re and General Re, the insured will have access to their financial statements and can draw comfort from their underlying financial strength.

A prime example of method two, reinsurance within the "Family," is Chicago Title, Fidelity and Commonwealth, all of which are owned by Fidelity National Title Group. Reinsuring within this "Family" will have a multiplying effect on the amount of maximum risk limits of any of these three (3) companies; in essence, each of Chicago Title, Fidelity and Commonwealth, through reinsuring within the "Family," can issue title insurance on any one transaction in the maximum amount of \$1,444,300,000.

Another example of method two is Stewart Title Insurance Company of New York ("Stewart Title NY"). Stewart Title NY is a wholly-owned subsidiary of Stewart Title Guaranty Company of Texas ("Stewart Title Guaranty"). For any single maximum liability in excess of Stewart Title NY's maximum liability limit, Stewart Title NY automatically reinsures with Stewart Title Guaranty for up to \$300,000,000.

An example of method three, reinsuring through an affiliate, is utilized by AmTrust Title. We have been advised by AmTrust Title that as a matter of company policy, for every title policy AmTrust

Title writes, an affiliate, AmTrust International Insurance, Ltd. (“AAIL”), a Bermuda-based international reinsurance company, having 1.9 billion dollars of surplus capital, automatically reinsures the liability risk for up to \$523,000,000. This reinsurance is effected through an intra-company reinsurance treaty, which was reviewed and approved by DFS in 2016. The AAIL/AmTrust Title reinsurance treaty provides that AmTrust Title, as Ceder, retains \$2,000,000 of primary liability and AAIL, as Reinsurer, reinsures each transaction for up to \$523,000,000. AAIL is a wholly owned subsidiary of AmTrust Financial Services Inc. (“AFSI”), a multinational insurance company. AFSI is a publicly traded company on the Nasdaq Exchange having in excess of 22 billion dollars in assets.

Representatives of the title companies listed below have advised us that their self-imposed single transaction maximum liability limits are as follows:

<u>Company</u>	<u>Self-imposed Maximum Liability Limit</u>
First American Title:	\$1,669,685,210
Chicago Title:	\$621,000,000 <sup>1</sup>
Fidelity National Title:	\$466,500,000 <sup>1</sup>
Commonwealth Land Title:	\$356,800,000 <sup>1</sup>
AmTrust Title:	\$525,000,000 <sup>2</sup>
Old Republic National Title:	[will not release this information]
Stewart Title Insurance:	\$300,000,000 <sup>3</sup>

## FINANCIAL ANALYSIS AND RATING AGENCIES

In addition to analyzing the DFS Maximum Risk and the Self-imposed Maximum Liability Limit,

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- <sup>1</sup> Chicago Title, Fidelity National Title and Commonwealth Title will reinsure within the Fidelity Family for any single transaction maximum liability in excess of the individual company’s self-imposed maximum liability limit.
  - <sup>2</sup> AmTrust Title will automatically reinsure with its affiliate, AAIL, for every single transaction in excess of \$2,000,000.
  - <sup>3</sup> Stewart Title NY will automatically reinsure with its parent company, Stewart Title Guaranty, for any single transaction up to a maximum liability of \$300,000,000.

real estate attorneys working on large liability transactions should periodically review the title companies’ annual Form 9 financial statements and quarterly statements, all of which are filed with DFS and are matters of public record. Moreover, a number of the major rating agencies, such as A.M. Best, Moody’s, S&P, Fitch, Duff & Phelps, and Demotech, issue ratings on many of the title companies, and should be consulted as part of a comprehensive review of a title company’s financial strength and outlook.

The underlying financial data used herein was gleaned from the title companies’ Form-9’s and quarterly statements, which can become outdated each quarter. Stroock & Stroock & Lavan LLP makes no representation and warranty regarding the accuracy of the reported financial information, and disclaims any obligation to update any of this information for any reason. In addition, the Self-imposed Maximum Liability Limits set forth above were provided by representatives of the applicable title company and should be confirmed periodically as these limits will no doubt change from time to time. Title company policy with regard to reinsurance within the title company “Family” and or parent guarantees may also change from time to time and should be confirmed directly with the applicable title company.

In sum, given the enormous market values of current New York City transactions, turning a blind eye to title company financial capability, or lack thereof, and merely relying on historical usage is short sighted. The real estate debacle of 2008 to 2010 and its deleterious impact on the title company industry, is too fresh to be ignored. There is a wealth of public information available regarding title company financial strength; prudence and best practices dictate that real estate counsel utilize all available resources to construct the title insurance coverage that best protects the economic interest of the client.

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### For More Information

Steven Horowitz  
212-806-6614  
shorowitz@stroock.com

Zachary Perron  
212-806-5621  
zperron@stroock.com

New York

180 Maiden Lane  
New York, NY 10038-4982  
Tel: 212.806.5400  
Fax: 212.806.6006

Los Angeles

2029 Century Park East  
Los Angeles, CA 90067-3086  
Tel: 310.556.5800  
Fax: 310.556.5959

Miami

Southeast Financial Center  
200 South Biscayne Boulevard, Suite 3100  
Miami, FL 33131-5323  
Tel: 305.358.9900  
Fax: 305.789.9302

Washington, DC

1875 K Street NW, Suite 800  
Washington, DC 20006-1253  
Tel: 202.739.2800  
Fax: 202.739.2895

[www.stroock.com](http://www.stroock.com)

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