

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: Banking and Insurance Committee

BILL: CS/SB 638

SPONSOR: Banking and Insurance Committee and Senator Wise

SUBJECT: Title Insurance

DATE: March 29, 2005

REVISED: _____

| | ANALYST | STAFF DIRECTOR | REFERENCE | ACTION |
|----|----------------|--------------------|-----------|---------------|
| 1. | <u>Knudson</u> | <u>Deffenbaugh</u> | <u>BI</u> | <u>Fav/CS</u> |
| 2. | _____ | _____ | <u>JU</u> | _____ |
| 3. | _____ | _____ | <u>RC</u> | _____ |
| 4. | _____ | _____ | _____ | _____ |
| 5. | _____ | _____ | _____ | _____ |
| 6. | _____ | _____ | _____ | _____ |

I. Summary:

The Committee Substitute for Senate Bill 638 authorizes the issuance of personal property title insurance policies for Uniform Commercial Code (UCC) transactions under Article 9 of the Revised UCC. The insurance product will be available for sale in conjunction with a transaction involving a UCC security interest. It is designed to insure against challenges to attachment, perfection, and priority (such as fraud, filing office errors, inaccuracies in a search report, and errors in documentation and perfection) and provides for the defense of the insured lender if a claim is made regarding the lender's collateral position. The product also provides "gap" coverage to insure the time between the closing/loan funding and the date of the most current data filed on a UCC security interest, increasing interest accruals for the lender by allowing credit to be fully funded at closing.

The legislation will allow a title insurer to sell UCC personal property insurance, but would disallow a property and casualty insurer from selling the product because of the title insurance monoline statute contained in s. 627.786, F.S., which prohibits an insurer from selling both title insurance and any other kind of insurance in Florida. An exception to this rule is contained in section 4 of the bill, which allows the sale of the property and casualty product until the form and rates for the title insurance product are approved by the Office of Insurance Regulation (OIR). The OIR has identified five property and casualty insurance companies that are licensed to sell a similar product that covers personal property, with two of the insurers currently having policies in force in Florida.

This committee substitute substantially amends the following sections of the Florida Statutes: 624.308, 627.7711, and 627.7845.

II. Present Situation:

Background on Article 9 of the Uniform Commercial Code (by the National Conference of Commissioners on Uniform Laws):

The Uniform Commercial Code has eleven substantive articles. Article 9, Secured Transactions, may be the most important of the eleven. Article 9 provides the rules governing any transaction (other than a finance lease) that couples a debt with a creditor's interest in a debtor's personal property. If the debtor defaults, the creditor may repossess and sell the property (generally called collateral) to satisfy the debt. The creditor's interest is called a "security interest." Article 9 also covers certain kinds of sales that look like a grant of a security interest. In the 2001 legislative session, the Revised Article 9 of the Uniform Commercial Code, as prepared by the National Conference of Commissioners on Uniform State Laws, with Florida modifications, passed and was subsequently enacted into law as Chapter 2001-198, L.O.F.

Article 9 operates using two key concepts: "attachment" and "perfection." These terms describe the two key events in the creation of a "security interest." Attachment generally occurs when the security interest is effective between the creditor and the debtor, and that usually happens when their agreement provides that it take place. Perfection occurs when the creditor establishes his or her "priority" in relation to other creditors of the debtor in the same collateral. The creditor with "priority" may use the collateral to satisfy the debtor's obligation when the debtor defaults before other creditors subsequent in priority may do so. Perfection occurs usually when a "financing statement" is filed in the appropriate public record. Generally, the first to file has the first priority, and so on.

Article 9 relies on the public record because it provides the means for creditors to determine if there is any security interest that precedes theirs--a notice function. A subsequent secured creditor cannot complain that his or her grant of credit was made in ignorance of the prior security interests easily found in the public record, and cannot complain of the priority of the prior interests as a result. Every secured creditor has a priority over any unsecured creditor.

The somewhat simple description in the prior paragraphs should not mislead anyone. Article 9 is not simple. There are substantial exceptions to the above-stated perfection rule. For example, filing is not the only method for perfection. Much depends upon the kind of property that is collateral. Possession of collateral by the secured party is an alternative method of perfection for many kinds of collateral. For some kinds of property, control (a defined term) either perfects the interest or provides a better priority than filing does. There are kinds of transactions for which attachment is perfection. Priority is, also, not always a matter of perfecting a security interest first in time.

The revision of Article 9 enacted by the Legislature expanded the types of property in which a security interest can be taken by a creditor as well as the kinds of transactions that are covered by that part of the UCC. Sales of payment intangibles and promissory notes, security interests created by governmental debtors, health insurance receivables, consignments and commercial tort claims were all added as collateral that could be used as a creditor for a security interest. Revised Article 9 also clarified that filing a financial statement perfects a security interest. It changed the choice of law in interstate secured transactions from the state where collateral is

located to the state where the debtor is located. A centralized filing system for financing statements was required (one central location in each state) and provided for the electronic filing of documents. The revised Article 9 contains a clearer distinction between consumer transactions. Finally, Article 9 created new rules for some of the new kinds of property subject to security interests, new rules for the interests of subordinate creditors with security interests in the same property, and new rules for enforcement when the debtor is a consumer debtor. All 50 states have enacted Revised Article 9 of the Uniform Commercial Code.

Title Insurance

Title insurance is defined by s. 624.608, F.S., as “insurance of owners of real property or others having an interest in real property or contractual interest derived therefrom, or liens or encumbrances on real property, against loss by encumbrance, or defective titles, or invalidity, or adverse claim to title.” Put simply, title is the formal right of ownership of property.¹ Title insurance is a policy issued by a title insurer that, after performing a search of the title, represents the state of that title and insuring the accuracy of its search against claims of title defects.² The title insurer keeps complete sets of abstracts or duplicates of the records and employs title-examiners to complete its task. Title insurance is usually taken out by the purchaser of property or an entity that is loaning money on a mortgage. That entity is attempting to establish that title is “clear”—the property is free from incumbrances,³ “good”—the property is free from litigation,⁴ palpable defects, and grave doubts, “marketable”—title is willing to be accepted in ordinary business practice,⁵ and merchantable⁶—title is clear and will enable the owner to hold the property in peace and sell it.

In Florida, purchasers of real property and lenders utilize title insurance to protect them against claims by others that they are the rightful owner of the property. Most lenders require title insurance when they underwrite loans for real property. Title insurance provides a duty to defend related to an adverse claim against title, and also promises to indemnify the policyholder for damage to the lender’s security interest created by a cloud on title, unmarketable title, or adverse title that was not discovered by the title insurer.

Uniform Commercial Code Article 9 Personal Property “Title” Insurance

Florida law does not authorize the sale of title insurance for personal property. Although revised Article 9 of the UCC authorizes “title insurance” on personal property, such insurance is different in scope than title insurance on real property. Article 9 title insurance insures the attachment⁷, perfection⁸, and priority of security interest⁹ in personal property, but does not

¹ DELUXE BLACK’S LAW DICTIONARY 1485 (6th Ed. 1990).

² DELUXE BLACK’S LAW DICTIONARY 806 (6th Ed. 1990).

³ DELUXE BLACK’S LAW DICTIONARY 1485 (6th Ed. 1990).

⁴ See fn. 4.

⁵ DELUXE BLACK’S LAW DICTIONARY 970 (6th Ed. 1990).

⁶ DELUXE BLACK’S LAW DICTIONARY 987 (6th Ed. 1990).

⁷ DELUXE BLACK’S LAW DICTIONARY 126 (6th Ed. 1990). Whether property may be seized by the creditor.

⁸ DELUXE BLACK’S LAW DICTIONARY 1137 (6th Ed. 1990). In connection with a security interest, the secured party has done what is necessary to give notice to make a security interest effective against lien creditors of the debtor.

⁹ See U.C.C. Art 1-201. Security interest is defined as “an interest in personal property or fixtures which secures payment or performance of an obligation.”

guarantee the actual ownership of the property. UCC Article 9 insurance is used in transactions involving a UCC security interest and is utilized for various asset based loans including multiple advance and revolving credit facilities, asset securitizations, syndications and mezzanine loans. UCC personal property insurance also provides for the defense of the insured lender if a claim is made with regard to the insured's security interest in personal property, and also insures against losses suffered by the policyholder. Twenty-eight states have authorized the sale of UCC personal property insurance under that state's title statute, including California, New York, Illinois, and Maryland.

Currently, verifying the availability of personal property to be used as collateral for a loan is often done via a personal property lien search and retrieval that is used by an attorney in providing a priority legal opinion explaining the condition of title for a loan.

Under current Florida law, this type of insurance on the security interest personal property can be sold by an authorized property and casualty insurer, but not a title insurer. Florida is a "monoline" title insurance state, meaning that an insurer that transacts title insurance cannot sell other kind of insurance in Florida.¹⁰ Because insurance on the security interest in personal property is not included within the definition of title insurance contained in s. 624.608, F.S., such insurance cannot be sold according to the monoline statute. Representatives from the Office of Insurance Regulation have identified five property and casualty insurance companies that are licensed to sell a similar product that covers personal property, but only two of the insurers currently have policies in force in Florida.

III. Effect of Proposed Changes:

Section 1. Amends the definition of "title insurance" contained in s. 624.608, F.S., to include insurance of owners and secured parties regarding the existence, attachment, perfection, and priority of security interests under Article 9 of the UCC. This will allow a title insurer to sell UCC personal property insurance, but would disallow a property and casualty insurer from selling the product because of the title insurance monoline statute contained in s. 627.786, F.S., which prohibits an insurer from selling both title insurance and any other kind of insurance in Florida. An exception to this rule is contained in section 4 of the bill, which will allow the sale of the property and casualty product until the form and rates for the title insurance product are approved by the Office of Insurance Regulation.

The insurance product will available for sale in conjunction with a transaction involving a UCC security interest. It is designed to insure against challenges to attachment, perfection, and priority (such as fraud, filing office errors, inaccuracies in a search report, and errors in documentation and perfection) and provides for the defense of the insured lender if a claim is made regarding the lender's collateral position. The product also provides "gap" coverage to insure the time between the closing/loan funding and the date of the most current data filed on a UCC security interest, increasing interest accruals for the lender by allowing credit to be fully funded at closing.

¹⁰ s. 627.786, F.S.

Section 2. The definition of “related title services” contained in s. 627.7711, F.S., is changed to include examining searches of the records of a UCC filing office and other necessary information. The bill also amends the definition of “primary title services” to include determining insurability after a search and evaluation of a UCC filing office and other necessary information.

Section 3. Amends s. 627.7845, F.S., to prohibit a title insurer from issuing a title insurance commitment, endorsement, or policy (for personal property) until the title insurer has made a reasonable search and examination of the records of a UCC filing office, as applicable. The title insurer must also examine other information as is necessary and must make a determination of insurability of title or the existence, attachments, perfection and priority of the UCC security interest, including endorsement coverage, in accordance with sound underwriting practices. The title insurer must preserve and retain for 7 years evidence of its search and examination of the records of a UCC filing office.

Section 4. States that once the bill is effective (July 1, 2005), any policy form for insurance that qualifies as title insurance under s. 624.608(2), F.S.—which includes Article 9 UCC personal property title insurance within the definition of “title insurance”—that has been previously approved by the OIR as property and casualty insurance may continue to be sold by that insurer until:

1. The OIR approves the title insurance form provided for in s. 624.608(2), F.S., and
2. The Financial Services Commission approves a corresponding rule for rates for the form.

Once both requirements occur, the property and casualty insurance form may no longer be sold.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The bill will create a new insurance product available for sale in Florida, which should result in increased insurance sales premiums for title insurers who choose to enter the market.

Since the bill will preclude property and casualty insurers from offering for sale a similar product once the title insurance form and rates are approved, it will result in a negative financial impact for these companies, and possibly decrease competition and result in higher premium costs for purchasers of such insurance.

C. Government Sector Impact:

There should be an increase in tax revenue from the sale of personal property UCC title insurance under s. 624.509, F.S., along with an increase in revenue and taxes due to additional licensures and appointments for title insurance agents and agencies. Under s. 624.501(27), F.S., the state will collect \$54 per new agent or agency appointment and \$10 per new agent's license filing. The state would also collect a \$200 annual surcharge for each new title insurance agency appointed by a title insurer and for each retail office of the insurer.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.

VIII. Summary of Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
