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Who Represents You in a Rhode Island Real Estate Closing?

Real Estate Attorneys' Liabilities after *Groff*

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Historically, most closing attorneys considered the lender their client. In short, the lender appeared to control the attorney. Or so we once thought.

Disciplinary counsel inquired, "Dave, exactly who are you representing in this closing?"

Without hesitation, I responded, "Well, the bank (of course)."

"Not so fast, counselor…I think you need to read Groff before you can say that…"

My breathing stopped for a few seconds upon hearing that statement.

Perhaps I should back up a bit…

The **Groff** decision (**Credit Union Central Falls v. Groff**, 2009 RI 966 A.2d 1262 (RI Sup Ct, 2009)) was decided February, in 2009. The essential holding of **Groff** is that a settlement attorney actually represents the borrower in a bank-financed, real estate closing *and* possibly owes duties to other non-client parties as well.[1] Those other parties, such as a lender, are now considered "third party beneficiaries" to the contractual agreement between the borrower and closing attorney.[2] It is a shift of the commonly-held understanding that will sweep through the bar of Rhode Island real estate attorneys.

In my situation, what appeared to be a normal, garden-variety closing developed into a problem when the lender failed to wire the settlement proceeds to my account in a timely manner. The situation was considerably tighter due to the fact that the prior lien to be paid was for an Federal Housing Administration (FHA) loan which required an additional month's worth of interest (and not a standard per diem interest amount) if the payoff were to be received after the first day of the next month. The borrower could not (and should not have had to) produce any such an additional amount. The lack of funds from the lender severely threatened my office's ability to assure a fully paid lien. My concern was that, without full payment, the borrower would still have an active amount on the loan, accumulating interest, and the new bank would not be in first position as the title policy I issued would have guaranteed. After the exchange of strained and demanding emails back and forth between the lender and my office, the funds finally arrived, but not before I had made a call to Disciplinary Counsel to ask about my next possible course of action. Disciplinary Counsel's inquiry (see above) as to whom I represent deeply concerned me. It was not for the matter at hand, but, rather, how I would operate going forward. What had appeared to be a quarrel between client and attorney (the lender and myself), now placed me at odds instead with the borrower, and all the implications that it conjures.

What is it about **Groff** that should make a real estate attorney worry? Historically, most closing attorneys considered the lender their client. The lender traditionally dictated the actions of the attorney, and the instructions delivered with most closing packages had directives followed without deviation. In short, the lender appeared to control the attorney. Or so we once thought.

After **Groff**, it is now the borrower whom the attorney represents. The difference may appear to be a nuance, but the fiduciary duties that such a shift places upon a closing attorney can wreak havoc with how one approaches title issues, questions from borrowers, dealings with lenders, and, most importantly, disbursements of monies from these closings.

The travel of **Groff** initially appears complicated, but it is not. Attorney Lawrence Groff acted as a settlement agent for a number of loans from Credit Union Central Falls (CUCF), now known as Navigant Credit Union. Allegations were leveled against Attorney Groff by two borrowers in two separate closings. Allegedly, Groff did not pay previously encumbered liens for those individual borrower's properties which were to be paid via the proceeds of the new loans (as identified in the settlement statements of the loans). The title insurer, Mortgage Guarantee, as a result of the title policies written by Groff, were obliged to provide the payoffs to assure the insured lender, CUCF, they would be in first position. Mortgage Guarantee then filed suit against their former agent, Groff, for reimbursement. CUCF also sued Attorney Groff for malpractice. As a result, Attorney Groff's escrow account was

frozen by court order. Mortgage Guarantee's claim was that the amounts in Groff's fund should be granted to them since they had made CUCF whole. Mortgage Guarantee's claim was based upon the fact that they had placed CUCF in first position by paying the liens left open by Attorney Groff. Ergo, they claimed the proceeds in Groff's escrow rightfully belonged to them.

The complication of this case developed with an action commenced by another client of Groff. That client was utilizing Attorney Groff in a probate matter, and she alleged she had furnished a large amount of money to Groff under false pretense and wanted her money returned. Since the court had placed a hold upon Groff's escrow, the probate client chose to intervene in the real estate suit so that her assets in that escrow account could be protected.

In discovery, the probate client sought to elicit communications between Groff and CUCF and also between Groff and the borrowers. Groff claimed those communications were protected by the attorney-client privilege and not subject to discovery. The case eventually found its way to the Rhode Island Supreme Court, seeking to clarify exactly who Attorney Groff represented, and subsequent to that determination, what, if any, of those communications were truly protected. However, the resulting decision was somewhat broader than that narrow question.

In **Groff**, the Court wrestled with a number of factors, including the relationship Groff had with CUCF, being one of a select few attorneys permitted to close their loans, as well as the written directions from CUCF that Groff was required to follow.[3] Another factor the Court considered was the client's ability to choose who may be used as the Title Attorney for the transaction.[4] What the Court finally appeared to have settled on is, quite simply, who paid the bills for the legal work and whether the borrowers accepted the specific attorney.[5] The Court pointed to the fact that since the borrower would be responsible for paying for the attorney fees, title examination, and the lender's title insurance (even though the title insurance would be only a benefit to the lender), the Court found the attorney-client relationship was formed between the borrower and attorney.[6]

How then was a bank such as CUCF, now without an attorney-client relation-

ship, able to sue Groff for malpractice if they were not his client? The Court stated that the bank was a "third party beneficiary" to the contractual agreement of the borrower and attorney. The rationalization was that the borrower required a loan from the bank and the bank required a number of legal actions performed to assure security. The attorney, acting for the borrower, would assure that those actions were done to satisfy the lender in order to induce them to loan the money.[7]

What appears missing from the facts, as it probably is in most real estate transactions, was any sort of retainer agreement. The documents signed by the borrowers indicated that, even though the borrowers could have chosen their own title attorney, they chose to allow the bank to choose one for them.[8] The Court is silent as to what the result would have been had the borrowers chosen an attorney not approved by CUCF. However, the result is unlikely altered by that variation. If the rationale is that the attorney is acting for the ultimate benefit of the client borrower, the approval of a bank may not preclude the attorney's duties to both the client (the borrower) and the third party beneficiary (the bank). It is likely that the third party beneficiary theory would apply to any attorney based upon the direct benefit derived by the transaction, even if that attorney was not an approved or preferred attorney of the lender.

The Court's decision may have a far-reaching effect outside of the scope of real estate. The decision may open attorneys to new liabilities to potential third party beneficiaries in other matters if, as the Court highlighted, those benefits were a direct result of the transaction.[9] In other fields of practice, such as estate planning, the potential liability of an attorney may now be heightened. However, there is little doubt that this decision certainly places a burden upon the real estate practitioner in very real and specific ways.

If the Court's ruling is a blanket statement that the client is the borrower, what happens next? Assume a borrower is sitting at a table alone with an attorney, signing paper work for a refinance, and asks a bit of legal advice about the loan. In the past, attorneys often rested on the comfort of not owing a duty to a non-client. Many, uneasy about expressing

any opinion (and possibly angering their perceived client, the bank), could easily say (as they believed) that they were representing the lender and avoid expressing any legal opinion. Now, that may have to change. What if a closing occurs that subsequently devolves into a contentious matter between the lender and the borrower? What position, if any, will the closing attorney have to take if the attorney was, and had always been, the representative of the borrower? Additionally, how muddy will the waters now be since the attorney may also owe a fiduciary duty to the lender?

After **Groff** was decided in Rhode Island, other states began to address dual representations in the context of real estate closings (*see* **Marsh v. Wallace** from the Mississippi Federal Court, citing that attorneys need to clearly indicate whom they represent to all parties in real estate closings per their Rules of Professional Conduct[10]). Since the Court in **Groff** did not address what effect a pre-emptive disclosure by an attorney may have, it still may be murky as to whether a disclosure that would counter the assumption of representation that **Groff** imposes would clarify the situation. Additionally, the recent problems surrounding errors in foreclosure actions in other states should give Rhode Island attorneys pause as to their true or perceived role at any real estate closing. Since a third party beneficiary now places additional liabilities upon the attorney, the answer may hold many more problems for the practitioner, especially ones who do not address the actual representation issue up-front.

Groff may now impact situations that involve potentially confidential communications. What if the borrower asks advice or reveals a fact about a potential title problem on the property in the middle of, before, or after the closing? Revealing that defect to the bank could violate the attorney-client privilege. Not revealing a known defect could place the attorney subject to problems with the third party beneficiary, the bank. Lastly, what duties does a closing attorney have toward a *pro se* seller in a conveyance closing? What if a deed is prepared to facilitate the conveyance and an error is made? Does the attorney have duties to *both* buyer and seller? **Groff** can easily extend to mean that now the sellers are also third party beneficiaries.

…Not so fast, counselor. Those old assumptions may no longer apply.

ENDNOTES

1 *Credit Union Central Falls V. Groff, 2009 RI 966 A.2d 1262 (RI Sup Ct, 2009).*
2 *Groff, 1274-75*
3 *Groff, 1269-70*
4 *Groff, 1273*
5 *Groff, 1274*
6 *Groff, 1274*
7 *Groff, 1274*
8 *Groff, 1270*
9 *Groff, 1272-3*
10 *Marsh V. Wallace, 666 F.Supp.2d 651 (S.D.Miss. 2009).* ❖