

# **LEASEHOLD TITLE INSURANCE WORTH A LOOK**

## **New Endorsement Increases Amount, Scope of Coverage**

By Harris Ominsky

Parties involved in real estate transactions frequently use title insurance to insure their interests as buyers or lenders. Although tenants may have even more significant interests to protect, many of them do not protect themselves with title insurance. For example, did you buy title insurance when you entered into your office lease?

### **OLD COVERAGE**

One reason you might not have was that leasehold policies did not provide very good coverage. That has changed, and, as of October 13<sup>th</sup>, a new leasehold endorsement has been made available by the American Land Title Association.

The ALTA developed this new endorsement with the assistance of a committee of the American College of Real Estate Lawyers. Before this new coverage, title companies would insure tenants by providing them either a separate leasehold title policy, or a leasehold endorsement attached to a standard fee owner's policy. For various reasons, neither method was satisfactory. Both the scope and the amount of coverage were too limited.

A new endorsement now broadens the events for recovery to an eviction, which includes the "lawful prevention of the use of the land or the tenant leasehold improvements for the purposes permitted by lease." Therefore, if the tenant is prevented from using a property because of an insured title matter, the tenant will be covered under the policy. This, of course, assumes that the title problem has not been listed in the title policy's exceptions to coverage.

The new endorsement also clarifies the definition of the insured "lease term," which includes not only the basic term, but also any renewals or extended terms if a valid option for those extensions is included in the lease.

## **AMOUNTS COVERED**

The most important change in the coverage to the remedies provided, and, in particular, the method of compensating the insured for the loss of its tenant leasehold improvements. Paragraph 3 of the leasehold endorsement provides the following:

“If, in computing loss or damage, it becomes necessary to value the estate or interest of the insured as a result of a covered matter that results in an eviction, then that value shall consist of the value for the remaining lease term of the leasehold estate and any tenant leasehold improvements existing on the date of the eviction.

The insured claimant shall have the right to have the leasehold estate and tenant leasehold improvements valued either as a whole, or separately. In either event, this determination of value shall take into account rent no longer required to be paid for the remaining lease term.”

This means that the insured’s remedies include two components.

First, the insured may collect the value of the remaining lease term of the leasehold estate. That is not a change from the earlier coverage that permitted recovery for the value of a lease at below-market rent. The tenant may determine loss by calculating the difference between comparable rentals and the “rent no longer required to be paid” on a terminated lease.

The second component, which includes the value of any tenant leasehold improvements, is new and significantly broadens the coverage. It is noteworthy that the endorsement doesn’t provide any method for valuing tenant leasehold improvements. Although the drafters of the endorsement discussed whether the policy should value those improvements on the basis of a useful life/straight-line depreciation method, or by some other method, they decided to leave that issue open.

## **INCIDENTL ITEMS**

The tenant may also recover incidental damages, including the following:

- Reasonable costs of relocating any personal property that the insured has the right to remove, together with the cost of transporting that property for 100 miles, and the reasonable cost of repairing it.
- Rent or damages that the insured might be obligated to pay to any other person who has paramount title to the landlord's lease.
- The fair market value of any lease or sublease that the insured had in place at the time of the eviction. For example, if the insured has subleased the premises and was evicted, the insured could recover the benefit of the value of that sublease. In addition, the insured could collect amounts it was obligated to pay to lessees or subleases, who are evicted as a result of the insured's eviction.
- Reasonable costs in securing a replacement lease, which should include brokerage commissions, costs to obtain zoning and other approvals, architectural and engineering fees, attorney fees and other consulting fees incurred.

### **ADVICE: USE IT**

Tenants and their lawyers should consider using the new leasehold endorsement, particularly for leases for which a tenant will spend a significant amount on improvements. In addition, when a lender is making a loan on those improvements, it should consider some type of coverage it would typically require for other types of real estate loans.

In using this coverage, tenants and their counsel should continue to focus on the same issues as they would in obtaining coverage for fee simple title. They should review all the customary title exceptions to determine how they might affect the tenant's proposed use and negotiate the appropriate endorsements.

This is only a short summary of a new type of coverage that has broad implications and significant limitations. Since this coverage includes several novel concepts, the actual endorsement should be carefully analyzed before it is used in a particular deal. In any event, it is a step forward in title coverage and should be viewed as a valuable tool for tenants and lenders.

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**NB Editors Note:** Mr. Ominsky has asked that I include a statement in this repost that the new Leasehold Endorsements are not (at the time of posting 2/14/02) currently available in Pennsylvania. The Minutes of the meeting of The Title Insurance Rating Bureau of Pennsylvania [TIRBOP] Forms Committee reflect “the Committee unanimously agreed to recommend the adoption of the (leasehold) form Endorsement, but noted that some minor changes to the forms will be necessary to make them consistent with already approved endorsements of the Bureau.” The Forms Committee referred the leasehold form Endorsements to the Rate Committee for a review of rate implications.