

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

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

Prepared By: The Professional Staff of the Banking and Insurance Committee

BILL: SB 1078

INTRODUCER: Senator Wise

SUBJECT: Personal Property Title Insurance

DATE: February 29, 2008

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Emrich</u>	<u>Deffenbaugh</u>	<u>BI</u>	<u>Pre-meeting</u>
2.	_____	_____	<u>CM</u>	_____
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

Senate Bill 1078 defines the term personal property title insurance within the title insurance definition to expand and make more specific the allowance for title insurers to issue personal property title insurance policies for Uniform Commercial Code (UCC) transactions under Article 9 of the Revised UCC. Personal property title insurance is designed to insure against legal challenges to attachment, perfection or priority of a security interest in personal property and provides for the defense of the insured lender or owner if a claim is made regarding the lender's or owner's collateral position. In 2005, the Legislature authorized title insurers to offer this type of insurance, but the two title insurers attempting to sell this product have been unable to get acceptable forms and rates approved by the Office of Insurance Regulation (OIR) due, at least in part, to differing interpretations of the current statute.

This legislation provides a broader and more specific definition of personal property title insurance that may be sold by title insurers. It authorizes the coverage to affirm or negate one or more of the individual elements of attachment, perfection or priority of the security interest in personal property or fixtures as may be appropriate to the particular collateral type being insured. According to insurer representatives, this will allow the issuance of buyer's personal property title insurance (analogous to "owners" in the real property context), assuring the absence of security interests in acquired assets.

The bill authorizes insurance as to the accuracy and completeness of the results of searches of various databases and permits coverage as to the effectiveness of filings with a particular office and of filings and lien status in multi-jurisdictional transactions. The bill allows insuring of priority of secured party status where perfection is by a method other than through the filing of a financial statement, such as possession of instruments or control of a deposit account. Finally,

the legislation amends the definition of “primary title services” to mean insurability based upon a search of records of appropriate databases.

This legislation is modeled after similar legislation adopted in Texas and according to title industry proponents is consistent with evolving industry standards.

This bill substantially amends the following sections of the Florida Statutes: 624.608 and 627.7711.

II. Present Situation:

Background on Article 9 of the Uniform Commercial Code¹

The Uniform Commercial Code (UCC) is an act that has been promulgated to harmonize the law of sales and other commercial transactions in all 50 states. Article 9 of the UCC pertains to Secured Transactions and 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.² If the debtor defaults, the creditor may repossess and sell the personal 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 are similar to a grant of a security interest.

Article 9 operates using two key concepts: “attachment” and “perfection.” These terms describe the two key events in the creation of a “security interest” in personal property. 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.³

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.

¹ National Conference of Commissioners on Uniform State Laws, Summary: Uniform Commercial Code – Revised Article 9 Secured Transactions (1999), at http://www.nccusl.org/Update/uniformact_summaries/uniformacts-s-uccra9st1999.asp.

² 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. Chapter 2001-198, L.O.F. (Chapters 670-680, F.S., are cited as the “Uniform Commercial Code.”)

³ There are 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 Florida Legislature made many changes which included expanding 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.⁴

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.⁵ 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 insures the accuracy of its search against claims of title defects.⁶

In Florida, purchasers of real property and lenders utilize title insurance to protect themselves 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.

In 2005, the Legislature expanded the title insurance definition to include “insurance of owners and secured parties of the existence, attachment, perfection and priority of security interests of personal property under the Uniform Commercial Code.”⁷ The effect of this provision allows a title insurer to sell UCC personal property title insurance in conjunction with a transaction involving a UCC security interest.⁸ Under the law, personal property title insurance is designed to insure against challenges to the existence, attachment, perfection and priority of a security interest (such as fraud, filing office errors, inaccuracies in a search report, and errors in documentation and perfection) and provides a defense of the insured lender if a claim is made regarding the lender’s collateral position.

UCC Article 9 personal property insurance is utilized for various asset-based loans including multiple advance and revolving credit facilities, asset securitizations, syndication and mezzanine loans. In real estate finance, mezzanine loans are often used by developers to secure supplementary financing for development projects. For example, with commercial real estate lenders only willing to loan up to 80 percent of the real property’s value, developers are looking

⁴ Specifically, 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 by a creditor for a security interest. Other revisions to Article 9 provided that filing a financial statement perfects a security interest. The revision 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 a Revised Article 9 of the Uniform Commercial Code.

⁵ BLACK’S LAW DICTIONARY (8th ed. 2004).

⁶ BLACK’S LAW DICTIONARY (8th ed. 2004).

⁷ Chapter 2005-153, F.S.

⁸ Section 671.201(37), F.S., defines “security interest” as “an interest in personal property or fixtures which secures payment or performance of an obligation.”

for ways to further leverage the equity in the real property, however, the commercial real estate lender will likely prohibit a second mortgage or deed of trust. The borrower can then pledge as collateral its membership interest or stock in the entity that actually owns the real property. This is the collateral for a mezzanine loan. In other words, mezzanine financing is financing secured by pledges of ownership interests in the entity that owns the real property rather than by security in the real property itself.

According to insurance industry sources, all states except Oregon allow the offer and sale of personal property title insurance. Of the 50 jurisdictions (including Washington DC), 27 authorize title insurers to offer this product while 23 states authorize property and casualty insurers to sell this type of insurance. Florida law specifies that a title insurer may not sell any other type of insurance, which prohibits property and casualty insurers from selling title insurance.⁹ Therefore, the 2005 law that added UCC personal property insurance within the definition of “title insurance” had the effect of prohibiting property and casualty insurers from selling this product, while also authorizing title insurers to sell it.

The 2005 legislation also contained a provision directing the Office of Insurance Regulation (OIR) to approve the title insurance form and corresponding rate for personal property insurance by January 1, 2006. On January 3, 2006, the OIR issued a final order approving model form and rates and ordered that any forms or rates submitted by title insurers must be in substantial conformity to the approved form and premium rates. The OIR received form and rate filings by two groups of title insurers, Fidelity National Title Group, Inc. and First American Title Insurance Company. One title insurer had its form filing disapproved by the OIR because the form did not include the word “existence.” That insurer brought the disapproval issue before a DOAH (Division of Administrative Hearings) law judge who found in favor of the OIR.

According to proponents of this legislation, title insurers have not been able to obtain approval by the OIR of their forms and rates and have not been able to offer personal property insurance in Florida due in part to differences in interpreting the provisions of the 2005 law. For example, the term “existence” of a security interest in the current law is not defined or used within the UCC, but the OIR is requiring the term to be in the insuring agreement for a UCC title insurance policy. One title insurer asserts that because the term “existence” is undefined, it is impossible for the insurer to determine what it is insuring if forced to issue a policy using this term. Proponents also argue that this legislation is necessary so that coverage can be provided for Florida commercial transactions, thus eliminating the need and related costs to either create an out-of-state nexus in order to obtain UCC personal property insurance or having such transactions not be covered by this insurance. The other concerns expressed by proponents are outlined below under the Effect of Proposed Changes section.

III. Effect of Proposed Changes:

Section 1. Amends s. 624.608, F.S., pertaining to the definition of “Title Insurance.” The bill consolidates real and personal property title insurance within the statutory definition of “title

⁹ Section 627.786, F.S.

insurance.” The legislation in subsection (2) creates the term “personal property title insurance” and defines it to mean coverage that insures:

(a) Whether affirming or negating, one of more of the elements of attachment, perfection, or priority of a security interest in personal property or fixtures;

According to insurer representatives, paragraph (a), will allow the issuance of a *buyer’s* personal property title insurance policy (analogous to “owners” in the real property context) that would insure the absence of (“negating”) any lien or security interest in the acquired assets. The bill eliminates the problem in the current law which limits UCC insurance to a lender’s policy that insures all the elements of priority, because existence, attachment, perfection and priority are all listed with the conjunctive “and.” Under the bill each individual element of attachment, perfection or priority of the security interest can be addressed and insured as existing or not-existing as appropriate for the transaction. The term “existence” as it relates to security interests in personal property is deleted from current law because it is not defined or used within the UCC and is subsumed within the term “attachment.”

(b) The results, as to correctness, completeness, or other criteria, of a search of:

- 1. The filing office of the financing statement record of a debtor; or*
- 2. Any other database, whether publicly or privately maintained, such as court dockets, tax records, motor vehicle department records, or the records of the Federal Aviation Administration as to aircraft, the United States Coast Guard as to vessels, or the United States Department of Transportation;*

Paragraph (b) authorizes personal property title insurance to cover the underlying search relied upon in a transaction, which may have posting or indexing errors. Under Article 9 of the UCC, liens and interests in certain types of title assets (e.g., vehicles, aircraft and vessels) are not recorded in the standard UCC records, but in specialized databases. Those databases must be searched in order to insure ownership free of liens or the priority of liens. The bill allows insurance as to the search of such non-UCC databases. The reference to “privately maintained” permits coverage of the accuracy and completeness of databases which are subcontracted by governmental entities or the private databases maintained by many title insurers for real property records.

(c) The status of ownership of, rights in, powers to, transfer rights in, or title with respect to personal property or fixtures;

(d) The effectiveness of the filing of a financing statement with a filing office, or any other record with any publicly maintained database or registry;

Paragraph (c) allows insurance coverage of the traditional elements of ownership. The use of the disjunctive “or” recognizes that not all elements of coverage will be available for all types of assets. Paragraph (d) authorizes supplemental affirmative coverage in an owners or lenders policy as to the effectiveness of filings with a particular office or registry. This would allow the coverage to insure that the filing to perfect the security interest was made in the appropriate filing office, database or registry, as required under the UCC.

(e) The lien status of personal property or fixtures, or compliance with the Uniform Commercial Code of another state, the Uniform Commercial Code of this state, international conventions such as the United Nations Commission on International Trade Law (UNICTRAL), or similar laws or regulations; or

(f) Any of the matters covered by this subsection with respect to the laws of any other domestic or foreign jurisdiction.

Paragraphs (e) and (f) relate to financing transactions that involve mobile assets, assets in multiple states and even multiple nations as well as required filings in multiple jurisdictions. These provisions permit a Florida title insurer to insure ownership and lien interests in such transactions.

Representatives with the OIR have concerns about this legislation and state that the bill significantly expands the types of personal property insurance that title insurers and agents can offer which is not appropriate, since such agents do not have special expertise in this area. Practice under the UCC which largely governs the sale of, and security interest in, personal property is a highly specialized area that is beyond the knowledge of the typical title agent, according to OIR representatives. These types of personal property insurance policies can carry a high risk of loss which raises significant solvency concerns for the OIR.

Section 2. Amends s. 627.7711, F.S., to conform the definition of “primary title services” to Section 1 of the bill to include searches of records of “an appropriate database” rather than records of “a UCC filing office.” Under Article 9 of the UCC, liens and interests in certain types of titled assets are not recorded in the standard UCC records, but in specialized databases. Those databases must be searched to insure ownership free of liens or priority of liens and a search of only the UCC filing office would be inadequate to insure such interests.

Section 3. Provides that the bill will take effect on July 1, 2008.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The bill will allow title insurers and agents to offer personal property title insurance for sale in Florida which should result in increased insurance sales premiums for insurers and agents who choose to market these products in Florida. The legislation will provide coverages for Florida commercial transactions and eliminate the need and related costs for such transactions that now either create an out-of-state nexus in order to obtain personal property insurance or go without the insurance entirely.

C. Government Sector Impact:

Representatives with the Office of Insurance Regulation (OIR) state that this bill would increase the number of title insurance companies formed to “underwrite” personal property title insurance, thereby increasing the number of entities that the OIR would regulate. In addition, the OIR would have to review new forms and rates as to personal property title policies. Therefore, OIR asserts that more staff and resources are needed by the OIR to perform these functions, but no specific estimate has been made.

There would likely be an increase in premium tax revenues based on increased insurance premiums paid by title insurers offering personal property insurance authorized under this bill. However, this revenue amount is indeterminate.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.