

CA App. Ct. Reaffirms Limited Duties of Escrow Holders
Opinion one of only a few to address "sub-escrow" law in CA

A new published California Appellate Court opinion reaffirms that the duties of escrow holders are very limited in nature, and almost non-existent relative to third parties to an escrow.

The Court holds that where a borrower has no contractual privity or other contact with a sub-escrow holder in connection with a refinance transaction, the sub-escrow holder owes the borrower no common law duties under negligence or fiduciary law.

The Court's reasoning begins with a mention of California's existing general rule of escrow liability: absent clear evidence of fraud, the obligation of an escrow holder is only to follow the escrow instructions, and such duty is owed only the parties to the escrow.

The Court then reasons that a lender's instructions to an escrow holder do not create indirect privity between the borrower and the escrow holder, even if the lender's instructions happen to be consistent with the borrower's interests. Further, such lender instructions are not a basis for a borrower to advance a "third party beneficiary" theory against the escrow holder unless there is sufficient evidence that the lender and escrow holder mutually intended for the instruction to benefit the borrower at the time the escrow agreement was made.

The Court also holds that escrow agents owe no statutory duties to borrowers based on California Civil Code Section 2941 (California's statutory protocol for reconveyances of liens following payoffs of loans secured by deeds of trusts). The Court reasons that Section 2941's literal language imposes mandatory obligations on lenders and trust deed beneficiaries (loan/lien holders) and trustees, but not on escrow holders.

It should be noted that the case involves a fact pattern involving both a "[main] escrow" and a "sub-escrow." "Sub-escrows" are a creation of long-standing custom in Southern California (and parts of Central California), but almost unheard of in Northern California.

Unfortunately, very few published California appellate opinions address the threshold issue of the basic legal nature of a "sub-escrow." This opinion inferentially suggests that a sub-escrow is an escrow completely independent from a main escrow. A competing view is that a sub-escrow is a licensed service provider merely assisting a main escrow fulfill portions of its escrow service obligations, akin to a vendor.

Resolving this issue is critical because under the later paradigm, a sub-escrow would, in fact, be in privity with a borrower (assuming the borrower is a party to the main escrow) and the main escrow can be vicariously liable for the sub-escrow's performance failures. The opinion fails to take advantage of a unique opportunity to resolve, or at least explore, this critical issue.

Upon request we will be happy to provide you with a more thorough recitation of the case, and a further criticism of the Court's analysis, regardless of its conclusion.

The case is *Markowitz v. Fidelity Nat. Title Co.* (August 30, 2006, B179923) ___ Cal.App.4th ___; ___ Cal.Rptr.3d ___; 2006 WL 1480052; 2006 DJDAR 11794 (CA Ct. of App., 2nd Dist., Div. 4) *