

TITLE INSURANCE

The Statute of Limitations and the Premature Claim

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As lenders attempt to clear inventories of defaulted loans, the foreclosure process can be stopped in its tracks with the discovery of a prior lien or other title defect. Standard loan policies

insure the lender against loss or damages from unexcepted title defects. However, the fact that there is a loan policy in place does not necessarily mean that the lender is home free. This is particularly the case in California where a lender may find itself squeezed between policy language that limits damages to "actual monetary loss" and a statute of limitations that commences upon the discovery of "loss or damage."

Consider, for example, a lender foreclos-

ing on a first lien who discovers a prior recorded \$100,000 lien that is not excepted from the loan policy. The lender promptly submits a claim with supporting documentation to its title insurer, expecting that the insurer either will pay off the prior lien or send the lender a check for \$100,000 so that it can clear the prior lien and foreclose with clear title. Instead, the response from the title insurer is that the claim is "premature" because there has not yet been an "actual monetary loss." The insurer requests that the lender contact the insurer after foreclosure if the value at foreclosure is insufficient to satisfy the lender's lien because of the title defect.

This response is based on provisions in the policy limiting the insurer's liability for damages to "actual monetary loss."¹ Case law holds that recoverable loss can be established only after foreclosure when it can be determined whether the value of the property is insufficient to cover both the non-excepted prior lien and the insured lien.²

The insurer's position that the claim is premature may cause the lender to conclude that, as there has not yet been an actual monetary loss to establish the insurer's liability for damages, there also has been no loss or damage sufficient to commence the statute of limitations. However, if the lender then defers pursuing its legal remedies until the claim has "matured" the claim may be barred altogether by the statute of limitations.

While most insurance claims may be brought within the four year statute of limitations applicable to written contracts,³ that is not the case with title insurance claims in California. Pursuant to Code of Civil Procedure §339(1), title insurance claims must be brought within two years from the "discovery of the loss or damage."⁴ California courts have held that the loss or damage that triggers the statute of limitations occurs when the lender has actual knowledge of the facts underlying the adverse claim.^{5,6}

In the above example, the lender's mistake was its misconception that the actual monetary

loss that is a prerequisite to the insurer's liability for damages under the policy is the same as the loss or damage that commences the statute of limitations. The peril from equating the two is illustrated in *65 Butterfield v. Chicago Title Insurance Co.* (1974) 40 Cal.App.3d 536, 528. There, the plaintiff purchaser sued the title insurer and the county after the county claimed an easement that was not excepted in the title policy. Despite the plaintiff's knowledge of the county's adverse claim for more than two years before he filed his lawsuit, he argued that his action was not barred by the statute of limitations because the policy provided that the insurer was not liable for loss or damage until there was a final disposition of the lawsuit against the county. The court held that the policy's preclusion of insurer's liability for damages until final disposition of the lawsuit did not mean that there was no loss or damage to trigger the statute of limitations. Instead, the statute commences "when the insured 'discovers the potential loss' which 'may be incurred if the title is not as represented.'"⁷

The effect of the statute of limitations in title insurance claims can be mitigated by equitable tolling. Equitable tolling halts the statute while the insurer determines whether to honor or reject a timely filed claim.⁸ Tolling does not apply from the time the insured learns of a potential covered loss⁹ until the insured presents the claim to the insurer.¹⁰ Tolling ceases when the insurer denies the claim.¹¹

While tolling appears simple enough, there are pitfalls for the unwary. For example, an insured who, at its own expense, pursues a legal action to cure the title defect before presenting a claim to the title insurer will find that, even if the lawsuit is successful, recovery of the cost of the litigation is barred if two years have passed.¹² However, where the claim is presented to the insurer first, time spent litigating the title issue tolls the statute.¹³

Virtually all responses by insurers invite the insured to provide additional pertinent information

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and assure that the information will be reviewed carefully to determine whether an initial denial of coverage should be changed. While the insurer is required to give reasonable consideration to new information,¹⁴ the statute of limitations is not tolled while the insurer determines whether the information requires that it provide coverage.¹⁵

In addition, it may not be clear if, or to what extent, an insurer's response is a denial. For example, where the insurer responds that an unexcepted condition is not a title defect and that the lender's claim of unmarketability is premature, sorting out what is denied and what is merely deferred may be difficult.

Considering the risk that a claim may be barred by the statute of limitations, a prudent lender should, at a minimum: (1) promptly submit a claim to the title insurer upon discovery of facts that may constitute a title defect; (2) if the time from discovery of the potential defect approaches two years, request that the title insurer enter into an agreement tolling the statute of limitations; and (3) if the title insurer refuses to enter into a tolling agreement, determine with counsel whether there is a reasonable basis to initiate a lawsuit for coverage under the policy.



1. See, e.g., *ALTA Loan Policy 10-17-92, Exclusion 3.(c) and Conditions and Stipulations section 7 limiting the insurer's liability to "actual monetary loss or damage" resulting from an insured defect. Comparable provisions are in the ALTA Loan Policy 6-17-06 at Exclusions 3.(b) and Conditions section 8.*
2. See, *Karl v. Commonwealth Land Title Ins. Co. (1997) 60 Cal. App. 4th 858, 870; Cale v. Transamerica Title Insurance (1990) 225 Cal. App. 3d 422, 427. These rulings are better understood in the context of the market conditions at the time they were decided, in which a rising market might well cover both the insured lien and the unexcepted senior lien, resulting in no loss to the insured lender.*
3. *C.C.P. 337(1) provides for a 4-year period for an "action upon any contract, obligation or liability founded upon an instrument in writing."*
4. *C.C.P. § 339 (1). Many other states are more forgiving, such as Nevada (6 years), Illinois (10 years), Texas (5 years) and New Jersey (6 years).*
5. See, *Contini v. Western Title Insurance Co. (1974) 40 Cal.App.3d 536, 548.*
6. *While insurers have contended that the statute of limitations commences even earlier, i.e., when the lender should have learned the facts constituting a potential claim, no court has adopted that position. See, 65 Butterfield v. Chicago Title Insurance Co. (1999) 70 Cal.App.4th 1047, 1053, fn. 1.*
7. *65 Butterfield v. Chicago Title Insurance Co. (1999) 70 Cal.App.4th 1047, 1060 – 1062.*
8. See, *Forman v. Chicago Title Ins. Co. (1995) 32 Cal.App.4th 998, 999-1000.*
9. *65 Butterfield, supra, 70 Cal.App.4th at 1061.*
10. *Forman, supra, 32 Cal.App.4th at 1001, 1004.*
11. *Id. [Citing Prudential-IMI Com. Insurance v. Superior Court (1990) 51 Cal.3d 674, 693]*
12. *Tabachnick v. Tigor Title Ins. Co. (1994) 24 Cal. App.4th 70.*
13. See, *Lambert v. Commonwealth Land Title Ins. Co. (1991) 53 C3d 1072.*
14. *Shade Foods, Inc. v. Innovative Products Sales & Marketing, Inc. (2000) 78 CA4th 847, 880.*
15. *Singh v. Allstate Ins. Co. (1998) 63 Cal. App. 4th 135*

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