

ALTA Owner's and Lender's Policies: *Procedures and Information*

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ALTA OWNERS' AND LENDERS' POLICIES

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PROCEDURES AND INFORMATION

A. Spectrum of Interests in Land

Conveyances, regardless of how carefully they are drawn, may not achieve their intended effect in the event that the property interest of the grantor is inalienable, or if there exists an estate in the same land vested in another party who does not co-sign the conveyance. Recordation of a document purporting to transfer or convey the grantor's interest does not in and of itself effectuate a transfer. Only an examination of the grantor's chain of title will reveal whether the estate the grantor holds is alienable, or subject to estates in others. Certain feudal estates recognized at common law, such as the estate tail, are no longer recognized or have been abolished. Other interests are not estates at all, but merely licenses; for example, a railroad, having granted a permit allowing a landowner to cross its railroad right-of-way, is under no obligation to allow the permit holder's successor a right to cross the right-of-way. Finally, certain land is vested in the sovereign and cannot be conveyed or used as security. Thus, airspace over land, such as a condominium unit, may be the proper subject of a mortgage; airspace over a lake bed or navigable water may not. State v. Trudeau, 139 Wis.2d 91, 408 N.W.2d 337 (1987).

1. Fee simple

Estates in fee simple are uniformly transferable and therefore interests in land for which title insurance is readily available. The term "fee simple" is used to characterize the interest conveyed by the grantor by the standard or prevailing conveyance forms of many states. Although the ALTA title insurance policy Covered Risks or Conditions do not recite or define the term fee simple, Schedule A is typically prepared to state that the vestee of the land holds a fee simple estate in the land described in the policies, and if they do not, the insured may be advised to require that the term be included.

The fee simple estate retains significant attributes when contrasted with the other lesser estates which are still important in conveyancing: Easements, life estates, remainders, leaseholds, and to a limited extent, the fee simple determinable. The fee simple estate has been described as the highest concentration of rights and privileges in the hands of an individual that can arise in a particular stage of the political economy. 2 Thompson on Real Property §1707, at 453 (1994). "An estate in fee simple was, and still is, the largest estate known to the law: It denotes the maximum of legal ownership, the greatest possible aggregate of rights, powers, privileges and

immunities which a person may have in land." Cornelius J. Moynihan, Introduction to the Law of Real Property §2 at 29 (1962).

At common law, if a fee simple estate was to be created, it was absolutely necessary for a conveyance to include words of general inheritance ("…and his heirs"). For example, a deed "to Snorlax *and his heirs*" gave Snorlax a fee simple, but a deed "to Charmander in fee simple" or "to Charmander and his assigns" gave the latter only a life estate. Use of words of inheritance is no longer necessary to transfer a fee simple title and has been abrogated by statute.

The term "absolute" (from "fee simple absolute") implies a right of the owner to have uncontrolled use and disposition of all of the legal and physical properties thereof. 2 Thompson supra §17.07 at 453. Although they were not identical at common law, today, the terms fee simple and fee simple absolute are typically used interchangeably by the drafters of conveyances. The latter is always preferable to the grantee so that there is no confusion with a lesser estate, the fee simple determinable.

Although the title to land is unlikely to involve a transfer by will to the same extent as was the case in a predominantly agrarian economy, when the title to land passes by will, it is still necessary to verify, when examining a title that passed by administration of the estate of the decedent that the will of the decedent devised a fee simple and not a lesser estate, such as a life estate. What is the estate that will have passed by the will if the will failed to expressly state that the devisee received a "fee simple?" There is a strong presumption that a will creates an estate in fee simple absolute and not a lesser estate. Byers v. Rumppe, 251 Wis. 608, 30 N.W.2d 192 (1947).

2. Fee simple determinable

Fee simple determinable is a fee simple which automatically expires upon the occurrence of a stated event (Exhibit 5). Titles of this kind can pose a serious risk to the transfer and development of real estate. The fee simple determinable subject to a possibility of reverter should be distinguished from a dissimilar but more commonplace estate, the fee simple subject to condition subsequent. The latter 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 (e.g. "…provided that the property may be used only for the construction of a single–family dwelling, and in the event of a violation the grantor may reacquire the property").

Fee simple determinable estates which are subject to the possibility of reverter are rare, but are occasionally encountered when examining the title to property held by a public school, religious society or church, public park, library or land owned by a charitable organization, such as the YMCA. In contrast to fee simple determinable estates, fee titles subject to condition subsequent were quite common and were routinely imposed during the first half of the 20th century in master restrictive

covenants affecting residential subdivision plats. The use of the condition subsequent in recent developments too has become rare, and their enforceability is time barred by the statutes of some states.

When the seller proposes to transfer a fee simple determinable subject to a possibility of reverter, title insurers are apt to be unwilling to extend coverage against claims on the part of reverter holders if the condition's violation only recently occurred or is about to occur. This is true regardless of how remote in time the deed containing the reverter was recorded, because there is no statute of limitation barring the enforcement of possibilities of reverter. Saletri v. Clark, 13 Wis.2d 325, 108 N.W.2d 548 (1961). However, if the violation of the condition upon which the reverter became automatically vested occurred on a date sufficiently remote from and under circumstances which the holder may be estopped from enforcing the reverter, the title insurer may agree to insure a transfer by the fee simple determinable holder to a purchaser. The title insurer may agree that the estate or interest transferred is no longer a fee simple determinable, but is in effect a fee simple absolute.

A possibility of reverter is the interest left in a transferor who creates a fee simple determinable. Possibilities of reverter, which are interests in real estate, are themselves transferable.

3. Leaseholds

Unlike fee simple estates which are perpetual, leaseholds have a fixed and certain period of duration. Certain leaseholds are prohibited by state law: "All lands within the state are declared to be allodial, and feudal tenures are prohibited. Leases and grants of agricultural land for a longer term than fifteen years in which rent or service of any kind shall be reserved, and all fines and like restraints upon alienation reserved in any grant of land, hereafter made, are declared to be void." Wisconsin Constitution, Sec. 14. A leasehold not prohibited by state law 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. If property subject to a mortgage is subsequently leased, the lease is subject to termination at the time the interest of the mortgage is terminated.

Leases which create leaseholds are not merely conveyances; they are also contracts which certain various covenants made by the parties and implied by law. Whether the interest of a lessee under a lease will support a mortgage requires an approach in which the lease covenants are analyzed. Does the lease require the lessor to execute a mortgage to secure a loan made to the tenant? Lacking this, are there clauses which require the lessor to induce its fee mortgagee to subordinate the lien of its mortgage to the lien of the ground lease? Ground leases are negotiated in order to assure the lessee financing for construction. "…(A)n unsubordinated ground lease is mortgageable when the attorney for a long-term permanent mortgage lender says it is. There is just no universally accepted standard of mortgageability." Emanuel B.

Halper, Mortgageability of Unsubordinated Ground Leases, 16 Real Est. Rev. 48-49 (Winter, 1987).

4. Easements

An easement is a permanent interest in another's land with a right to enjoy it fully and without obstruction. Hunter v. McDonald, 78 Wis.2d 338, 343, 254 N.W.2d 282, 285 (1977). Easements by express grant may be among the various interests in real estate enumerated by the state's Statute of Frauds, and if so, are therefore subject to the same formal requisites regarding conveyances generally. Thus, an easement created by grant must identify the parties, identify the land, be signed and delivered.

Easements that are appurtenant to land tend to enhance the value of the land by providing a right of vehicular access, reciprocal drives or parking, or right to a shared well or party wall. Occasionally, it is discovered that the latest deed in the chain of title had, for reasons that are unclear, omitted any reference to a potentially valuable easement, and this omission is brought to the attention of the parties to a proposed transaction. Should it be assumed that the easement remains in effect, notwithstanding its omission from the last conveyance? If in fact the easement was appurtenant when created, unless the deeds in the chain of title expressly negate the easement's transfer, rights pass with the conveyance of the dominant estate by operation of law. Bino v. City of Hurley, 14 Wis.2d 101, 109 N.W.2d 544 (1961). Therefore, assuming the easement is otherwise assignable and has not been extinguished, it should continue to be viewed as appurtenant to the fee parcel.

Not all easements are transferable. For example, the interest of a railroad in railroad right of way is nearly always an easement, not a fee simple, and the railroad's easement is not transferable unless the right of way continues to be used for railroad purposes. Williams v. Western Union Ry. Co., 50 Wis. 71, 5 N.W. 482 (1880); Pollnow v. Dep't. of Natural Resources, 88 Wis. 2d 350, 276 N.W. 2d 738 (1978). Certain easements are not transferable, as when the easement holder attempts to separate the easement from the dominant estate to which it is appurtenant. New Dells Lumber Co. v. Chicago, St. P., M. & O. Ry. Co., 226 Wis. 614, 276 N.W.2d 632 (1937). An easement granted to pass access to one lot does not confer access to another lot. Sicchio v. Alvey, 10 Wis.2d 528, 103 N.W.2d 544 (1960).

5. Mortgages

Mortgages and deeds of trust are subject to the Statute of Frauds and must therefore comply with the formal requisites that require that the mortgage contain a legal description and be duly executed and delivered. However, state laws pertaining to mortgages vary considerably, and before providing any assurance concerning the mortgage's validity or enforceability, applicable substantive mortgage law should be carefully reviewed. For example, state law may mandate that the loan's maturity

date, or variable interest rate provisions, and maximum amount of indebtedness, be stated by the mortgage.

In residential mortgage finance, the mortgage broker occasionally suggests that where the credit history of one spouse does not meet the lender's underwriting requirements that the name of the spouse with bad credit should be left off the mortgage that secures the loan. Contrary to such requests, it is imperative in many states that the mortgage be duly executed by the titleholder and if a married person, by the titleholder's spouse. Furthermore, if the mortgage is to encumber the interests of both co-owners, the granting clause of the mortgage should identify without qualification both as co-mortgagors. Where a mortgage was signed by both spouses but the name of only one spouse was designated as the borrower, the mortgage was invalid as to the interest of the other spouse, and the bankruptcy trustee for the estate of the spouse was entitled to sell his undivided fractional ½ interest free and clear of the mortgage signed by the debtor. In re Wirth, No. 04-C-5677, 2005 U.S. Dist. LEXIS 24925 (D.C. N.D. Ill. October 21, 2005).

In commercial mortgage lending, the lender may, rather than refinancing the borrower's existing loan, agree to modify, amend or extend the mortgage or make additional advances. Are such advances insured by the loan policy that insures the existing mortgage? The loan policy defines indebtedness.

> Indebtedness: The obligation secured by the insured Mortgage including one evidenced by electronic means authorized by law, and if that obligation is the payment of a debt, the Indebtedness is the sum of (i) the amount of the principal disbursed as of Date of Policy; (ii) the amount of the principal disbursed subsequent to Date of policy;…(iv.) interest on the loan;…*but the Indebtedness is reduced by the total of all payments*... (emphasis added).

Thus, the loan policy does not assure that any additional advance or re-advance of indebtedness provided by a post-policy modification agreement is secured by the existing loan policy.

The loan policy also contains an Exclusion from coverage for post-policy events: "The following matters are expressly excluded from the coverage of this policy, and the Company will not pay loss or damage, costs, attorneys' fees, or expenses that arise by reason of:… 3. Defects, liens, encumbrances, adverse claims, or other matters… (d) attaching or created subsequent to Date of Policy…" In such instances, in order to avoid a gap in coverage posed by a claim by a competing lien holder or creditor that the mortgagee's additional advance is subordinate to the lien of the competing lien holder, the mortgagee may be advised to seek an assurance from the title insurer that the borrower remains the property's owner, and that no intervening mortgages or liens have been created. To effectuate such coverage, the insured should request an endorsement to the loan policy that advances the Policy Date and reveals all intervening matters, and at such time as the insured mortgage is satisfied

with the status of title, a second endorsement that includes as a part of the insured mortgage the mortgage modification agreement or amendment, against advances the Policy Date, and increases the Policy Amount to identify the current indebtedness secured by the mortgage. The title insurer is likely to require, as a condition of issuing the endorsement to the existing policy, an opportunity to search and examine the title for intervening liens, and assuming it has satisfied itself that none exist, that the mortgagee record the executed, duly authorized mortgage modification or amendment displaying the total indebtedness as a condition of issuing its endorsement.

6. Other estates or interests

A *remainder* is an interest to take effect at the termination of a preceding interest created the same time or without the intervention of such a preceding interest. Remainders are classified as one of the 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, in one state, a quit claim 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). In many states, the distinction observed in some jurisdictions between vested remainders, which are alienable, and contingent remainders, which are not, is of no significance to conveyances: A deed executed by the holder of the remainder will effectuate a conveyance of the remainder regardless of whether the remainder is vested or contingent. Meyer v. Reif, 217 Wis. 11, 258 N.W. 391 (1935); In re North's Estate, 242 Wis. 72, 7 N.W.2d 705 (1942).

At common law, a deed to the grantee and a remainder to the grantee's heirs was transformed by the Rule in Shelley's Case, into a fee simple absolute in the named grantee; nothing was transferred to the grantee's heirs. However, many states have specifically abolished the Rule in Shelley's Case. See e.g. §700.10, Wis. Stats.

A *life estate* is an estate which 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. Moynihan, supra. §10 at 48. The life estate is classified as an interest which may be created for the duration of a life or lives of one or more human beings (Exhibit 6). Though the property owner may be granted a zoning variance for the right to possess a pet animal on the premises for its natural lifetime, a right that shall run with the land (Exhibit 7), life estates do not vest in non-humans. The creation of a life estate results in vested rights in two parties, the life tenant and the remainderman. Life estates may be created by grants of deed wherein the life tenant and the remainderman are grantees. Life estates are usually created when an existing owner, the holder of a fee simple estate, executes a deed to another, often a younger family member, and reserves a life estate. The deed should be drafted so that the life estate is clearly displayed, or the remainderman's prospective lender may not realize there exists a life estate and fail to have the life tenant join in the execution of its mortgage. The life

estate is freely alienable and may be mortgaged. 2 Thompson on Real Property, supra. §19.05, at 542. However, a mortgage executed by the life tenant but not the remainderman cannot bind the remainderman. A life estate does not terminate when the life tenant ceases occupying the property, and may be conveyed or the property leased by the life tenant during her life. Wagner v. Wagner, 80 Wis.2d 299, 259 N.W.2d 60 (1977).

Of course, not all estates or interests are those that date to the common law. Timeshares are popular in recreational areas, and timeshare estates are codified in many states as a right to occupy a unit designated for separate occupancy and use during at least separate periods over a period of years, together with a fee simple absolute interest or interest for years. Some but not all timeshares constitute interests in real property under the laws of the state where located. Certain timeshares consist of contractual rights only and do not give rise to an interest in real property under the laws of the state, contract rights that are, notwithstanding recordation in the public land records, subject to being rejected in bankruptcy. See, e.g. Allison v. Ticor Title Ins. Co., 907 F.2d 645 (7th Cir. 1990). Only if the timeshare interest meets the requisite statutory criteria is the title to the timeshare transferable by conveyance or capable of being mortgaged. If in fact the timeshare constitutes real property under the laws of the state, it is likely that title insurance will be available to the purchaser, though the scope of coverage will vary depending upon the terms and conditions of the applicable timeshare instruments. For example, knowing the widespread practice of hotel guest holdovers, the title insurer is unlikely to insure that the insured timeshare owner will enjoy or realize, as a part of its insured interest under the policy, a right to commence occupation of a unit at the very moment of vesting. Many timeshares provide an assurance that the timeshare owner enjoys a right to a season, subject to making timely reservations, yet it is not necessarily the case that the title insurance policy will specifically insure the right of the owner to enforce its claim to an oversubscribed season, over which a dispute might easily ensue.

7. On the periphery: Personal property, licenses, airspace, water

Not all tangible property located on the premises or at the site of land, and the buildings and improvements thereon, will necessarily transfer by virtue of a conveyance duly signed and delivered by the grantor that is recorded in the public land records. Thus, a deed conveying land occupied by a car dealership will not effectuate a transfer of the title to motor vehicles on the premises. The purchaser must assure itself that the operative laws pertaining to the titles of vehicles, manufactured homes, furniture, equipment and other personal property at the site, if a part of the transaction provide by the purchase agreement, will be reviewed and appropriate bills of sale and other transfer documents duly prepared.

Although most structural improvements constitute a part of the land on which they were constructed, and title thereto passes with the conveyance, not all buildings or improvements, such as equipment, located within or attached to buildings constitute a part of the real estate. Occasionally, leases, severance agreements and non-fixture

filings are revealed that require attention to the classification and ownership of improvements on the premises. States have adopted differing tests on the question whether an improvement affixed to the real estate constitutes a part of the land, and appropriate statute and case law, particularly in commercial transactions, must be carefully reviewed. If under applicable state law, the improvements are trade fixtures, the improvements are the property of a lessee, and are subject to the terms and conditions of the lease, including the right of the lessee to remove the improvements upon termination of the lease. Similarly, in the event that the improvements constitute equipment, or property that was severed from the land of which the prospective purchase has knowledge, the titling of the improvements may be subject to Revised Article 9, such that a bill of sale rather than a deed may be a prerequisite title document, and a financing statement rather than a mortgage may be a prerequisite to secure the lender's interest.

Acquisitions and financings of property interests that are in fact subject to Revised Article 9 necessitate a parallel search of the appropriate filing office, so that the existence of all security interests can be timely ascertained and any filings terminated. Certain types of improvements, judging from transfer and financing documentation, tend to possess a chameleonic character, so that they constitute personal property in some settings but real property in others. Transactions that involve manufactured housing, including mobile homes, require a review of laws applicable to the titling of manufactured housing units, and a transfer or surrender of the certificate of title for the unit may prove necessary. Though the property description of conveyances usually suggests that the boundaries of the land are two-dimensional or horizontal, when the title to improvements or structures located on the land requires, due to questions of their inclusion, clarification, the purchaser may be well served to insist that the conveyance include an a detailed description of the improvements the purchase agreement characterized as a part of the real estate.

Is title insurance available to insure security interests filed under Revised Article 9? Title insurance policies occasionally contain exceptions for financing statements that were filed in the public land records for the land described in Schedule A. Generally, however, title insurance is not available to insure the enforceability of non-fixture filings, financing statements, under Revised Article 9. There is a fundamental distinction between policies that insure and policies that except fixture filings, and the reader must take precautions to avoid confusing the two. Instances of policies that alluded to, or alternatively omitted, non-fixture filing financing statements have resulted in contentious coverage disputes. See, e.g. In re: Biloxi Casino Belle, Inc., 368 F.3d 491 (5th Cir. 2004). (A rider attached to Schedule A of a loan policy of title insurance included references to several UCC-1 financing statements.) In an important development, beginning in 1999, title insurers began to issue UCC insurance that provides coverage to secured parties having security interests under Article 9. For example, a UCC 9 loan insurance policy from one title insurer insures against loss or damage sustained or incurred by reason of "the failure of the Insured Security Interest to Attach to any portion of the Collateral for any reason." Such

coverage is available in most jurisdictions, though actual distribution does not approach that of loan policies that insure mortgages and deeds of trust.

The creation and transfer of airspace is important in urban areas where sky walks are important for development (Exhibit 8). The transfer of airspace over street requires an analysis of both the instrument granting the right and the operative enabling authority accorded to the highway authority or municipality granting such right.

Rights in submerged land, waters and airspace over waters have been the subject of conveyances. For example, "dockominiums" are a form of condominium ownership in which boat slips constitute the unit. Generally, state law does not expressly prohibit by the recordation of condominium declaration and conveyance of units, the adaptation of marinas, boat slips and piers, though the unit consists of waters of and airspace over navigable waters. Thus, the use of a marina as a dockominium form of ownership was found to be the highest and best use of the property for the purpose of determining the value of the secured claim under Section 553 of the Bankruptcy Code in the dockominium proprietor's Chapter 11 bankruptcy proceeding. In re: Newfound Lake Marina, Ch. 11 Case No. 04-12192, 2008 BNH 5; 2008 Bankr. LEXIS 1507 (Bankr. N. H. May 12, 2008). It has been claimed that the dockominium concept, however, represents a confrontation between a private claim in boat slip space and public interests in the water. Mark Cheung, Dockominiums: An Expansion of Riparian Rights that Violates the Public Trust Doctrine, 16 B.C. Envtl. Aff. L. Rev. 821, 825 (Summer 1989). Thus, the recordation of a declaration of condominium and subsequent conveyance of a small lock box that the declaration designated to be the unit together with the right to use a boat slip as a limited common element appurtenant thereto, though not a violation of the Public Trust Doctrine, nonetheless violated a statutory prohibition on transfers of riparian rights by easement. ABKA Ltd. v. Dep't of Natural Res., 2002 WI 106; 255 Wis. 2d 486, 648 N.W.2d 854 (2002). Floating docks and finger piers acquired by the taxpayer as a dockominium were real property, not personal property, and thus were properly assessed for real estate taxes. Taylor v. Township of Lower, 13 N.J. Tax 371 (1993). The extent to which title insurance is available to insure the rights of purchasers of riparian land is state and site specific, and requires a detailed review of the facts and circumstances of the case.

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