

# Understanding Land Records: *Transaction Marketplace, Universe of Competing Property Interests*

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# Understanding Land Records - Transaction Marketplace, Universe of Competing Property Interests

## A. Constructive notice

Public land records are an indispensable source of land ownership information for prospective purchasers and lenders. Whether they are first-time homeowners or experienced commercial investors, public land records accord the prospective purchaser a passing opportunity to assess the marketability of the seller's title, evaluate the potential for future amenities offering a premium resale value, and in some cases, avert financial loss by avoiding the acquisition of encumbered ownership that would frustrate or hinder expectations. The emphasis in accessing public land records is on the timing of their analysis: Before paying value at closing or settlement, the land records are of crucial significance, but after, they are no longer the source of critical information they might otherwise have been. The legal significance of public land records in the system of land transactions is that they impart *constructive notice* to prospective purchasers: Though the prospective purchaser was without any actual knowledge of liens, defects or encumbrances in the records, by law the purchaser is deemed to know of these liens, defects and encumbrances at the time of closing or settlement.

### Example:

- July 1, 2015: Savvy Investment LLC grants a mortgage to Camouflage Bank.
- July 2, 2015: Camouflage Bank's mortgage is recorded in the public records.
- August 2, 2017: Savvy induces Aquarius LLC to purchase its real estate, warranting that its title is "free and clear of liens" and that in light of Savvy's reputation, "searching the title would be a waste of time and an unnecessary expense." Aquarius, believing Savvy's explanation, consummates the closing for the purchase and receives a warranty deed, becoming the property's new owner.
- October 1, 2017: After a default in its mortgage loan occurs for non-payment, Camouflage Bank discovers that Savvy transferred its ownership to Aquarius and accelerates its loan, threatening a foreclosure against Aquarius.

In this example, Aquarius's lack of knowledge of Camouflage's Bank's mortgage, which would have been disclosed by a routine real estate title search, and its receipt of warranties provided by Savvy are not a defense to the enforcement of Camouflage's mortgage. Public land records are designed to protect purchasers who timely search and examine them, not purchasers like Aquarius, who are ignorant of or who cavalierly disregard them.

### 1. Relevance to purchasers

Demographic, anthropological or historical information found in the public land records that transcend eras and epochs, including periods of economic development or decline, natural resources, civil disturbances and migration, may prove of genuine interest to any number of readers. In some states, abstracts of title, a portable history of the property's ownership in book form, trace these events, answering such questions as: Who owned the real estate in question during the Great Depression? However, prospective purchasers whose time and resources are limited do not need or strive to know every facet of land ownership history dating to pre-colonial North America, unless past events, such as highways, private rights of passage, mineral interests, or aboriginal or treaty rights, continue to affect or restrict the property's use and enjoyment or transferability. Thus, prospective purchasers must investigate and verify, simply put: Who is the present owner, what is the property's description, and what liens and encumbrances currently affect the title? Public land records invariably produce answers to these questions. Professional title examiners, to be proficient, must know how to elicit the answers and how to do so expeditiously.

## 2. Role of the real estate professional, insurance

From the vantage of prospective property owners and incumbrancers, public land records do not always yield answers that are palpable, nor are the ramifications of title documents necessarily clear without analysis by trained specialists, such as legal counsel, land surveyors, environmental consultants, hydrologists, and others whose expertise may prove essential. Furthermore, certain essential information concerning ownership of real estate, including rights of possession and prescriptive rights, is seldom accessible from the public land records. Finally, the investor may discover that the professional they employ, though highly skilled, eschews professional liability for any number of potential issues that grow out of opinions they render concerning the public records, hence the role of insurance. Insurance in the form of standardized policies, title insurance, are issued by companies that base such policies on public land records, and view them as sufficient to issue their contracts of indemnity. Public land records in and of themselves pose risks to purchasers that may require professional advice and insurance.

### Example:

- |                   |   |
|-------------------|---|
| January 2, 2015:  | Prime Loan Bank begins negotiations for a \$10 million mortgage loan with borrower Georgetown Investments. Prime Loan Bank's counsel recommends the lender require title insurance as a condition of the loan commitment. |
| February 1, 2015: | After reviewing a commitment for title insurance showing Georgetown to be the owner, lender's counsel provides an opinion letter, and Prime Loan Bank closes and disbursed the loan.                                      |
| April 2, 2017:    | The United States Attorney files a civil action against both Georgetown and Prime Loan Bank claiming that Georgetown used the proceeds of the illicit sale of   |

securities to purchase the real estate, and asking that the court declare a constructive trust for the benefit of individuals who sustained financial loss as a result of Georgetown's illegal activities. The United States claims that Prime Loan Bank's mortgage, notwithstanding its status as a bona fide incumbrancer that relied on the public land records, should be subordinated to the claim of the class of parties who sustained a financial loss.

In this example, at the time of the closing, the title of record, pristine as it were, was vested in the name of the mortgagor, and not subject to any liens or encumbrances. Nonetheless, the title of the mortgagor was subject to the unknown claims of individuals who had incurred a financial loss as the result of unlawful activities of the mortgagor. The title insurer that issued the policy insuring the mortgage is obligated to defend the claim of the United States and to pay loss to the mortgagee in the event the mortgage is found to be void or subordinate.

Example:

- Joseph, who owned several properties, including his home, obtained a home mortgage loan from Careful Bank, and the mortgage was recorded.
- When Joseph sold another of his properties, the lender whose loan was secured by a mortgage, Embarrassed Bank, satisfied the mortgage, but through inadvertence, the satisfaction prepared and signed by Embarrassed Bank satisfied Careful Bank's mortgage.
- Joseph decides to sell his home to Mary. A search of the title shows no unsatisfied mortgages against Joseph's home.
- During the closing, Joseph discretely remains silent when asked about outstanding liens, he receives the net proceeds of sale *plus the amount of the unpaid loan balance he still owes Careful Bank* and after the closing, immediately relocates his place of residence to the Caribbean region.
- Careful Bank discovers Joseph's recent sale and notifies Mary that unless Joseph's outstanding loan balance of \$200,000 is paid, a foreclosure against her will be initiated.

In this example, the title insurer that insured Mary's ownership interest is obligated to defend Mary from Careful Bank's foreclosure and, if necessary, to pay Careful Bank's loan balance. The title insurer will likely then attempt to find Joseph's whereabouts in the Caribbean and seek recoupment of the payment it made to Careful Bank.

B. Estates or Interests in Real Property: Present, Future and Concurrent

1. Is the seller's interest transferable?

In a global economy where jurisdictional barriers to transactions generally are viewed as anachronistic, it may come as a surprise to prospective purchasers that owing to vestiges of common law that survive in the United States, not all real property, regardless its value as a development site, is necessarily transferable. Whether the real estate is transferable depends upon the type of estate or interest the prospective seller holds. Generally, real property of the seller is freely transferable by the seller if the seller's interest is a *fee simple estate* in land: An estate of inheritance without condition, belonging to the seller, and alienable by the seller absolutely in perpetuity, the largest possible estate an individual can have in land. The terms "fee simple" and "fee simple absolute" are sometimes used interchangeably in the preparation of conveyances, though the latter is preferable so that there is no confusion with a lesser estate, the fee simple determinable. The term "absolute" connotes a right of the owner to have uncontrolled use and disposition of all of the legal and physical properties thereof. 2 Thompson on Real Property, §17.07 at 453. However, in the event that the property of the seller is not an estate in fee simple, the seller's property interest may not be one that can be transferred or acquired without involving others whose outstanding interests require relinquishment, and who are thus indispensable parties to the transaction.

Rather than declining in importance, evidence suggests that non-fee simple common law estates in land are proliferating in both residential and commercial transactions. Separately, the use of easements, either by assigning existing easements or creating new easements, to provide amenities for developments continues to expand. Several estates at common law or codified by statute must be distinguished from the fee simple estate, and their characteristics carefully evaluated before a conclusion can be reached about transferability of the seller's property.

2. Fee simple determinable

Fee simple determinable is a fee simple estate that automatically expires upon the occurrence of a stated event. Though the use of the fee simple determinable in structuring present day transactions has become rare, they remain a potential transaction pitfall for which purchasers and title insurers must be vigilant. Fee simple determinable estates tend to occur among real estate owned by public school districts, religious organizations or churches, libraries or charitable organizations, and land used as public parks or for other public purposes. (Exhibit 1) Importantly, a transfer of fee simple determinable holder's interest may be strictly limited or prohibited by the terms of the original grant, and in the event that terms of the grant are violated may result in a reversion of the title to the original grantor, their heirs or assigns. State laws must be carefully analyzed to ascertain whether the grantor's reversionary right remains enforceable or whether it has become time-barred by statute of limitation or repose.

3. Fee simple subject to condition subsequent

Fee simple subject to condition subsequent is a fee simple subject to a power in the transferor to re-acquire the fee by reason of a future breach of certain conditions under which the estate was vested. In contrast to the fee simple determinable, which is rare, the fee simple subject to condition subsequent is commonplace and was routinely imposed during the first half of the 20th century in master restrictive covenants affecting residential subdivision developments. (Exhibit 2)

#### 4. Possibility of reverter

The possibility of reverter is the interest left in the transferor who created a fee simple determinable, or if the transferor is deceased or an entity that is dissolved, the heirs or assigns of the transferor.

#### 5. Leasehold estates

Unlike fee simple estates, which are perpetual, leasehold estates have a fixed and certain period of duration. A leasehold estate is an estate in land and can be conveyed and thus mortgaged subject to certain conditions. The effect of a lease is to carve out an estate for years and leave the lessor with a reversion in fee simple.

#### 6. Remainders

The remainder is an interest to take effect at the termination of a preceding interest created at the same time or without the intervention of such preceding interest. Remainders are classified as one of four types: indefeasibly vested, vested subject to open, vested subject to complete defeasance, and those subject to a condition precedent. At common law remainders were inalienable unless they were vested, and contingent remainders remain inalienable under the laws of some states. Thus, a quitclaim deed executed by the holder of a contingent remainder was held a nullity. Goodwine State Bank v. Mullins, 253 Ill. App.3d 980, 625 N.E.2d 1056 (1993).

#### 7. Life estates

The life estate is an estate that is not terminable at any fixed or computable period of time and has its duration measured by the life or lives of one or more persons. The creation of a life estate results in a vesting of rights in two parties, the life tenant and the remainderman. The life estate is created by a conveyance in which the estate is granted to the life tenant or, more commonly, reserved by the grantor. (Exhibit 3) The life estate is freely alienable and may be mortgaged. However, a mortgage executed by the life tenant but not by the remainderman cannot bind the remainderman. The life estate terminates at the death of the life tenant and not when the life tenant ceases occupying the property or becomes mentally incompetent or physically impaired.

#### 8. Powers of appointment

Not an estate or interest in land but a power, the power of appointment is a power conferred or reserved by one person by deed upon another to appoint or select the

persons who are to receive and enjoy and estate or income, after the donee's death or after the termination of an existing right or interest. In the event that the power was reserved by a deed in the grantor, the deed's grantee is subject to the right of the grantor to convey. (Exhibit 4)

## 9. Easements

An easement is a permanent interest in another's land with a right to enjoy it fully and without obstruction. Easements are of two types: *Easements appurtenant* and *easements in gross*. An appurtenant easement is a right that is attached to a superior right and inheres in land to which it is attached, and is in the nature of a covenant running with the land. An easement in gross is an easement not appurtenant to any estate in land but is a personal interest in or a right to use the land of another. An example of an appurtenant easement is an easement for vehicular ingress and egress that benefits the owners, past, present and future, of adjoining land. (Exhibit 5) In contrast, an example of an easement in gross is a conservation easement. (Exhibit 6) Though historically, easements were created for utility service lines, vehicular access and cross access, the purposes for which easements can be created are virtually unlimited. (Exhibits 7, 8 and 9) Not all easements are transferable. For example, the interest of a railroad in railroad right of way is frequently an easement, not a fee simple estate, and depending upon the nature of the grant and applicable federal and state law, the railroad's easement is not necessarily transferable unless the right of way continues to be used for railroad purposes. Furthermore, easements should not be confused with *licenses*, a privilege to go on a premises for a certain purpose, which are not transferable, and though the instrument may be nominally an easement, a careful analysis of the instrument in question must be made before proceeding with any assignment or transfer. (Exhibit 10)

## C. Mineral estates

Mineral lands are an important natural resource in some states, but virtually unknown in others. In some states, the term minerals includes sand and gravel, but in others only metallic substances. Mineral rights are an interest in land which may be created or transferred as any other estate in land. Gillett v. Treganza, 6 Wis. 343 (1858). Upon severance of the title to the minerals from that of the remainder of the land, each estate, that of the surface and that of the subsurface or minerals, is a freehold or an estate in fee simple. Carlson v. Minnesota Land & Colonization Co. 113 Minn. 361, 129 N.W. 768 (1911). However, the mineral estate is generally considered the dominant estate. P.N. Inv. Corp. v. Florida Ranchett, Inc., 220 S.2d 451 (Fla. 1969). Buchanan v. Watson, 290 S.W.2d 40 (Ky. 1956). Thus, the mineral estate carries with it the right to use so much of the surface as may be reasonably necessary to reach and recover the minerals. Jilek v. Chicago W. & F. Coal Co., 382 Ill. 241, 47 N.W.2d 96 (1943). Where there is a severance of the mineral estate from the surface, the title to one cannot be acquired by adverse possession of the other. Acquisition of minerals can be by conveyance in fee or by lease. As is the case for conveyances generally, conveyances and leases of minerals are recorded in the county public land records. (Exhibit 11)

## D. Mortgages and Deeds of Trust



The mortgage, which are known as deeds of trust in some states, is an interest in land created by a written instrument providing security for the performance of a duty or the payment of a debt. American states are divided into “title theory” states and “lien theory” states over the question, what interest does the mortgagee hold? In title theory states, the mortgage operates as a conveyance of the legal title to the mortgagee, subject to defeasance on payment of the debt. In lien theory states, the mortgagor retains legal title until foreclosure, and the mortgagee has no right to possession either before or after default. Mortgages are brought within the definition of a conveyance and must therefore comply with the formal requisites of the statutes that pertain to transfers of real property, the Statute of Frauds. Thus, particularly when they secure residential home loans, mortgages tend to reflect the use of standard forms.

E. Security Interests in Fixtures

Security interests created in fixtures are governed both by real estate law and by Article 9 of the Uniform Commercial Code. The lien of a mortgage will extend to fixtures where the mortgage so provides; the security interest created under Article 9 will extend to fixtures where the requirements of the statute pertaining to security interests are met. Thus, in the event that the interest in a fixture is a purchase money security interest, the interest may be secured by a financing statement duly filed in the public land records of the county where the land is located. (Exhibit 12)

F. Array of Statutory Liens

An important class of public land records that has witnessed fundamental changes both in the introduction of new types of liens, and in the manner in which lien information is accessed are statutory liens. The term statutory lien refers to any of a variety of liens arising by force of a state or federal statute laws, and not dependent upon an agreement to give security. Certain types of statutory liens affect only real property; other types not discussed here affect only personal property, and yet others affect both real and personal property. As among the diverse statutory liens that affect personal property: Liens of jewelers, launderers, cooks and animal breeders.

Statutory liens, of which there are many different types recognized by law, tend within the lien classification to be uniform in appearance across the state. However, different types of statutory liens display marked differentiation. The formal requisites with which lien claimants must comply in order to achieve statutory lien status and ensure enforcement remedies are governed by statute specific to the lien, and therefore types of liens vary considerably. For example, in many states judgment liens do not require any property description, but mechanic’s liens do. If statutory liens, as varied as they are, share a common trait, it is that they do not require as a condition to attachment to real property the consent of the landowner.

Historically, the earliest statutory lien laws were designed to protect individual laborers, tradesmen and artisans, who were accorded liens in personal property or chattels and real property, and statutory lien laws reflected a developing economy and rural workforce. The student of English usage will find vestiges of public policy in present day lien

statutes quixotic. Thus, log liens, of importance in protecting laborers employed in the lumber industry during one state's 19th century settlement period and, improbably, still available to contemporary loggers are liens that attached to "logs" (trees that were cut down for lumber) that are taken "personally, or by beast." Today, many of the latest statutory lien laws are regulatory or tax in nature, or secure claims of state and federal government civil and criminal authorities, not of private parties. (Exhibit 13) Concerning their filing frequency, certain statutory liens have become commonplace, but others, though based upon strong public policy goals, such as liens under the Employee Income Retirement Security Act ("ERISA") [29 U.S.C. §1368(a)], and environmental protection laws, including the federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA") (42 U.S.C. §9601 et. seq.) filed by the United States under the Superfund Amendment and Authorization Act of 1986 ("SARA"), remain rare. Because statutory liens are created by statute laws, it should be expected that new types of liens will continue to be introduced as new legislation is enacted.

#### G. Taxes

Most but not all states provide for the assessment of property taxes against real estate. Where such taxes are recognized, the lien of the tax extends to real estate described by appropriate assessment documents. Thus, the lien for unpaid property taxes assessed as against a seller continues though the property's ownership will have changed hands. In contrast to consensual lienors and statutory lien claimants, procedures for forfeiture of delinquent tax properties are rigid: Local government treasurers or auditors that assess, collect and enforce property taxes often lack, under applicable tax collection laws, flexibility concerning the negotiation of tax payments, forgiveness of delinquency, extension of payment deadlines and redemption for non-payment, such that a failure on the part of the owner to pay amounts though nominal, will trigger an irrevocable loss of their ownership. It is therefore imperative that a thorough search and examination of applicable property tax records be made prior to a transfer of ownership so that all unpaid property taxes are revealed and timely paid. In some states, it is possible for an investor to purchase delinquent tax certificates entailing a right to enforce their collection from the county, and in others it is not.

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