ALTA Best Practice #6 – Just Because "Stuff Happens"

When the Real Estate Title Insurance Company of Philadelphia issued the first title insurance policy in Pennsylvania in 1876, there was a need to protect a consumer's investment in real estate because "stuff happens." Some refer to this explanation for bad things happening to good people for no particular reason as "*Así es la vida*," "*C'est la vie*" or "*Que Sera Sera*." Others observe that life is full of unpredictable events, and we know Murphy's Law to state: "If anything can go wrong, it probably will." So what do we do to guard against "stuff happening" to us or our clients? We buy insurance, in case "stuff happens."

To cover the eventuality that "stuff happens" to our real estate clients, we recommend that they purchase title insurance. Title insurance protects against a number of risks that are symptomatic of the recording system in the United States, such as unknown legitimate claims to title that were not discoverable in the public record. In many instances, the lender does more than request title insurance; they make lender's coverage mandatory. Lenders want the protection in the event "stuff happens" to their security because they generally wind up holding the bag when it does.

Furthermore, just in case "stuff happens," we may choose to or be required to purchase multiple forms of insurance. The title insurance underwriter or state law may require additional forms of insurance, such as Errors and Omissions Professional Liability Insurance, Fidelity Coverage, Surety Coverage, or Cyber Theft and Fraud Coverage. In the case of ALTA Best Practice #6, the standard is simple – agents must carry whatever the title underwriter or state law requires.

ALTA Best Practice #6:

> **Maintain appropriate professional liability insurance and fidelity coverage.**
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> **Purpose:** Appropriate levels of professional liability insurance or errors and omissions insurance help ensure title agencies and settlement companies maintain the financial capacity to stand behind their professional services. In addition, state law and title insurance underwriting agreements may require a company to maintain professional liability insurance or errors and omissions insurance, fidelity coverage or surety bonds.

Errors and Omissions Insurance

Errors and omissions insurance is for professionals who provide advice or service to clients. It protects the client in the event of a negligent act of the professional that has caused financial harm to the client. In short, it would protect the client if "stuff happens." While the client would have a claim against the professional, the errors and omissions insurance would step in and protect the client from the financial loss. The professional could be pursued by the errors and omissions insurance company, but, ultimately, the errors and omissions insurance makes the client whole and does not rely upon the professional for the compensation to the client.

In the case of a real estate transaction, title insurance covers many things that might ultimately be the error of the professional performing the title examination. For example, if the professional does not discover an uncancelled lien or judgment that takes priority over the purchaser's deed or lender's new security instrument, title insurance would potentially be called upon to make the purchaser or lender whole. In such an instance, the title insurance company, having paid the claim, by virtue of subrogation would stand in the shoes of the purchaser or the lender to make a claim against the professional. When "stuff happens," if there is a responsible party, the resulting liability would come back to that professional that made the negligent error. At this point, the professional would refer the title insurance company to their errors and omissions carrier to make them whole. In short, professional errors and omissions insurance protects the professional as well as the client, when "stuff happens."

Other Relevant Forms of Insurance

While professional errors and omissions insurance is required by nearly every underwriter, there are other types of insurance that may be required by the title underwriter or the professional may wish to have, just in case "stuff happens."

Fidelity Bond

A fidelity bond is an insurance policy that protects the professional from the fraudulent acts of specified individuals. In particular, the professional might purchase this insurance and/or bond to protect from the malfeasance or dishonesty of employees. These acts could include many things, including, theft, fraud, or forgery. A review of the terms of the policy would reveal the exact coverage limitations. A fidelity bond is significantly different from a professional errors and omissions policy because it protects the professional for wrongful acts and not mere negligence. Some might refer to a fidelity bond as a type of "crime insurance" policy. A fidelity bond will certainly protect the professional when "stuff happens," but, in this instance, it is not a case of bad things happening to good people. It is rather a case of bad things happening *because of* bad people.

At present, ALTA Best Practice #6 only requires a fidelity bond if it is required by the title underwriter or the prevailing laws of the jurisdiction. Consult the title underwriter and licensing authority for the requirements in this regard.

Surety Bond

There are many types of surety bonds, but they are all generally three-party agreements. The surety bond protects a second party in the event that the first party fails to meet a certain obligation. The type of surety bond that is applicable in the context of a professional providing real estate settlement services would be a fiduciary obligation to monitor the funds held in trust. In other words, a surety bond is in place to make sure that professional or principal does not steal the money. If it sounds odd to buy an insurance policy to make sure that the professional does not steal, it is; however, in some instances, there may be a level of assurance required by a client that cannot be achieved another way.

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Cyber Fraud and Cyber Theft Insurance

Cyber fraud and cyber theft insurance is currently NOT required by the ATLA Best Practice #6. We cannot, however, have a complete conversation about insurance without mentioning this growing area of the insurance marketplace. Twenty years ago, when assessing the risk for theft from our entrusted funds in the trust account, we looked to our employees, our partners, and our clients. Today, we have to consider threats that did not exist last week, let alone twenty years ago.

The advent of online banking has provided crooks in a foreign land an avenue to potentially rob our trust account. This is a new threat that has to be carefully examined to make sure that the trust that has been placed in us is warranted. The next time we sit down at the computer to perform an online banking function, consider that a criminal halfway around the world could potentially do anything online that we can do. Compare this type of coverage to the coverage offered by a fidelity bond and consider that the opportunity to interview an employee exists before they sit at a computer with access to online banking. In both instances, a professional may be the victim of theft due to the malfeasance of another. Purchasing cyber fraud and cyber theft insurance is not a substitute for appropriate risk management measures regarding online banking; it is a complement to those efforts in case "stuff happens."

Conclusion

There are many types of insurance available to protect us and our clients in the event that "stuff happens." At the end of the day, the different forms of insurance are not a substitute for professional policies, procedures, and practices. Title insurance is not a substitute for a complete and thorough title examination. Errors and omissions insurance is not a substitute for adhering to standards of professionalism. Fidelity insurance is not a substitute for a background check and interview of potential employees. Cyber fraud and cyber theft insurance is not a substitute for a firewall and virus protection software to protect online communications. Try as we might to guard against all of the risks present in our everyday professional responsibilities, "stuff happens." The insurance that we purchase, some required by our title underwriter and some required by state law, is merely a safety net when "stuff happens" so that we can live another day to provide professional real estate services to another client.