



SUTTON ALLIANCE LLC

MEMORANDUM - LEGAL SERVICES UPDATE

From: Howard J. Kopel
Date: June 15, 2006
Subject: 15% Owners Title Insurance Rate Decrease (New York)
Effective June 15, 2006 for Owners Policies less than \$1,000,000

The title insurance world has seen considerable turmoil in the past several weeks and months. We at Sutton Alliance believe that it is important for our clients and friends to know what exactly is going on, how it affects your respective practices and business, and what, if anything, needs to be done.

Attorney General Spitzer Investigation

The New York Attorney General's office (the "AG") has for about the past year and a half been conducting an investigation into various title insurance market practices. This investigation has involved all the major title insurance underwriting companies, as well as some agents. While we are unable to specify with certainty all the areas targeted by this investigation, several have clearly become areas of intense interest. We are able to provide this information due to the occurrence of a number of events that have already been covered in various publications, and have been the subject of announcements by the AG. These events have included settlements reached by the AG and (so far) First American Title Insurance Company of New York and Fidelity National Title Insurance Company, as well as a wave of subpoenas recently served upon numerous title insurance agencies throughout New York State. It is known that some of the other major underwriters are in various stages of discussion with the AG's office with additional enforcement actions and/or settlements in the offing.

Kickbacks of title insurance premiums

The settlements reached by the AG with each of First American and Fidelity are in the form of executed documents called "Assurance of Discontinuance" (sometimes referred to as the "Settlement.") These settlements contain a recitation of allegations by the AG, not admitted by First American or Fidelity, that these companies have been engaged in various forms of inappropriate rebating of premiums to purchasers of title insurance, or to parties related to the purchasers that had not earned these sums in accordance with the law. Such activities would, if proved, violate Insurance Law Section 6409(d), which provides that:

No title insurance corporation or any other person acting for or on behalf of it, shall make any rebate or any portion of the fee, premium or charge made, or pay or give to any applicant for insurance, or to any person, firm, or corporation acting as agent, representative, attorney, or employee of the prospective owner, lessee, or mortgagee of the real property or any interest therein, either directly or indirectly, any commission, any part of its fees or charges, or any other consideration or valuable thing, as an inducement for, or as compensation for, any title insurance business.

Fidelity and First American have agreed to settle these allegations by:

- paying a penalty of \$2,000,000.00 each;
- temporarily reducing certain rates on lower end (up to \$1,000,000.00) title insurance policies for purchasers only;
- establishing consumer websites allowing rates to be independently checked;
- refraining from imposing certain “add-ons;” and
- monitoring certain of these activities by their agents.

Copies of both the Fidelity and First American Settlements are available on the AG website at http://www.oag.state.ny.us/press/2006/may/may23a_06.html. It is widely expected that other major companies will agree to similar concessions as contained in the Fidelity and First American Settlements, whether as the result of pressure from the AG or simply out of competitive pressures. The New York State Department of Insurance is, moreover, expected to conduct hearings within several months to consider a new permanent rate structure.

Subpoenas to Title Agencies

Approximately 80 agencies throughout the state (including Sutton Land Services, LLC) have received subpoenas from the AG for information relating to costs incurred for, and pricing of, certain services and information products commonly provided to consumers, ancillary to the issuance of title insurance. No indication is given as to whether any further action is contemplated, or if this is informational in nature, and part of the larger, ongoing investigation.

RESPA and other, State Regulator, Activity

As is often the case - geographically speaking - with respect to trends both real estate-related and otherwise, there has been increasingly skeptical scrutiny of the real estate, mortgage, settlement (closings) and title insurance industries sweeping the country starting on the West Coast and moving steadily eastward. The AG’s investigation should be seen as constituting a part, but not necessarily representing the entirety, of that scrutiny. For one instance relating to title, the California Insurance Commissioner has issued a report that contends that there is a lack of true competition for title insurance consumers and that such competition as does exist is for people in a position to refer title insurance business of others, and not always for motives that were purely the best interests of the person paying for the insurance. Another targeted practice is splitting of premiums that is not related to real work performed. This has led to allegations that reinsurance treaties and joint ventures are often shams, intended merely as covers for referral fees, resulting in the imposition of hefty fines and even criminal charges. We have not seen any of these allegations made with respect to New York - yet. However, we cannot predict the future.

Besides the increasingly heated regulatory environment already existing, there have been articles in various publications, including the New York Law Journal suggesting that other enforcement actions, both governmental and otherwise, may be available and are being considered by various parties.

Future Regulatory Activity

Clearly, we at Sutton Alliance are not confidants of any regulatory authorities and are not privy to their plans and thoughts. However, it seems fair to say that we can expect continued - or even increased - scrutiny of industry business practices. This is an outgrowth of public pressure to reduce costs to the consumer generally and the considerable focus that we see on corporate misbehavior (Enron, Tyco, etc.). Areas of particular concern of which we are aware include the ethical treatment of consumers in charging for items such as departmental, bankruptcy, and Patriot Act searches and continued inquiry into illegal activities along the lines being pursued in other jurisdictions, as described above.

Effect on Consumers of Title Insurance

Hopefully, this is all good news! Some title insurance rates will be lower, at least for the time being. You or your clients should look forward to a market less distorted by factors not directly related to getting a deal done competently and expeditiously. We at Sutton Alliance strive to achieve an ethical and professional relationship with all our valued clients. In this connection we draw your attention to the following principles:

- Kickbacks of title insurance premiums are illegal under numerous federal and state laws. That is not to say there are not valid and proper payments to third parties under the law. If, for example, there is a properly conceived and operated joint venture company, distributions to the companies would not be kickbacks. Similarly, work and fees shared among companies for core title services performed by each of the companies may be altogether proper and even sensible. However, be sure that you, or your clients, are in compliance.
- Title insurance premiums in most states, including New York, are fixed by statutory or regulatory action, and deviation is not permitted. An ethical title insurance provider will work with you to ensure that the most advantageous rates are made available to fit a given deal. Moreover, a competent legal staff can often help structure a deal with a view to legally and properly minimizing transactional taxes and other costs.
- It is illegal in New York (and many other states) to insist on the use of any particular title insurance company or agent as a condition of making a mortgage loan of any type. (Banking Law, Section 595(a) and Insurance Law, Section 2502(a)(2).) Do not attempt to make any such requirement when making a loan for your company, or on behalf of a client. Sutton Alliance will not knowingly cooperate in any such forced designation of our company to serve as agent.
- Ask lots of questions! We will be happy to meet with you to discuss any questions or issues that you might have and to seek our outside counsel's advice where appropriate.

Final Thoughts

We at Sutton Alliance are committed to providing the highest quality professional service, at the price that is the best available to our clients, taking into account our clients' individual needs and preferences. We believe that turmoil, as uncomfortable as it may sometimes be, creates opportunity. We want to work with each and every one of our valued clients to ensure that your needs and those of your clients are met in a manner consistent with the high professional and ethical standards.