



WHAT'S IN YOUR ESCROW AGREEMENT? THREE CLAUSES TO LIMIT OHIO ESCROW AGENT LIABILITY

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What's in your escrow agreement?

Too often escrow agreements are the last document to receive the escrow agent's scrutiny. Often the language in an escrow agreement is "standard" language borrowed from other escrow transactions without reflection on how very important the language in the escrow agreement is to the particular escrow agent's business. If you are the title agent, the language in your escrow agreement, the terms of the escrow agreement, is just that, your language, your choice. You employ the language just like you employ any of your other employees. You choose the conditions in your escrow agreement. The standard conditions of escrow, sometimes called the "Conditions of Acceptance of Escrow," are your standard conditions. What's in your escrow agreement is your responsibility.

What's an escrow agreement?

The leading case in Ohio regarding escrows is an Ohio Supreme Court case from 1936 where the Court held:

An escrow in Ohio, as between grantor and grantee of real estate, *is witnessed by a written instrument* known as an escrow agreement, delivered by mutual consent of both parties to a third party denominated the depositary or escrow agent, in which instrument certain conditions are imposed by both grantor and grantee, which conditions the depositary or escrow agent, by the acceptance and retention of the escrow agreement, agrees to observe and obey. [Emphasis added.]

Squire, Supt. Of Banks, v. Branciforti , 131 Ohio St. 344, (1936) syllabus one.

First and foremost, an escrow is an agreement. An escrow is a contract. The intent of the parties to a contract resides in the language they choose to employ in the agreement. *Kelly v. Med. Life Ins. Co.* (1987), 31 Ohio St.3d 130, paragraph one of the syllabus. You employ the language in your escrow agreement just like you employ any of your other employees. You choose the conditions in your escrow agreement.

The escrow agreement is the title agent's first witness.

When a title agent is sued for breach of an escrow agreement, the first source of information, perhaps of liability, or perhaps exoneration, is the escrow agreement itself. Your escrow agreement is your first witness, your most important employee. According to *Squire, supra* "an escrow *is witnessed by a written instrument.*" But your escrow agreement witness can only testify to what you have chosen for it to say. Unlike all the other employees of a title agency who may testify in a case involving an alleged breach of your escrow agreement, you can choose now what the escrow agreement will say later in court. You choose the conditions in your escrow agreement. The standard conditions of escrow are your standard conditions. If the language in your escrow agreement is clear and unambiguous, your escrow agreement will speak for itself. As stated in *The Tillotson & Wolcott Co. v. The Scottdale Machine & Mfg. Co.*, 23 Ohio App. 399, (1926, Eighth App., Cuyahoga, C.A.), where the court was construing a written instrument, a guaranty:

If the writing is unambiguous, then it speaks for itself, for it is an axiom that the court must adhere to the language if the context is clear and unmistakable, and must only resort to extrinsic aid when the language falls short of explaining itself.

You want your escrow agreement to speak for itself. If the language in your escrow agreement is unclear or is ambiguous, only then will outside evidence be considered in an effort to give effect to the parties' intentions. *Kelly, supra*, at 13. When the terms in a contract are unambiguous, courts can not create a new contract by finding intent not expressed in the clear language employed by the parties. *Alexander v. Buckeye Pipe Line Co.* (1978), 53 Ohio St.2d 241, 246. You are solely responsible for choosing the language in your escrow agreement. Your first witness should testify for you clearly and unambiguously. But, what should your first witness say?

Fifteen years to bring a claim is too long.

An escrow agreement, as a written contract, is subject to the fifteen (15) year statute of limitations for written contracts. *Ohio Revised Code, section 2305.06*. In *Saad v. Rodriguez*, 30 Ohio App. 3d 156, (1986, Eighth App., Cuyahoga, C.A.), the client agreed to buy property. The client buyer hired an attorney who drafted a purchase agreement in which the attorney's law firm was to act as the escrow agent. The seller agreed to provide title insurance. The escrow agent, the law firm, closed without title insurance. There was an unpaid judgment lien. The client sued the seller, the attorney, and the law firm alleging, in part, that the attorney and the law firm breached the escrow agreement. The attorney and the law firm moved for summary judgment in the trial court arguing that as a matter of law the claim was too late, barred by the one-year statute of limitations for legal malpractice. The trial court agreed and granted the motion. The attorney and law firm escaped from liability in the trial court. But, on appeal, in *Saad*, (pronounced "sad") the appellate court reversed, holding:

If the trier of fact determines Saad's damage, if any, was proximately caused by a breach of Weinberger and T, C, K & W acting in their capacity as attorneys, then the cause of action against them would be barred by *R.C. 2305.11*, the statute of limitations governing malpractice. However, if the trier of fact determines Saad's damage, if any, was proximately caused by a breach of Weinberger and T, C, K & W acting in their capacity as escrow agent, pursuant to the escrow agreement, then the misconduct is governed by *R.C. 2305.06*, the fifteen-year statute of limitations governing contracts in writing.

The *Saad* fact is, pun intended, parties to a written escrow agreement, to your escrow agreement, have fifteen (15) years to bring suit against you. You need to limit your liability. Class action lawyers will bring suits against title agents based on fifteen (15) years of transactions. You need to clearly and unambiguously limit the time period.

The first clause every escrow agreement should contain: a one year time limit on claims.

Why not choose language in your escrow agreement now which clearly and unambiguously limits your liability to claims for which notice in writing is given to you within one year of the closing? Every time a new Ohio closing protection letter is issued, title insurance companies, underwriters, limit their liability to one year after closing. Do not pass go and collect \$35.00! Title agents should play "follow the leader". Title agents should follow the lead of the title insurers. The new Ohio closing protection letters state:

The Company shall not be liable hereunder unless notice of claim in writing is received by the Company within one year from the date of the Closing.

What's in your escrow agreement? A possible escrow agreement clause is:

The Escrow Agent shall not be liable hereunder unless notice of claim in writing is received by the Escrow Agent within one year from the date of the Closing.

The escrow agreement should have the escrow agent's address and contact information. The Ohio Supreme Court held in *Colvin, v. Globe American Casualty Company*, 69 Ohio St. 2d 293, (1982), that:

Generally, in the absence of a controlling statute to the contrary, a provision in a contract may validly limit, as between the parties, the time for bringing an action on such contract to a period less than that prescribed in a general statute of limitations provided that the shorter period shall be a reasonable one.

> . . .

Although this case and its fact situation may present some degree of hardship, we cannot say as a general rule that a period of one year provided by the insurance contract entered into by the parties is an unreasonable period of time within which to bring an action against the company on the uninsured motorist provision of the policy.

The issue will be whether the shorter period, one year, is a reasonable time for claims under an escrow agreement. In a leading, national, closing protection letter case, *National Mortgage Warehouse, LLC, v. Bankers First Mortgage Co., Inc.*, 190 F. Supp. 2d 774, (2002, U.S. D. Ct. D. of Md.), the court held

The insured closing protection letter is, on its face, as clear and unambiguous as possible about the length of time in which its offer of protection stands. It is a one-page document, dated July 12, 1999, which provides, "the protection herein offered will be effective on the date of this letter for any real estate transactions occurring on or subsequent to such date and will continue for a period of one year from the date of this letter or until canceled by written notice from the Company, whichever occurs first." . . . As previously stated, Sovereign disbursed funds for the twelve fictitious loans after the letter's cancellation date. . . . The court sees no reason to obviate the clear language and intent of the parties by allowing the closing protection letter to survive beyond its express termination date.

If one year is good for the new Ohio closing protection letters and the title insurer, one year should be good for an escrow agreement and the escrow agent. For the most part, both involve the same transaction. One year is certainly long enough for parties to determine if an escrow has been properly disbursed. Under *Ohio Revised Code, § 1304.35*, (UCC 4-406) Customer's Duty to Discover and Report Unauthorized Signature or Alteration, customers of banks must review their bank statements, discover and report unauthorized signatures within one year. The statute provides:

(F) Without regard to care or lack of care of either the customer or the bank, a customer who does not within one year after the statement or items are made available to the customer discover and report his unauthorized signature on or any alteration on the item is precluded from asserting against the bank the unauthorized signature or alteration

If one year is a reasonable time for a customer to review a bank statement for unauthorized signatures, one year should be more than a reasonable time for escrow customers to review an escrow transaction.

But, is language in an escrow agreement limiting an escrow agent's liability enforceable?

Yes. Limiting language in a contract is sometimes referred to as an "exculpatory clause." In Ohio, exculpatory clauses are generally enforceable parts of written contracts, of escrow agreements. *Hurst v. Enterprise Title Agency, Inc.*, 157 Ohio App. 3d 133 (2004, Eleventh App., Lake, C.A.). In *Hurst*, the escrow agreement, executed by the parties, stated that the escrow agent "assumes no responsibility as to *** compliance with any local or municipal requirements, point of sale inspections or ordinances." (What's in your escrow agreement?) After occupying the physically unsatisfactory and municipally un-inspected residence, the land contract buyer sued the seller and the escrow agent claiming, in part, that the exculpatory language in the escrow agreement was void, unenforceable, against public policy, unconscionable and violated Ohio's Consumer Sales Practices Act. The trial court and the court of appeals ruled in favor of the escrow agent.

Another example, where a court in Ohio upheld an exculpatory clause in an escrow agreement is *Pippin v. Kern-Ward Building Co.*, 8 Ohio App. 3d 196, (1982, Eighth App., Cuyahoga, C.A.), where the buyer, borrower sued the bank, escrow agent for failing to withhold funds upon the buyer's written instructions concerning construction disputes. The court held in favor of the escrow agent, stating:

Whether the plaintiffs requested that the bank withhold the funds is irrelevant. An escrow agent's duties are fixed and limited by the escrow agreement. The escrow agreement between the plaintiffs and defendant builder stated that the 'bank * * * assumes no responsibility as to * * * physical conditions of premises * * * alterations or additions to the premises.

Continental could not alter the terms of the agreement on the request of one of the parties. Continental's duties could only be changed by mutual consent of both parties. Because there was no agreement, the bank had no

obligation to withhold funds. When the bank received all the materials necessary to allow it to close the transaction, it properly did so.

In *Pippin*, the escrow agent had no responsibility for the physical condition of the premises. What's in your escrow agreement?

The second clause every escrow agreement should contain: a no liability clause for negligent title searches.

. In Ohio, there is a critical difference between a title agent and an escrow agent. Ohio title agents are licensed; Ohio escrow agents are not. *Ohio Revised Code section 3953.23(B)* now provides:

(B) A title insurance agent may engage in the business of handling escrows of real property transactions provided that the agent shall maintain a separate record of all receipts and disbursements of escrow funds and shall not commingle any such funds with the agent's own funds or with funds held by the agent in any other capacity;

Unless the escrow agreement specifically provides for disclosure of title defects, an escrow agent has no duty to disclose the status of title. In *Shafron Enterprises Defined Benefit Pension Plan v. Midland Title Security, Inc.*, 1992 Ohio App. LEXIS 3301, (1992, Eighth App., Cuyahoga County, C.A.), Shafron retained Midland to issue title insurance and perform escrow duties. Midland conducted the search, recorded the deed and mailed the title policy to Shafron. The policy disclosed a utility easement. Shafron later was denied a building permit because of the utility easement. Shafron filed suit claiming Midland should not have disbursed the escrow funds once the utility easement was discovered. The court held Midland was under no obligation to contact Shafron about the easements.

Most agency agreements between a title insurance company, the insurer or underwriter, and the title agent, make the title agent's business of handling escrows of real property transactions, a separate business. As an escrow agent, the title agent does not act as the agent of the underwriter. Underwriters do not usually review, comment on, approve or disapprove the language in a title agent's escrow agreement. The escrow agent is on its own. You as an independent title agent are responsible for your escrow agreement and your escrow business.

But, when you act as a title agent, you act on behalf of a disclosed principal, the title insurance company. The title agent does not act on its own behalf. As stated in *Stryker Farms Exchange v. Mytczynskyj*, 129 Ohio App. 3d 338, (1998, Sixth App., Williams County, C.A.)

. . . [A]n agent may only be held personally liable for the debt of his principal if the principal is undisclosed, *Davis v. Harness (1882)*, 38 Ohio St. 397, paragraph one of the syllabus, only partially disclosed, *Givner v.*

United States Hoffman Machine Co. (1935), 49 Ohio App. 410, 413, 197 N.E. 354, or is fictitious or non-existent, *Seasongood & Mayer v. Riddle (1923)*, 18 Ohio App. 88, 90. An agent for a disclosed principal, acting within the scope of his authority and in the name of the principal, may not ordinarily be held personally liable. *Dobell v. Koch (1921)*, 16 Ohio App. 41, 43.

By statute in Ohio, *Ohio Revised Code section 3953.07*, "No policy or contract of title insurance shall be written unless it is based upon a reasonable examination of the title" Title agents perform title searches as a basis for issuing a title policy. The question is: "To whom does the title agent owe a duty?" The duty is a contractual duty arising from the agency agreement. The title agent's search is done for a disclosed principal pursuant to contractual undertakings arising from the purchase agreement. If there is a title defect, chances are that the injured party will mistakenly sue both the title agent who allegedly, negligently failed to perform a reasonable title search and the title insurance company whose policy the allegedly, negligent title agent issued. If there is a problem with the search, title agents are sued for negligence. But, negligence is a tort. The negligence claims should fail.

Two recent cases are instructive. In *McMullian v. Borean*, 167 Ohio App. 3d 777, (2006, Sixth App., Ottawa, C.A.), the appellate court reversed a trial court's dismissal of a complaint filed against Firelands Abstract and Title Agency, Inc., that searched the record and failed to disclose a sewer line easement, the existence of which prevented the buyer from constructing a home. The appellate court held:

Assuming all facts in the complaint are true, appellants have sufficiently pled a claim against Firelands. Appellants have alleged that Firelands had a duty to disclose all easements of record that it failed to disclose an easement of record, and that the particular easement prevented them from constructing their residence as planned and approved. Firelands has not argued that appellants lack privity of contract. Because it does not appear beyond a doubt that appellants can prove no set of facts entitling them to recovery, appellants' first assignment of error is well-taken.

Firelands performed the title search and acted as title agent for General Title & Trust which issued a title insurance policy which policy made no exception for the undiscovered sewer line easement. The *McMullian* court found that Firelands had a duty to disclose all easements of record. The court does not describe the source of the duty to disclose all easements of record. The source is the agency agreement to which the buyer and the seller are not parties and are not third party beneficiaries. The *McMullian* question every title agent in Ohio should ask is: "Why, if there is a title policy issued, is the title agent liable?" The answer should be that the title agent should not be liable to an insured for a negligent title search done for a disclosed principal. The insured's claim should be limited to a claim under the title insurance policy. But, the title insurance policy is between the insured and the insurer. Where is the limiting language in the title

policy which clearly and unambiguously states that the title agent has no separate liability? There is no such language in the policy.

In contrast to the *McMullian* case, is the case of *Eller Media Company v. Stewart Title Guaranty Co.*, 2004 Ohio 4748, 2004 Ohio App. LEXIS 4298, (2004, Eighth App., Cuyahoga, C.A.), where the facts were a little more complicated than *McMullian*, but the issue as to the title agent was similar. In *Eller*, DGE, Ltd., ("DGE"), a buyer of commercial real estate, purchased a building with a large billboard attached. The seller had said that the billboard was on a month to month lease and that a buyer of the building could make money from the rent of the billboard. DGE bought. Surety Title Agency was selected as the title and escrow agent, and Stewart Title as the underwriter for the owner's policy of title insurance. After the transfer, but before the title policy was issued, Eller Media advised DGE that Eller Media owns the billboard and has an unrecorded lease which lease does not expire for a year. DGE notified Stewart Title of the Eller Media claim and requested that the title policy be issued. Stewart Title issued a title policy which contained an exception on Schedule B for "rights of others, if any, in and to, the billboard." Eller Media sued. DGE cross claimed against Surety and Stewart. Stewart denied any duty to defend DGE. The trial court granted summary judgment to DGE against Surety and Stewart. For our purposes as to Surety's appeal, the appellate court held:

Surety's role in this transaction was twofold: it was to serve as escrow agent for the . . . transaction, and act as a title agent for Stewart. It [Surety Title Agency] contends that it had a contractual obligation to DGE as escrow agent, but not as a title agent. Under the terms of the Title Insurance Underwriting Agreement between Stewart and Surety, Surety was Stewart's agent and, because DGE was not a party to this agreement, it cannot claim rights under that agreement.

...

Surety acted as an agent for Stewart with respect to the issuance of a title commitment and owner's policy of title insurance. An agent for a disclosed principal, acting within the scope of his authority and in the name of the principal, may not ordinarily be held individually liable. . . . As an agent for Stewart, Surety had no obligation to ensure DGE against loss, or defend or indemnify it.

...

Surety was acting as the escrow agent . . . with a disclosed relationship with Stewart. The main function of an escrow agent is to hold documents and funds until the conditions are met, whereupon the escrow agent releases the documents and funds. . . . When Surety fulfilled the escrow instructions and the property transferred, its duties and responsibilities ceased.

Every escrow agent in Ohio should be aware of the *Eller Media* decision. When an escrow agent fulfills the escrow conditions, the escrow agent's duties and responsibilities cease. When a title agent acts on behalf of a known principal there should be no agent liability.

In, *Chicago Title Insurance Company v. Commonwealth Forest Investments, Inc.*, 2007 U.S. Dist. LEXIS 47023 (2007, U.S. D. Ct. for the Middle D. of Fla.), the court granted the title agent's motion to dismiss, where a buyer sued a title insurer and title agent, finding, in part, that the "economic-loss rule" bars tort actions when the parties are in contractual privity and one party seeks to recover damages in tort for matters arising from the contract.

Ohio follows the economic-loss rule. In *Corporex Development & Construction Management, Inc. v. Shook, Inc.*, 106 Ohio St. 3d 412; (2005) the Ohio Supreme Court held that the economic-loss rule bars a building project owner from recovery of purely economic damages in tort against a subcontractor, based upon breach of contractually created duties. In *Corporex*, the court stated:

The economic-loss rule generally prevents recovery in tort of damages for purely economic loss. The well-established general rule is that a plaintiff who has suffered only economic loss due to another's negligence has not been injured in a manner which is legally cognizable or compensable. This rule stems from the recognition of a balance between tort law, designed to redress losses suffered by breach of a duty imposed by law to protect societal interests, and contract law, which holds that "parties to a commercial transaction should remain free to govern their own affairs. Tort law is not designed * * * to compensate parties for losses suffered as a result of a breach of duties assumed only by agreement. That type of compensation necessitates an analysis of the damages which were within the contemplation of the parties when framing their agreement. It remains the particular province of the law of contracts. [Citations omitted.]

The limits of the economic-loss rule were set forth in *Lee, v. Dublin Manor Corp.*, 2007 U.S. Dist. LEXIS 56703, (2007, U.S. D. Ct. S. D, OH, E. D.) where the buyers alleged that during the closing, they asked the closer whether a valid and permanent certificate of occupancy existed for the property; that the closer, as an employee and agent of the title agency and the insurer, said the certificate was contained in the papers that the buyers would receive at the closing; that, the buyers contend that a permanent certificate of occupancy had not been granted; and that, the insurer through its agent, falsely misrepresented this fact to them, thereby causing them to rely upon the representation. The court held the tort claims of fraudulent inducement and negligent misrepresentation were not barred by the economic-loss rule. The court also held that the merger clause in the policy was not broad enough to exclude the tort claims.

The question is: "Are there contractual steps an escrow agent can take to clearly and unambiguously limit its liability from the tort claims of negligent title search?" The answer once again is: the escrow agent should play follow the leader, that is, follow the lead of the title insurers and the ALTA.

In Ohio, there is no independent tort claim against a title insurer for negligence.

The title insurance companies have successfully argued that the title insurance policy controls and there is no independent tort claim against the title insurance company for negligence. The Ohio Supreme Court agrees. In *Chicago Title Insurance Company v. The Huntington National Bank*, 87 Ohio St. 3d 270 (1999), the Court held:

HNB filed an independent tort claim based upon Chicago Title's negligent failure to discover and disclose the existence of a superior mortgage. Based on the merger clause in Section 14(b) of the policy's Conditions and Stipulations section that restricts any claim of loss or damage, including negligence claims, to the policy provisions, we find that HNB's negligence claim fails. The policy language explicitly precludes an independent tort action by HNB for negligence arising out of the status of its lien or of title to the secured property. Therefore, HNB is limited to the contractual remedies available in the policy, and its negligence claim fails.

You as the title agent cannot so easily point to the title insurance policy, to which you are not a party, (other than having issued the policy on behalf of the insurer) to preclude your liability for search negligence. So why not place into your escrow agreement, which is your contract with the parties, a clause modeled after the title insurance policy language to limit your search liability. What's in your escrow agreement? Here's a possible clause:

Escrow Agent shall not be liable for the status of title. If Escrow Agent searches title, directly or indirectly, issues a title commitment and / or issues a title policy of insurance, any such search or any such issuance are on behalf of a disclosed principal, the title insurance company. No party to this escrow agreement shall have any claim including any claim for negligent title search or for failure to disclose an encumbrance or other matter, against the Escrow Agent as to any title search, any issuance of a title commitment or any issuance of a title insurance policy. Any claim of loss or damage, or any action, whether or not based on negligence, which arises out of the status of the title to the estate or interest which is the subject of this escrow agreement, or which relates to a title search, title commitment or title policy, shall be exclusively limited to the amount of the charge or fee paid for the search, if there is no commitment or policy issued, or shall be exclusively limited to the terms of the title commitment or title insurance policy issued.

In addition, there should be a merger clause or integration clause to tie up any loose ends. A possible merger clause is:

This is the complete agreement between the parties. Each party has had the opportunity to read this agreement, to understand it, to make changes where requested and agreed and, to consult with the experts of their choice, including legal experts. All prior representations, agreements and discussions are merged herein. No party, person, employee or agent may modify this agreement by any oral statement or representation. All modifications of this agreement must be in writing signed by all parties. The signing of this agreement is the free and voluntary act of each party.

Conclusion: It is time for Ohio title agents and escrow agents to revise the standard conditions of acceptance of escrow.

Placing any language into an escrow agreement will not guarantee that you as escrow agent are immune from being sued. There is no such inoculation effect. But taking prudent, reasonable steps to clarify your duties and obligations and to limit your liabilities always makes sense.

No agreement, including the so-called standard conditions of escrow, is a standard forever. The "standard conditions of acceptance of escrow" is not the U.S. Constitution. Its terms are not sacrosanct; and, are much easier to change. It is time for you as an independent title and escrow agent to review your escrow agreement, to choose language which clearly limits your liability in any reasonable ways possible. In the end, the consumer and the title industry will be better served. Clauses, other than the three suggested here, should also be added. Other language for the clauses suggested here may be more appropriate for a particular agent. Care should be taken. The views expressed in this article do not constitute legal advice. Consult your lawyer. Consult a knowledgeable title insurance and escrow agent lawyer.

Remember each time you hear the excellent, Capital One commercial question: "What's in your wallet?", think: "What's in your escrow agreement?" It's your responsibility. It's your choice. The answer could seriously affect your wallet.

Respectfully submitted,

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