



# RATE RULES: THE CONSTRUCTION RULES

## Mastering the Dark Art

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Bill Pratt  
Texas Underwriting Counsel  
5900 Shepherd Mtn Cove., Bldg. 2, Ste 200  
Austin, TX 78730  
WATS (800) 252-9229  
bpratt@stewart.com



## RATE RULE R-2: "Pay-As-You-Go" Policies.

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(Thanks to Richard Black)

\*\*General Rule: Premium must be paid in full to the issuing title company prior to delivery of the Policy or Endorsement to the Insured.



## RATE RULE R-2: "Pay-As-You-Go" Policies.

\*\*Authorized Exception to the General Rule: A Policy premium can be paid in progressive installments if a) the face amount of the Policy is \$5,000,000 or more and includes the value of future construction, b) the Policy's Schedule "B" includes the two contemplated-improvements exceptions from Rule P-8(b) [Mortgagee Policy] or P-8(a) [Owner Policy], PLUS added language for the "Liability" or "Pending disbursement" exceptions required by Rule P-8, and c) Down-Date Endorsements under Rule P-9(b)(4) or P-9(a)(3) are at each stage after the initial closing, at cost of \$50 per Endorsement [Rule R-11(c) for the Mortgagee Policy, and Rule R-15 for the Owner Policy]. "Pay-As-You-Go" can be applied to a Mortgagee Policy alone, an Owner Policy alone, or both Owner and Mortgagee Policies in the same transaction. When both Policies are issued, the Owner Policy is charged for at a simultaneous-issue \$100 rate under Rule R-5(B), plus the difference in premium if the Owner Policy amount exceeds the Mortgagee Policy amount.



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**EXAMPLE:** January closing is a land acquisition in the amount of \$600,000 with upcoming construction-cost of \$5,400,000. An Owner Policy for \$6,000,000 (\$27,699 computed premium) and a Mortgage Policy for \$5,700,000 (\$26,577 computed premium) are being required. At closing, Lender advances \$700,000, being \$300,000 toward land-purchase and \$400,000 for initial site work, followed by: \$1,500,000 in February, \$2,000,000 in April, \$1,000,000 in July, and \$500,000 in September. "Pay-As-Go" premium collection would take place as follows:



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- i. January—Mortgagee Policy: Collect \$3,263.66 [ $\$700,000 \div \$5,700,000 = 12.28\% \times \$26,577$ ].  
January—Owner Policy: Collect \$1,222 [ $\$27,699 - \$26,577 = \$1,122 + 100$ ].
- ii. February—Mortgagee Policy: Collect \$6,995.07 [ $\$1,500,000 \div \$5,700,000 = 26.32\% \times \$26,577$ ] plus \$50 Date-Date Endorsement premium.  
February—Owner Policy: Collect \$50 Down-Date Endorsement premium.
- iii. April—Mortgagee Policy: Collect \$9,325.87 [ $\$2,000,000 \div \$5,700,000 = 35.09\% \times \$26,577$ ] plus \$50 Down-Date Endorsement premium.  
April—Owner Policy: Collect \$50 Down-Date Endorsement Premium.
- iv. July—Mortgagee Policy: Collect \$4,661.61 [ $\$1,000,000 \div \$5,700,000 = 17.54\% \times \$26,577$ ] plus \$50 Down-Date Endorsement premium.  
July—Owner Policy: Collect \$50 Down-Date Endorsement premium.
- v. September—Mortgagee Policy: Collect \$2,330.79 [ $\$500,000 \div \$5,700,000 = 8.77\% \times \$26,577$ ] plus \$50 Down-Date Endorsement premium.  
September—Owner Policy: Collect \$50 Down-Date Endorsement premium.



## RATE RULE R-2: "Pay-As-You-Go" Policies.

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R-2 requires payment of the fraction of the premium and Down-Date Endorsements as the loan is disbursed. Failure to meet these Conditions results in the entire remaining premium being immediately due and payable.



## RATE RULE R-3: Owner Policy Coverage for Contemplated Improvements and Increased Coverage

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Owner Policies may be issued for:

- a. Current sales price,
- b. Current sales price, plus contemplated improvements,
- c. If no sale, value of the land and improvements,
- d. If no sale, value of the land and improvements, plus contemplated improvements.

**EXAMPLE:** Buyer is purchasing \$50,000 tract of land. Buyer intends to build \$200,000 (total premium of \$1699). Typically, Seller pays for the Owner Policy on the land (\$520 premium). Buyer pays \$1179 (\$1699-\$520).



## RATE RULE R-3: Owner Policy Coverage for Contemplated Improvements and Increased Coverage

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Owner Policy can be “surrendered” and a new owner policy issued that includes the cost of completed improvements. The premium for the new policy will be LESS the premium paid for the surrendered policy. NO time limit.

**EXAMPLE:** Buyer has \$50,000 Owner Policy and has completed a \$200,000 house. Buyer surrenders the existing policy and receives a new policy for \$250,000. Buyer pays \$1179(\$1699-\$520).



## RATE RULE R-3: Owner Policy Coverage for Contemplated Improvements and Increased Coverage

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Owner Policy can be endorsed to reflect increased value under R-3c using the Increased Value Endorsement, the T-34. Insured must satisfy the company as to the current value according to the Procedural Rule P-9(a)(2). Premium is based on basic rate of current value, less premium paid for existing policy and any prior Increased Value Endorsements. Premium cannot be less than minimum policy Basic Premium Rate.

**EXAMPLE:** Insured has a \$30,000 Owner Policy (premium of \$378) and has constructed \$150,000 worth of improvements several years ago. Appreciation has raised the total value to \$250,000, as evidenced by an appraisal. Premium for the Increased Value Endorsement is \$1321 (\$1699-\$378).



## RATE RULE R-5A: Simultaneous-issue of Owner and Mortgagee Policies.

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Rate Rule R-5A provides for what is sometimes referred to as an “up-front” construction loan. The first part of the paragraph provides for the basic simultaneous issuance rate. But the second part, appearing in parentheses, provides that if the new Owner Policy is to include the cost of contemplated improvements (Procedural Rule P-8a) and an Owner Policy has been issued to the current owner, covering the identical property, and within the last four years, a credit on the new Owner Policy **SHALL** be given for the amount of premium paid for the existing Owner Policy and the Mortgagee Policy shall be issued for \$100, plus endorsements. There is no requirement the prior policy has to have been issued by the same agent or underwriter and there is no requirement the prior policy has to be surrendered.



## RATE RULE R-5A: Simultaneous-issue of Owner and Mortgagee Policies.

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**EXAMPLE:** Insured has a \$50,000 Owner Policy issued in 2004 (\$520 premium). Currently owes \$30,000 on a purchase money deed of trust. Insured is going to sign a \$200,000 mechanic's and materialsman's lien contract with a builder for a new home. This lien will be assigned to a lender that will be making a \$230,000 loan renewing and extending the existing purchase money deed of trust and the construction contract. The owner Policy will be issued for \$250,000, land cost (\$50,000) plus cost of contemplated improvements (\$200,000). The premium for the owner Policy will be \$1179 (\$1699-\$520). The premium for the Mortgagee Policy will be \$100, plus endorsements.



## RATE RULE R-5A: Simultaneous-issue of Owner and Mortgagee Policies.

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**EXAMPLE:** Insured has an Owner Policy issued in 2004 for \$200,000 on an improved property (\$1423 premium). The Insured's house has burn and the insurance has paid off all but \$30,000 of the old loan. Insured is going to sign a \$200,000 mechanic's and materialman's lien contract with builder for a new home. This lien will be assigned to a lender that will be making a \$230,000 loan renewing and extending the balance owed on the existing deed of trust and the construction contract. The Owner Policy will be issued for \$250,000, current land value (\$50,000) plus cost of contemplated improvements (\$200,000). The premium for the Owner Policy will be \$276 (\$1699-\$1423). The premium for the Mortgagee Policy will be \$100, plus endorsements.



## RATE RULE R-5A: Simultaneous-issue of Owner and Mortgagee Policies.

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Rate Rule R-5B provides for the simultaneous issuance of the Owner Policy for \$100 plus any difference in the basic premium for the Owner Policy and the basic premium for the Mortgagee Policy in “pay-as-you-go” situation. It also provides for a credit against the premium for the Mortgagee Policy for the premium for an existing Owner Policy covering the identical land and issued to the same owner. There is NO 4 year limitation.



## RATE RULE R-5C: Simultaneous-issue of Owner and Mortgagee Policies.

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Rate Rule R-5C provides for the simultaneous issuance of an Owner Policy and a Mortgagee Policy with a credit for an existing Owner Policy AFTER completion of improvements. This rule appears to have been an effort to extend the credit for an existing Owner Policy to Insureds that did not purchase “upfront” policies under R-5A, but instead acquired binders. It pre-dates the limitations on the issuance of binders and the changes to Procedural Rule P-16 appear to have made this section almost useless. Application of this section required the existing Owner Policy not contain any exceptions for construction (Procedural Rule P-8), be done after completion of improvements, be done only on “residential property” (NOT “residential real property”), the existing Owner Policy cover the identical land, be issued within 4 years of the date of existing Owner Policy, and that there had been no change in ownership. This section does require the existing policy be “turned in”.



## RATE RULE R-18: "Going to Perm"

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When a Mortgagee Policy is to be issued on a loan which renews and extends or satisfies a construction loan covered by an existing Mortgagee Policy, the premium for the new Mortgagee Policy will be the **GREATER** of minimum policy Basic Premium Rate (currently \$237) **or** the difference between the basic rate for the existing Mortgagee policy and the basic rate for the new Mortgagee Policy.

**EXAMPLE:** A \$230,000 construction loan is covered by an existing Mortgagee policy. A new loan renewing and extending the construction loan will also be for \$230,000. Premium will be \$237 plus endorsements.



## RATE RULE R-18: "Going to Perm"

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**EXAMPLE:** A \$200,000 construction loan is covered by an existing Mortgagee Policy (premium of \$1423). A new loan will renew and extend the construction loan and an existing land loan \$30,000 into a new loan of \$230,000 (premium of \$1589). The premium will be \$237 plus endorsements. The difference between the premium for the new loan and the premium for the construction loan is \$166. Since this is less than the minimum policy Basic Premium Rate, \$237, the minimum policy Basic Premium rate is charged.



## RATE RULE R-9: Additional Chains of Title

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Just because the transaction involves a construction loan, don't forget that other charges are still applicable.

- \* There is an additional chain of title charge for each additional lot or tract not in the same ownership.
- \* There is an additional chain of title charge for each additional platted lot out of subdivisions that weren't platted on the same day. Multiple lots out of another subdivision still count as just one additional chain of title charge.
- \* There is an additional chain of title charge for each non-continuous, acreage tract out of the same county.
- \* There is an additional chain of title charge for each additional county where all or part of a tract or lot is located.



## RATE RULE R-13: Mortgagee Title Policy on Interim Construction Loan

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The changes to Procedural Rule P-16 have limited the use of binders. They can now only be issued for construction loans that do not include the execution of a mechanic's and materialman's lien contract and where the owner, contractor and obligor on the debt are all the same. The charge for a Binder is minimum policy Basic Premium Rate (\$237). Binders are good for one year and up to 6 extensions for 6 month periods can be purchased for \$25 per extension. There is no prohibition on purchasing these extensions up front.



## RATE RULE R-13: Mortgagee Title Policy on Interim Construction Loan

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A credit of 50% of the cost of the binder is authorized where:

A new Mortgagee Policy is issued on a loan that takes renews and extends or satisfies a lien already covered by a binder, or

A new Owner Policy is issued on a sale of the property, and the lien covered by the binder is released prior to or simultaneously with the sale.

The subsequent policy has to be issued within one year of the original binder to qualify for the credit.

**EXAMPLE:** Binder issued November 1, 2004. Builder sells house on January 3, 2006. There is no binder credit given because the binder wasn't issued within one year of the subsequent policy.



## RATE RULE R-13: Mortgagee Title Policy on Interim Construction Loan

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Only the first subsequent policy qualifies for the credit if the binder covers multiple properties.

**EXAMPLE:** Builder obtains a binder issued November 1, 2004 that covers 5 lots. Builder sells one house on July 1, 2005, two houses on July 28, 2005, and the last two houses on July 31, 2005. Only the Owner Policy on the first house is entitled to a binder credit.



## RATE RULE R-13: Mortgagee Title Policy on Interim Construction Loan

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Only property being improved with one to four residential units qualifies for the binder credit.

**EXAMPLE:** Owner/contractor/obligor obtains a binder for a 24 unit condominium project on April 1, 2005. The first unit out of the project is sold on December 1, 2005. There is no credit on the Owner Policy since the binder didn't cover property being improved with one to four residential units.



## RATE RULE R-15: Owner Policy Endorsement

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This is where the \$50 charge for the Down-Date endorsement of the “pay-as-you-go” Owner Policy appears



## RATE RULE R-16: Survey Deletion

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The exception as to area and boundaries that appears in Sch. "B", Item No. 2 of both the Owner Policy and the Mortgagee Policy can be limited to the phrase "shortages in area" as set out in Procedural Rules P-2 and P-8a(2). There is no charge for the deletion in the Mortgagee Policy.

The charge for the deletion in the Owner Policy is 15% of the basic rate in T-1 Owner Policy and 5% of the basic rate in a T-1R Owner Policy. Procedural Rule P-38 says that the T-1R can only be issued on property that is "Residential Real Property" (this term is defined in Procedural Rule P-1u.) and the policy is issued to a natural person. The T-1R can be issued prior to the construction of improvements where the policy contains the construction exceptions (P-8a exceptions).



## RATE RULE R-16: Survey Deletion

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**EXAMPLE:** Existing house is sold to husband and wife. Premium for the survey deletion is 5% of the basic rate for the Owner Policy, Form T-1R.

**EXAMPLE:** Lot is sold to husband and wife. Premium for the survey deletion is 15% of the basic rate for the Owner Policy, Form T-1. Property is not improved and policy doesn't include cost of contemplated improvements.

**EXAMPLE:** Lot is sold to husband and wife who immediately enter into construction loan for new house. Premium for the survey deletion is 5% of the basic rate for the Owner Policy, Form T-1R



## RATE RULE R-16: Survey Deletion

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**EXAMPLE:** Existing house on 10 acres is sold to husband and wife. Premium for the survey deletion is 15% of the basic rate for the Owner Policy, Form T-1. Why? Unplatted property of over 5 acres must be used for agricultural purposes by individual insureds to fall within the definition of "Residential Real Property".

**EXAMPLE:** Existing house is sold to limited partnership. Premium for the survey deletion is 15% of the basic rate for the Owner Policy, Form T-1. Owner is not a "natural person".



## RATE RULE R-20: Owner Policy after Construction

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Where an Owner Policy in an amount of \$5,000,000 or more has been issued that includes the cost of contemplated improvements, and the improvements have been completed, accepted by the owner, and all bills have been paid, within one year of the completion a new Owner Policy may be issued by the company that issued the original Owner Policy for minimum policy Basic Premium Amount (\$237). If the new policy exceeds the old policy, the premium shall be minimum policy Basic Premium Amount, plus the premium difference. There is no requirement the Owner Policy be issued to the same owner. The property can be sold and this rule will still apply.