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OPINION
OF
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Opinion No. 87-30

BY: Stephen J. Rhoades
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To: Vicente B. Jasso
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State of New Mexico
Department of Insurance
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FACTS:

Title insurance companies acting as closing agents or escrow agents accept escrowed funds received by parties to a sales transaction in anticipation of a sales or loan closing. These funds commonly are placed into interest-bearing accounts until disbursement subsequent to the actual sales or loan closing. In lieu of paying interest, some banking institutions are offering other benefits to the companies initiating such accounts such as no service fees, free check printing, and similar in-kind services.

QUESTION:

Whether a title insurance company acting as escrow agent can retain for its own benefit interest paid by a financial institution on escrow accounts without express permission from the customer or written contract allowing this payment of interest as compensation.

CONCLUSION:

No.

ANALYSIS:

The practice of title insurance is governed by the New Mexico Title Insurance Law, Sections 59A-30-1 to 59A-30-15 NMSA 1978 (1986 Cum. Supp.). Section 59A-30-14 NMSA 1978 expressly incorporates Articles 1 through 12, 15, and 16 of the Insurance Code, Chapter 127, Laws of 1984, including the general article governing insurance agents, brokers, and solicitors and makes these articles applicable to the New Mexico Title Insurance Law. Section 59A-12-22 NMSA 1978 (1984 Orig. Pamp.) therefore is applicable to title insurance companies and title insurance agents.

Section 59A-12-22 NMSA 1978 provides that all funds of other persons or entities received by any persons licensed or acting as an insurance agent, broker, or solicitor, are received and held by such person in a "fiduciary capacity." The receipt, holding, and disbursement of escrowed funds create fiduciary obligations of the title insurance company or agent to the funds' owner. Any diversion, misappropriation, taking, or secreting of funds for the fiduciary's own use or with intent to embezzle, without consent of the person entitled to such funds, is punishable as larceny by embezzlement.

Section 59A-12-22B(2) NMSA 1978 allows the establishment and maintenance of an escrow account in a commercial bank or other financial institution, separate from accounts holding general personal, firm, or corporate funds, to hold funds of all principals of the insurance agent, broker, or solicitor, as long as the amount held for each principal is readily ascertainable from the depositor's records. The principal expressly can waive in writing this section's segregation requirements. The statute is silent whether the disbursement of the interest on such funds to the title insurance company, agent, broker, or solicitor is proper.

The New Mexico Insurance Code, Section 59A-1-1 to 59A-53-17 NMSA 1978 (1984 Orig. Pamp.), is silent on the definition of "fiduciary capacity." Under New Mexico law, an agent cannot place its own self interest above the interest of its principal who is relying upon the agent. Rice v. First National Bank in Albuquerque, 50 N.M. 99, 171 P.2d 318 (1946). An agent breaches its fiduciary duties to the principal when the agent places its own interest above those of the principal. Gelfand v. Horizon Corporation, 675 F.2d 1108 (10th Cir. 1982).

The standard of care required of a person standing in a fiduciary capacity is one of the highest that the law imposes. A person or entity standing in a fiduciary capacity to another must conduct its affairs with "scrupulous honesty, skill and diligence," Tucson Title Insurance Company v. D'Ascoli, 94 Ariz. 230, 234, 383 P.2d 119, 121-2 (1963). When applying a fiduciary duty to an escrow agent, courts in other jurisdictions have prohibited any personal profit to the escrow agent as a result of handling the transaction without either express consent or prior agreement. An escrow agent owes its utmost good faith to its principal and will not be permitted to profit personally from the agency without its principal's knowledge and consent. French v. Orange County Investment Corporation, 125 Cal. App. 587, 13 P.2d 1046 (Ct. App. 1932); Holmes v. McKey, 383 P.2d 655 (Okla. 1962). See also Lenchner v. Chase, 98 Cal. App. 2d 794, 220 P.2d 921 (Ct. App. 1950) ("utmost good faith"). The cardinal principle of agency is good faith. The depositary cannot pervert this agency relationship to its own advantage. Collins v. Hertman, 225 Ark. 666, 284 S.W. 2d 628 (S.Ct. 1955).

From a review of these principles, it is a violation of a person's fiduciary duty, absent written consent or an agreement from the funds' principal or owner to the contrary, to retain any interest created by the depositing of escrowed funds in an interest-bearing account to the benefit of the title insurance company, agents, brokers, or solicitors. The acceptance of other in-kind services and consideration in lieu of interest on such escrow accounts are also in violation of the fiduciary duties of the title insurance company, agent, broker, or solicitor to the principal. By close analogy, this analysis is supported by the Supreme Court of New Mexico's position on interest generated by the trust accounts that lawyers maintain for funds from clients. The law firm does not retain the interest generated by those funds, but provides the earnings to the client or to a nonprofit fund to be used for certain public purposes. See Rule 16-115, Code of Professional Responsibility.

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