

# Using rate rules in complex situations

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# The Rate Manual

- The rate manual contains the rules, procedures, forms and regulations promulgated (established) by the Texas Insurance Department.
- These matters have been around since well before the 1950's.
- There were numerous members of the (then) Board of Insurance Commissioners, State Board of Insurance from the 1950s to the 1990s and at least 4 commissioners since the 1990's.

# Rate Manual p.2

- The Manual has been the work product of numerous rates, rules and forms committees of the Texas Land Title Association and during the 1980's and into the mid-1990's the State Bar Title Insurance Committee.
- Like many other things created over a long period by many hands, it is a complex and difficult creature.

# Rate Manual p.3

- Because most forms and most procedures require some change in the rates, the process of getting a form, a rule and a rate is complex, cumbersome and fraught with politics.
- The hearings are contested cases with TDI staff, OPIC and industry witnesses and experts battling over every issue.
- It is thus no wonder that fine-tuning of the rules for ease of understanding just doesn't happen.

# Rate Manual p.4

- There are some basic principles:
  - You must get a full premium in every deal
  - After you get the full premium, credits are sometimes available
  - OTP's are preferred; SI MTP's are allowed because of the same risk and work so the cost are \$100 each.
  - There is always a minimum premium for a policy. That amount is to cover the basic search and exam and closing the transaction and risk premium. (currently \$237).

# Rate Manual p.4a

- Let's think a minute about the minimum premium.
  - How much does it cost you to produce a commitment? When was the last time you actually sat down and figured your time, your compute expenses, plant costs, employee costs and benefits and divided that by the number of orders you close?
  - Big Cities aim for \$100 per commitment.
  - That leaves some actual profit at the minimum premium level.

# Rate Manual p.4

- The full value of the property must be insured (R-2)
- Any credit may be given by any company whether it issued the original policy or not.
- Commitments are free.
- Title Companies don't cure title (P-1f)
- Rebates aren't allowed (P-53)

# Commercial vs. Residential

- There are very few places in the manual where the rules apply differently to commercial vs. residential.
  - Some endorsements like access (T-23), first loss (T-14), last dollar (T-15), non-imputation (T-24) and contiguity (T-25) are only for commercial deals.
  - Other places, like pay as you go (R-2) and post construction OTP (R-20) have \$5 million limitations which mean effectively that they are primarily intended for commercial deals but can be used for both.

# Commercial vs. Residential

- Rates are the same for commercial and residential properties.
- The “breaks” come as the values go up. But notice that as each break comes into play, the full amount of the lower rates are paid.
  - Minimum \$10,000 = \$237; \$100,000=871
  - Up to \$1 million, \$871 plus \$.00552 per \$ for the amount over \$100,000. and likewise for the other break amounts down to \$.00159 for all amounts in excess of \$25,000,000.

# Commercial vs. Residential

- Texas follows a rate theory that the larger deals help subsidize the smaller ones.
- Somewhere around 90% of all deal done in Texas are less than \$250,000.
- As the size of the deal goes up, the rates go down:
  - \$.00552 from \$100,000 to \$1 million
  - \$.00453 from 1 million to 5 million
  - \$.00374 from 5 million to 15 million
  - \$.00266 from 15 million to 25 million
  - \$.00159 over \$25 million
  - Each reduction is 18% ; rate over \$25 million is 72% less than the highest rate.

# Example #1

- The customer is building a \$7,000,000 office building on property that is currently worth \$400,000. He wants you to close it. But he only wants to pay the premium for the land value. What do you do?
  - R-3 requires that the OTP be issued for the land and at the option of the owner, contemplated improvements ... but under R-4 the MTP must be issued for the amount of the loan or the land value the lesser if the land isn't all of the security.

# Example #1

- So, in this case since the loan is for \$7,000,000 and the land is worth \$400,000, the OTP should be for \$7,400,000 and a MTP simultaneously issued for \$7 million.
- OTP:  $7400000 - 5000000 = 2400000^*$   
 $.00374 = 8976 + 23959 = \$32,935$
- MTP: \$100 plus endorsements
- TotalL \$33,035. But there is another way ...

# Example 1 p.2

- OTP: \$400,000-  
 $100000 = 300000 * .00453 = 1656 + 837 = 2493$
- MTP: \$7,000,000-  
 $5000000 = 2000000 * .00374 = 7480 + 23989 = 31469$   
 $+100(SI) - 32469 - 2493(\text{OTP amount}) = \$28,976.$
- Total: 2493 for OTP and 28976 for  
MTP=\$31,469
- Or 1466 less expensive than the previous way
- But the owner isn't getting full coverage so is it a good deal for him?

# Example #2

- Your customer is getting a loan for \$20,000,000 to build an office building but he doesn't want to pay the MTP premium all at once. What do you tell him?
- That he can pay the premium over time as construction draws are made provided that he understands that if he fails to pay for down date endorsements, the coverage stops where he stops paying.

# Example 2 p2

- MTP for \$20,000,000 = 20,000,000 - 15,000,000 = 5,000,000 \* .00266 = 13300 + 61359 = \$74,659. (to be paid in installments)
- 1<sup>st</sup> draw = \$4,500,000  
 $4500000 / 20000000 = 22.5\%$   
 $* 74659 = \$16,798$
- 2<sup>nd</sup> draw = \$7,250,000
- $7250000 / 20000000 = 36.25\% * 74659 = \$27,064$

# Example 2 p2

- So that at the end of the 1<sup>st</sup> 2 draws, the loan will have been advanced by \$11,750,000 (4.5 million +7.25 million) or 58.75% and the premium will have been paid by \$43,862 (16798+27064) or 58.75%.
- And so on until all of the draws have been made and all of the premium has been paid.

# Example 3

- You have been asked to issue an OTP for \$85,000 and 2 MTPs, one for \$60,000 and one for \$25,000. This isn't homestead. What can you do?
- R-5 deals with this issue. The OTP premium is at the basic rate=767 and each of the MTPs is \$100. Total=\$967 plus any endorsements.

# Example 4

- You have been asked to issue an OTP for \$85,000 and 2 MTPs, one for \$60,000 and one for \$30,000. This isn't homestead. What can you do?
- R-5 deals with this issue. When the MTP amounts exceed the OTP, then the combination of the MTP amounts creates your basic premium and the OTP is actually the one issued simultaneously. The OTP premium is at the basic rate=767. Each of the MTPs is \$100.

## Example 4 cont.

- Then since the totals of the MTP exceed the OTP, you compute the MTP totals ( $\$90,000=801$ )
- Then  $801$  less OTP premium of  $\$767=\$34$
- $801+34+200=\$1034$  plus endorsements

# Example #5

- Buyer is acquiring 2 acreage tracts in different surveys and 5 lots in 3 subdivisions. Each tract has a different owner. Are there additional chain charges?
- Each acreage tract is a chain. (2)
- Since each lot has a different owner, there are 4 additional chains here. So the additional chain charge =  $237 * 4 = 948$ . Since each tract has a different owner it doesn't matter if any lots are contiguous.

# Example 6

- Customer is buying 75 acres in the country for \$75,000 cash. Access is by a county road. Customer wants to buy access to a highway across 2 of this neighbors' properties. What is his premium?
- $\text{OTP for } \$75,000 = 696$
- 2 additional chains (since different owners) is  $237 * 2$  or 474.
- $\text{Total} = 696 + 474 = \$1170$

# Example 7

- US Postal Service is building a post office in your town. The amount is \$476,000. What do you do?
- 1<sup>st</sup>, say thanks.
- 2<sup>nd</sup>, call or email Brenda Sarah in forms in Houston ([bsarah@stewart.com](mailto:bsarah@stewart.com)) and ask for the T-11 USA Policy and T-12 Endorsement

# Example 7 p.2

- 3<sup>rd</sup>: premium is  $476000 - 100000 = 376000 * .00552 = 20755 + 871 = \$21,626$
- 4<sup>th</sup>: add the special language of the new paragraph 9 as set out in R-17
- 5<sup>th</sup>: change the forms to read US Postal Service instead of USA.

# Example 8

- Mr. Smith inherited a house in your town from a maiden Aunt he never knew he had. He has never seen the place but wants to sell it. Missy Jones has agreed to buy the property but her wise counsel has put in the contract that Smith will execute a general warranty deed. He refuses to do so and your \$80,000 deal is about to crater. What can you do to help.

# Example 8 p2

- R-21 to the rescue!!!
- You can sell Smith a “warrantor’s policy for 30% of the rate that Missy will pay. He is then covered against any claims she might have under her warranty and since he is an insured, the title company can’t seek subrogation from him.

# Example 8 p3

- OTP for \$80,000=730
- MTP for \$72,000= 100 plus endorsements
- OTP to Smith for \$80,000=730\*30%=219

BUT WAIT, that amount is less than the minimum basic rate so his premium is \$237.

# Example 9

- 2 years ago, your competitor issued a \$25,000,000 MTP on a construction loan for a major project. The work is now done and the permanent lender has asked you to issue a new MTP to them for \$22,000,000. Before you run out and get an new Ferrari, what should you think about.

# Example 9 p.2

- First, you must think about R-8 credits. But even more, you have to think about R-18.
- Under R-18, the new lender can get a new MTP for the minimum premium of \$237.00. Do you really want to take this deal? Probably because of the relationship that the lender has with you.

# Example 10

- You are issuing an OTP for \$110,000 and an MTP for \$95,000. The lender wants a T-19. What is the premium?
- OTP: 110,000-  
 $100000 = 10000 * .00552 = \$55 + 871 = \$926$
- MTP: \$100 plus endorsements
- T-19:  $838 * 5\% = \$42.00$  (residential)
- T-19:  $838 * 15\% = 126.00$  (non-residential)

# Example 11

- You are issuing an OTP on a commercial transaction for \$110,000 and an MTP for \$95,000. The lender wants a T-19. The owner wants a T-19.1. What is the premium?
- OTP:  $110,000 - 100,000 = 10,000 * .00552 = \$55 + 871 = \$926$
- T-19.1:  $= 926 * 15\% = \$139$
- MTP: \$100 plus endorsements
- T-19:  $838 * 15\% = 126.00$  (non-residential)
- OTP total: 1065 (926+139)
- MTP:  $\$100 + 126 = 226$
  
- Remember: you charge for the MTP endorsement as though it were a stand-alone policy not at the SI rate

# Example 12 R-3

- You are being asked to insure a lease of a national fast food store. The land value is \$100,000. The lease terms are for \$12,500 per month for 60 months. They are planning to build a \$750,000 store. What should the policy amount be and what premium is charged. How much is the leasehold endorsement.

# Example 12 p2.

- Step one: what is the value of the lease?

$$12,500 * 60 = 750,000$$

- Step two: what is the value of the land + the immediately contemplated improvements?

$$100,000 \text{ (land)} + 750,000 \text{ (improvements)} = \$850,000$$

**Step three: value of land and existing improvements**

$$= \$100,000$$

Insured has option to pick any of the 3 amounts as the policy amount.

# Example 12 p3

- How much is the leasehold endorsement?
- \$0.00.
- The endorsement changes the terms of the policy in ways to be more favorable to the insurer; thus, there is no charge to the borrower.
- It does provide that in case of a total title failure and they have to move, we will pay to move their stuff 100 miles so they get something.