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Appellate Division Upholds Title Insurer's Application of Exclusions

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Though considered to be "[o]ne of the most litigated clauses in standard title insurance policies," New Jersey courts have not devoted significant time to interpreting Exclusions 3(a) and 3(b) of the standard title policy promulgated by the American Land Title Association (ALTA). Joyce Palomar, 1 Title Ins. Law §6:10 (2015 ed.). These exclusions bar coverage for title defects "created, suffered, assumed or agreed to by the Insured Claimant" or "not Known to the Company, not recorded in the Public Records at Date of Policy, but Known to the Insured Claimant and not disclosed in writing to the Company by the Insured Claimant," respectively.

This article will discuss the general applicability of these exclusions to title claims and focuses on their applicability in the recent Appellate Division decision of *Carrington v. Chicago Title Ins. Co*. (N.J. App. Div. Nov. 6, 2015). There, though the court focused primarily on Exclusion 3(b), both exclusions were addressed and deemed sufficient to bar coverage.

Exclusion 3(a)

Exclusion 3(a) of a standard ALTA title policy excludes any "[d]efects, liens, encumbrances, adverse claims, or other matters created, suffered, assumed or agreed to by the Insured Claimants …." Under Exclusion 3(a), "[defects] are 'created, suffered, assumed or agreed to' by the insured where they arise from the insured's deliberate act or omission." *Lawyers Title Ins. Corp. v. JDC (Am.) Corp*., 818 F. Supp. 1543, 1546 (S.D. Fla. 1993). In *Feldman v. Urban Comm'l*, the New Jersey Appellate Division sustained the denial of a title claim made by an insured mortgagee after it found that the mortgagee created the defect. The insured was aware that the property could not be encumbered without specific consent and it "affirmatively determined to accept the mortgage without such consent and did so." 87 N.J. Super. 391, 404 (App. Div. 1965) ("We hold that the word 'create' connotes the idea of knowledge, the performance of some affirmative act by the insured, a conscious and deliberate causation. The term 'suffer' implies the power to prevent or hinder, and includes knowledge of what is to be done under the sufferance and permission, and the intention that what is done is to be done."). The terms "assumed" and "agreed to" mean that the insured assumed or contracted for the risk. *See American Sav. & Loan Ass'n. v. Lawyers Title Ins. Corp*., 793 F.2d 780, 784 (6th Cir. 1986) ("'Assume,' under this definition requires knowledge of the specific title defect assumed. And 'agreed to' carries connotations of 'contracted,' requiring full knowledge by the insured of the extent and amount of the claim against the insured's title.").

Exclusion 3(b)

Exclusion 3(b) of the standard title policy expressly excludes coverage for: [d]efects, liens, encumbrances, adverse claims or other matters … not Known to the Company, not recorded in the Public

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Records at Date of Policy, but Known to the Insured Claimant and not disclosed in writing to the Company by the Insured Claimant prior to the date the Insured Claimant became an Insured under this Policy.

The title policy proceeds to define "Public Records" as "records established under state statutes at Date of Policy for the purpose of imparting constructive notice of matters relating to real property to purchasers for value and without knowledge …." *See* Policy Definitions 1(i).

This exclusion "'is akin to a notice requirement for an insured. Its effect is to impose on the insured a duty to disclose to the insurer any defects of which the former has knowledge….'" *See* Barlow Burke, Law of Title Insurance, §4.05 (3d. Ed. 2016 supp.) (citation omitted). It has also been applied and upheld in New Jersey. In *Manchester Fund, Ltd. v. First Am. Title Ins. Co.*, the attorney of an insured purchaser learned before the issuance of the title policy that the United States had filed a notice of lis pendens on the property but that the lis pendens was improperly indexed. 332 N.J. Super. 336, 346 (Ch. Div. 1999). He did not inform the title company. The parties disagreed over whether a mis-indexed lis pendens was part of the public record, but the court held that it was not. As such, it held that because the insured was aware of an adverse claim that was not part of the public record and did not disclose that fact to the insurer, it triggered the express 3(b) exclusion and the insured was not entitled to coverage.

The Carrington Decision

Though not the subject of many decisions in New Jersey, both 3(a) and 3(b) were raised in the Appellate Division's recent decision of *Carrington v. Chicago Title Ins. Co.* (N.J. Super. Ct. App. Div. Nov. 6, 2015). In *Carrington*, June Carrington and two other individuals purchased a property in 1998. Chicago Title issued her a title policy which covered certain risks, including the risk that "[s]omeone else owns an interest in your title." In 2001, the property was transferred to Carrington's name only. In 2011, four individuals referred to as the "Siblings" filed a complaint against Carrington, alleging that they and Carrington had reached an agreement in 2001 whereby the property would be sold to Carrington and each of the four siblings. According to the complaint, the parties had agreed to keep title to the property in Carrington's name only because the Siblings had poor credit ratings. They further alleged that the parties had agreed that title to the property eventually would be adjusted to reflect all five true owners. Instead, Carrington refinanced her original mortgage in her own name only and allegedly violated the parties' agreement.

Carrington then sought coverage from Chicago Title for the lawsuit. Chicago Title denied the claim based on the fact that: (i) the alleged title issue was created by Carrington and therefore was excluded under Exclusion 3(a) of the policy; and (ii) the alleged agreement was known to Carrington, not recorded and not disclosed to the title company, and therefore was excluded under Exclusion 3(b) of the policy. Though Chicago Title also noted that the allegations in the complaint indicated that the title issue arose after the policy was issued, that defense is not relevant to the present analysis. Carrington informed Chicago Title that the allegations were false and that she neither entered into any agreement with the Siblings nor failed to disclose anything to Chicago Title, but Chicago Title nonetheless denied her claim.

Carrington then sued Chicago Title, alleging that Chicago Title failed to provide a defense, acted in bad faith in investigating the claim, and violated the Consumer Fraud Act. Chicago Title moved for summary judgment, and the trial court granted the motion, holding that Carrington had entered into an agreement with the Siblings before Chicago Title had issued the policy and had not disclosed the same to Chicago Title in violation of the policy. Carrington appealed the decision.

The Appellate Division affirmed the decision, holding "[t]he policy clearly excluded coverage for the claims asserted in the underlying action[.]" In doing so, the court affirmed prior New Jersey decisions, stating, "'[a]n insurer's duty to defend an action brought against its insured depends upon a comparison between the allegations set forth in the complainant's pleading and the language of the insurance policy … [and] it is the nature of the claim asserted, rather than the specific details of the incident or the litigation's possible outcome, that governs the insurer's obligation.'" Despite Carrington's complete denial of the Siblings' allegations, the "nature of the claim asserted" in the Siblings' complaint was that Carrington and the Siblings had an agreement whereby they were all co-owners of the property but that title would remain only in Carrington's name for a brief period. Therefore, regardless of whether the allegations had any basis in fact—and the litigation between the Siblings and Carrington settled with Carrington remaining as the sole owner of the property—the facts as pled alleged a title defect that either (i) Carrington created through her agreement with the Siblings; or (ii) arose out of an unrecorded, undisclosed agreement of which Carrington was aware but Chicago Title was not. As the allegations of the complaint were plainly excluded by Exclusion 3(a) and 3(b) of the policy, Chicago Title had no duty to defend Carrington against same.

The practical effect of the *Carrington* decision is a reminder that Exclusions 3(a) and 3(b) continue to protect title insurers from title defects that their insured either created or knew about. Moreover, the decision reaffirmed the doctrine that an insurer's duty to defend is defined by the four corners of the complaint and the policy, and that allegations that are plainly excluded under the policy do not trigger this duty, regardless of the merit of the claims. Carrington's repeated pleas to Chicago Title to assign counsel—based primarily on the argument that the claims were false and she had done nothing to trigger either Exclusion 3(a) or 3(b)—were wisely ignored. Finally, the decision is a pointed reminder that attorneys representing clients involved in real estate transactions must disclose to the title insurer any unrecorded agreements affecting title they or their clients are aware of in order to have a chance at obtaining coverage for same.