

TITLE ISSUES

WHO IS "INSURED" UNDER A TITLE INSURANCE POLICY?

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Unlike most kinds of insurance (casualty policies, such as fire and automobile liability insurance or life insurance) title insurance policies remain in force without the payment of annual or more frequent premiums. A single title insurance premium is paid when the policy is purchased. For an owner's policy this usually means the insurance is obtained and paid for when title to the land insured is purchased. For loan policies it means the insurance is purchased when a loan secured by a mortgage or trust deed is closed. The policies remain in full force and effect so long as the insured retains an interest in the land insured. This article will focus on who is the insured in a title insurance policy.

Whom do title insurance policies insure? Do they insure parties other than the "insured" named in Schedule A?

LOAN POLICIES

Let us first consider ALTA (American Land Title Association) Loan Policies. A loan policy insures the mortgagee named in Schedule A. The named insured usually is the mortgage lender. If a trust deed is used as the security instrument, however, only the trustee is listed as an insured. Sometimes at the request of a customer, the title insurer will add to Schedule A the name of a lender (a noteholder or assignee) as an additional insured with the words "as its interest may appear." The customer may also request the title insurer to add to the named insured the phrase "and its successors and/or assigns." Both of these additions are not really necessary. The "insured" as defined in the Conditions and Stipulations of loan policies, is "the owner of the indebtedness secured by the insured mortgage and each successor in ownership."¹ The title insurer reserves against successor insureds all rights and defenses it may have against predecessor insureds.² Some specialized interests are also covered in the Conditions and Stipulations of the policy.³

When the indebtedness secured by a mortgage is sold to another party, such sale is evidenced by an assignment of

the mortgage and a transfer of ownership of the note(s) securing the indebtedness. When the assignment is included as an insured item in Schedule A of a loan policy, and the assignee is the insured in Schedule A of the policy, the validity and enforceability of the assignment is insured. An assignment of the insured mortgage should be placed of record and if insurance of the validity of the assignment is desired, a date down of the loan policy should be ordered covering the recording of the assignment. An endorsement to a policy insuring the assignee will be issued which not only brings the policy to a date covering the recording of the assignment but changes the name of the insured from the original mortgagee to the assignee. In addition the endorsement will add to Schedule A the recorded assignment of mortgage as an insured item and will also add to Schedule B any and all items affecting the priority and enforceability of the mortgage first appearing in the public record since the date of the original title insurance policy. As noted above, if no insurance of the validity and enforceability of the assignment is desired and no search of the record to the date of the assignment is desired, the terms of the policy include any assignee as an insured; but of course, the policy only covers its date of issuance. If a trust deed is used as the security instrument, there will be no change in the trustee, only of the ownership of the notes. The new noteholder may, of course, request that the original loan policy be dated down to cover the date of the assignment. With a trust deed, however, the title insurer will not insure the validity of the assignment of the note and there is no need to assign the trust deed to a new trustee. The title policy insuring the trustee remains valid, insuring title as of the date of its issuance.

OWNER'S POLICIES

As to ALTA Owner's Policies, the named insured is the party listed in Schedule A. This party is the titleholder at the date of the policy. In the Conditions and Stipulations of the policy "insured" is defined as:

the insured named in Schedule A, and subject to any rights or defenses the Company would have had against the named insured, those who succeed to the interest of the named insured by operation of law as distinguished from purchase,

including, but not limited to, heirs, distributees, devisees, survivors, personal representatives, next of kin, or corporate or fiduciary successors.⁴

This definition does not include, for instance, a person's new spouse with whom one chooses to share ownership and to whom the insured conveys an interest in the land. Neither does it include a trustee to whom the insured named in Schedule A deeds the land or the reverse situation in which a trustee named in Schedule A deeds the land to the beneficiary of the trust. Such conveyances given for no consideration (often done as gifts or for estate planning purposes) will usually be at least in part to parties not included within the definition of "insured" under the title insurance policy. The new titleholder will not be insured under the outstanding title insurance policy.

One may wish to take comfort under provisions of the Conditions and Stipulations of an ALTA Owner's Policy, Paragraph 2, entitled "Continuation of Insurance After Conveyance of Title." This paragraph extends coverage to the insured named in Schedule A (and the successors as defined by "insured") if the insured retains some estate in the land: for example, the one-half interest retained by the person adding a spouse to the title originally held solely by that person at the time the title insurance policy was obtained, or for example, one who holds a security interest in the land (purchase money mortgage or contract vendor's lien), or for example, if liability remains in the insured by reason of covenants of warranty made by the insured when conveying the insured land that the land is free of a recorded covenant when such covenant was not shown as an exception in the policy. The wish to retain coverage by means of this paragraph may be somewhat illusory in the context of a conveyance made for no consideration. It will provide coverage for the percentage of interest retained and not conveyed (e.g. the one-half interest retained when adding a spouse to title originally held solely in one name). But if one warrants title to other family members, for such family members to be included in title coverage, such family members would have to allege damage by virtue of the warranty and be willing to sue the grantor! Also, one has to consider all the terms of the policy as a whole. Coverage might be excluded by other terms of the policy such as the Exclusions from Coverage. Actual knowledge of the original insured party would for instance, make it possible for the Company to deny this new person coverage against any item known to the original insured under the Exclusions from Coverage.

CONTINUATION OF INSURANCE AFTER CONVEYANCE OF TITLE

An insured will find that title insurance coverage may continue even after title has been conveyed. Section 2 of the ALTA Owner's Policy⁵ provides coverage in certain circumstances even after the insured (hereinafter termed

insured seller) has conveyed title to another. First, if the insured seller holds indebtedness secured by a purchase money mortgage, the insurance will continue so long as the insured seller retains ownership of the indebtedness and the mortgage has not been released. Coverage does not continue in favor of anyone to whom the indebtedness is assigned. If an insured seller in reliance on the title policy warrants title free of a recorded interest or covenant or restriction which should have been shown as an exception in Schedule B of the policy but was not, and claim is made against the insured seller on the basis of the warranty, coverage of the insured seller continues under the terms of the policy. Contrast these remarks, however, with those dealing with the same section of the Conditions and Stipulations where the conveyance made by the insured was without consideration.

ASSIGNMENTS OF POLICY AND ENDORSEMENTS CHANGING THE NAME OF THE INSURED

To be sure one has continuing coverage as of the date of the policy, the safe and sure course of action is to obtain an Assignment of Policy from the title insurer. This amendment to the title insurance policy does not date the policy down to a current date or in any way insure the validity and enforceability of conveyances since the date of the policy (the deed one has recorded to add a spouse, the deed to one's children, to a trust etc.). The amendment does add these new parties as additional named insureds as their interests may appear. It will bring these parties within the definition of "insured" under the policy and enable them or their successors as defined by the term "insured" to be able to bring claims under the policy should this be necessary. Title insurers will provide such coverage at relatively nominal premiums as long as the parties being added are given their interest without consideration. To do this, the title insurer need not check the record, but may rely solely on the information furnished by the customer. A copy of an Assignment of Policy form is attached hereto as Exhibit A-1. Another way of obtaining the same coverage is by endorsement to the policy changing the name of the insured, but not changing the date of the policy. A copy of such an endorsement is attached hereto as Exhibit A-2.

Title insurers will not issue the Assignment of Policy or Change in Name of Insured Endorsement if the change in the name of the insured has come about because of a sale of the interest for consideration. Rather, the title insurer will insist that a new policy bringing coverage to a current date at regular premiums be purchased. The insurer will then examine the record from the former policy date to the current date, issuing a new policy covering that date and any instruments recorded between the date of the original policy and the new date.

PARTNERSHIPS AND LIMITED LIABILITY COMPANIES

Some years ago, a title insurer denied coverage under an owner's policy by reason of the fact that the partners constituting the insured partnership had changed. The title insurer successfully claimed that the partnership insured under the policy no longer existed and that the partnership consisting of the new partners was not the insured under the terms of its policy.⁶ A similar problem might exist if the members of a limited liability company changed. In many States it is clear that if the partners under a partnership change or change their percentage of ownership, the partnership dissolves and a new partnership is formed. In such cases, a deed conveying title from the old to the new partnership should be placed of record. In other States, or by the terms of a particular partnership agreement, it may be clear that despite a change in either who constitutes the partners or by what percentage they hold their interests, no new partnership is formed and no conveyance is required. Similar issues may arise under a limited liability company form of ownership. If a new partnership is formed, it is not included in the definition of "insured" in a title policy. An endorsement overcoming such problems has been created. It commonly is called a Fairway Endorsement after the case noted at the beginning of this section. Title

insurers, however, are only willing to issue such an endorsement in cases in which the change in interests underlying the insured partnership or limited liability company come about either without consideration or in a very limited period of time from the date of the original policy. If the change is coming about because a partner or member is selling an interest for consideration, the title insurer will insist on charging a premium commensurate with the amount of this sale and dating its policy down to cover the date of such sale. If, on the other hand, the change is without consideration or happens within the limited time designated in the endorsement, an endorsement insuring who is "insured" can be issued for an additional premium. Copies of various Fairway Endorsements are attached hereto as Exhibit B-1 and B-2 illustrating these concepts.

CONCLUSION

When conveyancing is being done without consideration for estate planning or other purposes, to be sure the new owner is included as an "insured" under a title insurance policy, the wisest course of action is to purchase an Assignment of Policy or an endorsement naming the new title holder as an insured.

NOTES

¹ Sections 1 (a) (i) and 12 (c) of the Conditions and Stipulations of the ALTA Loan Policy (10-17-92). These sections limit the definition of insured to exclude one who only holds the indebtedness for security for an indemnity, guarantee or similar interest. The insured must be an owner of the indebtedness, not merely a collateral assignee who may or may not become the owner of the indebtedness. In collateral assignment situations, ownership of the indebtedness is dependent upon whether another event does or does not occur: usually whether the assignor performs or fails to perform the obligation for which the collateral assignment was taken.

² *Ibid.* Section 1 (a). This section of the Conditions and Stipulations of the Policy makes plain that any successor insured takes no better title or has no better claim against the title insurer than its assignor. Therefore the title insurer reserves against the successor insured any and all defenses it may have had against the original or any other prior insured. Therefore if the original insured obtained its interest by fraud, the title insurer is able to assert fraud as a defense even against the unwary, unknowing successor insured who may have relied on the additional insured language of the policy. It should be noted that, although an assignee of the indebtedness is included, unless the assignment is included in the items described in Schedule A, the validity and enforceability of such assignment is not insured. In contrast, an assignee specifically named as an insured in Schedule A will take free of defenses the Company has against prior insureds because the policy was dated down to cover the recorded assignment to this named assignee. The title policy insures the bona fide nature of an assignment listed in Schedule A unless specific exception is taken in Schedule B of the

policy.

³ *Ibid.* Section 1 (a) (ii). The definition of "insured" on a Loan Policy includes governmental agencies or instrumentalities which insure or guarantee the indebtedness, such as HUD (The Department of Housing and Urban Development), FHA (Federal Housing Administration) or FNMA (Federal National Mortgage Association). If such agency has become the owner of the insured mortgage because such agency has paid a claim to the mortgagee or its assignee.

⁴ Section 1 (a), Conditions and Stipulations, ALTA Owner's Policy (10-17-92).

⁵ Section 2, Conditions and Stipulations, ALTA Owner's Policy (10-17-92) entitled CONTINUATION OF INSURANCE AFTER CONVEYANCE OF TITLE reads:

The coverage of this policy shall continue in force as of Date of Policy in favor of an insured only so long as the insured retains an estate or interest in the land or holds an indebtedness secured by a purchase money mortgage given by a purchaser from the insured, or only so long as the insured shall have liability by reason of covenants of warranty made by the insured in any transfer or conveyance of the estate or interest. This policy shall not continue in force in favor of any purchaser from the insured of either (i) an estate or interest in the land, or (ii) an indebtedness secured by a purchase money mortgage given to the insured.

⁶ *Fairway Dev. Co. v. Title Ins. of Minn.*, 621F. Supp 120 (N. D. Ohio 1985)

OWNERS

LOAN

ENDORSEMENT

ATTACHED TO AND FORMING A PART OF
POLICY NUMBER

ISSUED BY

CHICAGO TITLE INSURANCE COMPANY

CHANGE OF INSURED OWNER ENDORSEMENT

SCHEDULE A OF THE ABOVE POLICY IS HEREBY AMENDED BY DELETING THEREFROM THE NAME OF THE INSURED RECITED THEREIN, AND SUBSTITUTING THEREFOR THE FOLLOWING:

NOTWITHSTANDING THE ABOVE, NOTHING CONTAINED HEREIN SHOULD BE CONSTRUED AS EXTENDING THE EFFECTIVE DATE OF SAID POLICY, AND NO LIABILITY IS ASSUMED FOR DEFECTS OR ENCUMBRANCES ATTACHING OR CREATED SUBSEQUENT TO THE DATE OF POLICY. THE RIGHTS OF THE ASSIGNEE UNDER SAID POLICY SHALL BE SUBJECT TO THE DEFENSES, IF ANY, WHICH THIS COMPANY MIGHT HAVE AGAINST THE ORIGINAL INSURED. NO LIABILITY IS ASSUMED FOR LOSS OR DAMAGE RESULTING FROM ANY FAILURE TO RECORD OR FILE THE INSTRUMENT OR INSTRUMENTS NECESSARY TO EVIDENCE OF RECORD THE ASSIGNEE'S ESTATE OR INTEREST IN THE LAND.

THIS ENDORSEMENT IS MADE A PART OF THE POLICY AND IS SUBJECT TO ALL OF THE TERMS AND PROVISIONS THEREOF AND OF ANY PRIOR ENDORSEMENTS THERETO. EXCEPT TO THE EXTENT EXPRESSLY STATED, IT NEITHER MODIFIES ANY OF THE TERMS AND PROVISIONS OF THE POLICY AND ANY PRIOR ENDORSEMENTS, NOR DOES IT EXTEND THE EFFECTIVE DATE OF THE POLICY AND ANY PRIOR ENDORSEMENTS, NOR DOES IT INCREASE THE FACE AMOUNT THEREOF.

CHICAGO TITLE INSURANCE COMPANY

BY _____
AUTHORIZED SIGNATORY

NOTE: THIS ENDORSEMENT SHALL NOT BE VALID OR BINDING UNTIL COUNTERSIGNED BY AN AUTHORIZED SIGNATORY.

CHICAGO TITLE INSURANCE COMPANY
ASSIGNMENT OF POLICY

FOR VALUE RECEIVED, _____
_____ (Assignor)

hereby assigns and transfers to _____
_____ (Assignee),

the benefits of its policy number _____ issued by Chicago Title Insurance Company insuring
title in the Assignor, all subject to and in accordance with the terms, provisions and conditions of said
policy; this assignment, however, to become effective only upon the consent of CHICAGO TITLE
INSURANCE COMPANY, acting by its proper officer.

Dated _____

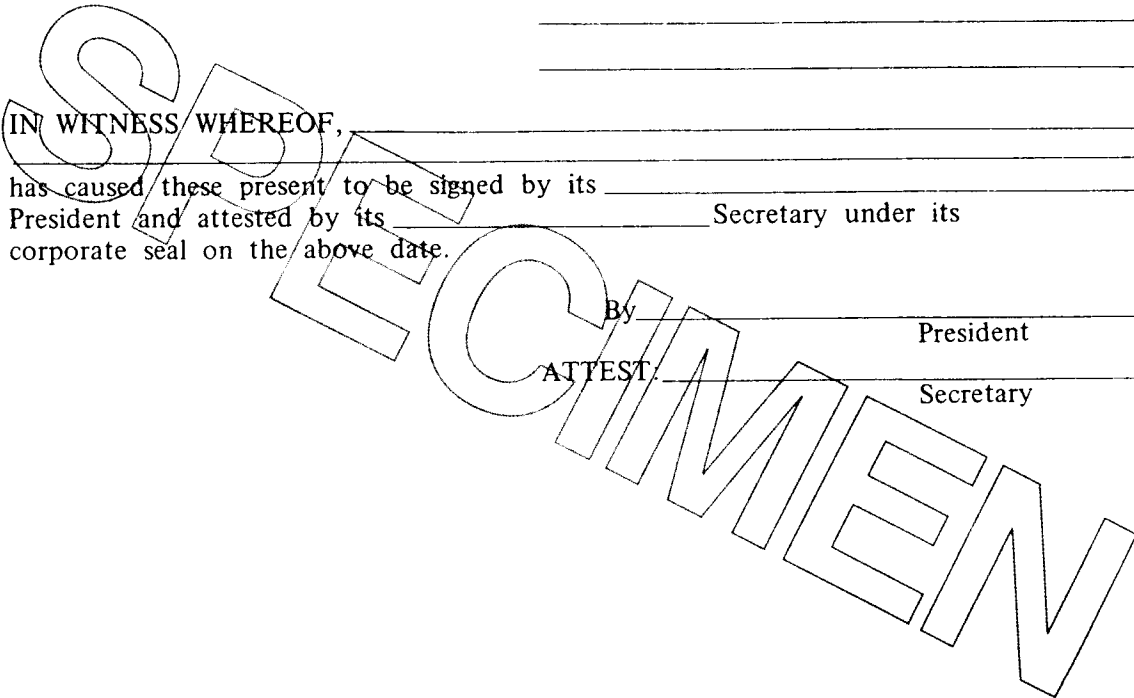
INDIVIDUALS

_____ (SEAL)

CORPORATIONS

IN WITNESS WHEREOF, _____
_____ has caused these present to be signed by its _____
President and attested by its _____ Secretary under its
corporate seal on the above date.

By _____ President
ATTEST _____ Secretary



CHICAGO TITLE INSURANCE COMPANY hereby consents to the foregoing assignment, subject to the following:

1. Nothing herein contained shall be construed as extending the effective date of said policies, and no liability is assumed for defects or encumbrances attaching or created subsequent to the date of the policies.
2. The rights of the Assignee under said policies shall be subject to defenses, if any, which this company might have against the original insured.
3. No liability is assumed for loss or damage resulting from any failure to record the instrument or instruments necessary to evidence of record the Assignee's estate or interest in the land described in Schedule A of the policies.

Dated this _____ day of _____, 19____.

CHICAGO TITLE INSURANCE COMPANY

Owners
Loan

EXHIBIT B-2

ENDORSEMENT

ATTACHED TO AND FORMING A PART OF
POLICY NUMBER

ISSUED BY

CHICAGO TITLE INSURANCE COMPANY

FAIRWAY ENDORSEMENT

The Company hereby agrees that the insurance provided is for the benefit of and is enforceable by _____ (the LLC/Partnership). The Company further agrees that it will not interpose as a defense to a claim of coverage under this Policy (a) that any transfer, direct or indirect, of all or any part of the membership [partnership] interests in the LLC/Partnership to any transferee without consideration after the Effective Date of this policy constitutes a dissolution or termination of the LLC/Partnership or (b) that any such transfer creates a new LLC/Partnership or any other entity.

This endorsement is made a part of the commitment or policy. It is subject to all the terms of the commitment or policy and prior endorsements. Except as expressly stated on this endorsement, the terms, dates and amount of the commitment or policy and prior endorsements are not changed.

CHICAGO TITLE INSURANCE COMPANY

BY _____

NOTE: THIS ENDORSEMENT SHALL NOT BE VALID
OR BINDING UNTIL COUNTERSIGNED BY AN
AUTHORIZED SIGNATORY.

Owners
Loan

EXHIBIT B-1

ENDORSEMENT

ATTACHED TO AND FORMING A PART OF
POLICY NUMBER

ISSUED BY

CHICAGO TITLE INSURANCE COMPANY

PERMITTED PARTNERSHIP TRANSFER ENDORSEMENT (FAIRWAY)

The Company agrees that it will not interpose as a defense to a claim of coverage under this Policy the fact that within a period of two years from [date of policy], a dissolution of the insured partnership has occurred, or a new partnership has been formed solely by reason of the withdrawal or replacement of one or more of the partners of the original insured partnership so long as the insured remains as the titleholder, and no new partnership is explicitly formed. The Company reserves all of its rights and defenses under the policy which it would have had against the insured or its constituent partners before or after any withdrawal or replacement.

This endorsement is made a part of the commitment or policy. It is subject to all the terms of the commitment or policy and prior endorsements. Except as expressly stated on this endorsement, the terms, dates and amount of the commitment or policy and prior endorsements are not changed.

CHICAGO TITLE INSURANCE COMPANY

BY _____

NOTE: THIS ENDORSEMENT SHALL NOT BE VALID
OR BINDING UNTIL COUNTERSIGNED BY AN
AUTHORIZED SIGNATORY.