



## **Unpacking Title Insurance - Past, Present...and What's Next?**

Matt Meade, ACAS, MAAA

Chris Schubert, FCAS, MAAA

Art Randolph, FCAS, MAAA, CPCU, ARM, ARe

September 20, 2022

# Antitrust Notice

- **The Casualty Actuarial Society is committed to adhering strictly to the letter and spirit of the antitrust laws. Seminars conducted under the auspices of the CAS are designed solely to provide a forum for the expression of various points of view on topics described in the programs or agendas for such meetings.**
- **Under no circumstances shall CAS seminars be used as a means for competing companies or firms to reach any understanding – expressed or implied – that restricts competition or in any way impairs the ability of members to exercise independent business judgment regarding matters affecting competition.**
- **It is the responsibility of all seminar participants to be aware of antitrust regulations, to prevent any written or verbal discussions that appear to violate these laws, and to adhere in every respect to the CAS antitrust compliance policy.**



# About the Presenters

---



## **Matt Meade, ACAS, MAAA**

Associate Actuary, Pinnacle Actuarial Resources

- 11 years of experience in the property/casualty (P/C) insurance industry
- Experience in assignments involving loss reserving, captive renewals, funding studies, loss cost projections, risk margin calculations, personal and commercial lines, self-insureds
- Serves as lead analyst for several of Pinnacle's title insurance clients

# About the Presenters

---



## **Chris Schubert, FCAS, MAAA**

Consulting Actuary, Pinnacle Actuarial Resources

- 11 years of experience in the P/C insurance industry
- Experience in assignments involving loss reserving, pricing/product management, rate filings, regulatory reporting, funding studies, personal and commercial lines
- Serves as project manager for several of Pinnacle's title insurance clients

# About the Presenters

---



## **Art Randolph, FCAS, MAAA, CPCU, ARM, ARe**

Principal, Pinnacle Actuarial Resources

- 20+ years of experience in the P/C insurance industry, focused on ratemaking and reserving for property and long-tailed exposures
- CAS Finance Council & Diversity Impact Group
- American Academy of Actuaries' Committees:
  - Medical Professional Liability (former member)
  - P/C Extreme Events and Property Lines
  - Workers' Compensation
- Serves as appointed actuary for the majority of Pinnacle's title insurance clients

# Agenda

---

- ▶ Title Insurance Background
- ▶ Policy Types and Comparison to P/C Insurance Market
- ▶ Reserving Characteristics
- ▶ 2007 - 2008 Real Estate Market Crash
- ▶ Historical Financial and Underwriting Results
- ▶ COVID-19 Impact
- ▶ Recent Market Observations
- ▶ Future Challenges

# Title Insurance Background



# What is Title Insurance?

---

- Protects real estate owners and lenders from financial loss arising from defects in the title to real property
  - Title: evidence of ownership of a piece of property
- Defects include:
  - Liens
  - Easements
  - Fraud
  - Forgery
  - Documentation
  - Errors
  - Undisclosed heirs
  - Property boundary disputes, etc.

# Purpose of Title Insurance

---

- To protect the financial interests of the parties involved in real estate transactions
- To assure that property transfers are secure
- To facilitate transactions in the real estate market

# How is a Title Insurance Policy Created?

---

- Title Search: process of searching and reviewing public records for ownership history
  - Occurs after sales contract is signed, but before property transaction is closed
  - Labor-intensive, largely manual process
  - 25% of title searches reveal defects
- Title company prepares report and issues policy at closing
  - One-time lump sum premium payment
  - Covers cost of fixing defects and future claims from errors in title search

# How is a Title Insurance Policy Sold?

---

- Lenders require title insurance to protect interest in the collateral of mortgage loans secured by real estate
- Most policies are written by referral through affiliate networks
- Majority of homeowners are unaware that they may select their own title insurance company

# Claim Examples

---

- Errors in public records
- Unknown liens
- Illegal deeds
- Missing heirs
- Forgeries
- Undiscovered encumbrances
- Unknown easements
- Boundary/survey disputes
- Undiscovered will
- False impersonation of previous owner

# Claim Example #1

---

- Boundary/survey dispute:
  - The former owners of your home put up a fence that was thought to be on your property but is actually on land owned by your neighbor
  - Your neighbor might file a claim requiring you to move the fence back to your own property
  - You can then file a claim with your title insurance company to resolve this dispute
  - Your title insurer might pay you to hire a contractor to remove the fence and put up a new one



# Defalcations

---

- Occur when title insurance agent misappropriates or misdirects money held in trust for parties involved in a real estate transaction
- Can be negligent or intentional act by agent
- Title insurance companies are liable for defalcations
  - Pursue subrogation through title agent's E&O policy, identification of third parties who have benefited, restitution from criminal prosecution
  - Defalcations can lead to insolvency

# Claim Example #2

---

## Defalcation (real life example)

- Maryland agent inflating mortgage costs and pocketing the difference
- License revoked for both agent and insurance company

# Policy Types and Comparison to P/C Insurance Market



# Types of Title Insurance Policies

---

- Owner's Policy: protects the buyer
  - Covers the amount of the purchase price
  - Remains in effect until property is sold
- Lender's Policy: protects the lender
  - Covers the amount of the loan
  - Remains in effect until mortgage is paid off or refinanced
- Most are uniform American Land Title Association (ALTA) policies modified for state rules and regulations

# New Home Purchase vs. Refinance

---

- New Home Purchase: requires owner's policy and lender's policy
  - Protects investments of both parties in transaction
- Refinance: requires new lender's policy
  - Protects mortgage lender's investment on refinance loan
  - Original loan is paid off and new title search is performed
- Proportion of title insurance premium from refinance varies based on interest rates, strength of housing market, economic variables

# Comparison to P/C Insurance – Risk Transfer

---

## Title Insurance

- Focuses on risk prevention
- Past events: losses are incurred before policy effective date

## P/C Insurance

- Focuses of risk assumption
- Future events: losses are incurred after policy effective date

# Comparison to P/C Insurance – Market Structure

---

## Title Insurance

- Low competition
- Mono-line restrictions
- Four families accounted for over 80% of written premium in 2021

## P/C Insurance

- Competition varies by line
- Multi-line is common

# Comparison to P/C Insurance – Premium

---

## Title Insurance

- One-time lump sum payment
- Calculated as standard rate per \$1,000 of purchase price – rates vary by state
- Policy period: until property is sold or mortgage is paid

## P/C Insurance

- Recurring payments
- Calculated through risk classification
- Policy period: 6-month, 12-month, etc.

# Reserving Characteristics



# Reserving Characteristics

---

- Loss development patterns
  - Long-tail
  - Influenced by economic variables, shifts in urban/suburban/rural population densities, homeownership patterns
  - Adjustments for housing crisis years
- Market influences on loss trends
  - Influenced by home prices, wages, unemployment, etc.
  - Health of real estate market and economy as a whole are primary drivers
  - New home purchases vs. refinancing

# Frequency and Severity

---

- Frequency
  - Low frequency
  - Related to health of housing market
- Severity
  - High severity
  - Related to home prices

# Reserving Approach

---

- Influenced by Schedule P structure for title insurance companies
- Analysis by policy year and report year
- ALAE and ULAE vs. DCC and A&O
- Comparison of actuarial reserves to statutory reserves

# Types of Reserves – Schedule P Reserve

---

- Known Claims Reserve: calculated from report year analysis
  - Case reserves and bulk reserves on known claims
- IBNR Reserve: difference of policy year analysis and report year analysis
  - “Unknown” claims
- ULAE reserve
- Schedule P reserves = Case + Bulk + IBNR + ULAE

# Types of Reserves – Statutory Premium Reserve (SPR)

---

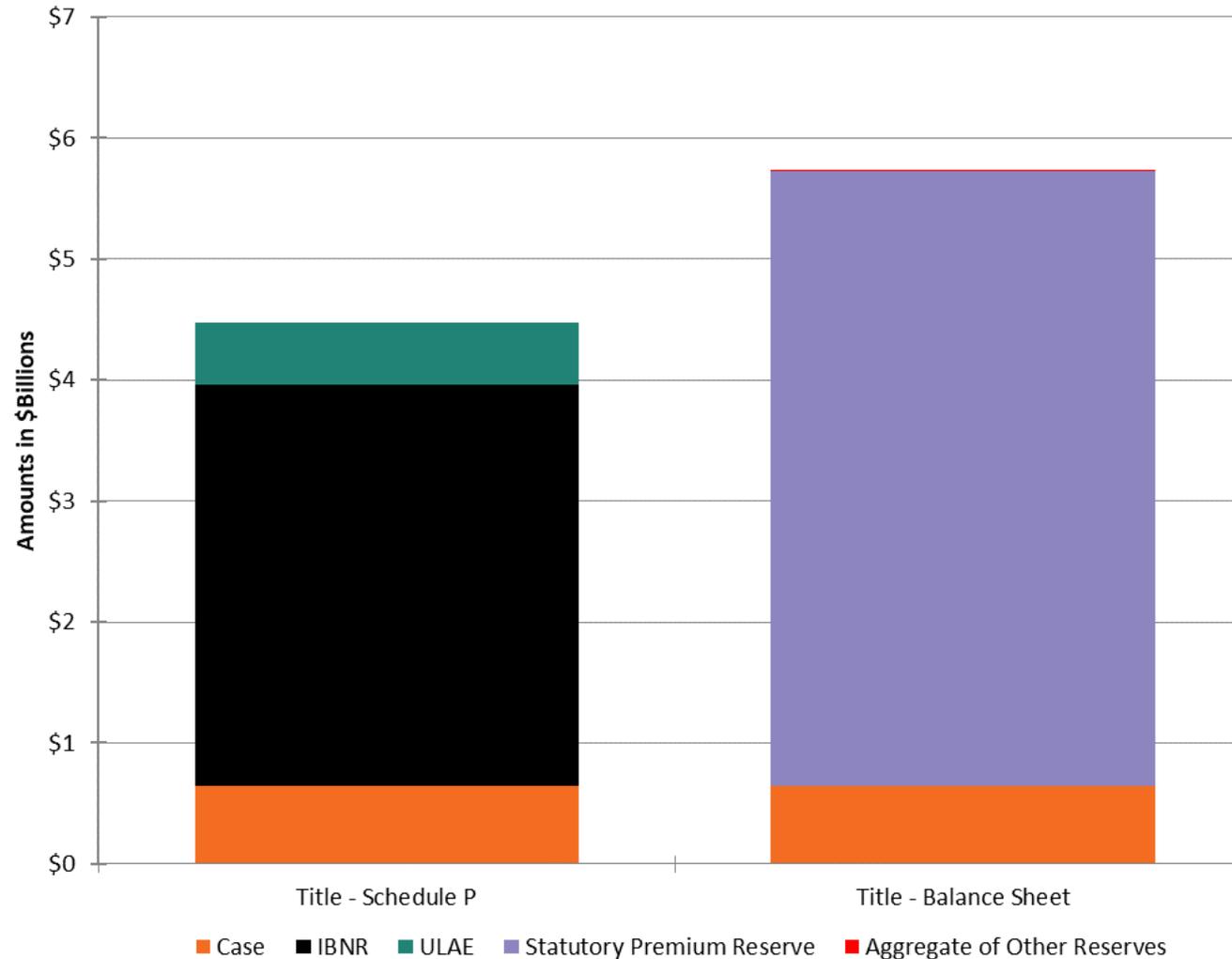
- Unearned premium reserve
- Calculated by formula based on state of domicile
- Based on written premium volume and take-down pattern over 10-20 year period
- More reflective of state's underlying title framework and customs than company's loss experience

# Types of Reserves – Supplemental Reserve

---

- Compare Schedule P reserves to  $SPR + \text{Known Claims Reserve} + \text{Agg Reserves}$ 
  - $\text{Schedule P reserves} = \text{Case} + \text{Bulk} + \text{IBNR} + \text{ULAE}$
- Supplemental Reserve
  - Excess of Schedule P reserves above  $SPR + \text{Known Claims} + \text{Agg Reserves}$
  - Equal to 0 if  $\text{Schedule P} < \text{SPR} + \text{Known Claims} + \text{Agg Reserves}$

# Types of Reserves – Supplemental Reserve



Supplemental Reserve = \$0

# 2007 - 2008 Real Estate Market Crash



# 2007 - 2008 Real Estate Market Crash

---

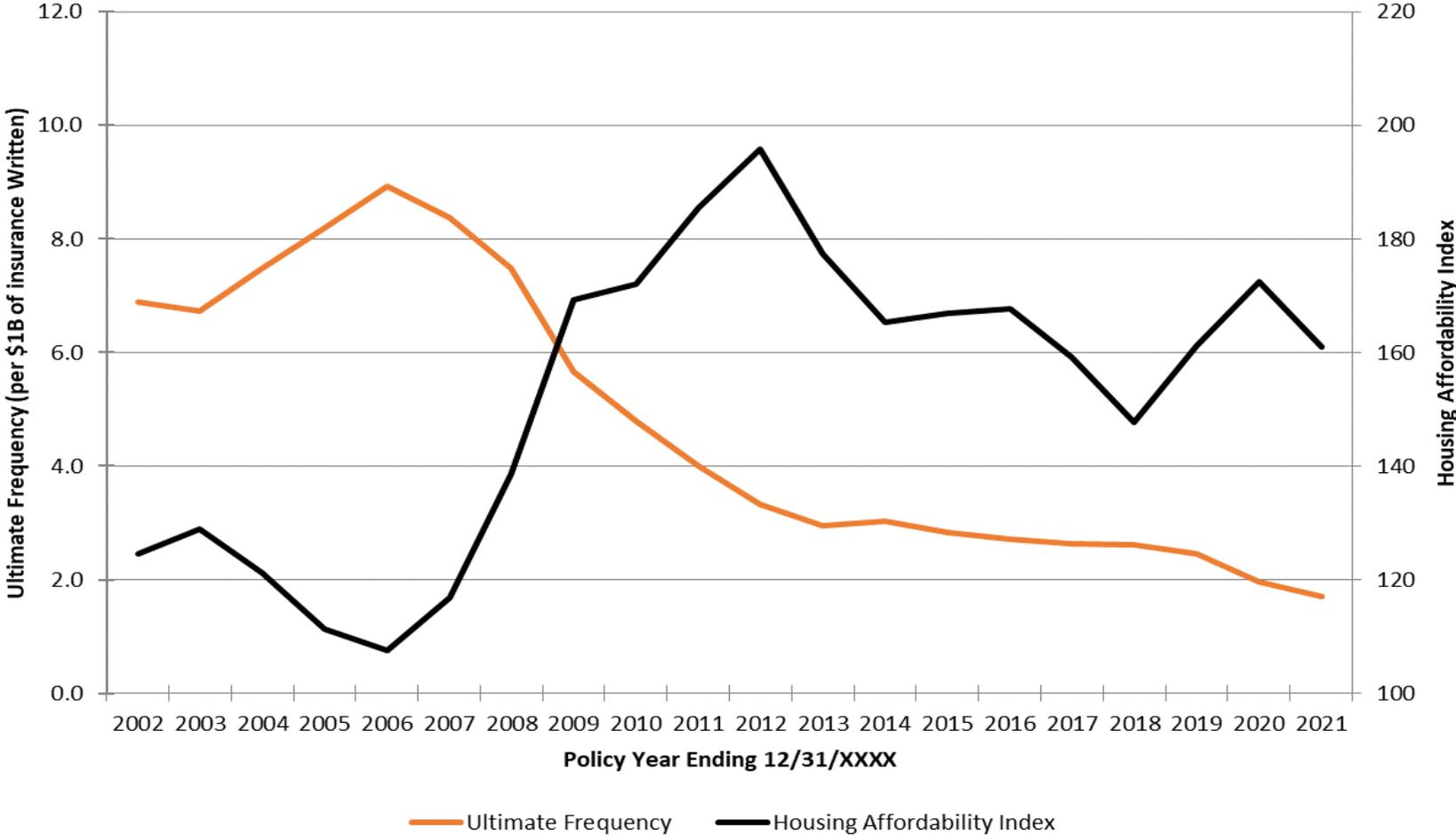
- 2007: credit markets tighten
- 2008: credit markets freeze
  - Plummeting real estate sales
  - Declining home prices
  - Owners unable to borrow (or sell) their way out of trouble
  - Increasing delinquencies, defaults
  - Spike in foreclosures
  - More lenders find themselves with financial losses

# Impact on Claims

---

- Foreclosure searches trigger wave of reported claims
  - Surge in reported claim frequency
  - Higher percentage of claims closed with no payment
- Mortgage fraud on the rise: What is the title agent's role/responsibility?
- Large defalcations emerge as business volumes drop off
- Claims not brought in a rising housing market are an issue in a declining one

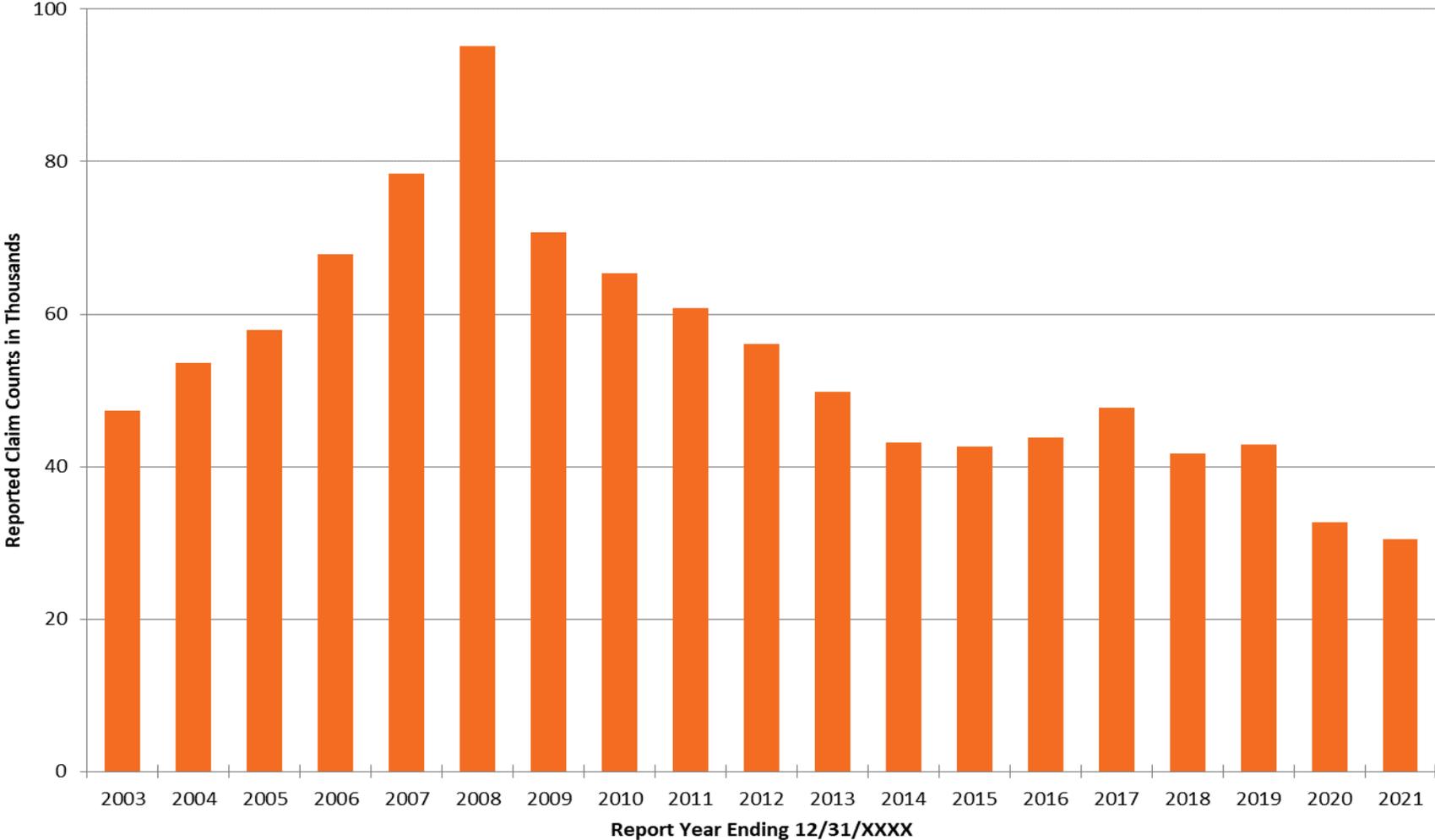
# Ultimate Frequency vs. Housing Affordability - Family



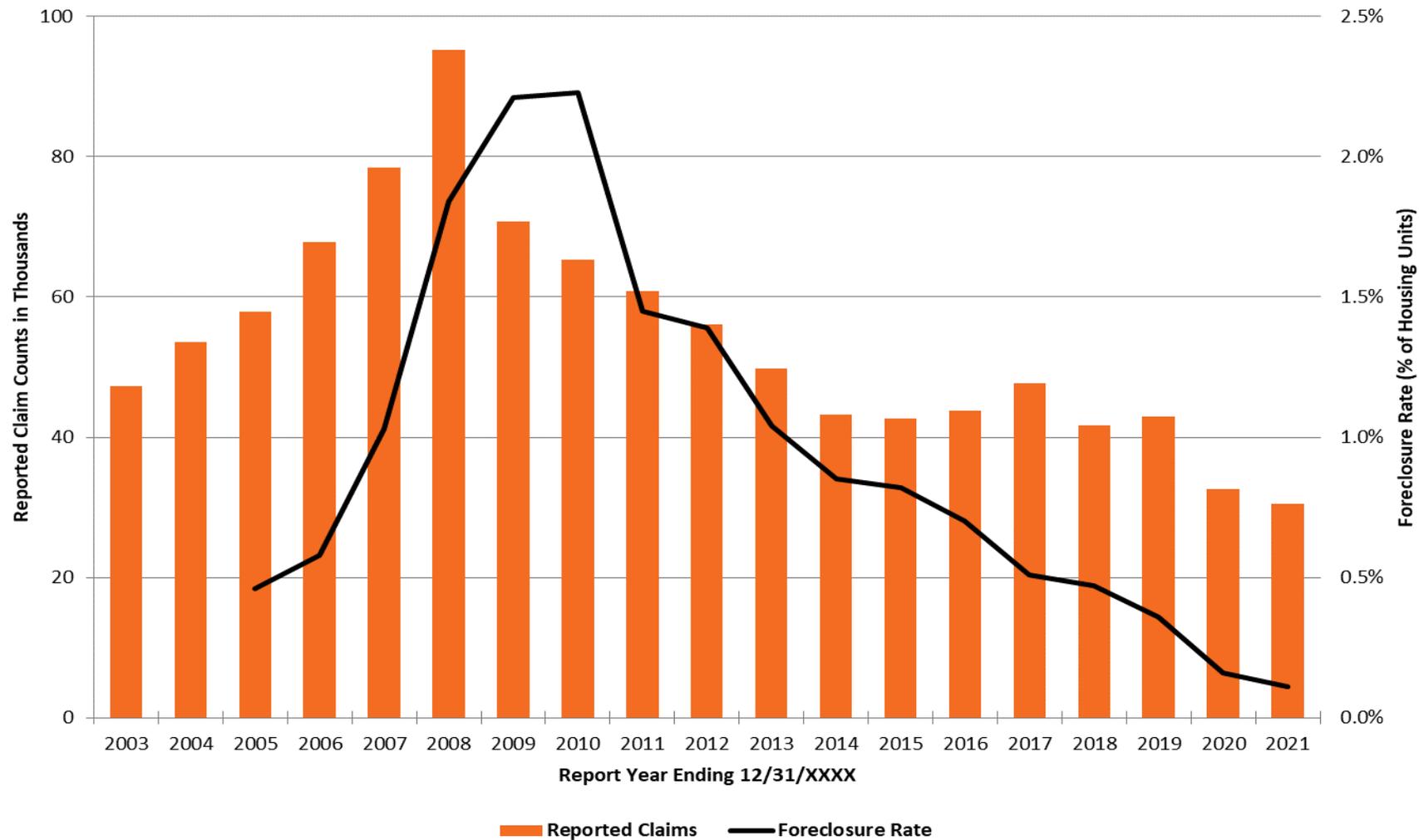
Frequency based on reported claims x-CNP; Housing affordability index from Moody's



# Reported Claim Counts by Report Year - Family

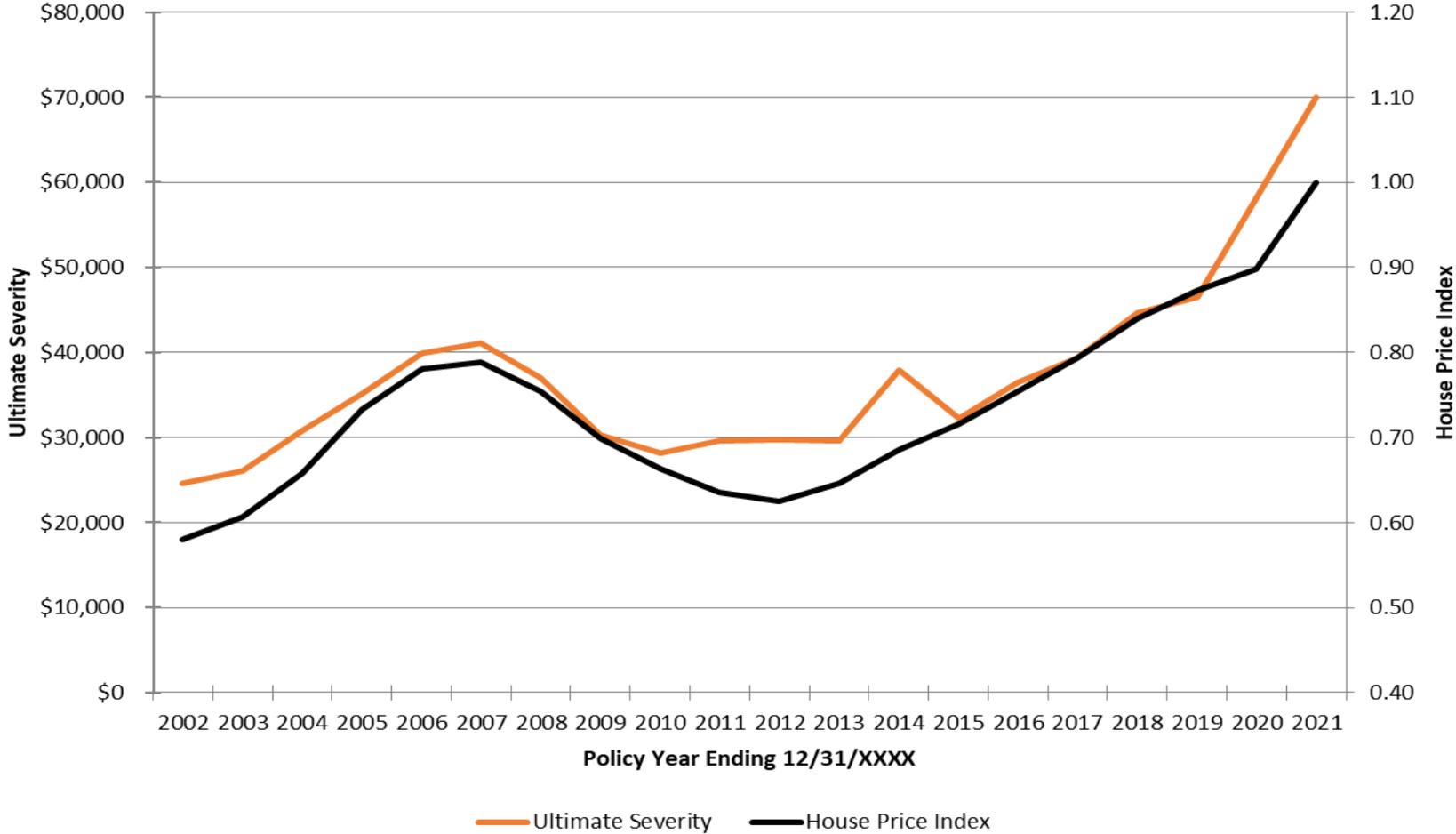


# Reported Claim Counts by Report Year vs. Foreclosures - Family



Foreclosure Activity Source: [www.attomdata.com](http://www.attomdata.com)

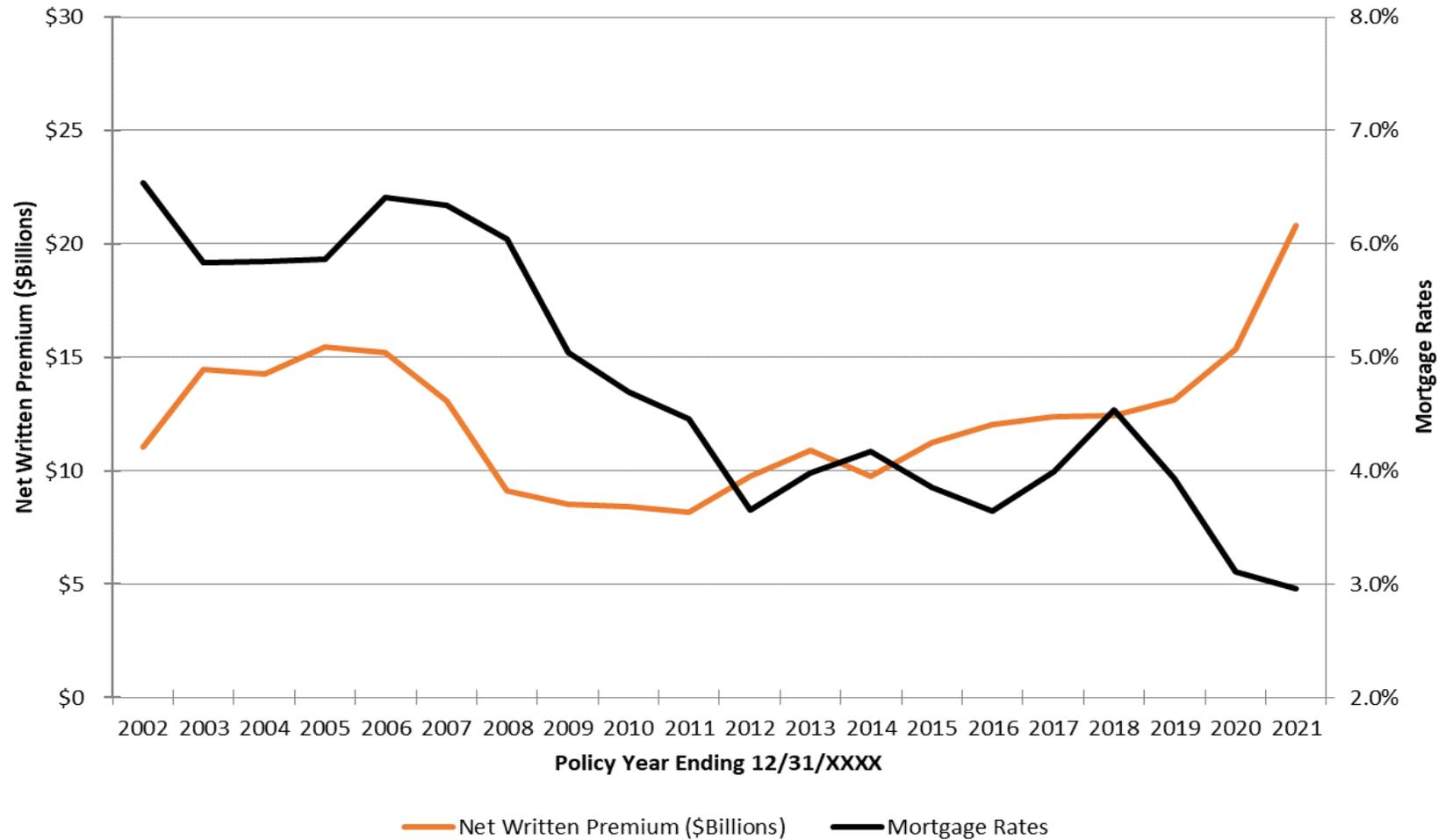
# Ultimate Severity vs. Home Prices - Family



Severity based on reported claims x-CNP; House price index from Moody's



# Net Written Premium vs. Mortgage Rates - Family



Mortgage rates from Moody's

# Historical Financial and Underwriting Results

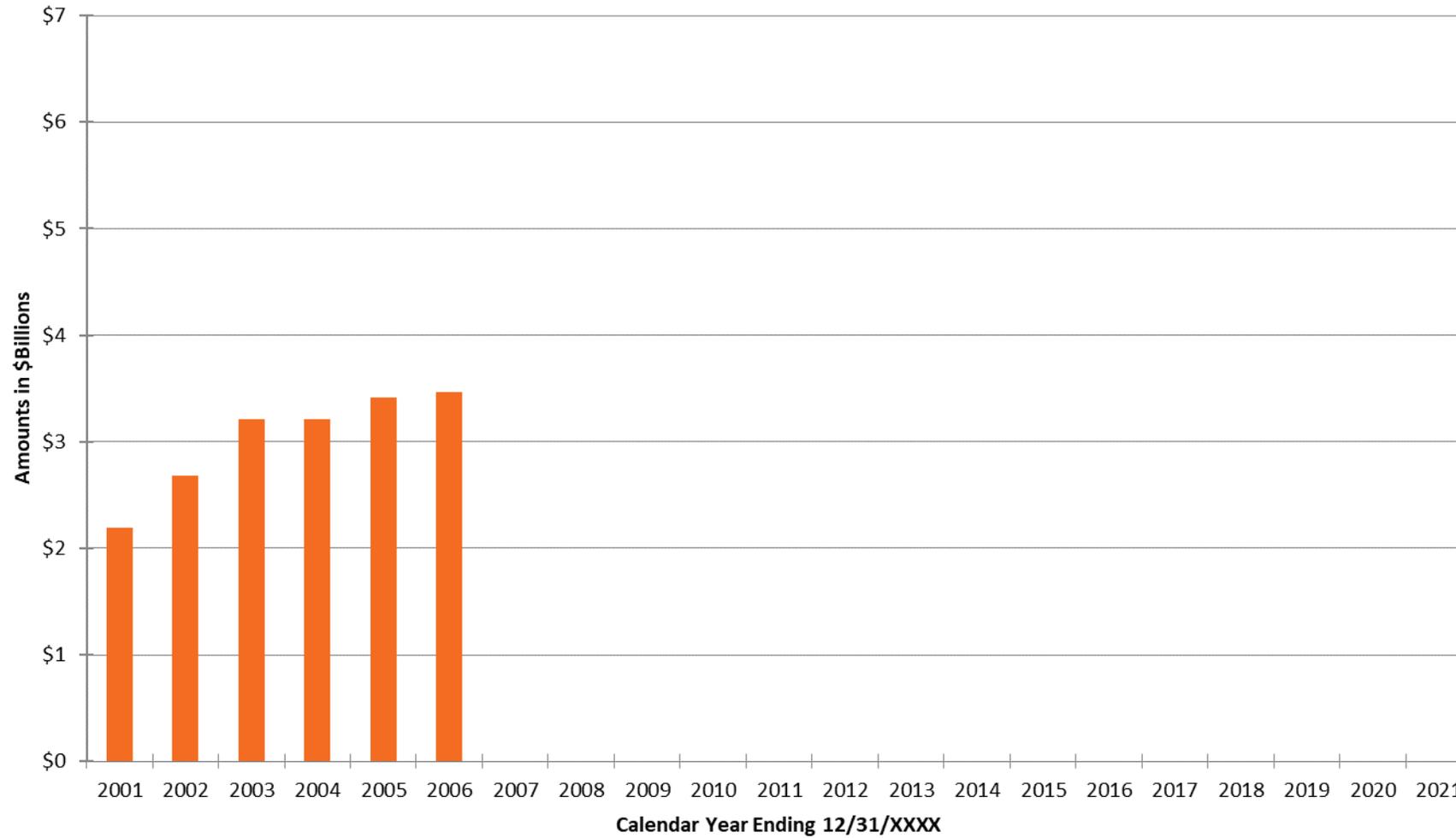


# Historical Financial and Underwriting Results

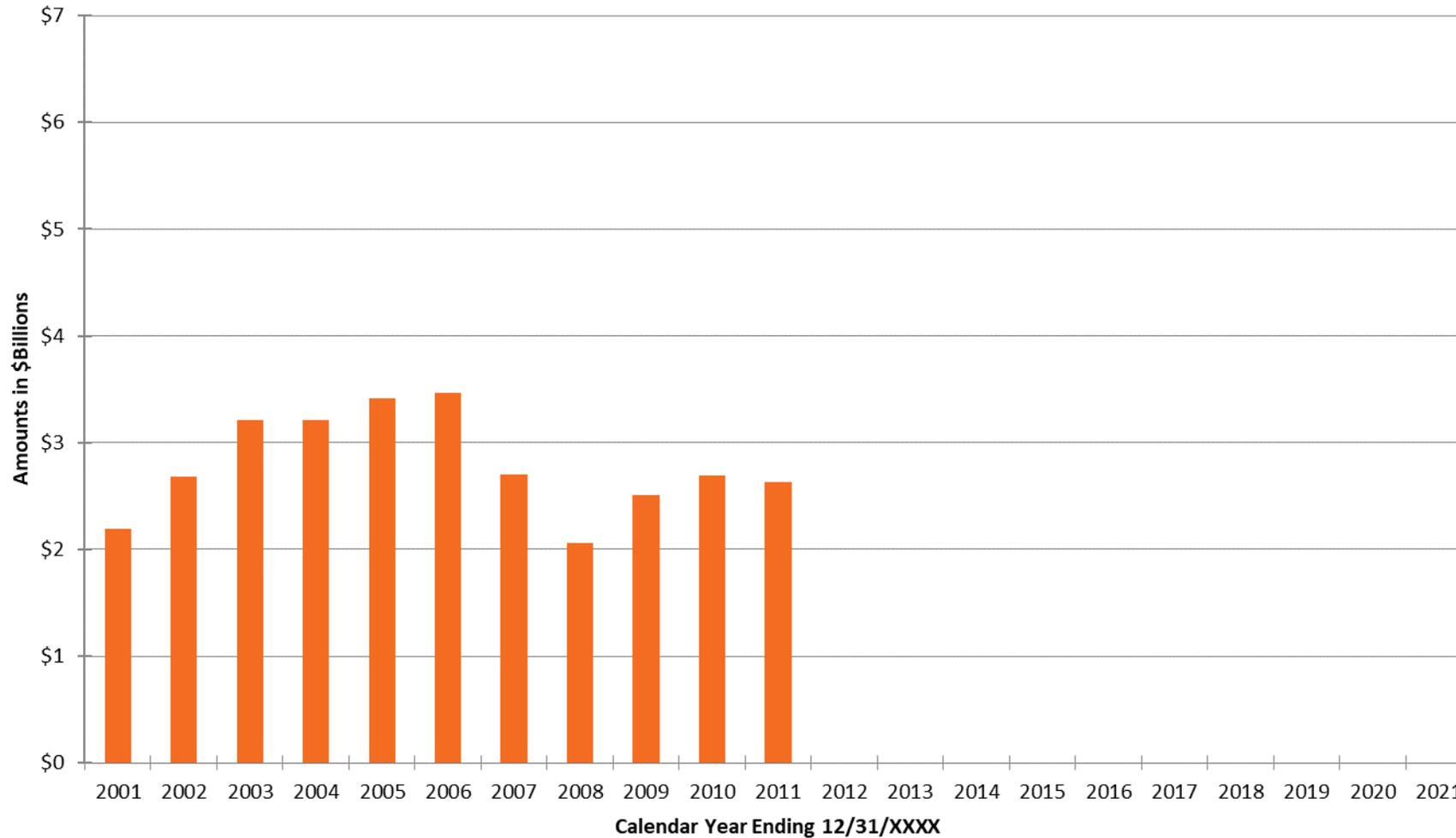
---

- Calendar years 2001 through 2021
- Presented for the total title industry (four families and all other)
  - Fidelity
  - First American
  - Old Republic
  - Stewart
  - Independent companies

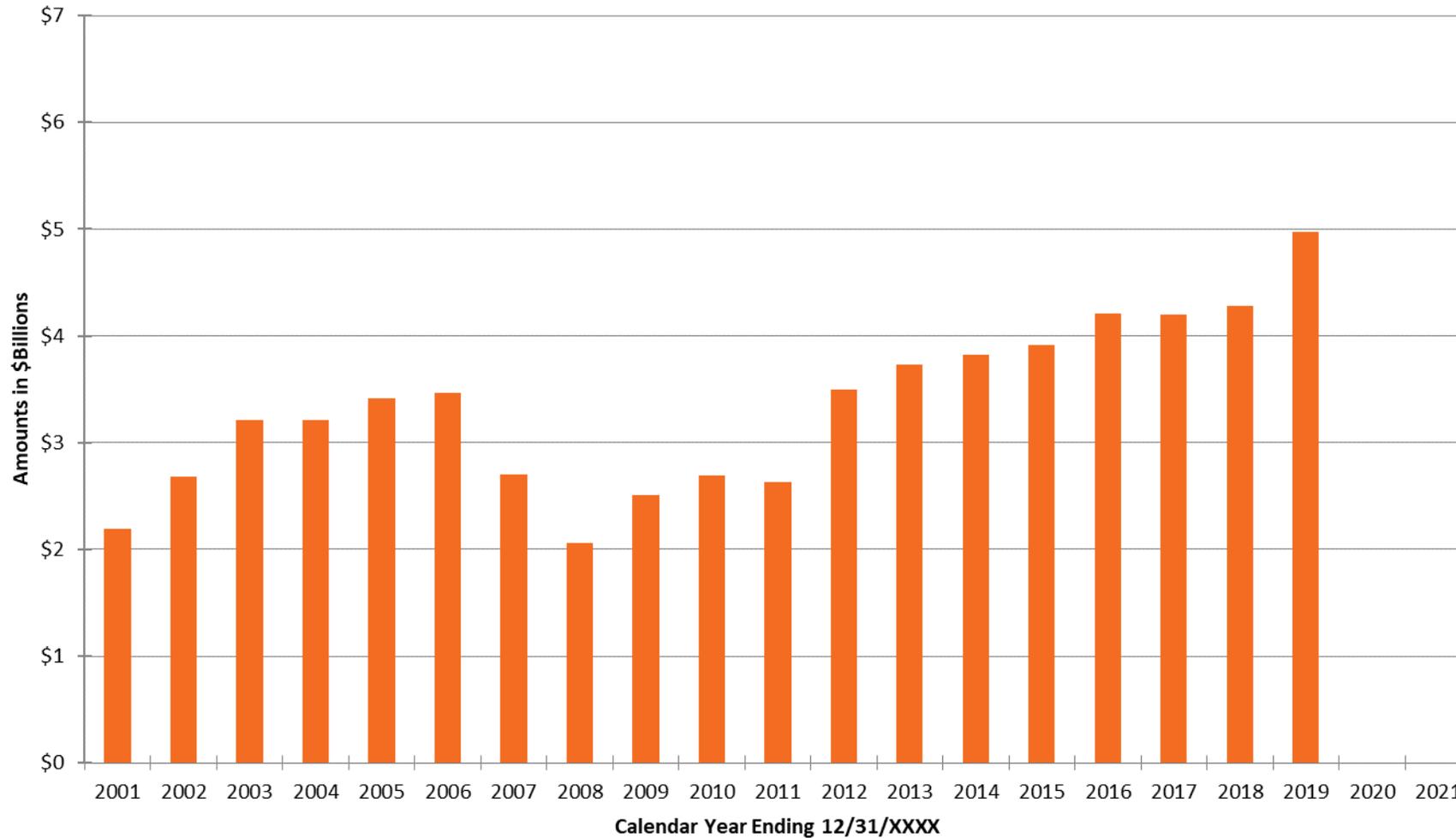
# Surplus (2001 - 2006)



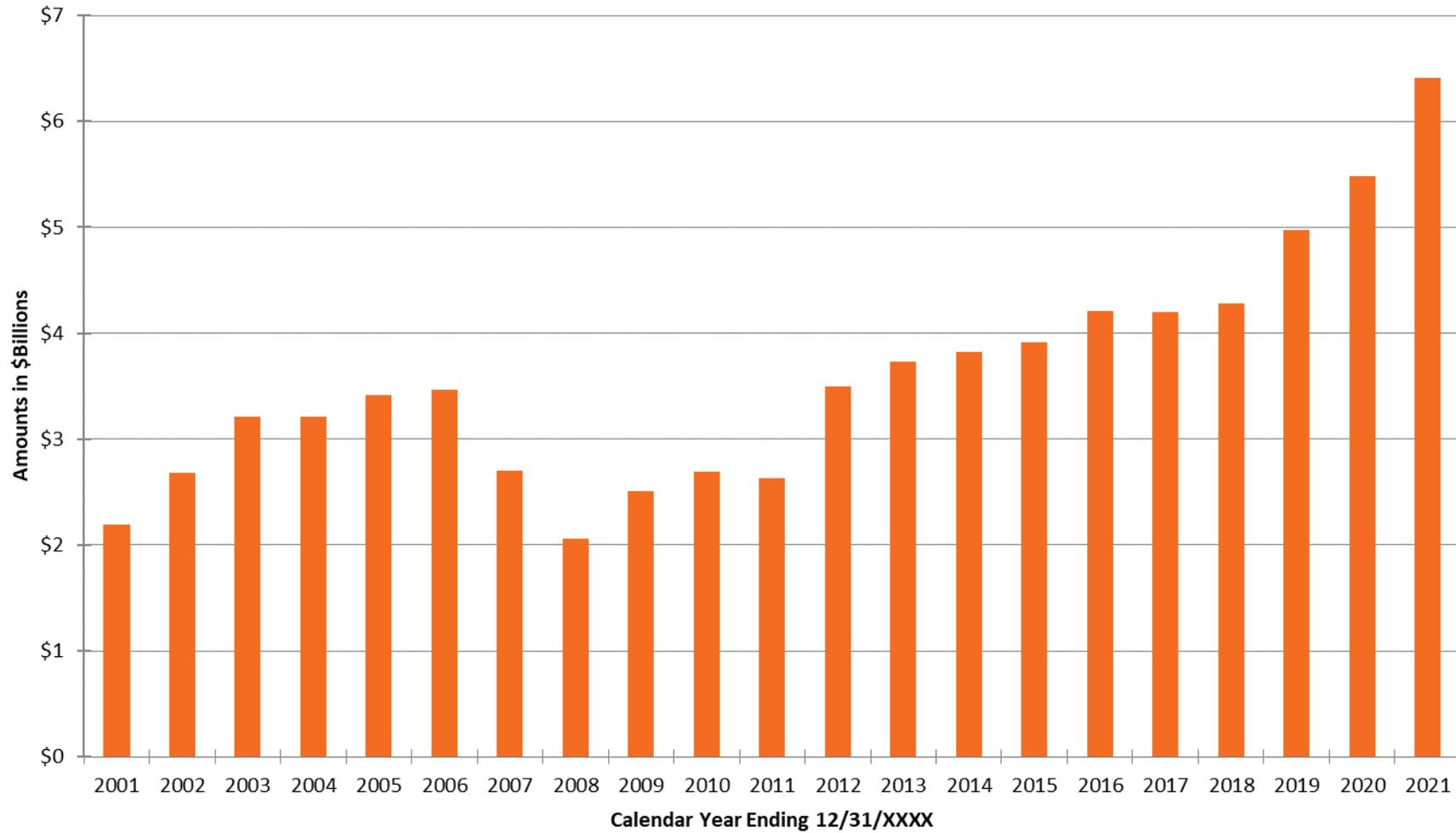
# Surplus (2001 - 2011)



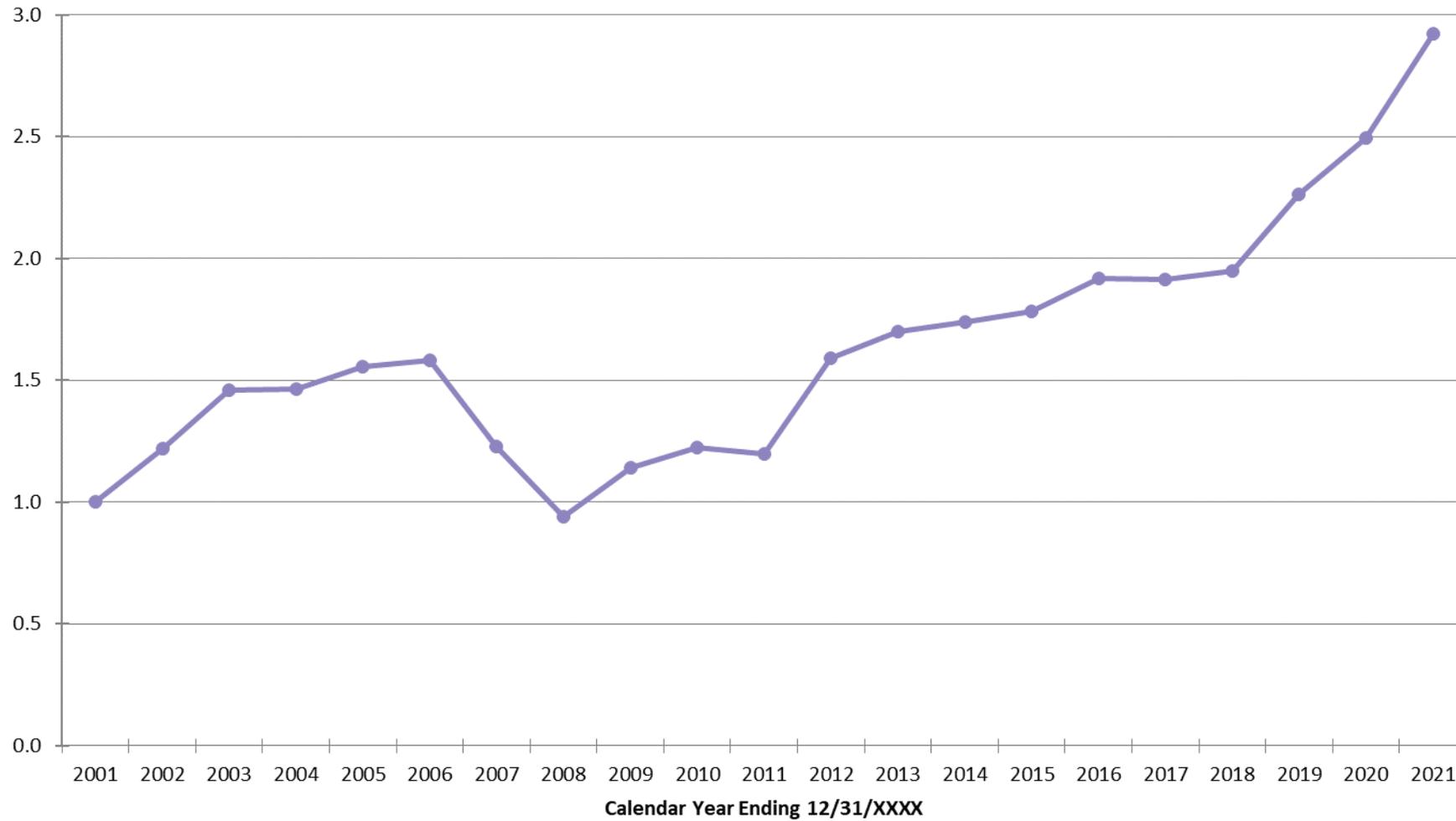
# Surplus (2001 - 2019)



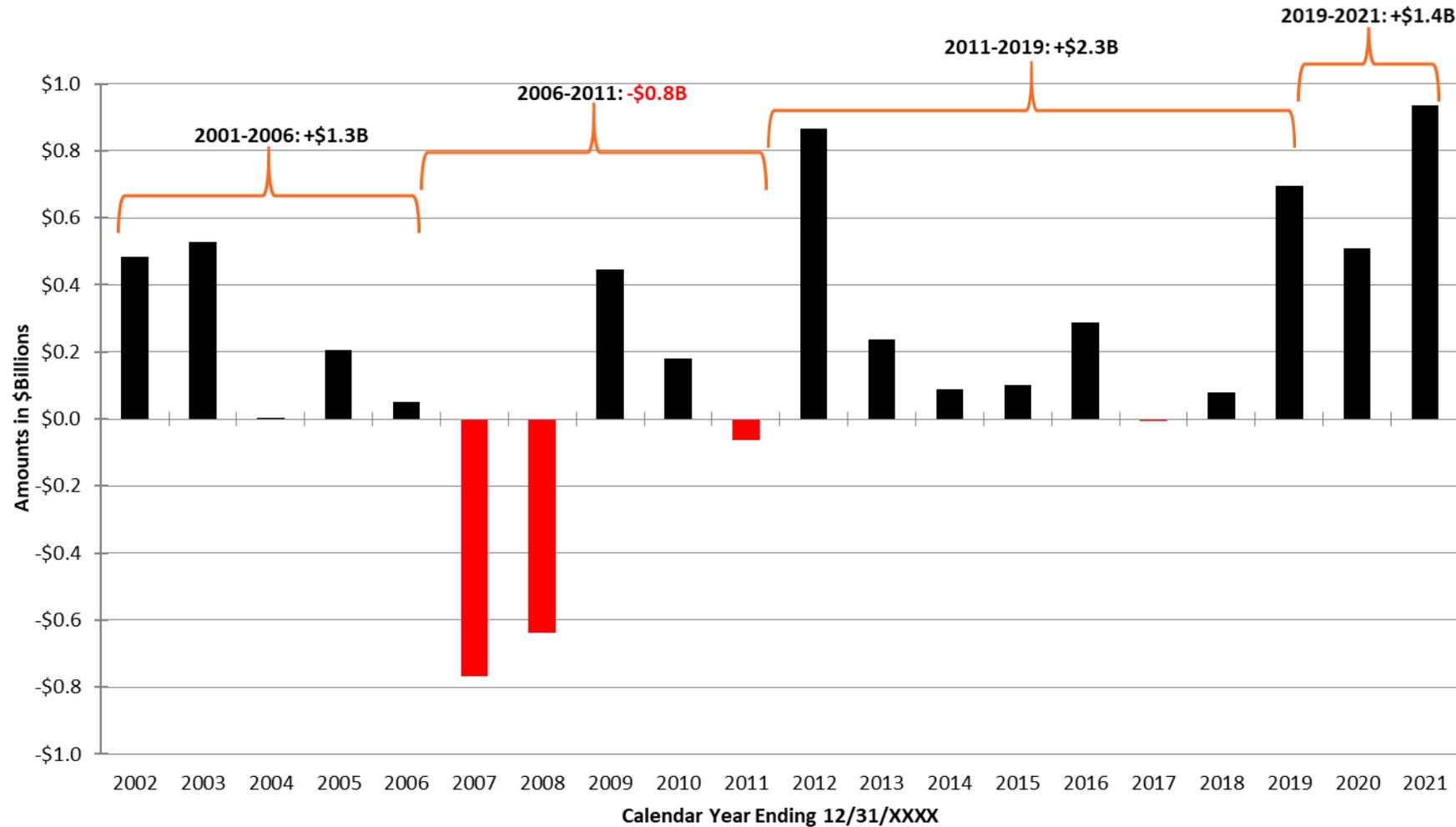
# Surplus (2001 - 2021)



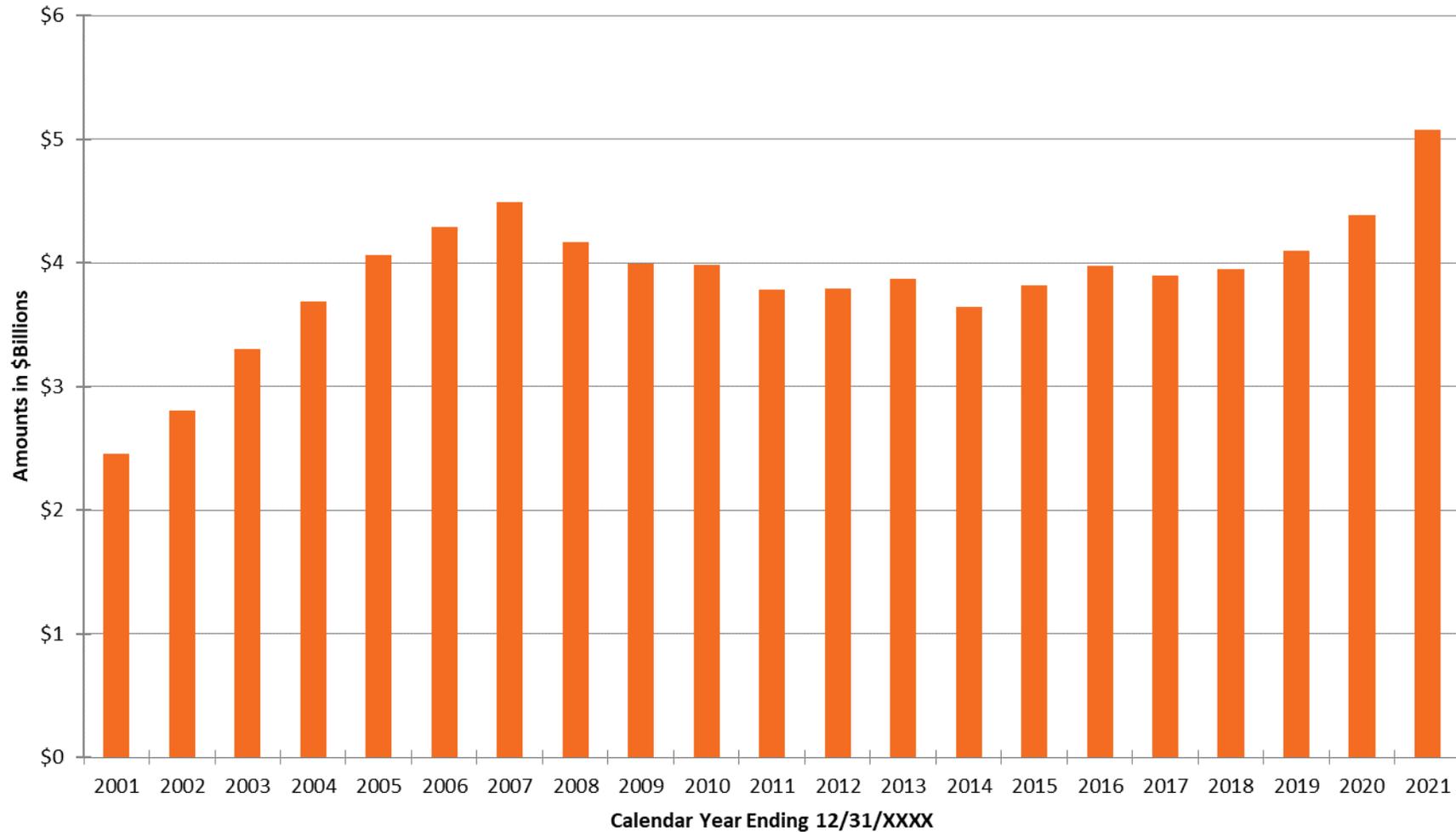
# Surplus: Indexed to 2001



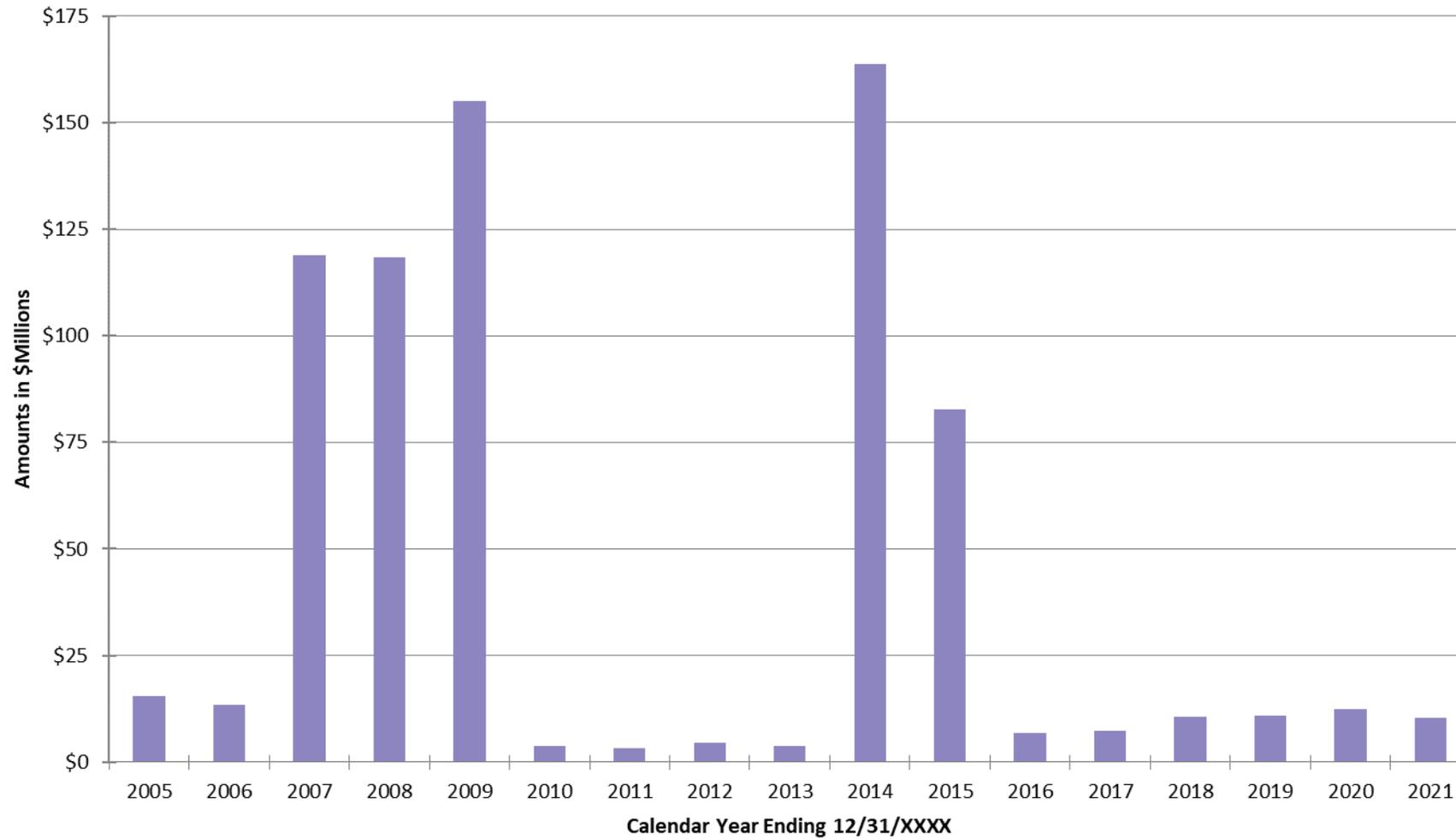
# Change in Surplus



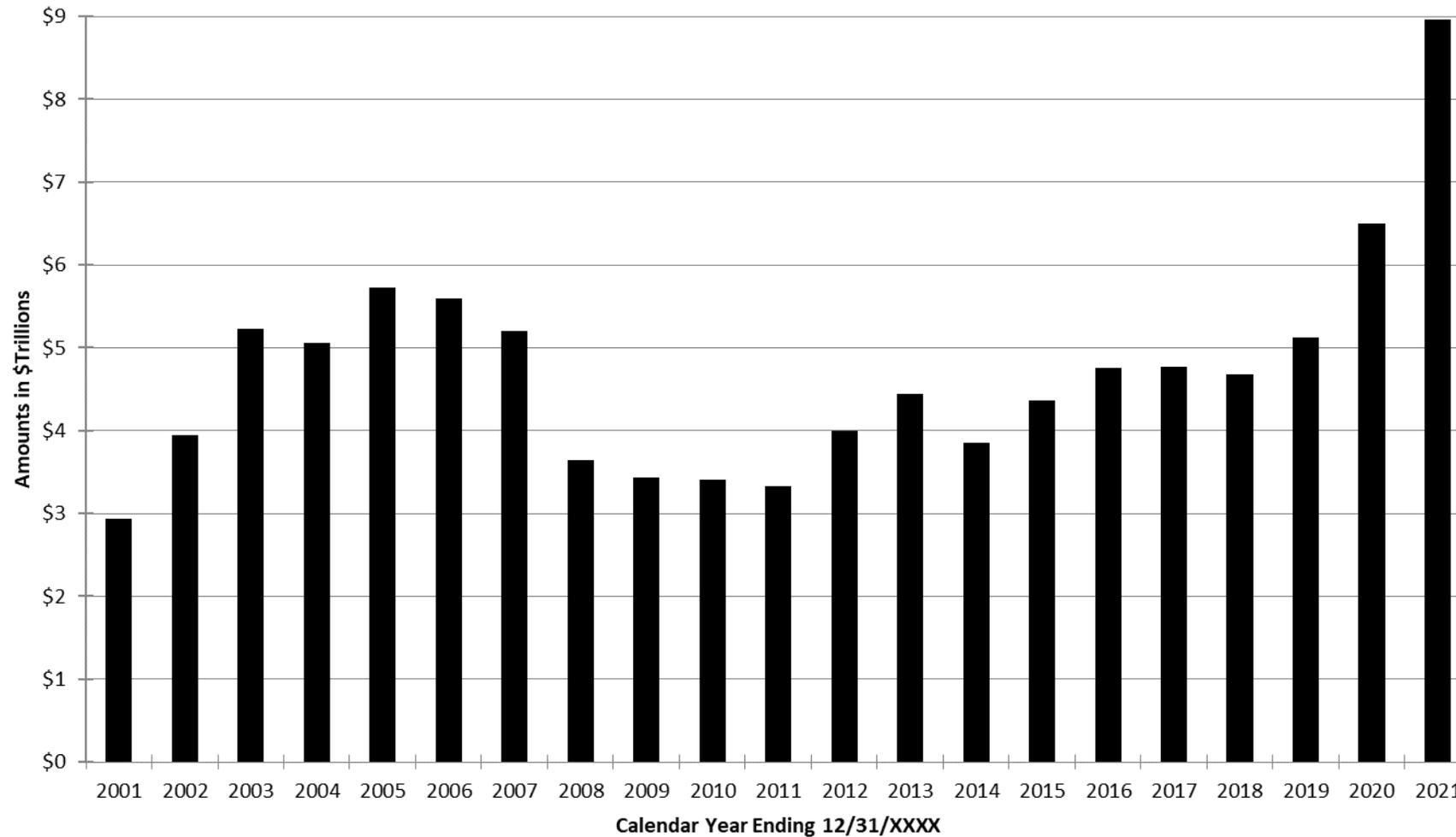
# Statutory Premium Reserve



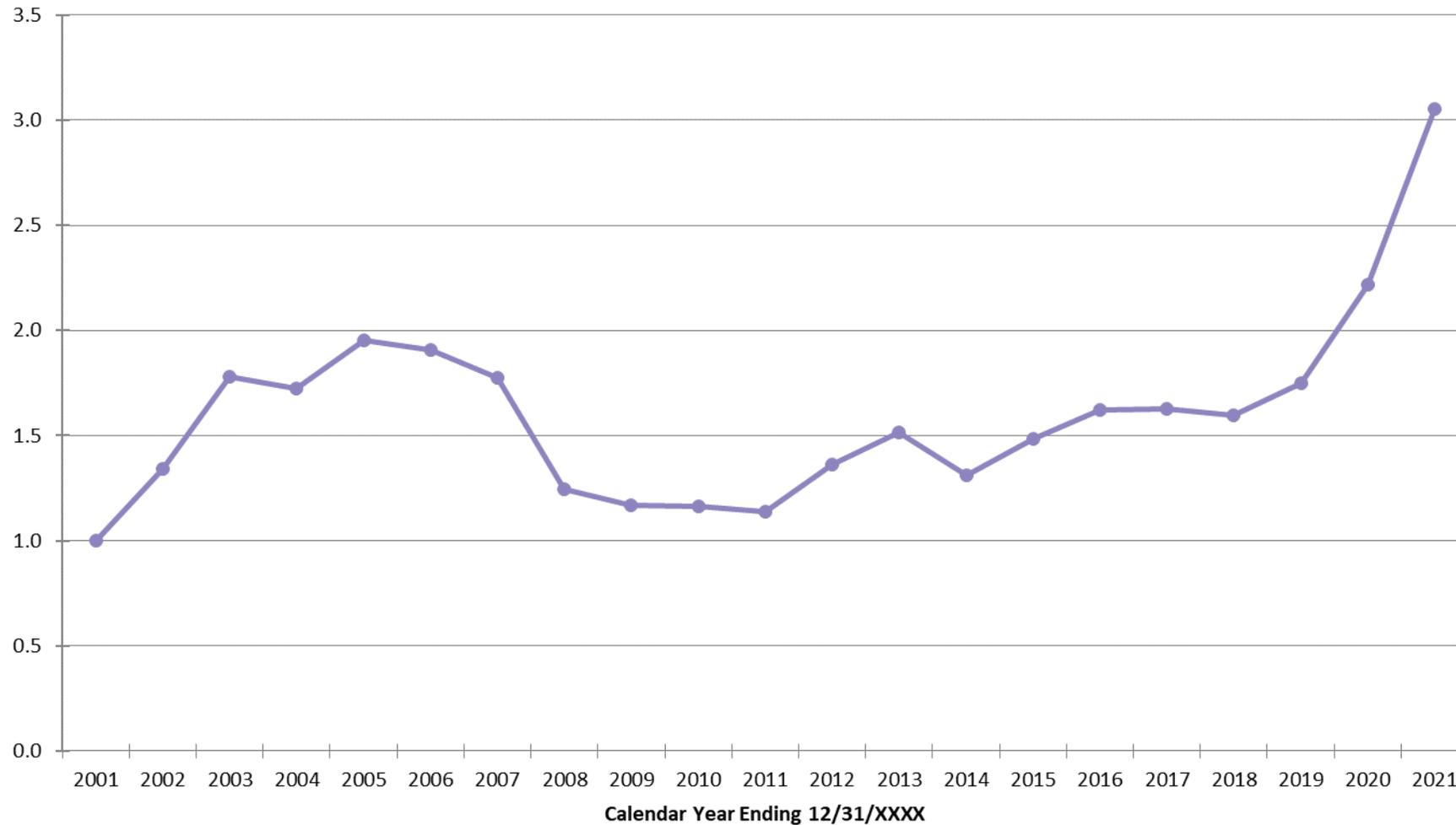
# Supplemental Reserve



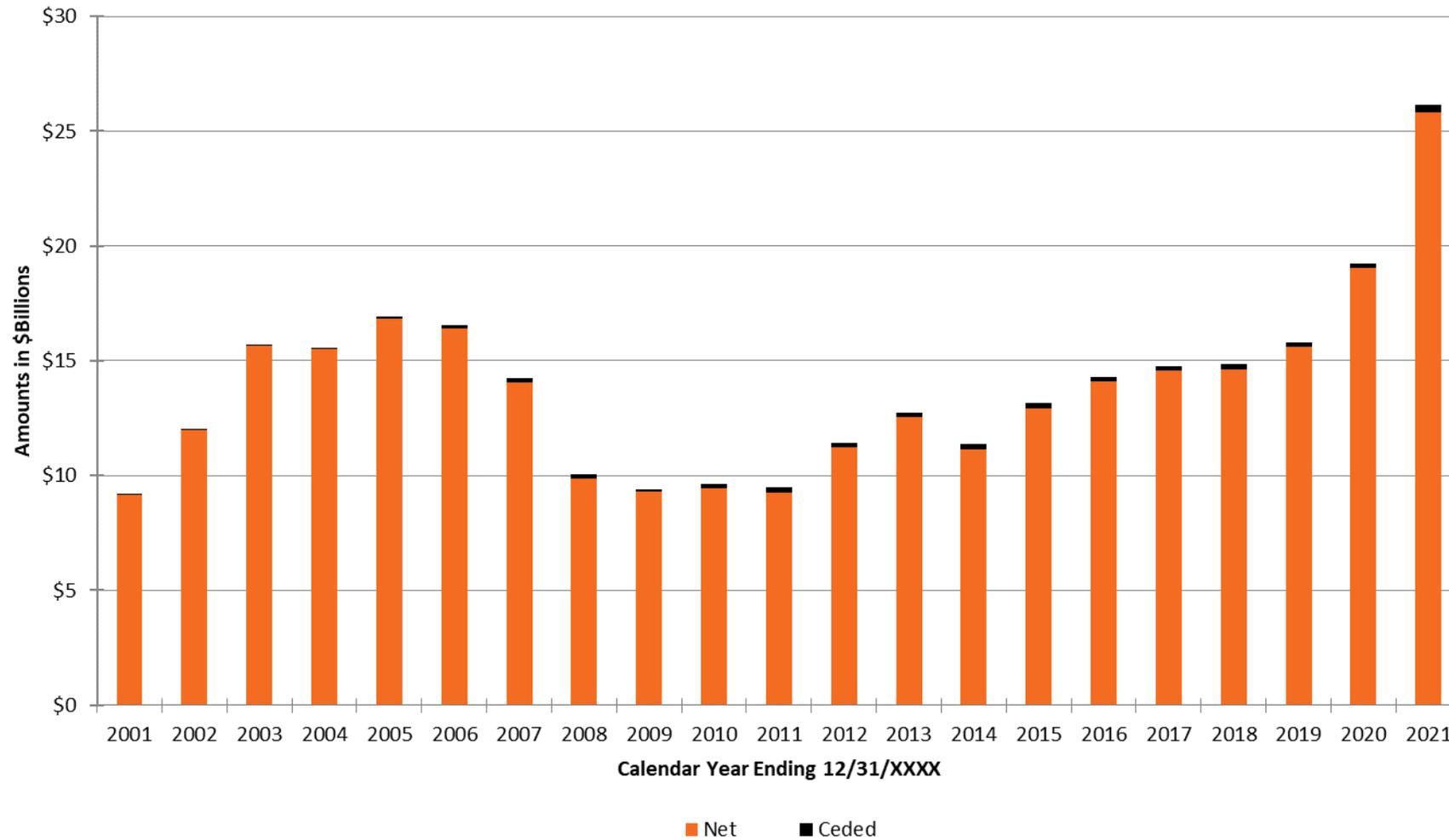
# Amount of Insurance Written



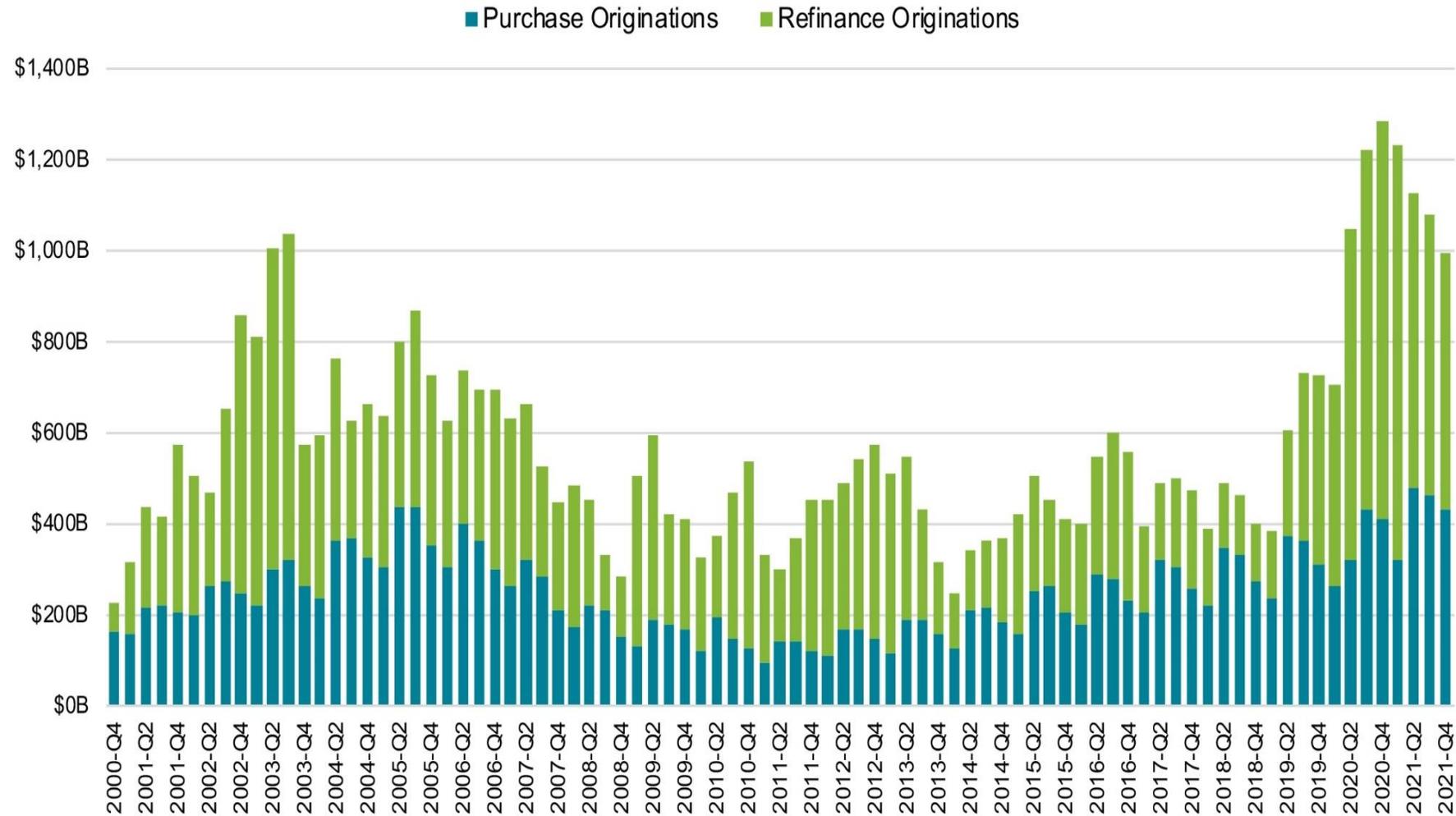
# Amount of Insurance Written: Indexed to 2001



# Written Premium by Component

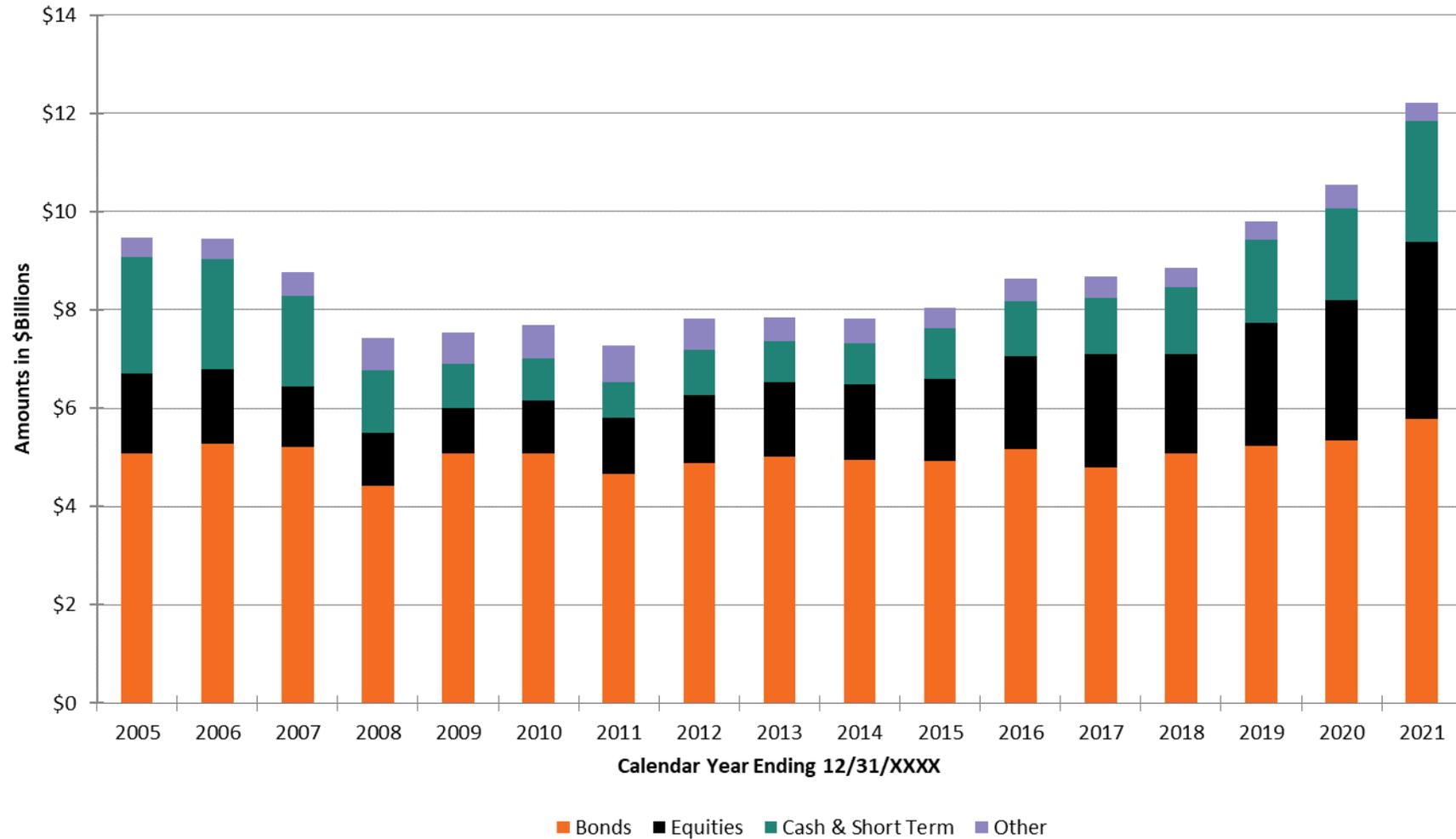


# First Lien Mortgage Originations by Quarter



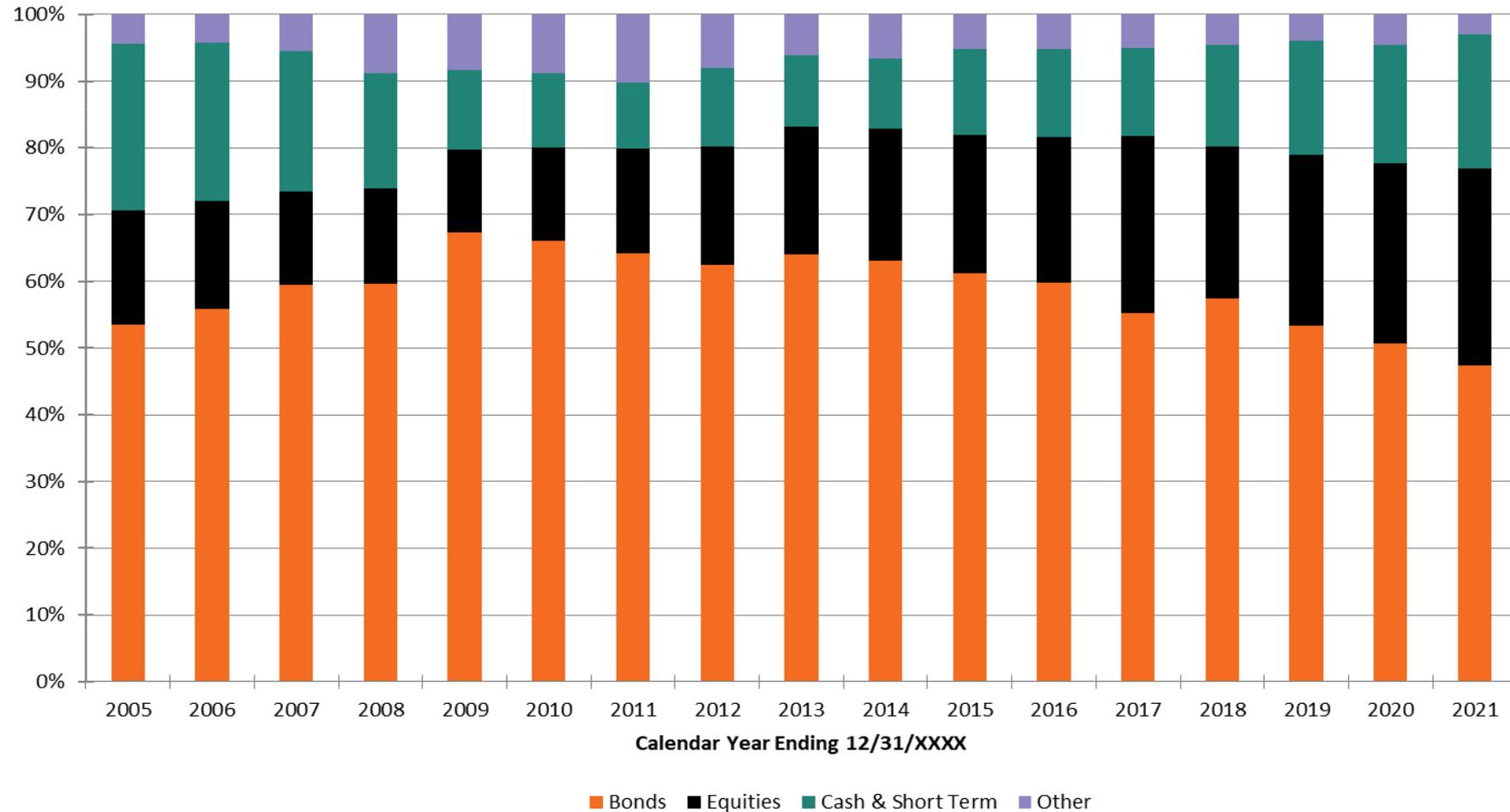
Source: Black Knight

# Assets by Class



Totals tie to cash and invested assets, subtotals line in annual statement.

# Assets by Class – Distribution by Type



# Profitability

---

$$\text{Combined Ratio} = \frac{\text{Losses} + \text{Operating Expenses}}{\text{Premium}}$$

$$\text{Operating Ratio} = \frac{\text{Losses} + \text{Operating Expenses} - \text{Investment Gain}}{\text{Premium}}$$

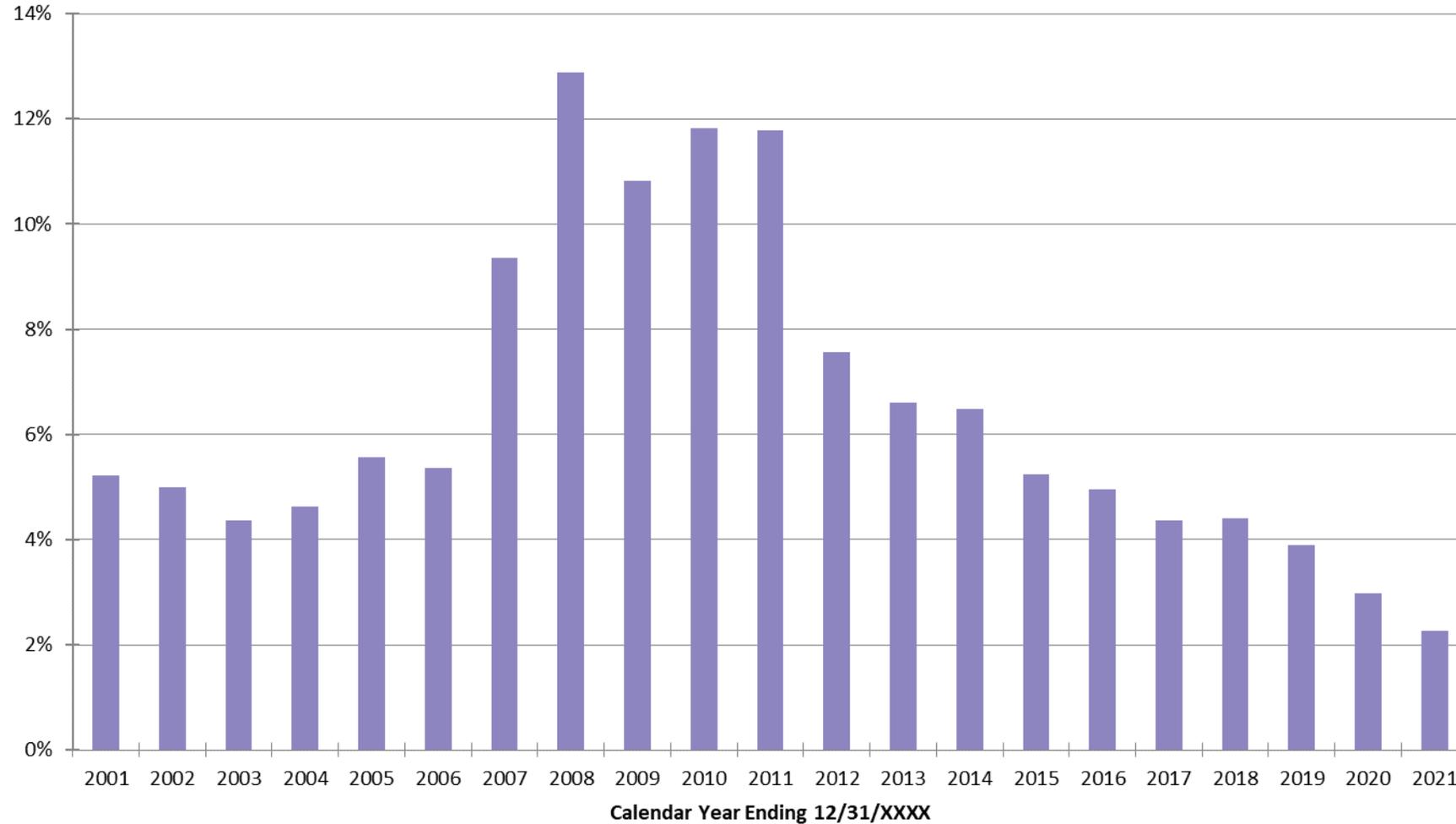
Operating Expenses: analogous to underwriting expenses for P/C insurance

## Polling Question

**What was the 2021 calendar year net loss & LAE ratio for the title insurance industry? What was the operating expense ratio?**

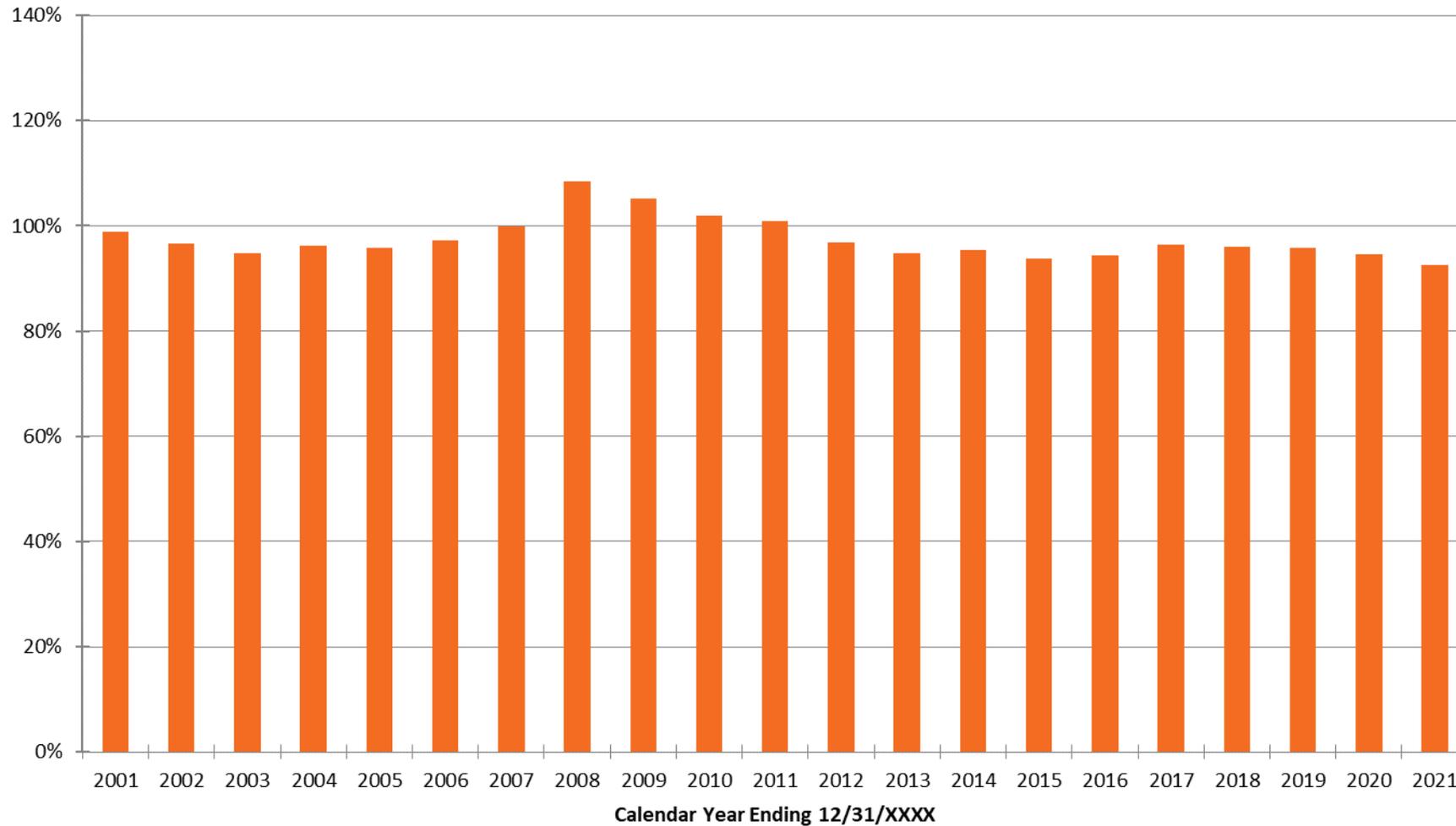
- A** Net loss & LAE ratio: 60.5%; Operating expense ratio: 32.4%
- B** Net loss & LAE ratio: 70.8%; Operating expense ratio: 22.9%
- C** Net loss & LAE ratio: 25.7%; Operating expense ratio: 64.1%
- D** Net loss & LAE ratio: 2.3%; Operating expense ratio: 92.6%
- E** Net loss & LAE ratio: 40.3%; Operating expense ratio: 59.8%

# Calendar Year Net Loss & LAE Ratio



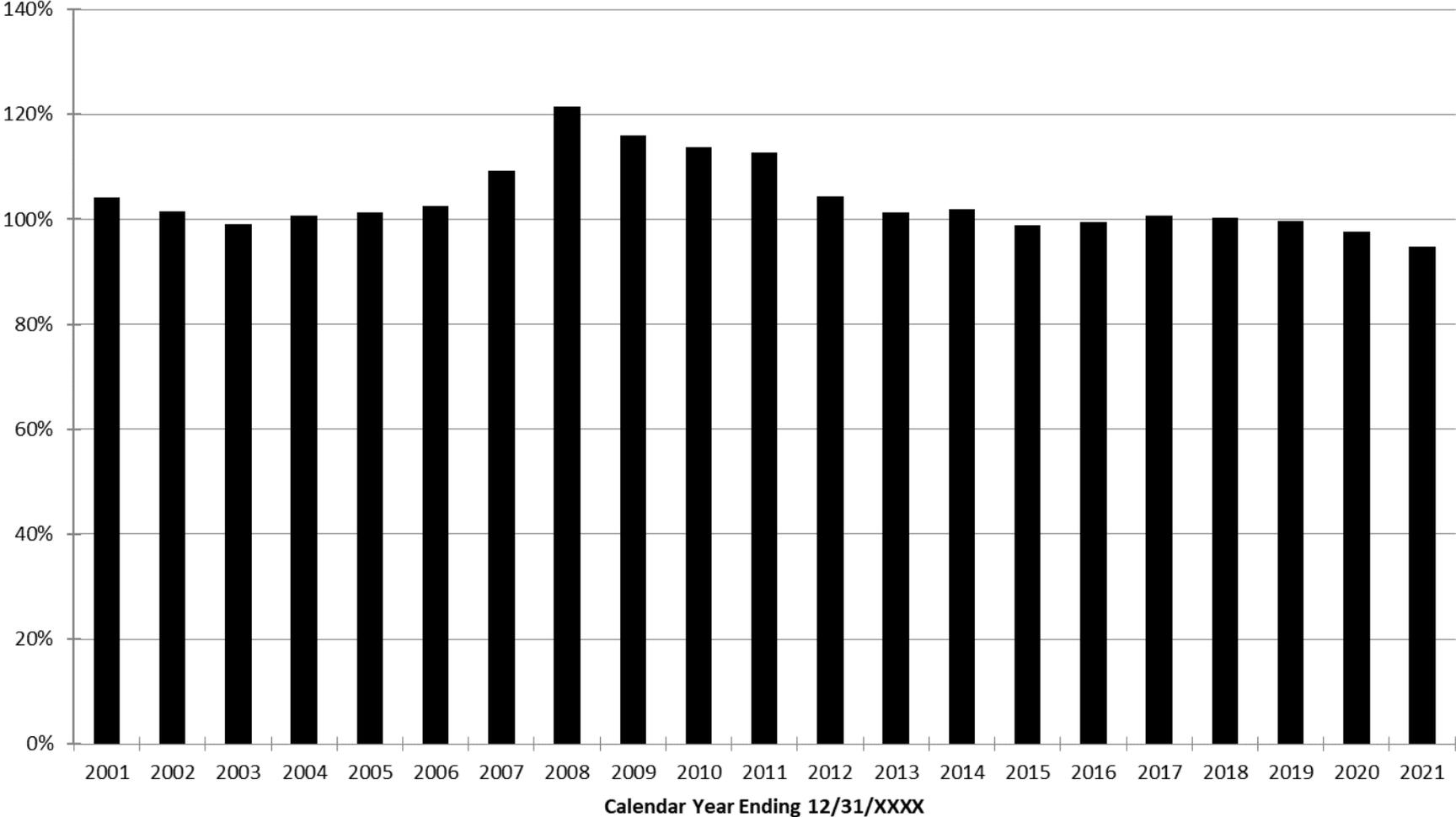
Ratio to net earned premium.

# Operating Expense Ratio

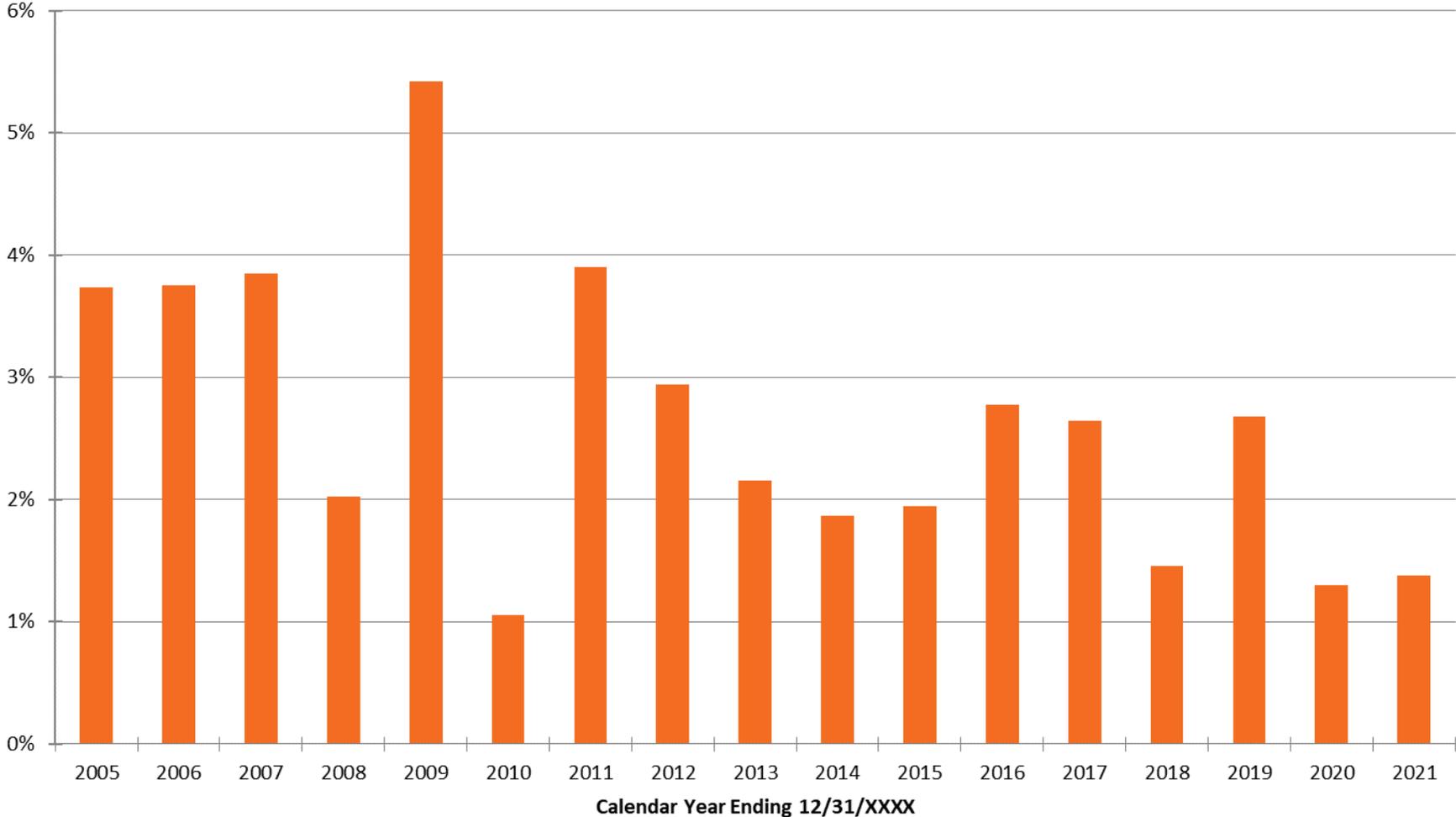


Ratio to net written premium.

# Loss & LAE Ratio + Operating Expense Ratio

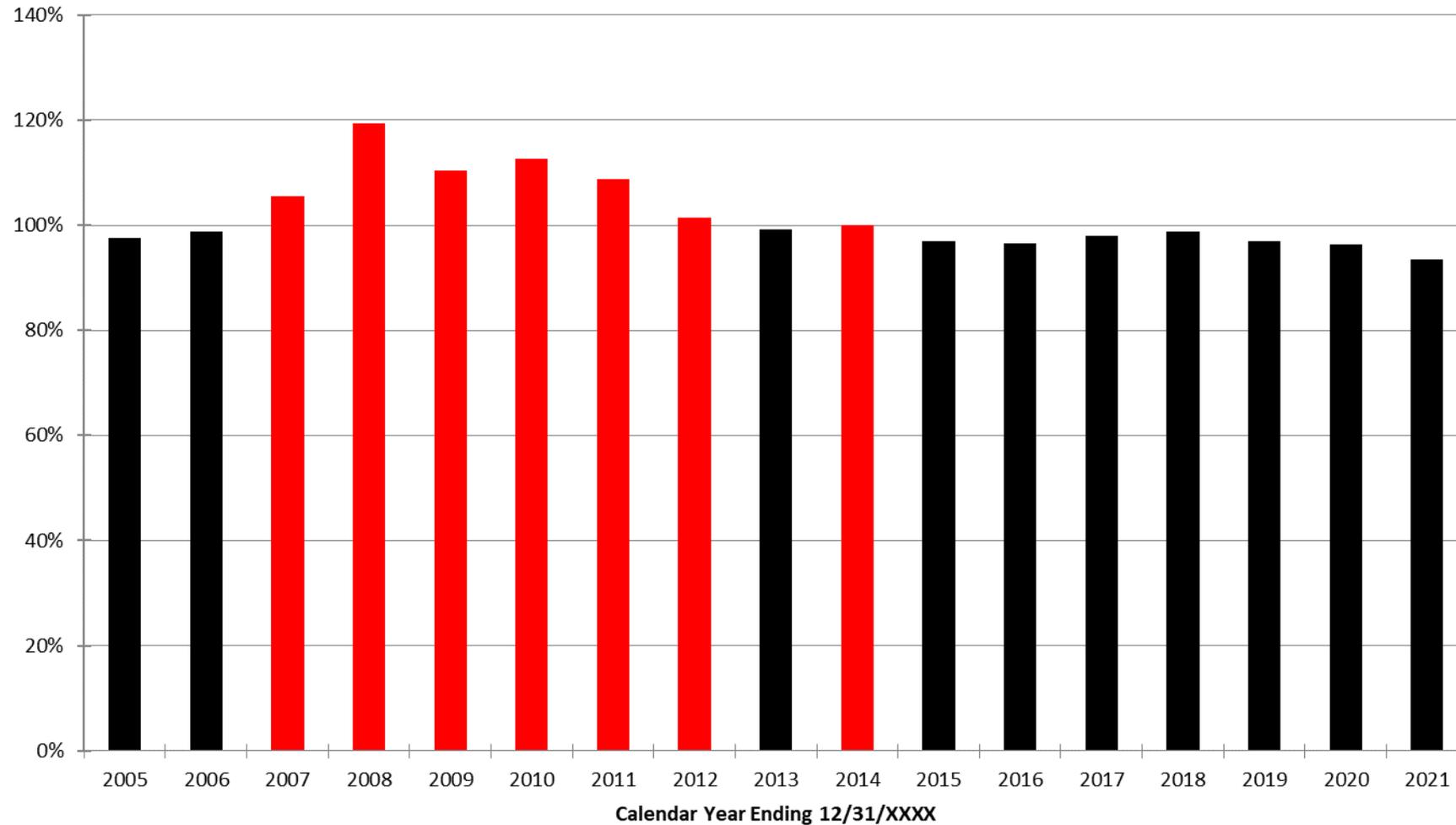


# Investment Gain

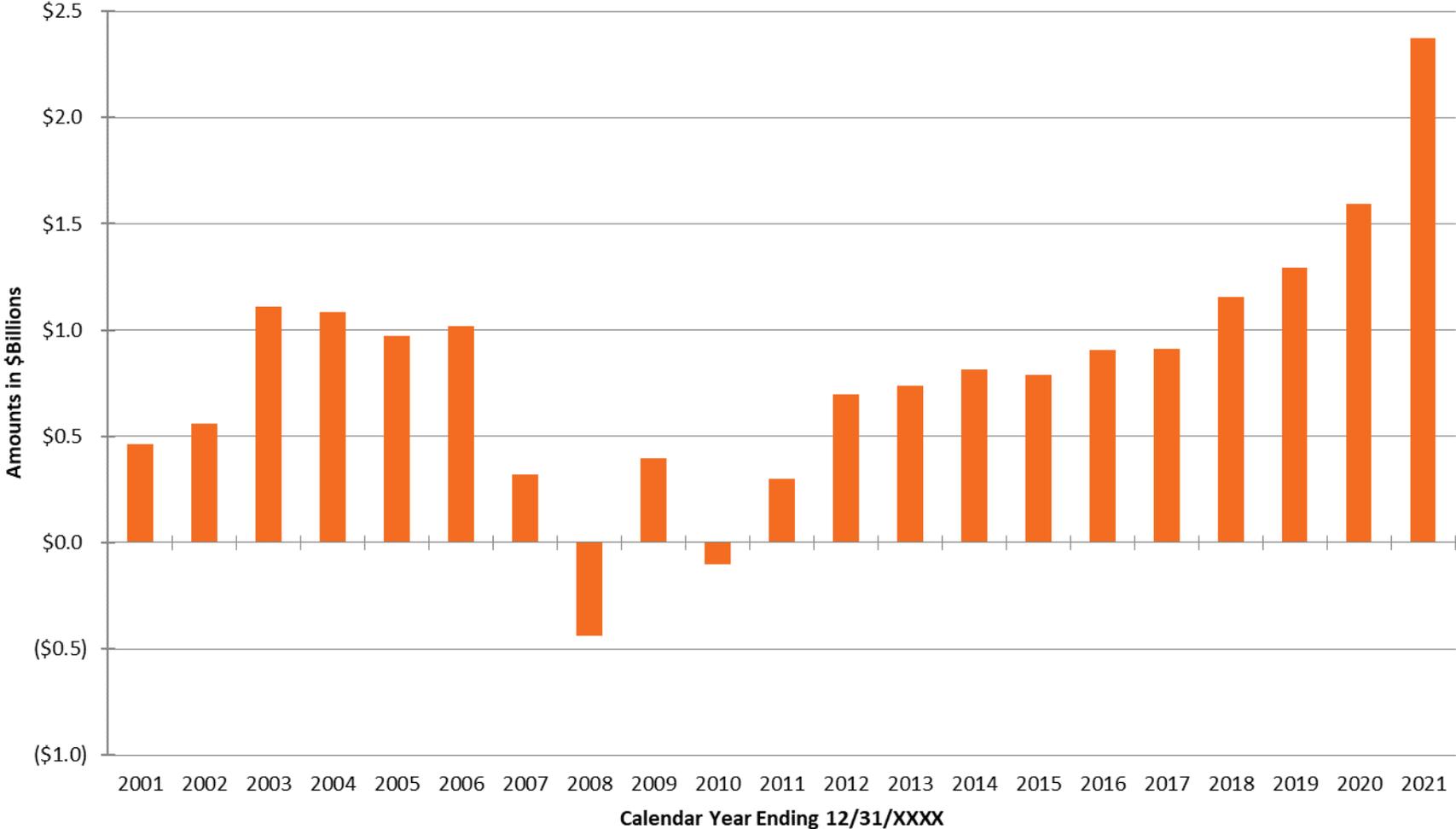


Ratio to net earned premium.

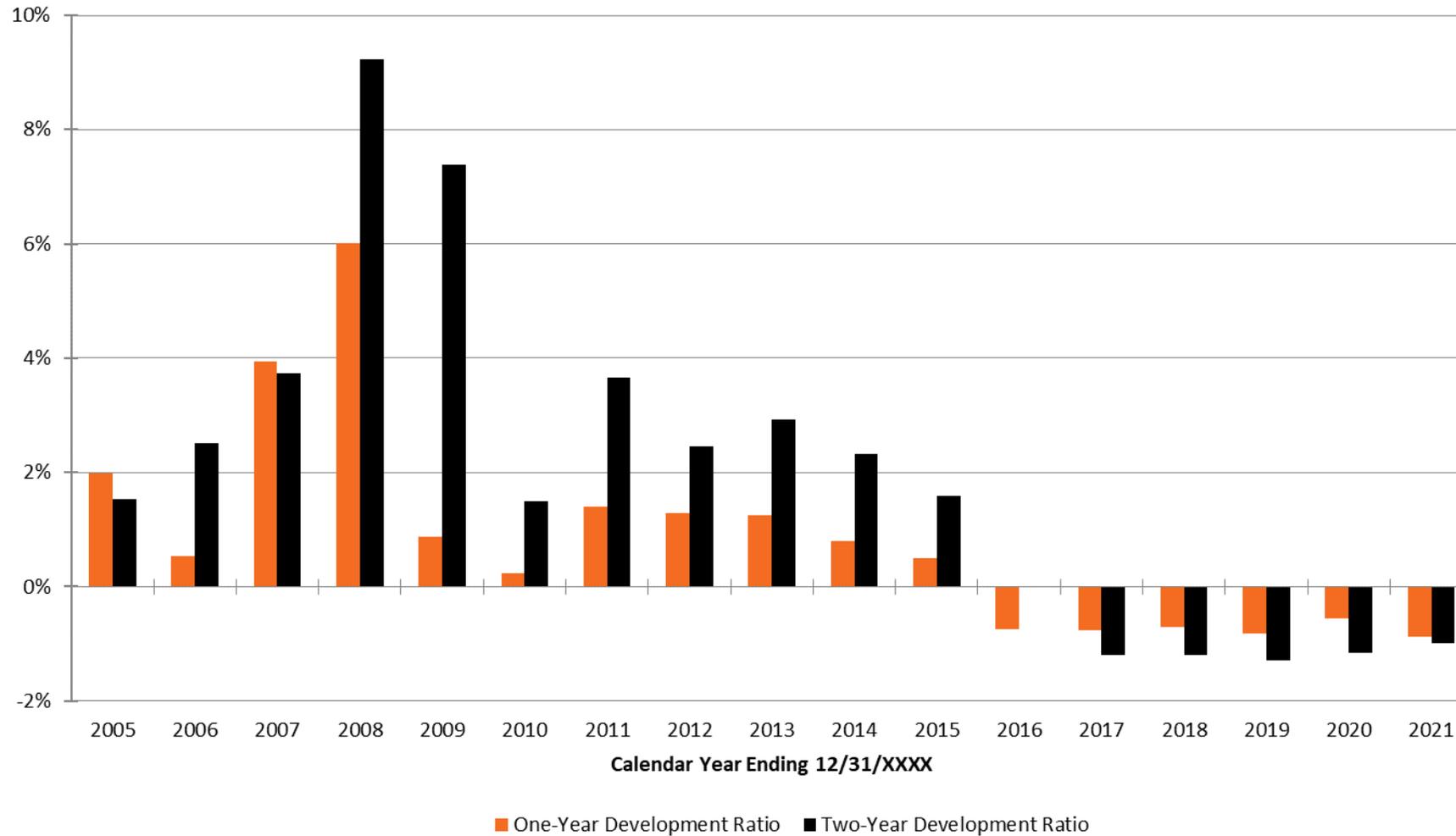
# Operating Ratio = Combined Ratio - Investment Gain



# Net Income

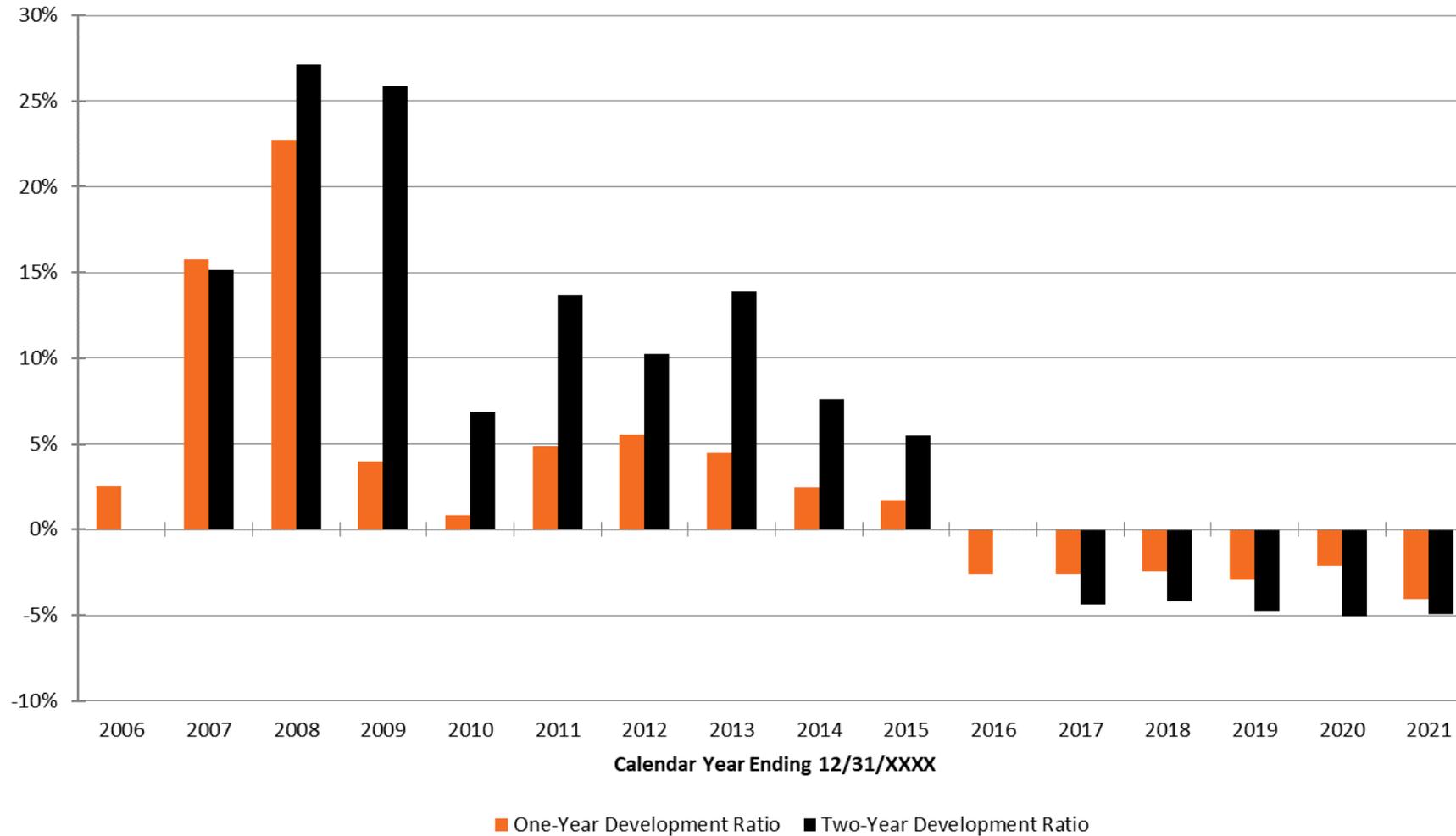


# % Change in Net Ultimate Loss & ALAE through 12/31/2021 (to Prior NEP)



Includes losses and ALAE; excludes ULAE.

# % Change in Net Ultimate Loss & ALAE through 12/31/2021 (to Prior Surplus)



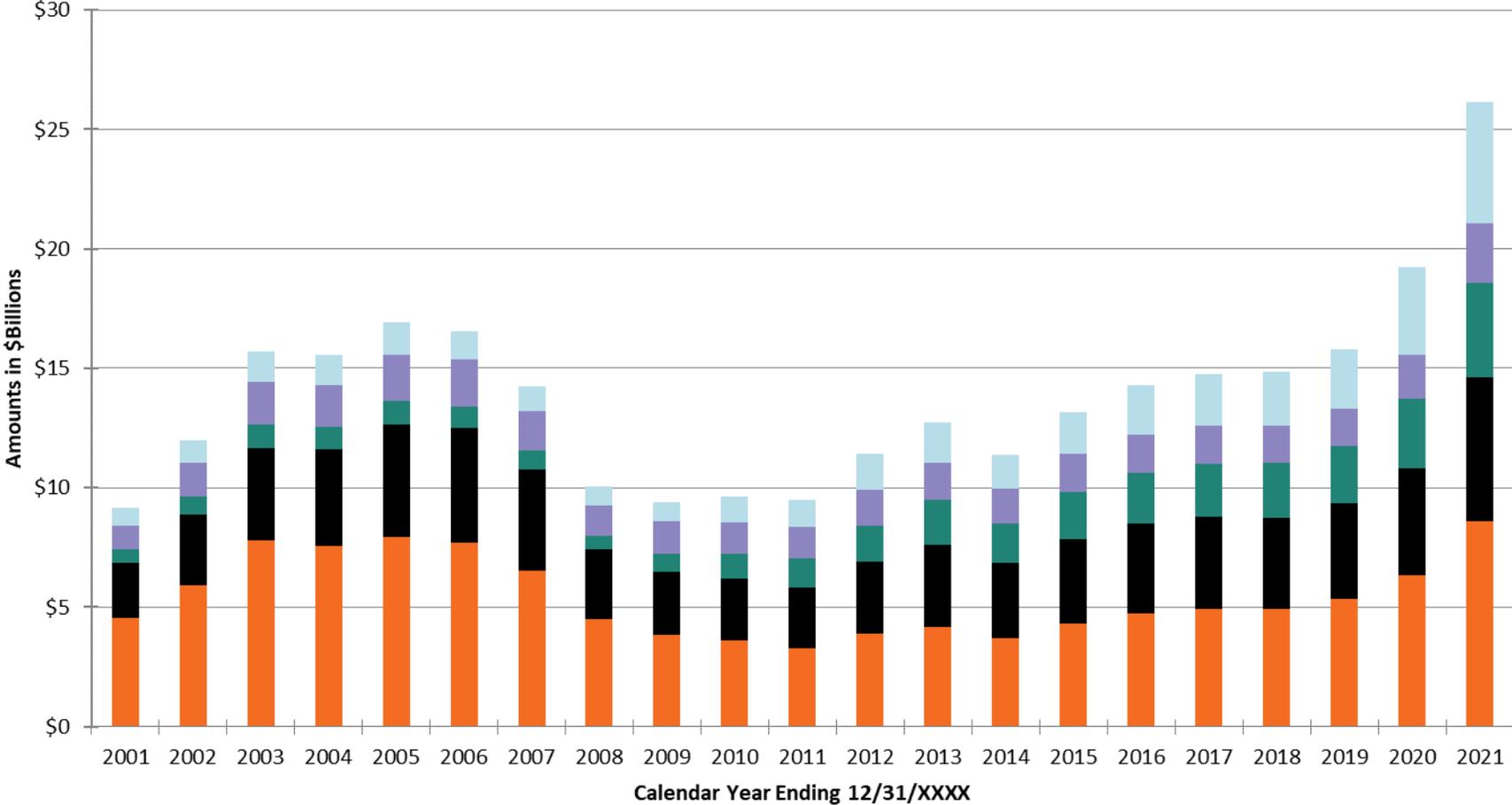
Includes losses and ALAE; excludes ULAE.

# Market Share

---

- Title insurance industry dominated by four families:
  - Fidelity
  - First American
  - Old Republic
  - Stewart
- Market share of independent companies has increased in recent years

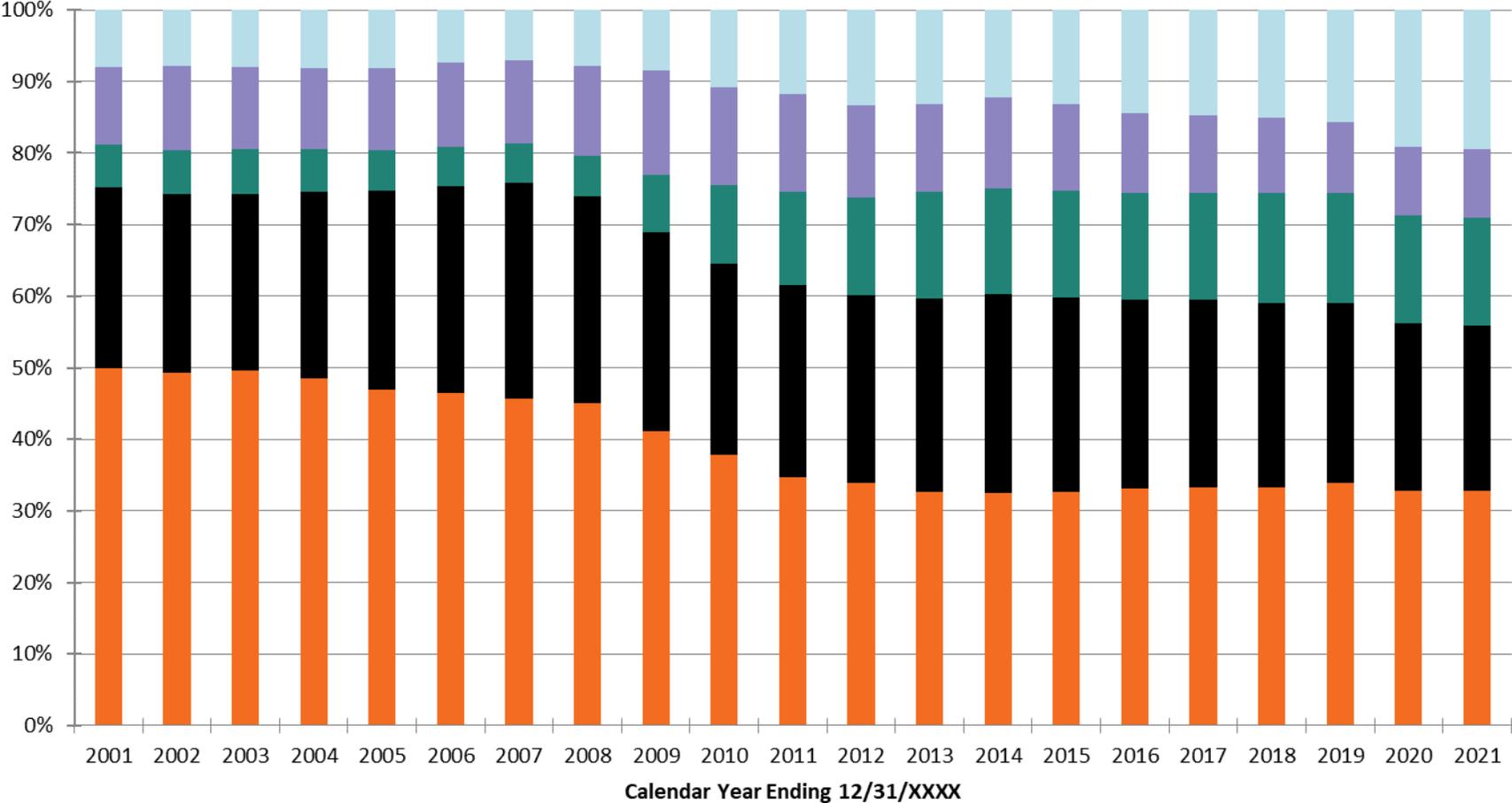
# Direct Written Premium by Segment



■ Fidelity 
 ■ First American 
 ■ Old Republic 
 ■ Stewart 
 ■ Independent



# Market Share of DWP by Segment



■ Fidelity 
 ■ First American 
 ■ Old Republic 
 ■ Stewart 
 ■ Independent



# Mergers & Acquisitions

---

- 2019 proposed merger between Fidelity and Stewart valued at \$1.2 billion
  - Blocked by Federal Trade Commission due to antitrust concerns
  - Combined company would have had 43% market share
- Stewart increases acquisition activity in 2021 and 2022
  - Regional title insurers
  - Data and analytics firms
- Companies looking to control more aspects of the mortgage process

# COVID-19 Impact



# COVID-19 Impact

---

- Low mortgage rates
  - Substantial increase in refinancing activity during 2020 and 2021
- Increasing home values
  - Severity: average claim amounts increase
- Recordors' offices closed during pandemic
  - Claims reporting: delayed recording led to backlog in claim reporting

# COVID-19 Impact (cont'd)

---

- High premium growth
  - Independents gain considerable market share
- Housing forbearance
  - Delayed mortgage payments and eviction moratorium
- Remote working
  - Increase in neighbor disputes

# Recent Market Observations



# 2021 Observations

---

- Slowdown in refinancing due to increasing interest rates
- Eviction moratorium ending
- Transition to work-from-home environment
  - Remote notarizations
  - Virtual closings
  - Possibility of increased fraud or disputes

# 2022 Observations

---

- Slowdown in refinancing due to increasing interest rates
- Slowdown in mortgage originations due to interest rates and home affordability
- Aggressive Federal Reserve monetary policy
- Eviction moratorium ends

# Future Challenges



# Future Challenges

---

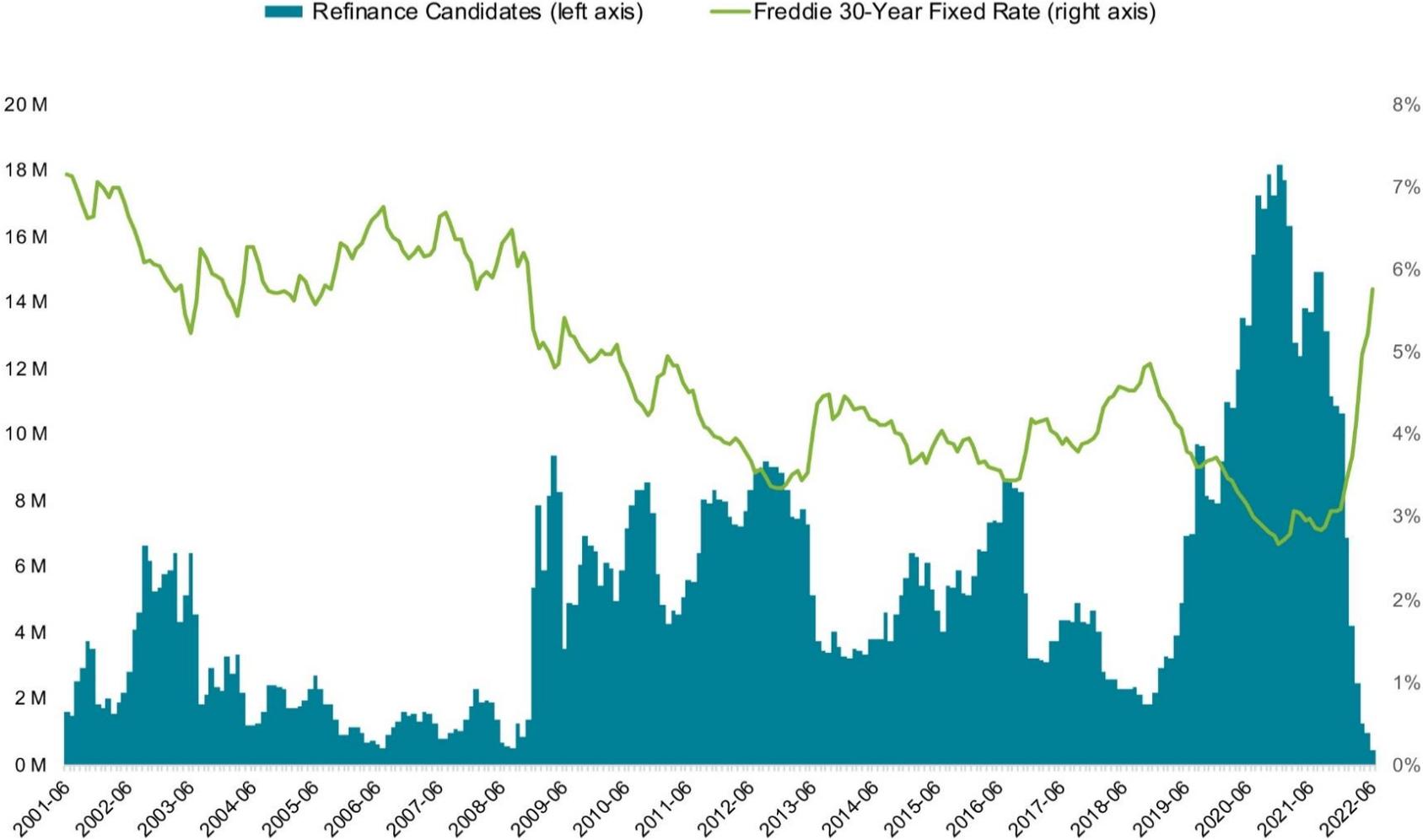
- Returning to a “normal” environment
- Data security
  - Title insurance data vulnerable to cyber attacks
  - Mortgage contracts hold wealth of sensitive data
- Technology
  - Title industry becoming more digital could lead to increased defalcation risk
  - Ability of independents to adapt and implement
- Is there a new housing bubble emerging?
- New competitive landscape

# InsureTech

---

- Operating expense ratio is primary driver of underwriting performance
- InsureTech perspective: expense management and reduction through technology
- Talent gap: younger generation will not embrace outdated infrastructure
- InsureTech opportunity: complacency of current market participants
- Leading by example / foreshadowing
  - Oscar Health, Inc.
  - Hippo Holdings, Inc.
  - Root Insurance

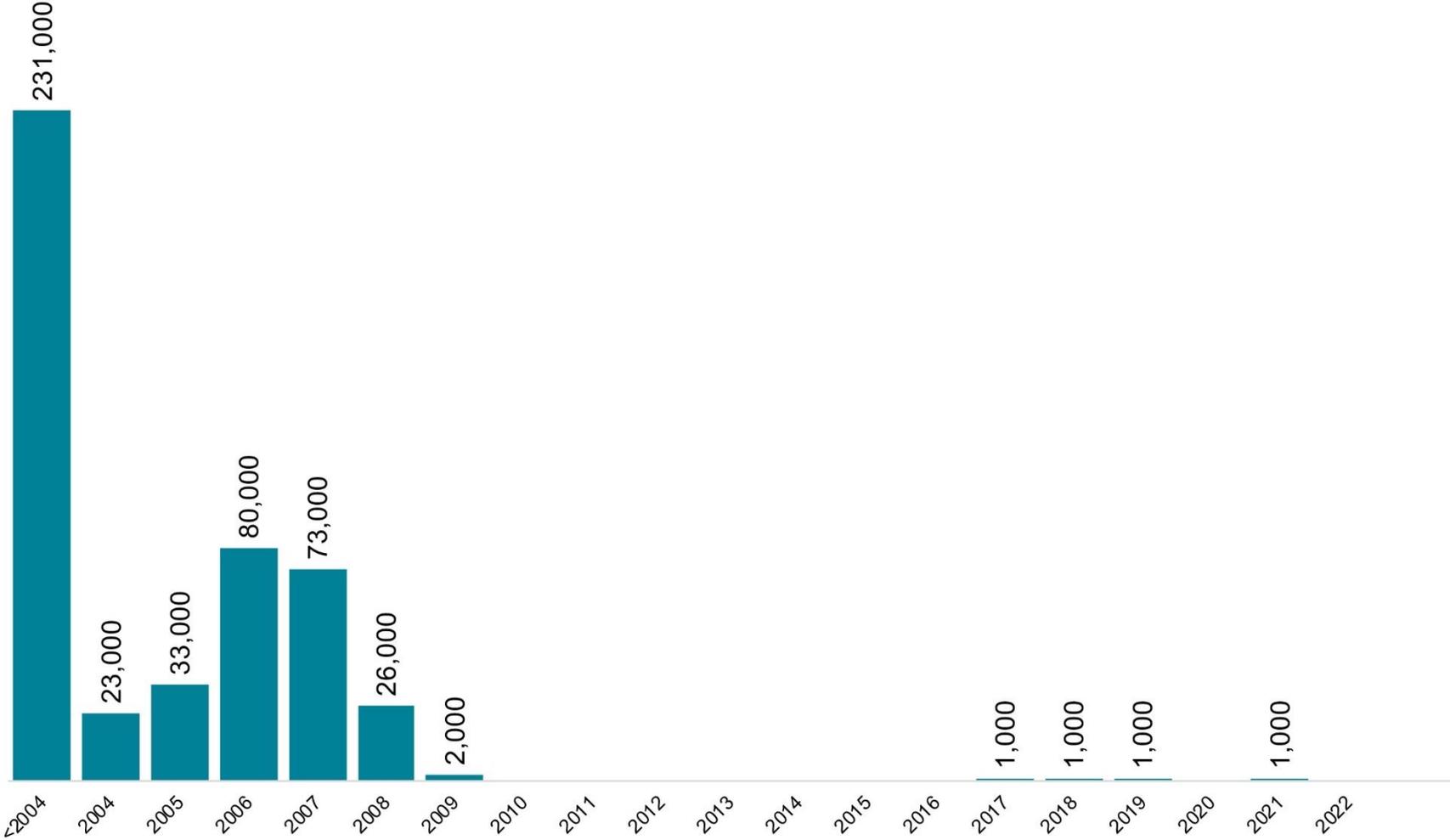
# Refinance Candidates by Month



Source: Black Knight, McDash Primary, Federal Reserve  
 June data as of 6/16

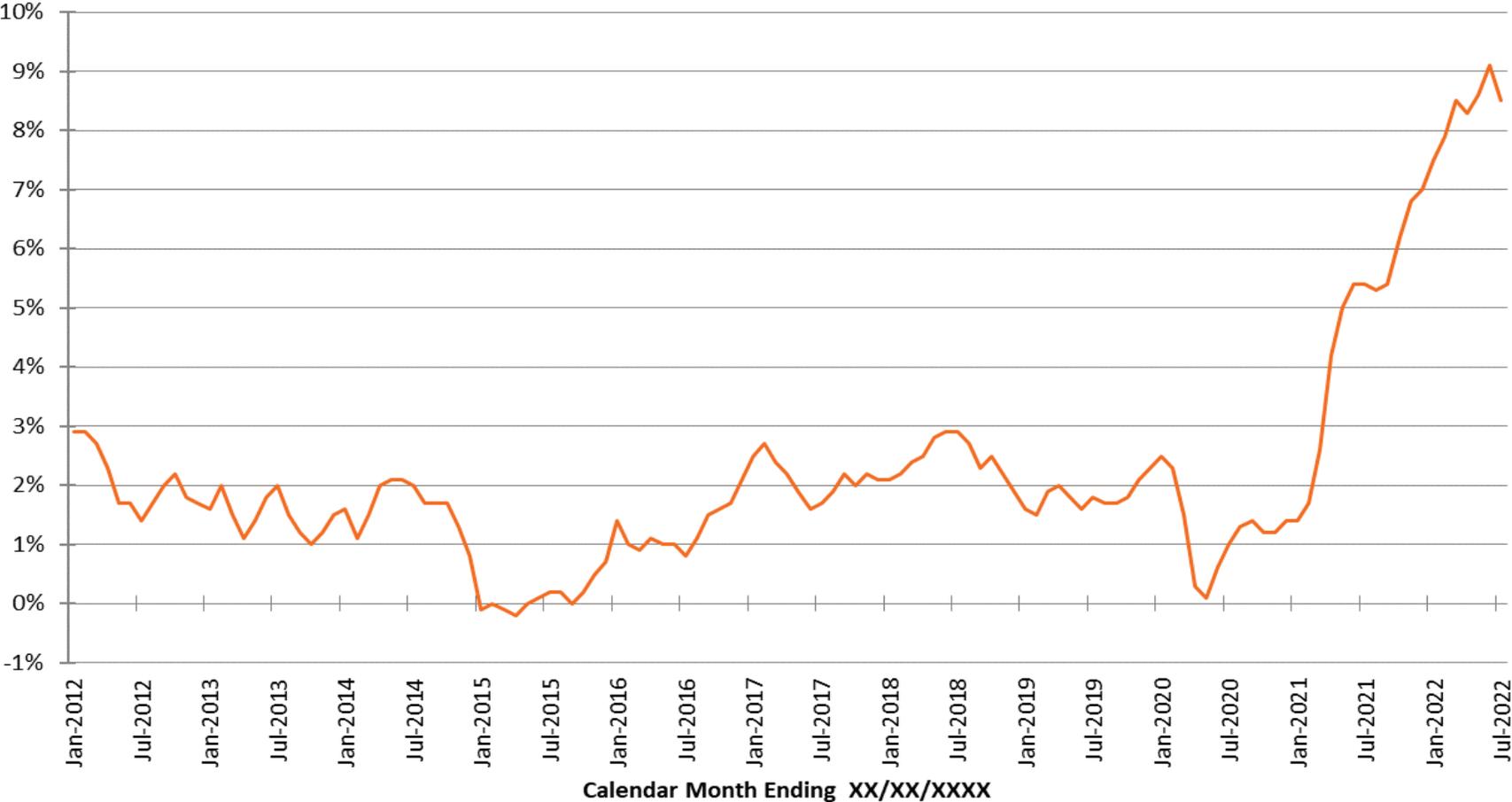


# Distribution of Refinance Candidates by Vintage



Source: Black Knight, McDash Primary

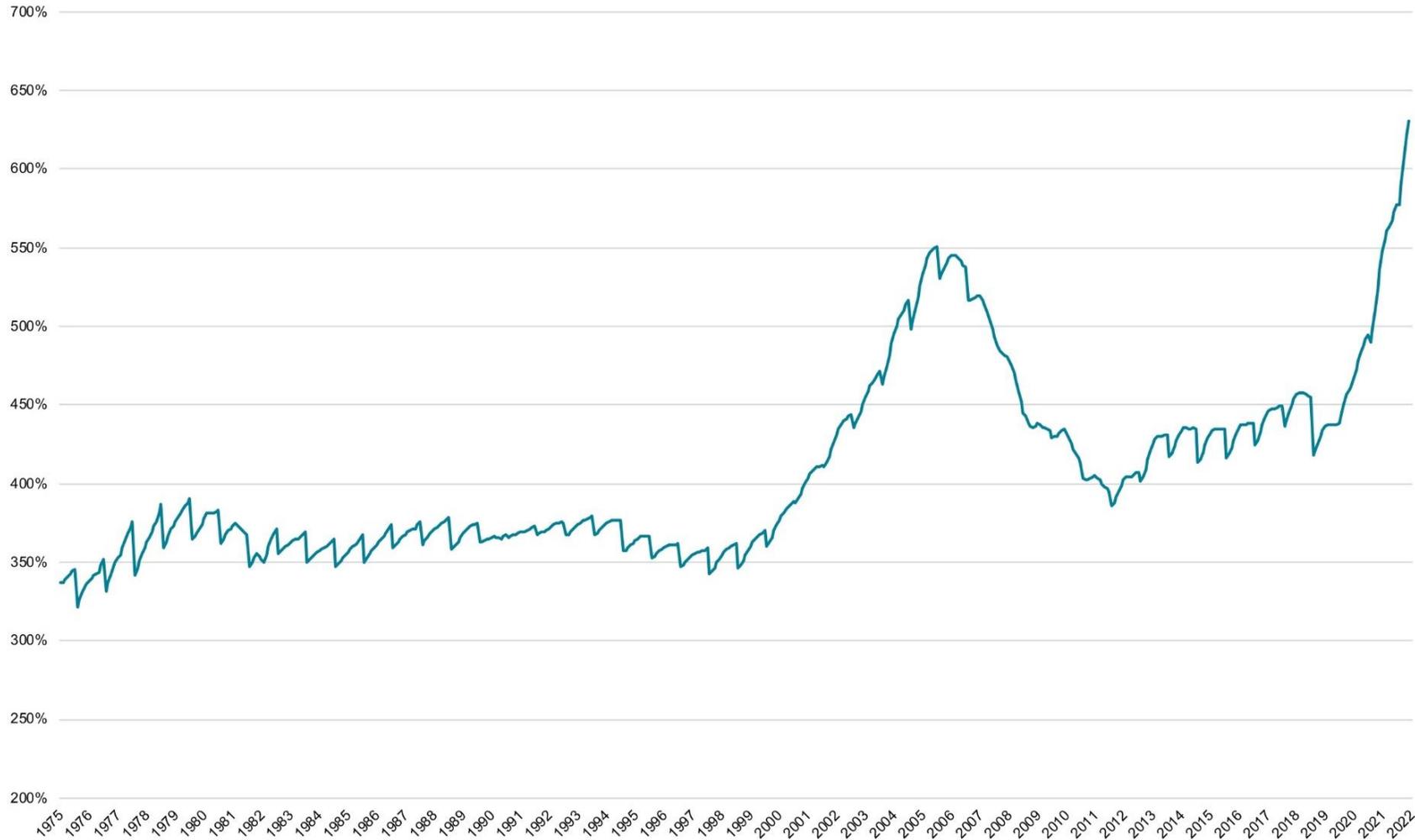
# Inflation



— 12-month percent change

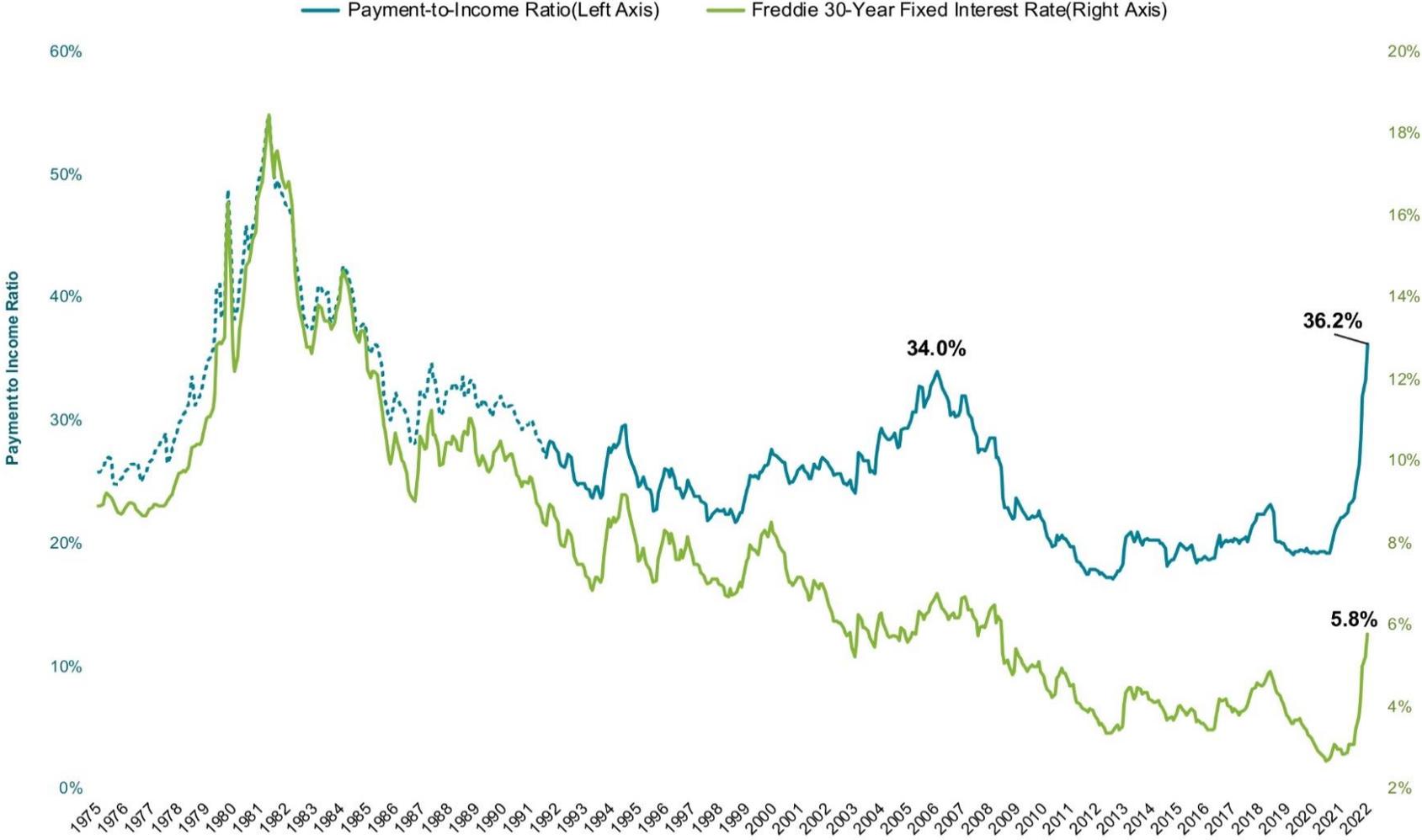
Source: Bureau of Labor and Statistics  
Consumer Price Index for All Urban Consumers

# Average Home Price as % of Median Household Income



Source: Black Knight HPI, Realtor.com, Census Bureau, Moody's  
Assumes a 20% down payment and utilization of a 30-year fixed rate mortgage at the prevailing interest rate; Data as of May 2022

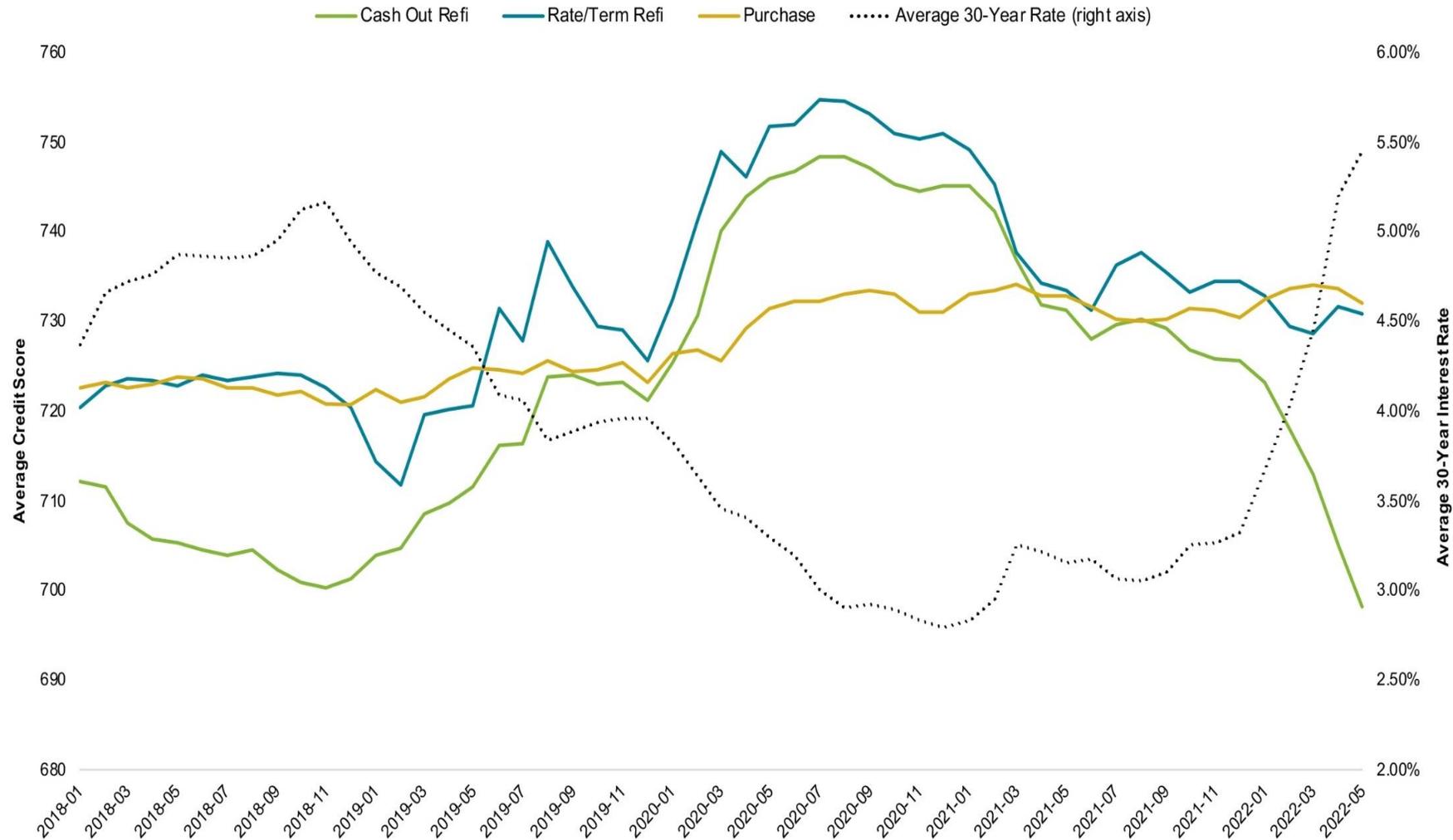
# National Payment to Income Ratio



Source: Black Knight HPI, Census Bureau, FHLMC PMMS, Moody's  
 The National Payment to Income Ratio is the share of median income needed to make the monthly principal and interest payment on the purchase of the average-priced home using a 20% down 30-year fixed rate mortgage at the prevailing interest rate; 2022 data as of June 16th, 2022

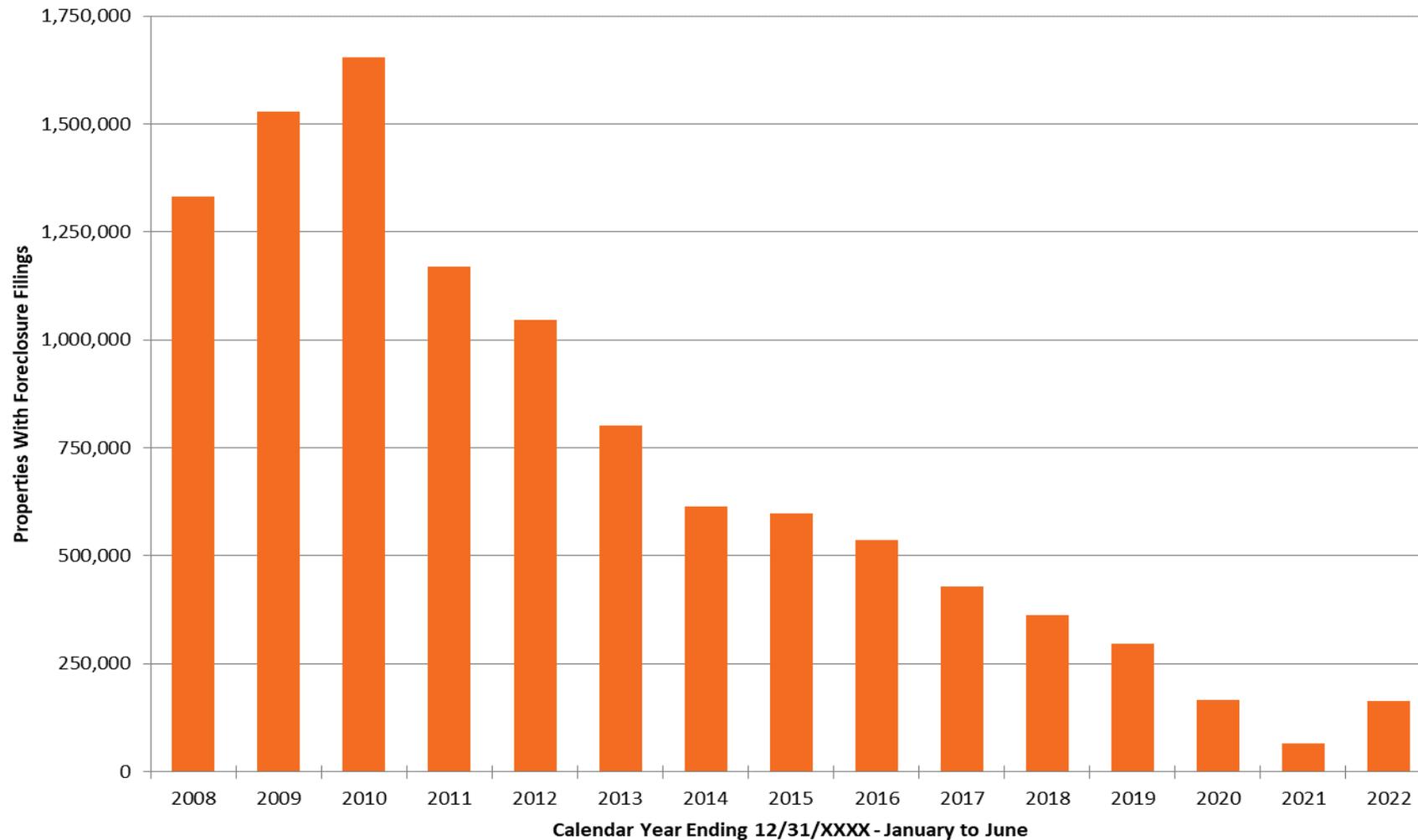


# Average Credit Score of Rate Lock by Loan Purpose



Source: Optimal Blue, a division of Black Knight

# First-Half US Foreclosure Activity by Year



Source: [www.attomdata.com](http://www.attomdata.com)



Questions

# Thank You

---

**Matt Meade**

mmeade@pinnacleactuararies.com

**Chris Schubert**

cschubert@pinnacleactuararies.com

**Art Randolph**

arandolph@pinnacleactuararies.com

