The Fine Line between Bank Attorneys and Title Companies

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As we all know, New York is an "attorney state" with respect to real estate transactions. Historically, this means that each party (seller, buyer, and lending bank) engages an attorney to represent its interests throughout the transaction. Given how expensive New York City residential real estate is and how unique the cooperative and condominium unit asset class is, it remains imperative that each party involved in a transaction engages experienced local counsel.

In recent years, there has been a noticeable shift with respect to how residential mortgages are closed in New York. Many lending institutions have decided to engage settlement companies and/or title insurance companies to represent their interests in a loan transaction. This begs the question as to whether the bank's interests are being appropriately protected.

In my opinion, there needs to be a red line between legal services and title insurance. As I understand the laws in New York, attorneys and law firms are not supposed to own interests in title insurance companies. Furthermore, attorneys and law firms are certainly not allowed to act as title agents (where a percentage of title premium is received) and bank attorneys/settlement agents on the same deal. Using this logic, I wonder why it would be acceptable for a title company to do just that. There seems to be a double standard.

Recently, I was contacted by a longtime friend in the title business who called to tell me his abstract company had been approved as a "closing attorney," or settlement agent, for a lending institution that our office also represents. This scenario has played out several times in recent years, and each time I wonder to myself: *Aren't you now our competition?* In this particular example, the person involved historically would try and make introductions to loan officers and, in turn, we would try and reciprocate with title business. Helping those that help you is a business model that I happily subscribe to. However, in this instance, the abstract company effectively lost its ability to help us for the opportunity to receive title premiums on loan transactions. So, if a title company has a vested interest in the insurance that the bank requires be purchased to insure its security interest, does it truly have the bank's interest in mind?

More than 95 percent of the residential loan engagements our firm receives involve purchase transactions where the purchaser's attorney (and not the bank attorney) selects the title company. This is a telling statistic, as the refinance loans (where the bank attorney typically selects the third-party title company he/she is comfortable with) are headed elsewhere—often directly to the title company or the settlement company. Although I fully understand the convenience factor and am a fan of streamlining, I wonder aloud whether this practice is in the bank's best interest. Isn't the primary purpose of a title company to sell title insurance? And, with that in mind, if you are selling title insurance, can you truly be an independent legal advisor looking out for the bank's best interests?

A glaring example highlighting the need for experienced bank attorneys in New York City is the CEMA process. A CEMA (Consolidation, Extension, and Modification Agreement) is the vehicle by which a borrower can reduce the New York State Mortgage Tax (2.175 percent on mortgages over $500,000.00) when refinancing. Using this vehicle, the new bank issuing a mortgage (generally at lower rates and better terms) arranges for the existing mortgage to be assigned and then issues a Gap Mortgage to secure any "new" money being issued (over and above outstanding principal balance). Although it sounds relatively straight forward, it is actually a complicated process and requires a review of all prior mortgage documents in the chain of title. Historically, this was a role reserved for only experienced New York bank attorneys.

When it comes to CEMAs, which account for a majority of refinance transactions in New York City, the risk to the bank is substantial. If a CEMA is not prepared properly or if there is a title defect in the mortgage chain, then that would render the newly issued mortgage unsellable (meaning a bank would need to keep a loan on its own books as opposed to selling). The conflict of interest that comes to mind is an obvious one, as the company that is issuing title insurance is the same company that is reviewing the legal documents protecting the bank's interest. The residential bank attorney that historically receives $800–$1,200 per loan transaction does not share this conflict.

In this day and age, where banking regulations are at historic highs, one has to wonder whether the separation between the title insurance company and the residential loan being issued is more important than ever.

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