

**POLICY LECTURE OUTLINE**

- I. History of 1992 Policy.
  
- II. Six Elements of a Title Insurance Policy.
  - (a) Insuring Clauses: Contain the contractual provisions which obligate the Company for damage sustained by the insured which arise from matters listed in these clauses.
  
  - (b) Exclusions: List matters which may be included within the broad language of the insuring clauses but for which the Company does not assume liability.
  
  - (c) Conditions & Stipulations: List matters which are interpretive of the other Policy provisions; states how a claim should be made under the Policy and define the extent of the Company's obligation in connection with the claim.
  
  - (d) Schedule A: Identifies the following
    - (i) the insured
  
    - (ii) the estate or interest in the land being insured
  
    - (iii) the owner
  
    - (iv) the land
  
    - (v) the amount of insurance
  
    - (vi) effective date of the Policy
  
    - (vii) the mortgage being insured (Loan Policies)
  
  - (e) Schedule B: List matters which are within the insuring clauses, but for which the Company does NOT assume liability and which are not listed in the exclusions from coverage.
  
  - (f) Endorsement: is attached to the Policy which extends or alters its coverage or interprets its provisions.
  
- III. Explanation of "EXCLUSIONS FROM COVERAGE" -- 1992 Forms
  
- IV. Explanation of CONDITIONS AND STIPULATIONS

## **HISTORY**

The ALTA 1992 policies were developed in response to objections of certain lenders to the broad wording of the "Creditors Rights" exclusion found in the ALTA 1990 policy. (FannieMae Announcement 94-13). They expressed concern that a literal reading of the exclusion could exculpate (to free from blame) the Title Company from liability where (for example) a mortgage was not timely recorded (and thus was deemed "unperfected" under the Bankruptcy Code), even though the delay was caused by the title insurer.

## THE TITLE INSURANCE POLICY

### GENERAL

Despite the fact that there are a great number of title insurance forms currently in use throughout the country, there are only two principal types of title insurance policies used on the east coast. The first of these is the ALTA Loan Policy, which insures the validity, enforceability and priority of a mortgage or deed of trust (or assignment) of an interest or estate in real property given by the parties at the time of its making as security for the payment of a debt or the performance of some other obligation. The second is the Owner's Policy, which insures the ownership of a particular interest or estate in real property. The preprinted language set forth on the policies facing page, the exclusions and the conditions and stipulations, constitute the "boilerplate" of **standard coverage**. Modification of either type of policy for particular circumstances represents **extended coverage** and can be readily accomplished by endorsement; the available and permitted printed policy and endorsement forms allow the flexibility necessary to permit title insurance to be issued on any number of different interests in real property, subject to compliance with the title insurer's underwriting requirements.

Each form of policy affords the insured some protection against risk of loss or damage to the insured from a variety of title defects. This chapter will undertake to explain the loan policy in more detail. An explanation of the Owner's Policy will follow.

### NATURE OF INSURANCE

A policy of title insurance is the written opinion of the issuing company as to the validity of the title, backed by an agreement to make that opinion good in case it should prove to be mistaken and as a result thereof the insured should suffer a loss. A title insurance policy is a contract of indemnity [C&S 7 & 13, Excl. 3 (c)] whereby the insurer, for a valuable consideration, agrees to indemnify the insured in a specific amount against loss sustained by reason of defects of title wherein the latter has an insured interest. In return for the premium paid, the insured, in relying on the contract, is assured that the policy is backed by the full faith and integrity of the Company and substantial assets from which losses could be paid.

### BRIEF DESCRIPTION OF ALTA LOAN POLICY

The ALTA Loan Policy is issued for the benefit of the lender only, and can be issued when the insured loan encumbers the fee, an easement or leasehold other than an oil leasehold.



## **BACKGROUND**

A mortgage is the security for the debt and the note is the evidence of the debt. When a mortgage is granted, the property owner pledges title to the real estate as security until the debt is repaid. Prior to the execution of the mortgage the borrower signs a personal promissory note for which he is personally liable to the lender. For repayment of the debt. In the event the borrower defaults in the repayment of his obligations, the lender will initiate foreclosure proceedings in order to recover the debt. Naturally, the lender wants assurance that its mortgage lien is a valid and enforceable lien on the land. He also wants assurance that he is the first creditor to partake of the proceeds from the foreclosure sale. It is the trend for lenders to seek such assurance from title insurance companies and their agents rather than rely upon Attorneys Opinion of Title, as they have in the past.

## **POLICY FORMAT**

The title insurance policy is issued in a standard format promulgated by the American Land Title Association. The Policy is divided into four parts. The insuring clauses, the Exclusions from Coverage, Schedule B exceptions, and the Conditions and Stipulations. The Policy consists of a foldover cover with the exclusions, stipulation and conditions set forth on the inside of the jacket. Within the jacket are inserted the various schedules and endorsements. The statement of coverage provided by the insurer is set forth on the face page of the policy.

The starting point for any review of title insurance coverage is the insuring clauses. The other three sections of the policy serve in general to modify or limit the coverage's provided by the insuring clauses.

The preamble to the insuring clauses in both policies reads as follows:

*Subject to the Exclusions from Coverage, The Exceptions from Coverage Contained in Schedule B and the Conditions and Stipulations, Blank Title Insurance Company, herein called the Company, insures, as of Date of Policy shown in Schedule A, against loss or damage, not exceeding the Amount Of Insurance stated in Schedule A, sustained or incurred by the insured by Reason of:*

This opening statement contains two important elements. First, it states that the title company insures "as of Date of Policy . . ." Unlike other types of insurance, a title policy is locked into a specific time frame, typically the date of recording of the insured instrument. Claims may arise after the Date of Policy, but the coverage provided extends in general only to defects, liens or encumbrances which existed prior to the Date of

Policy. This provision is reinforced in Paragraph 3(d) of the Exclusions from Coverage which, excludes from coverage "Defects, liens encumbrances, adverse claims or other matters attaching to or created subsequent to Date of Policy."

NB The coverage provided for under the "expanded coverage policies" differ in this regard.

The second element of the preamble is the statement that the policy insurers "against loss or damage . . . sustained or incurred by the insured . . ." In a similar manner, Paragraph 3(c) of the Exclusions from Coverage states that coverage is not provided for "Defects, Liens, encumbrances, adverse claims or other matters *resulting in no loss of damage to the insured claimant*" (emphasis mine). Consistent with this language, the courts in most states, including Pennsylvania, have stated the title policies are contracts of indemnity [see Sattler v. Philadelphia Title Insurance Company, 192 Pa. Super 337, 162 A2d 22(1960)]. Of course, as noted below in Ex Cl. 3(c), and elsewhere (Palomar, Title Insurance Law, Ch. 6) the question of whether an insured has sustained a loss is not always clearly apparent.

## **POLICY COVERAGE**

Subject to the Exclusions, Schedule B Exceptions and Conditions and Stipulations stated elsewhere in the policy, the 1987, 1990 and 1992 versions of the *standard* ALTA Owner's Policy insure, as of the Date of the Policy, against loss or damage by reason of:

1. Title to the estate or interest described in Schedule A being vested other than as stated therein;
2. Any defect in or lien or encumbrance on the title;
3. Unmarketability of title;
4. Lack of a right of access to and from the property.

The 1987, 1990 and 1992 versions of the ALTA Loan Policy also insure against loss or damage sustained by reason of:

5. The invalidity or unenforceability of the lien of the insured mortgage upon the title;
6. The priority of any lien or encumbrance over the lien of the insured mortgage;
7. Lack of priority of the lien of the insured mortgage over any statutory lien for services, labor or material, [mechanics liens etc];

8. The invalidity or unenforceability of any assignment of the insured mortgage, provided the assignment is shown in Schedule A, or the failure of the assignment . . . to vest title to the insured mortgage in the named insured assignee free and clear of all liens.

## THE INSURING CLAUSES

The foregoing clauses are known as the policy insuring clauses [Ins. Cl.] and they are set forth on the facing page of the policy jacket. *The insuring clauses contain the contractual provisions of the policy which obligate the company for loss or damage sustained by the insured which arise from matters listed thereon.* **NB** Professor Palomar refers to these clause as **Risks transferred to the insurer**

**Title Rule 1:** Courts generally construe the insuring clause(s) in a straightforward manner and hold the insurer responsible to *indemnify the insured if title is not as vested as stated in the policy.*

**Title Rule 2:** All underwriting decisions and affirmative coverage provisions must be made in consideration of their effect upon the insuring provisions of the policy.

**For discussion purposes,** let's examine each of the insuring clauses individually. Examples will be provided. Supplementary material and case citations may be found in Gosdin, Title Insurance A Comprehensive Overview, 2<sup>nd</sup> Ed., beginning at page 50 and ***Title Insurance From Commitment to Claim***, PBI Seminar No. 2000-2476R. The reader is encouraged to review both texts and the discussion and examples set forth therein. The texts referred to in the **Introduction to Policy Claims Issues** and the **TLA Multiple Claims Index** should also be reviewed at length.

*Ins. Cl. (1): Title vested "Otherwise than as Stated" in the Policy*

**Comment:** The policy insurers against loss if the title is not vested in the described party.

For example, if title is defective because of a forgery, the policy indemnity applies. Other facts that have resulted in liability to the insurer under this clause include:

- Title insured as a joint tenancy is actually held as a tenancy in common [Elliot v. CTIC, 462 NE2d 640 (Ill.App. 1984) (insurance company liable on summary judgment to have deed reformed)];
- Title insured as a "fee simple" is a lesser estate, e.g., it is more accurately described as a *fee simple determinable* or *fee simple [or contingent fee] subject to condition subsequent*;
- A fee simple estate exists instead of the easement described in the policy. [see Black v. PNTI, 225 SE2d 689 (Ga. Ct. App. 1976) (summary judgment in favor of title insurer reversed where policy insured a single tract bisected by and easement, but the "easement" was in fact a strip of land owned in fee simple by another landowner)]. This may also apply in the case of the underlying title to railroad property.
- A governmental entity has an easement over a portion of the insured property via eminent domain [see Hahn v Alaska Title Guar. Co., 557 P2d 143 (Alaska 1976) (Congressional Record case resulting in 1987 Change in Ex. Cl 1)].

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**Discussion:** The first of the insuring clauses in the Owner's and Loan Policies transfers to the insurer the risk that title to the insured estate or interest is vested otherwise than as stated in the policy. **NB** In the Owners policy, three (3) separate clauses actually describe the insured estate:

1. One clause, *Schedule A item 2*, names the estate in the land that is insured;
2. A second clause, *C&S 1 (a), Schedule A item 1 and 3*, identifies the party in whom title to that estate in land is vested;
3. A third clause, *Schedule A item 5*, describes the property in which the insured interest is held.

In the context of the Owner's Policy, this insuring clause entitles the insured to compensation for either (i) a complete failure of title or (ii) a diminished title. For example, if Schedule A describes the title as vested in fee simple in the seller of the property, the insured purchaser has a claim if it is later determined that the seller had either no interest in the property or an interest less than fee simple. *However, any loss claimed by the insured must be caused by the title being vested otherwise than as stated, not merely by reason of a third party's interference with the insured's rights.*

In the context of the Loan Policy, insured lenders making claims will also raise the insuring clause relating to loss caused by the invalidity or unenforceability of the lien of the insured mortgage by reason of the fact that title is vested otherwise than as stated in the policy.

*Ins. Cl. (2): Any defect in or lien or encumbrance on such title*

**Annotation:**

- 18 ALR4th 1311; *Defects Affecting Marketability of Title Within Meaning Of Title Insurance Policy*;
- 87 ALR3d 764; *What Constitutes a Charge, Encumbrance or Lien within Contemplation of Title Insurance Policy*

Comment: **A defect in title is something which prevents it from being technically marketable but which does not subject it to being defeated, notwithstanding the fact that the insured received less than he bargained for. The question then becomes whether the mere discovery of the existence of a defect in title triggers a loss within the policy's coverage, or whether an insured must first experience an out-of-pocket loss before making a claim (Palomar, Title Insurance Law, Ch 6, page 6-54). Further examples of "defects" and "encumbrances" in title which are both within and beyond the scope of 9/2001 rev.**

policy coverage may be found in Gosdin, *Supra*, at pages 50-56 and Lecture 2, *The*

*Nature of the Basic Underwriting Risk.*

**Discussion:** In addition to insuring that title to the estate or interest described in Schedule A is correctly vested as stated, the title company insures against loss or damage that the insured may sustain if such title is found to be subject to a defect, lien or encumbrance not otherwise set forth in the limiting provisions of the exclusions, exceptions or conditions or stipulations. This is perhaps the most litigated insuring provision in the policy.

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The terms "defect", "lien" and "encumbrance" are not defined within the terms of the policy and courts use them loosely and interchangeably in cases relating to title insurance coverage.

For underwriting purposes I should like to suggest the following definitions be employed and considered. In general a "defect" exists in title when a third party *claims or is able to claim* an interest in the insured premises which either interferes with the insureds:

- use and/or enjoyment of the property;
- limits the quantity or quality of the insured estate;
- puts the insured in a position of peril or
- subjects the insured to the threat litigation or serious financial loss.

Defects may vary in terms of underwriting significance. Some may be the result of a minor technicality, overcome by either validating acts or title standards. Others may go directly to the question of marketability.

A "lien" is a claim or charge on property as security for the payment of a debt or the fulfillment of an obligation. They may be in rem or in personum, choate or inchoate. Examples of such liens were set forth in Lecture 1 and include any and all outstanding mortgages, D/T, Installment Sale Contracts, Judgment, Mechanics or Materialmen's Liens, Tax liens and assessments and superliens, etc. not otherwise satisfactorily disposed of, excepted or excluded in the policy.

An "encumbrance" is any right of a third party in real property that diminishes the property's value but does not prevent the passing of title. Examples include inter alia, easements, restrictions, leases, options, rights of first refusal, encroachments and/or overlaps which interfere with the use and enjoyment of the property

There are a number of case annotations on this subject. *See, inter alia, Smith, Defects Affecting Marketability of title within the meaning of Title Insurance Policy, 18 ALR4th 1311 (1982) and others cited in [titlelawannotated.com/bibliography](http://titlelawannotated.com/bibliography).*

*Ins. Cl. (3): Unmarketable Title*

**Annotation:** 31 ALR4th 11, *Construction and Effect of Marketable Record Title Statutes; See also: ALR Index 2, 3, 4 & 5, Marketable and Clear Title;*

**Other reference sources:** Gosdin, supra., page 56; Bayse, Clearing Land Titles, Chapters 2 and 22; Maupin, Marketable Title to Real Estate, 3d Ed.; Cribbet & Johnson, Principles of the Law of Property, pp 174-176 (3d ed. 1898); 3 American Law of Property, sec. 11.48 et seq. (Casner ed. 1952); Palomar, Title Insurance Law, 5-18.1; Burke, Law of Title Insurance, 3d Ed. Sec. 3.07, pp. 3-102 et seq.

**Comment:** Differences of opinion as to what exactly constitutes a marketable varies among attorneys astute in such matters and may in fact be dependent upon some personal piccadillo's and claims experience of a given practitioner. While the definition of marketable title may vary from state to state, most authorities will agree that a marketable title is a title legally free from doubt, or free from the treat of potential litigation [Smith, supra., 18 ALR4th 1311, 1313; In Pennsylvania marketable title is usually said to be title which does not expose the purchaser to the hazard of a lawsuit. see LaCourse v. Kiesle, 366 Pa. 385 (1951). Other definitions of marketable title may be found in Bayse, supra., Chapter 22, section 371. Therein the Author also suggest "the Modern Concept of Marketability" at section 374.

For a ***list of specific matters*** and points to consider which have formed the basis of litigation when determining the question of marketability see Thompson of Real Property, Thomas Ed., Chapter 93.03(a)(4) at paragraph 1, page 370.

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The concept of exactly what constitutes a "Marketable Title" is the subject of various treatise including one devoted entirely to that subject, Maupin, supra., Harold L. Reeve, the former SVP of Chicago Title and Trust Company wrote a text in 1951 entitled Guaranteeing Marketability of Titles to Real Estate, wherein he suggested there are four (4) types of title to real property:

1. Perfect Title;
2. Marketable Title;
3. Insurable Title, and
4. Uninsurable Title

Therein, he defined Perfect title as "record title without fault, defect or omission."

Marketable Title was defined as "an indefeasible title in fee simple, whether had by deed, devise or by Statutes of Limitations . . . evidence by an abstract, together with explanatory affidavits".

Insurable Title was identified as "a sound title which is subject to defects which prevent it from being technically marketable, but which is not subject to being defeated, is defensible and insurable and which in fact is covered by a title policy generally acceptable to purchasers and lenders". He emphasized that the concept of insurability is a test of much greater value and flexibility. And that is the type of title which we, as title insurers, frequently insure.

**Discussion:** While it is important to keep the concept of insurability in mind, as underwriters we must distinguish between the concept of insurability and marketability. Insurable and marketable title are not synonymous. When a title insurance policy covers unmarketability of the insured title, the insured will be indemnified for loss if it is later determined by a court of competent jurisdiction that the title is not marketable because of a defect which existed prior to the title insurance policy's effective date. And that is precisely our concern as underwriters. More to the point, almost any claim tendered under insuring clauses 1, 2, 5 and 6 is going to include a count for unmarketability. In 1987 the ALTA added to C&S 1 (g) a definition of unmarketability of title.

Paragraph 1(g) of the Conditions and Stipulations defines unmarketability of title as *"an alleged or apparent matter affecting the title to the land, not excluded or exception from coverage, which would entitle a purchaser or the estate or interest described in Schedule A to be release from the obligation to purchase by virtue of a contractual condition requiring the delivery of marketable title."*

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**NB** Take note that the policy does not insure that title is marketable. Under the Preamble it only insures the insured for loss or damage in the event it is later determined not to be marketable. There is difference. *The coverage is conditional to the extent that the insured must both suffer a loss and be damaged in some manner.* Furthermore, the definition does not state what is or is not the delivery of marketable title. One must review state law to determine how marketability is defined.

The policy definition encompasses any *“alleged or apparent matter affecting title to the land”*. This language establishes the fact that the insured is not required to first obtain a judicial determination that the title is unmarketable before requesting defense of the title. Failure to provide such a defense (with or without a reservation of rights) subjects the insurer to potential claims of bad faith and extra-contractual tort theories based on damages for breach of such duty. Furthermore, the added language would more likely than not entitle a prospective purchaser to rescind under a contract of sale on the basis that title is unmarketable unless the contract of sale addresses the character of the title to be conveyed as either marketable or insurable.

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Many states (19) have marketable title record title acts that purportedly clear away old claims and make it easier to establish marketable title if there is a muniment or "root of title" and a search of the record discloses there a no adverse claims filed within the specific time frame. Approximately 30 states have Bar Title Standards as guides to marketability. However, the latter do not have the same force and affect as the former, i.e., they have not been sanctioned by the state legislature and passed into law. They are merely a guide to recommended practice.

*Ins. Cl. 4: Lack of right of access to and from the land*

**Comment:** The standard ALTA policies insure against loss by reason of lack of access rather than insuring the right of actual access to the property. Note the distinction. In this case the title insurer agrees to reimburse or indemnify the insured in the event the insured suffers a loss because the insured does not have access to the property, provided that coverage is not otherwise removed from the policy with the inclusion of an "Land Locked" exception in Schedule B. Where affirmative coverage is provided and the insurer does insure access, the policy insures only some adequate right of access, and not access along all roads bounding the insured parcel.

**Discussion:** The term "access" should be construed to mean a legal right of access and not a physical means of access. It should be emphasized that the useability of access is not insured. If a particular private driveway is to be used for access, the insured's counsel should require the title company to include specific language describing the appurtenant r/w in Schedule A

The Company has filed with the Dept. of Insurance Endorsement forms providing affirmative coverage with respect to access. In some cases this form of coverage may require submission of a survey. See Hart, Title Insurance Underwriting, Principles and Exception Language, for further guidelines. Consideration should also be given as to whether the insured may have suffered no loss since they took into consideration the lack of access when negotiating the purchase price.

*Ins. Cl. 5: The invalidity or unenforceability of the lien of the insured mortgage.*

**Comment:** The Loan Policy insures the validity and enforceability of the mortgage. It does not insure the manner of enforcement. It does not insure that all the provisions of the mortgage are enforceable. It does not insure against loss by reason of a defect in the execution of the note. It does not insure repayment of the debt [Narberth Bldg & Loan Ass'n v BMTCo, 126 Pa Super 74, 190 A. 149, 151 (1937)] or anything else beyond the title to the lend securing the debt. It does not insure the origin of the debt or insure its payment or validity. It does not insure that an instrument identified on its face as a "mortgage" meets the requisite requirements, terms, conditions and provisions

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established by statute to constitute a mortgage. It does not insure that the security for the loan is equal to the loan amount [Brucha Mortgage Bankers Corp. v Nations Title of NY, 2000 N.Y. App. Div Lexis 8692 (August 14, 2000)]. Rather, if the value of the property is less than the debt, the property value become the maximum amount of the policy liability [Nielsen, footnote 1051].

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*Inc. Cl. 6: Priority of any Lien or Encumbrance over the Insured Mortgage Lien*

**Comment:** This provision insures that the mortgage is a “first and paramount lien” on the insured premises subject to the exclusions and exceptions from coverage.

**Discussion:** The title insurance loan policies also assume the risk of loss of another lien being given priority over the lien of the insured mortgage. This is important coverage for lenders as it provides assurance that sufficient security exists to satisfy the mortgage debt of the borrower defaults. Courts have found insurers liable where the search and examination of title reveals prior mortgages, judgment liens, mechanics liens, leasehold estate with purchase and financing options, and special municipal assessments which are not paid, satisfied and disposed of. Frequently it is this clause which determines whether the insured lender has suffered a loss under the policy. If a prior lien is determined by a court of law to be enforceable its existence only triggers the policy’s coverage if its existence cause the insured mortgagee to become undersecured. So long as sufficient value remains in the real property after payment of the prior lien to cover payment of the loan, the insured will not have suffered a loss under the policy. On the other hand, if the amount of the lien is not satisfied and the judgment creditor levy’s and executes, that is sufficient to trigger the title insurers defense obligations. Usually, whenever a claim is made under insuring clause 1 or 2 there is a count included in the claim and complaint under this clause.

*Ins. Clause 7 and Ins. Cl. 8: see Gosdin, Supra., pages 60 and 61 and Fromhold, Advanced Principles of Title Insurance in Pennsylvania, NBI, July 7, 2001, Chapter 1, pages 15 through 17 inclusive.*

**EXCLUSIONS FROM COVERAGE DISCUSSION BEGINS ON THE FOLLOWING PAGE**

**EXCLUSIONS FROM COVERAGE - OWNERS 1992**

**Comment:** Exclusions from coverage list matters which may be included within the broad language of the policy insuring clauses but for which the Company does not intend to assume liability. They identify those matters that do not constitute "title" matters or that are not within the expertise of the title insurer. The 1<sup>st</sup> four exclusions apply to both the Owner's and Loan Policy.

"The following matters are expressly excluded from the coverage of this policy and the Company will not pay loss or damage, costs, attorney's fees or expenses which arise by reason of:"

- 1(a) Any law, ordinance or governmental regulation (including but not limited to building and zoning laws, ordinances, or regulations) restricting, regulating, prohibiting or relating to (i) the occupancy, use, or enjoyment of the land; (ii) the character, dimensions or location of an improvement now or hereafter erected on the land; (iii) a separation in ownership or a change in the dimensions or area of the land or any parcel of which the land is or was a part; or (iv) environmental protection, or the effect of any violation of these laws, ordinances or governmental regulations, except to the extent that a notice of the enforcement thereof or a notice of a defect, lien or encumbrance resulting from a violation or alleged violation affecting the land has been recorded in the public records at Date of Policy.
- (b) Any governmental police power not excluded by (a) above, except to the extent that a notice of the exercise thereof or a notice of a defect, lien, or encumbrance resulting from a violation or alleged violation affecting the land has been recorded in the public records at Date of Policy.

**Discussion:** exclusion 1(a) is a practical necessity for four basic reasons:

- (1) Although all such laws, ordinances, and governmental regulations are contained in the public records, they seldom appear in the land records. Therefore, the title examiner for the Company cannot discover such regulations through a title examination. Therefore Exclusion #1(a) is used.
- (2) It would also be very difficult to conduct the kind of detailed examination of the property itself that would be necessary in order to determine its conformity with the myriad requirements of the building code and other laws, ordinances, and governmental requirements. Exclusion #1(a) eliminates the necessity of such an examination.
- (3) Exclusion #1(b) reminds the insured that the Company has no way of predicting whether or not the property in question will ever be affected by an exercising of any governmental police power except for those of record in the public records at Date of Policy;

**Comment:** see Gosdin, supra., page 65 for case cites interpreting Ex. Cl. 1

(4) Exclusion 1(a)(iv) relates to environmental matters: The ALTA title policies were modified in 1987 (without subsequent change in 1990 and 1992 ALTA policies) to state with more particularity the fact that the insurer does not undertake to assume liability for environmental claims where no notice is filed in the public records accessible to title insurers.

For a comparison of Exclusion Clause 1 in the various ALTA policies see Gosdin, *Supra.*, page 63. For further discussion including case citations, see e-mail of October 2, 2001 regarding *Environmental Use Restriction and Title Insurance*, included as a handout/exhibit.

2. Rights of eminent domain unless notice of the exercise thereof has been recorded in the public records at Date of Policy, but not excluding from coverage any taking which has occurred prior to Date of Policy which would be binding on the rights of a purchaser for value without knowledge.

**Comment:** This exclusion removes liability for prior takings unless notice is recorded in the public records or unless the taking is binding on a *bona fide purchaser*. The Policies do not exclude coverage where a taking would be effective against an innocent purchaser. The exclusion would apply to a taking if no lis pendens or judgment is recorded.

**Discussion:** This exclusion retains the basic language of the 1970 policy and once again reminds the insured that the Company has no way of predicting whether or not the property in question will ever be affected by an exercising of governmental rights, such as eminent domain. Therefore, it would be impossible for the Company to include protection against such an event in policy coverage. While the 1992 policy retains the basic language of the earlier exclusion, the new exclusion provides for protection in cases of a prior taking which would be effective against a purchaser for value without knowledge.

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3. Defects, liens, encumbrances, adverse claims or other matters:
- (a) created, suffered, assumed or agreed to b the insured claimant;
  - (b) not known to the Company, not recorded in the public records at Date of Policy, but known to the insured claimant and not disclosed in writing to the Company by the insured claimant prior to the date the insured claimant became an insured under this policy;
  - (c) resulting in no loss or damage to the insured claimant;
  - (d) attaching or created subsequent to Date of Policy; or
  - (e) resulting in loss or damage which would not have been *sustained if the insured claimant had paid value for the estate* or interest insured by this policy.

**Comment:** The third exclusion contains five separate parts. We will address and discuss them separately.

- (a) **Discussion:** The first clause is based on the fact that there is no sound reason for insuring the policyholder against his own acts. Various acts or agreements of the insured are generally considered "acts of the insured". In order to be an act of the insured, there is the requirement of knowledge by the insured. Negligent creation by the insured of the defect is insufficient.
  - A matter is "created" by an insured if brought about by an affirmative act by the insured;
  - A matter is "suffered" by and insured if permitted by the insured, or if the insured has the power to prevent or prohibit such matter with full knowledge of it.
  - A matter is "*assumed*" by an insured when it may be determined that the insured knowingly assumed or agreed to a personal obligation

Examples may be found in Gosdin, supra., at pages 69 through 76..

- (b) **Discussion:** This clause refers to matters that the insured had knowledge of when the policy was issued, but were not known to the Company or disclosed in writing to the Company and not a matter of public record. The "knowledge exclusion" does not apply if the matter is recorded in the public records and constitutes constructive notice. The insured must acquire knowledge of the matter *on or before* the date of Closing and Policy Date and not reveal it to the insurer. If intentional concealment is tantamount to fraud, the insurer may bring an action to rescind the policy.

*See also the Title Insurance Law Newsletter*, August, 2000 citing Kirwan v.

CTIC, 2000 WL 781109 (Neb.App.) There the Neb. S.Ct. discussed Ex CL. 3(b) stating the proposed insured must disclose adverse claim of which it had knowledge. This is an exhibit and part of the class handouts.

Two additional matters or concerns here:

- What is the effect of this exclusion if the insured discloses the of-record matter?
- Has this exclusion been applied to transactions relating to substitutions of corporate ownership/partnership/LLC interests?

In response to the first matter, where the insured makes full disclosure to the insurer, if the insurer thereafter and in consideration of the facts nonetheless undertakes to insure without exception it loses its right to thereafter invoke the exclusion in the event a claim is tendered. It also runs the risk of not disclosing matter within its knowledge to the prospective lender.

With regard to the second question the matter has been applied and decided. See Carefree Living of Am. Inc. v CTIC, 2000 Minn. App. Lexis 258 (Minn. Ct. App. March 21, 2000)

- (c) **Discussion:** The third clause of this exclusion again states that the Company is not liable to the insured unless he actually suffers loss or damage.

**Comment:** See Gosdin, supra., pages 80-84 and Palomar, supra., Ch. 6 for further discussion and case citations.

- (d) **Discussion:** Once again, the insured is notified that the policy is effective only as of the date shown on Schedule A. Because of the importance of this point -- and to avoid any possible confusion in the mind of the policy holder -- the significance of the policy's effective date is mentioned several different times.
- (e) **Discussion:** The laws of most states afford protection to purchasers dealing in good faith who are giving valuable consideration. They are known as "bona fide purchasers for value". If the insured is not a bona fide purchaser for value, this protection may not be available to him. This clause excludes from coverage any loss or damage suffered by the insured that he would not have sustained had he paid value for the property.

The failure of the insured to pay value could be a matter that is an act

of the insured [Ex Cl 3 (e)] or a matter known to the insured and not disclosed in writing to the company [Ex Cl. 3(b)]. The principal purpose of the value exclusion is to allow the insurer to deny liability if the insured does not avail itself of the protection of the recording statutes. The recording statutes require the insured to be a bfp (or lender) for value in order to extinguish any previous unfiled interests not reflected by actual possession. The exclusion does not require the insured be an "*innocent purchaser for value*" although the "Knowledge exclusion" would be relevant here. The value exclusion does not define the adequacy of value although we should insist that the consideration paid closely approximate "current value" and certainly no less than that contemplated under the old Durrett 70% Rule. Surely payment of a grossly inadequate amount is not insurable because of the possibility of issues of competency and collateral advantage.

4. Any claim, which arises out of the transaction vesting in the insured the state or interest insured b this policy, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws, that is based on:
  - (a) the transaction creating the estate or interest insured by this policy being deemed a fraudulent conveyance or fraudulent transfer; or
  - (b) the transaction creating the estate or interest insured by this policy being deemed a preferential transfer results in failure:
    - (i) to timely record the instrument of transfer; or
    - (ii) of such recordation to impart notice to a purchaser for value or a judgment or lien creditor.

**Comment:** The fourth exclusion is transactional in nature; in other words, its applicability is limited to circumstances where the estate or interest insured by this policy is subject to a flaw which renders it vulnerable to attack. This exclusion does NOT extend to situations where a prior transaction is the source of the problem.

**Discussion:** This exclusion has been added primarily because of the inability of the title insurer to determine the solvency of the grantor or mortgagor and to clarify that title insurers do not ordinarily insure against insolvency to the insured transaction. Insolvency frequently triggers a creditors' rights issue under sections 544(b), 547, 548 and 510 of the Bankruptcy Code, under state Fraudulent Transfer Laws and under state Corporation Acts. The issue

of creditors' rights is more particularly addressed in the hand-out/exhibit entitled: *Creditors' Rights and Title Insurance*, which you are expected to read and review. The exclusion, in a much broader form, was first added to the 1990 ALTA policies and was limited and modified in the

[Continued]

1992 policies. The present exclusion does not protect the insurer against and attack upon title made by a trustee under Sec 544(b) The exclusion would apply if the current transaction were attacked as a voidable preference [548] or fraudulent transaction [547].

Title companies have experienced substantial losses because of attacks on LBO transaction as fraudulent transfer and, as a consequence, have become acutely aware of their inability to analyze the economics of those transactions.

The creditors' rights exclusion will apply only if the issue arises out of the current transaction. It does not apply or protect the title insurer where the issue arises in a prior transaction in the chain of title, such as the delivery of a deed-in-lieu of foreclosure after the workout and mortgage modification failed.

NB This discussion is equally applicable to ALTA Loan Policy Ex Cl. 7

[Continued}

### **EXCLUSIONS FROM COVERAGE - LOAN 1992**

"The following matters are expressly excluded from the coverage of this policy and the Company will not pay loss or damage, costs, attorney's fees or expenses which arise by reason of:

- 1(a) Identical to Exclusion 1(a) of the Owners Policy
- 1(b) Identical to Exclusion 1(b) of the Owners Policy
2. Identical to Exclusion 2 of the Owners Policy
3. Defects, liens, encumbrances, adverse claims or other matters:
  - (a) Identical to 3(a) of Owners Policy
  - (b) Identical to 3(b) of Owners Policy
  - (c) Identical to 3(c) of Owners Policy
  - (d) attaching or created subsequent to Date of Policy (except to the extent that this policy insures the priority of the lien of the insured mortgage over any statutory lien for services, labor or material); or
  - (e) resulting in loss or damage which would not have been sustained if the insured claimant had paid value for the insured mortgage.

**Discussion:** Exclusion 3(d) is identical to exclusion 3(d) of the Owners Policy except for one exception; the parenthetical phrase refers to the coverage provision on mechanics' liens - liens attaching or created subsequent to the effective date of the policy are excluded from coverage EXCEPT for mechanics' liens on work financed through the mortgage.

**Discussion:** Exclusion 3(e) is a restated and clarified limitation of coverage. It excludes loss which arises because the insured claimant did not pay value (ie. mortgages acquired by descent or gift.)

4. Unenforceability of the lien of the insured mortgage because of the inability or failure of the insured at Date of Policy, or the inability or failure of any subsequent owner of the indebtedness, to comply with applicable doing business laws of the state in which the land is situated.

**Discussion:** Exclusion 4, which applies exclusively to loan policies, refers to foreign corporations lending money for the purchase of local property. The laws of certain states make this exclusion necessary. These states require a foreign corporation to obtain a "Certificate of Authority" from the Secretary of State of the state where the property is located before they can lend money for the purchase of that property. The fourth exclusion alerts the insured to the fact that his coverage does not include losses or damages suffered as a result of noncompliance with such state laws. Exclusion 4 also contains clarified language (as compared to the basic language of the 1970 Policy) which now specifically states that no coverage exists if the insured is unable to qualify to do business and as a result suffers loss because the mortgage lien cannot be enforced.

5. Invalidity or unenforceability of the lien of the insured mortgage, or claim thereof, which arises out of the transaction evidenced by the insured mortgage and is based upon usury or any consumer credit protection or truth in lending law.

Exclusion 5 originally appeared in Insuring Provision 5 of the 1970 Policy; there is no change in coverage.

6. Any statutory lien for services, labor or materials (or the claim of priority of any statutory lien for services, labor or materials over the lien of the insured mortgage) arising from an improvement or work related to the land which is contracted for and commenced subsequent to Date of Policy and is not financed in whole or part by proceeds of the indebtedness secured by the insured mortgage which at Date of Policy the insured has advanced or is obligated to advance.

**Discussion:** This exclusion is the converse of the mechanic's lien insuring provision set forth as insuring clause 6 of the ALTA Loan Policy. Exclusion 6 avoids any duty of defense when the lien claims are post-policy (claims for payment for work not funded by the loan and not relating to a prior contract or stipulation) and where the claimant asserts priority or preference. It disallows coverage of losses resulting from statutory liens for services or materials that were contracted for and commenced after the date of the policy and that were not financed by proceeds of the loan secured by the insured mortgage which at the Date of Policy the insured had advanced or was obligated to advance. Originally appeared as part of the mechanics' lien priority Insuring Provision 7 of the 1970 Policy.

7. Any claim, which arises out of the transaction creating the interest of the mortgagee insured by this policy, reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws, that is based

on:

- (a) the transaction creating the interest of the insured mortgagee being deemed a fraudulent conveyance or fraudulent transfer; or

[Continued]

- (b) the subordination of the interest of the insured mortgagee as a result of the application of the doctrine of equitable subordination; or
- (c) the transaction creating the interest of the insured mortgagee being deemed a preferential transfer except where the preferential transfer results from the failure;
  - (i) to timely record the instrument of transfer; or
  - (ii) of such recordation to impart notice to a purchaser for value or a judgment or lien creditor.

**Discussion:** Exclusion 7 is transactional in nature. The comments made under Ex Cl 4 of the ALTA Owner's policy are equally applicable here. In other words, its applicability is limited to circumstances where the estate or interest insured is subject to a flaw which renders it vulnerable to attack. The exclusion does not extend to situations where a prior transaction is the source of the problem. It is also note worthy that the this exclusion makes specific reference to the doctrine of equitable subordination.

For further discussion of policy exclusions refer to *POLICY LECTURE THREE*, Hart, The Law if Titles in Pennsylvania, Chapter 54, 1992 Policy Exclusions, for completed coverage, citing:

- Gosdin, *Supra.*;
- Palomar, Chapter 6, *supra.*;
- Thompson on Real Property, Thomas Ed., Ch. 93, *Title Insurance*, prepared by Professor John L. McCormack, Loyola University, Chicago;
- **As to Ex. Cl. 1(a)(iv)** see Gosdin's Policy Comparison, page 63 *and the* three cases listed in Bob Ellis text, The Title Insurance Law Handbook, namely:
- Lick Mill Creek Apts. V. CTIC, 283 Cal Rotr. 231 (CA App. 1991);

[Continued]

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- CTIC v. Kumar, 506 NE2d 154 (Mass. App. 1997);
- South Shore Bank v STG, 688 F. Supp. 803 (D. Mass. 1988) aff'd 867 F2d 607 (1<sup>st</sup> Cir. 1988);
- ***As to Ex. Cl. 3(a)*** see 87 ALR3d 515, *Title Insurance: Exclusions of liability for Defects, Liens, or Encumbrances Created, Suffered, Assumed, or Agreed to by the Insured* [Ex Cl.3(a);
- ***As to Ex. Cl. 3(b)*** see 75 ALR3d 600, *Duty of Applicant or his Agent to Disclose Facts Arising or Discovered After Application for Title Insurance* & 17 ALR4th 1077 [Ex. Cl. 3(b)];
- *The Title Insurance Law Newsletter*, August 2000, citing Kirwan v. Chicago Title Insurance Company, 2000 WL 781109 (Neb.App.) "*Proposed Insured Must Disclose Attack on Title* [Ex. Cl. 3(b)];

## **CONDITIONS AND STIPULATIONS**

**Comment:** The Conditions and Stipulations list matters which are interpretive of the various policy provisions; state how a claim should be made under the policy and define the extent of the Company's obligation in connection with a claim.

**Discussion:** The terms and conditions of insurance comprise the balance of the pre-printed language of the policy. These paragraphs provide some basic definitions; a description of the events after which the policy will or will not continue; procedures for asserting a claim; an outline of the relationship between the insurer and the insured and their respective obligation to one another; a measure for determining the amounts payable on a claim; the reduction in the amount of insurance effected by any payment of a claim; an arbitration clause; and an "entire contract" clause.

**NB** Particular attention should be paid to Coverage Limitations Imposed by C&S 2 Refer to [titlelawannotated.com/endors.html](http://titlelawannotated.com/endors.html) at page 11 of 16. These limitations were also discussed on great length on DIRT during the Fall of 2001. See the Outlook Express Folders relating to Corporate Merger & Acquisition; Transfers to Revocable Trusts; and Transfers LLC's for a further discussion of this issue.

Refer to *POLICY LECTURE FOUR* citing case law and further discussion of this issue by: Burke, Law of Title Insurance, Chapter, Ch. 5;

Gosdin, *supra.*;

Hart, [www.titlelawannotated.com](http://www.titlelawannotated.com) Endorsement Link page 12 of 16 *Coverage Limitations Imposed by Conditions and Stipulation* [C&S 2] and Articles Cited

Palomar, *supra.*; Ch. 8;

Thompson, Thomas Ed., *supra.*

## **FREQUENTLY ASKED QUESTIONS**

Set forth below are a series of frequently asked questions with regard to the Outline of Policy Coverage provided in the 1992 ALTA Owner's and Loan Policies

### **COVERED RISKS – ALTA Loan Policy**

**[NB** For a further discussion of covered risks including examples of matters of an exclusionary nature for which endorsements may be obtained refer to [titlelawannotated.com/endors.html](http://titlelawannotated.com/endors.html) page 9 of 16]

Matters covered to the extent they are not excepted in Schedule B or excluded by the Exclusions from coverage are set forth on the facing page of the Loan Policy insuring clauses and the insuring clause preamble. More particularly, the face page of the policy describes the coverage afforded by the policy, subject to the exclusions, exceptions, conditions and stipulations, all of which are set forth in detail on the inside of the jacket. Assurance is given that the insured mortgage constitutes a valid and enforceable lien on the described estate or interest in real property. Insuring provisions of a specific nature are set forth and described in clauses (1) through (8). The company insures the lender against loss or damage sustained or incurred if the assurance therein set forth shall prove to be incorrect, i.e. the lenders suffers a loss by reasons of the fact that:

1. Title is vested other than as shown [see Ins, Cls. 1, Sch A-5 and C&S 1 (d)];
2. A defect, lien or encumbrance is not excepted in Schedule B or by the Conditions and Stipulations of the policy and we fail to disclose it [Ins. Cls 2]

[CONTINUED]

3. Title is determined to be unmarketable, as insured [Ins. Cls 3 & C&S 1 (g)];
4. there is lack or right of access to and from the land [Ins. Cls. 4];
5. The insured mortgage\* is determined to be invalid or unenforceable (except where a claim is based on usuary or any consumer credit protection or truth in lending law) as a result of defects in execution [Ins. Cls. 5; \*Sch. A-4, C&S 1 (e)];
6. Liens superior in time to the insured mortgage are found on the public record and are not shown in Part I of Schedule B [Ins. Cls. 6];
7. Statutory liens for labor or materials gain priority over the insured mortgage as a result of the commencement of construction prior to time of closing the loan excludes those liens arising from an improvement contracted for or begun after the policy date and not financed by the insured loan [Ins. Cls. 7 (a) and (b)];
8. Any assignment of the insured mortgage is determined to be invalid or unenforceable including the failure of such assignment to vest title to the insured mortgage in the named insured assignee free and clear of all liens [Ins. Cls. 8];

Liability for costs, attorneys fees and expenses to defend matters covered by the policy may be found on the last paragraph on the facing page of the policy.

The cover of the ALTA Loan Policy (10/17/92) contains the pre-assigned serial number for the policy and is, therefore, a controlled and audited form. If the cover is damaged or voided for any reason, it must be returned to the Home Office for cancellation and credit,

#### **WHO IS COVERED UNDER THE POLICY?**

1. The insured named in Schedule A, See also Conditions and Stipulations [C&S 1 (a)];
2. Any owner of the indebtedness secured by the mortgage [C&S 1 (a) (1)];
3. Governmental Agencies insuring repayment of the debt [C&S 1 (a)(ii)];

4. Any owner of the indebtedness secured by the insured mortgage who acquires the title to the estate of interest in the land by foreclosure, deed in lieu of foreclosure or any other method which extinguished the lien of the insured mortgage [C&S 1 (a)(iii) & 2 (a)(i)];
5. Parent or wholly owned subsidiaries of the owner of the party acquiring title if title is transferred to them [C&S 1 (a)(iii), 2 (a)(ii)];
6. Governmental agencies which acquire the title as the result of a guarantee of payment as in 3 above [C&S 1 (a)(iii) & 2 (a)(iii)]

#### **DURATION OF COVERAGE**

1. Until the debt secured by the mortgage is paid [C&S 7 (a)(11)];
2. Until an insured who acquires title to the insured interest in the land (a) transfers it to another party who is not insured and (b) no longer has any liability for covenants of warranty it gives in the transfer [C&S 2 (b)].

#### **MATTERS EXCLUDED FROM COVERAGE UNDER THE POLICY**

See Endorsement Link on [www.titlelawannotated.com](http://www.titlelawannotated.com) pages 8 and 9 and discussion of Pedowitz Article;

As with other types of insurance policies, a title insurance policy's stated coverage is modified by express exclusions and exceptions. The function of exclusionary language is to eliminate the insurer's duty to indemnify for losses resulting from the excluded risk, even if they exist in fact. The exclusions are standardized, i.e, they are not tailored to the individual transaction, but are rather the stated limits of every transaction undertaken by the insurer. Policy exclusions address four general category of title defects: (1) those that cannot be discovered from an examination of the public; (2) those for which the insured bears responsibility; (3) those that do not cause any loss to the insured, and (4) miscellaneous matters including those that result from avoidance of the insured real property interest as a result of the application of federal or state creditors' rights laws. These four categories are addressed with more particularity below.

1. **Laws, ordinances or governmental regulation (and the effect of their violation) which relate to any of the following categories unless notice of enforcement appears in the public records [C&S 1 (f)] or a notice of a defect, lien or encumbrance resulting**

**from an actual or alleged violation appears in the public records:**

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General**

a. Occupancy, use or enjoyment of the land [excl. 1 (a)(i)];

examples would include zoning laws; building codes and federal or state forfeitures based on the use of the land.

b. Physical qualities of improvements on the land or their location on the land [excl. 1 (a)(ii)];

c. Subdivision laws or regulations [excl. 1 (a)(iii)];

d. Environmental protection [excl. 1 (a)(iv)];

e. Other governmental police powers [excl. 1 (b)].

2. **Matters within the insured's knowledge or control, i.e.,**

a. matters created, suffered, assumed or agreed to by the insured [excl. 3 (a)]; or

b. matters actually [C&S 1 (c)] known to the insured, not known to the company and not shown in the public records [excl. 3 (b)];

**or for which the insured bears responsibility by reason of**

c. failure to comply with applicable state laws [excl. 4 & 5]

3. **Matters which result in no loss to the insured** [excl. 3 (c)];

4. **Miscellaneous matters:**

a. **Rights of eminent domain, but only if:** [excl. 2]

1. no notice of exercise is recorded in the public records at policy date; or

2. In a pre-policy taking, the taking would not be binding on a purchaser for value without knowledge.



- b. Matters which are created or attach after the policy date, except to the extent insured against future mechanics liens in insuring clause 7 [excl. 3 (d) and 6];
- c. Matters creating loss the insured would not suffer if it had paid value for the insured mortgage [excl. 3 (e)]

examples would include limitation on recording act protections for donees, heirs, and devisees, and corporate or fiduciary successors who acquire land interests by operation of law;

- d. **Creditors Rights** under bankruptcy and insolvency laws but only if: [excl. 7]
  - 1. the claim arises out of the transaction vesting the estate or interest insured (the instant transaction) and
  - 2. that transaction is determined to be a fraudulent transfer; or
  - 3. that transaction is determined to be a preferential transfer which was not created by:
    - (a) failure to timely record the instrument creating the interest [10 days 11 USC 547 (e)]; or
    - (b) the failure of the recordation to impart constructive notice to a purchaser for value or judgment or lien creditor; or
  - 4. the interest of the insured mortgagee is subordinated under the doctrine of equitable subordination.

**POLICY FORMAT REVIEW** *see email discussion of December 14, 2001*

**SCHEDULE A - ALTA LOAN POLICY 1992**

Every loan policy must contain a Schedule A. This is the Schedule which gives the specific details of the insured lien, the effective date of the policy, the amount of insurance, etc.

Letters shown below correspond to those on the illustrated form. Beside each letter below is an explanation of the information which should be inserted where the corresponding letter appears on the form.

- A. Showing of Rate and/or Premium is mandatory in some jurisdictions; optional in others.
- B. Policy Number should be shown exactly as it appears on front cover of policy.
- C. The Date of Policy should be the month, day year, and time through which title has been examined, which must be through time of recording of the instrument on which exposure is based.
- D. The Amount of Insurance cannot be less than the full principal debt secured by the mortgage. The policy can, however, be issued for an amount in excess of the principal debt to cover interest, foreclosure costs, etc. in accordance with regulations of the state where the land is located.
- E. The full name of the insured as it appears in the mortgage should be shown. If the mortgage is FHA insured, also insert "and/or The Secretary of Housing and Urban Development, his successors and/or assigns, as their interests may appear" or if VA guaranteed, also add "and/or the Administrator of Veterans' Affairs, his successors and/or assigns, as their interests may appear."
- F. Insert the type of estate owned by the mortgagor which is the subject of the mortgage, e.g. Fee Simple. If the estate is other than Fee Simple it must be accurately described or you will have contradicted insuring clause one on the facing page of the policy.
- G. Insert the name or names of the owner of record of the estate or interest encumbered by the insured mortgage, which should be the same as the mortgage (s) shown on the insured mortgage.
- H. Insert the complete record information of the mortgage and any assignments of it covered by the policy. Frequently assignments of it covered by the policy. Frequently assignments are recorded after the policy is issued and an endorsement is issued to show such assignment.
- I. Insert T.A. application number.

**SCHEDULE A**

T.A. File No [1]

Policy No. [B]

Amount of Insurance \$[D]

Premium \$ [A]

Date of Policy [C] at [C] a.m.  
[C] p.m.

1. Name of Insured: [E]

2. The estate or interest in the land which is encumbered by the insured mortgage is:  
[F]

3. Title to the estate or interest in the land is vested in:  
[G]

4. The insured mortgage and assignments thereof, if any, are described as follows:  
[H]

[5. The land referred to in this policy is described as follows:]

If Paragraph 5 is omitted, a Schedule C, captioned the same as Paragraph 5, must be used.

**LOAN**

**SCHEDULE B I, ALTA LOAN POLICY**

Every loan policy must contain Schedule BI. This Schedule states the exceptions from coverage of the policy.

Letters shown below correspond to those on the illustrated form. Beside each letter below is an explanation of the information which should be inserted where the corresponding letter appears on the form.

- A. Policy Number should be shown exactly as it appears on front cover of policy.
- B. Ordinarily current year will be inserted unless taxes therefor have been paid and receipt is in file.
- C. Schedule BI should contain in consecutively numbered paragraphs all matters such as easements, restrictions, leases, encumbrances, defects, etc. which must be excepted from the coverage of the policy.
  - (1) Restrictions and easements should be set forth in detail with recording information given and, in appropriate cases, with copies attached to the policy. Most institutional investors require that exceptions for restrictions include language assuring that the restrictions do not embody and are not accompanied by right of reverter and have not been violated, and that the policy insures that any future violation will not cause a forfeiture or reversion of the title. Such assurance may be included if it has been determined that there has been no violation of restrictions and there is no reverter clause.
  - (2) Blanket exceptions of easements, restrictions, etc. of record should not be made.
  - (3) Exceptions for (a) rights of parties in possession, (b) facts that an accurate survey of the premises would show, and (c) unrecorded mechanics liens must be included unless there is adequate evidence including affidavits, releases of liens, and current survey, etc. which support the waiver.
  - (4) All exceptions appearing in prior exposures related to this policy should appear as exceptions herein.
  - (5) Municipal assessments, or liens for public improvements should be excepted as follows:

"Pending municipal assessment liens for public improvements, notice of which is contained in Resolution No. \_\_\_\_\_ or Ordinance No. \_\_\_\_\_. The amount of the assessment or levy, if any has not been determined."
  - (6) Be careful to specifically except any reservations for mineral, petroleum, and road rights-of-way which may appear in prior conveyances in the chain of title.
  - (7) Zoning should not be shown as an exception in Schedule BI since it is excluded in the "Exclusions from Coverage" contained in the policy.
- D. Refer to any continuation sheet or sheets, if used.

**SCHEDULE B**

T.A. File No [I]

Policy No. [A]

**EXCEPTIONS FROM COVERAGE**

This policy does not insure against loss or damage (and the Company will not pay costs, attorneys' fees or expenses) which arise by reason of:

**PART I**

- [B] 1. The Lien of all taxes for the years 19 \_\_\_ and thereafter.
- [C] 2. Restrictions set forth in Book \_\_\_ page \_\_\_ or Easements set forth in Book \_\_\_ page \_\_\_\_.
- 3. Preprinted survey exception [if not removed from commitment]  
Rights of parties in possession [if not removed from commitment]  
Mechanics lien exception [if not removed from commitment]  
Road, ways, streams or easements, if any, not shown of record, etc., [if not removed from prior commitment]
- 4. All title exceptions appearing in prior back title or policies are to be excepted.
- 5. Municipal assessments, if any.
- 6. Mineral reservations and Oil and Gas Leases, if any, are to be excepted if disclosed of record.

*[ THIS IS A SAMPLE / INSTRUCTIONAL FORM ]*

Note: If there are matters which affect the title to the estate or interest in the land described in Schedule [A] [C], but which are subordinate to the lien of the insured mortgage, Part II of Schedule B must be added, or Part I of Schedule B must contain the following statement:

"Matters which affect the title to the estate or interest, but which are subordinate to the lien of the insured mortgage."

**LOAN**

**Lecture On Matters which should be shown in Schedule B:**

(matters which the insured intends to take subject to)

- (a) Any matter which can result in Loss or Damage to the insured, which is within the scope of those matters listed in the "insuring clauses", and for which the Company does not intend to assume liability must be shown in Schedule B unless it is clearly within the Exclusions from Coverage.
  - (i) General Exceptions: Current taxes, future installments of special assessments, mortgages, easements & restrictions.
  - (ii) Actual defects in title - must be corrected prior to the closing of title.
- (b) The deposit of satisfactory indemnity with the Company to protect it against matters shown on Schedule B DOES NOT justify their omission.
- (c) If satisfactory indemnity has been deposited with the Company, it is proper procedure to show the matter for which the indemnity has been posted in Schedule B, and to insure against loss occurring because of the endorsement of such matter.
- (d) The ALTA Mortgage Policy requires that all matters affecting the title as of the Policy Date be shown, even though such matters are inferior to the lien of the Mortgage being insured. Such matters are shown in Schedule B Part II, Subordinated Matters.

**Title Insurance Underwriting Process Lecture V [Owner's Policy].**

The Identity & Nature of the Insured as Affecting the Issuance of a Policy -- Schedule A (Owners):

- (a) It is very important to determine "who" or "what" the proposed insured is; as it may effect the issuance of or the exceptions in the Policy.
- (b) The proposed insured must be definitively identified and have the legal capacity to acquire the ownership of the land.
- (c) The acquisition of ownership must be absolute rather than security for payment of a debt.
  - (i) If we are certain that the estate in the land which we have described in Schedule A has actually been created and vested in the insured, it is not necessary to make a Schedule B exception.
- (d) If the estate being insured is limited by the instrument which creates it, and that instrument is referred to in the description of the estate in Schedule A, it is not necessary to reference the limitations contained therein in Schedule B.
- (e) Liens and encumbrances which have been created or suffered by the insured owner, and which automatically attach to the land upon acquisition of ownership by the insured, need not be excepted in Schedule B.

**Title Insurance Underwriting Process Lecture V [Loan Policy]**

The Identity & Nature of the Insured as Affecting the Issuance of a Policy -- Schedule A (Loan):

- (a) It is of extreme importance, in certain situations, to determine whether a corporate mortgagee is a domestic corporation; or if a foreign corporation it is licensed "to do business" in the state where the land is located.
  - (i) Please note that exclusion 4 of the Exclusions from Coverage in the ALTA Loan Policy -- 1992 from, does not apply to all situations. In those cases where a "doing business" issue exists, the Home Office must be notified. At the very minimum, the insured should be warned before the Policy is issued as to the exclusion & possible complications upon assignment.

NOTE: Doing Business end is prohibited in PA.

- (b) Care should be taken in regards to the relationship between the Mortgagor and Mortgagee, as some relationships may cause the Mortgage to be unenforceable.

[Continued on Next Page]

- (i) The common situation would occur if the Mortgagor is a Partnership or Limited Liability Company; and the Mortgagee is either a general partner or limited partner.

## Policy Lecture VI

### Endorsements:

- (a) Rate increase as contained in the New Manual became effective 3/1/1995 and subsequent revisions were approved 5/1/1995.
- (b) Section 2.7 states in part: "No form of Policy, Endorsement or other coverage may be issued which varies terms, conditions or exclusions of a Policy unless FIRST approved by the Department of Insurance". This section specifically prohibits any form of coverage which changes the Policy "boilerplate".

## **LECTURE 7 POLICY FORMS COMPARISON**

### **COMPARISON OF COVERAGE IN THE VARIOUS AMERICAN LAND TITLE ASSOCIATION POLICY FORMS WITH EMPHASIS IN DIFFERENCE IN EXCLUSION LANGUAGE**

#### **INTRODUCTION**

The American Land Title Association is an industry-wide association of title insurance companies. One of its major functions is the promulgation of title insurance forms for the use of its members.

The Association cannot and does not require its members to use the forms promulgated. However, there is much to be gained by the use of forms throughout the country by title insurers in that as time passes, both insurer and insured become familiar with the coverage furnished by the various forms and there is created a body of law relating to their interpretation.

These American Land Title Association forms are generally promulgated through the Title Insurance Forms Committee. The Committee, composed of general counsel of a number of member companies, receives requests from both customers and member companies for the consideration of forms to be issued on a national basis. Based on a decision of its Executive Committee, the Title Insurance Forms Committee drafts proposed forms which are then adopted by the Association. Over the years the forms have undergone changes and revisions. Highlights of those changes are discussed here.

#### **1970 ALTA LOAN POLICY:**

The following matters are expressly excluded from the coverage of this policy:

1. Any law, ordinance or governmental regulation (including but not limited to building and zoning ordinances) restricting or regulating or prohibiting the occupancy, use or enjoyment of the land, or regulating the character, dimensions or location of any improvement now or hereafter erected on the land, or prohibiting a separation in ownership or a reduction in the dimensions or area of the land, or the effect of any violation of any such law, ordinance or governmental regulation.
2. Rights of eminent domain or governmental rights of police power unless

notice of the exercise of such rights appears in the public records at Date of Policy.

3. Defects, liens, encumbrances, adverse claims, or other matters (a) created, suffered, assumed or agreed to by the insured claimant; (b) not known to the Company and not shown by the public records but known to the insured claimant either at Date of Policy or at the date such claimant acquired an estate or interest insured by this policy or acquired the insured mortgage and not disclosed in writing by the insured claimant to the Company prior to the date such insured claimant became an insured hereunder; (c) resulting in no loss or damage to the insured claimant;  
  
(d) attaching or created subsequent to Date of Policy (except to the extent insurance is afforded herein as to any statutory lien for labor or material).
4. Unenforceability of the lien of the insured mortgage because of failure of the insured at Date of Policy or any subsequent owner of the indebtedness to comply with applicable "doing business" laws of the state in which the land is situated.

**1984 REVISION OF THE 1970 ALTA LOAN POLICY:**

The following matters are expressly excluded from the coverage of this policy:

1. (a) Governmental police power.  
  
(b) Any law, ordinance or governmental, regulation relating to environmental protection.  
  
(c) Any law, ordinance or governmental regulation (including but not limited to building and zoning ordinances) restricting or regulating or prohibiting the occupancy, use or enjoyment of the land, or regulating the character, dimensions or location of any improvement now or hereafter erected on the land, or prohibiting a separation in ownership or a change in the dimensions or area of the land or any parcel of which the land is or was a part.

- (d) The effect of any violation of the matters excluded under (a), (b) or (c) above, unless notice of a defect, lien or encumbrance resulting from a violation has been recorded at Date of Policy in those records in which under state statutes deeds, mortgages, lis pendens, liens or other title encumbrances must be recorded in order to impart constructive notice to purchasers of the land for value and without knowledge; provided, however, that without limitation, such records shall not be construed to include records in any of the offices of federal, state or local environmental protection, zoning, building, health or public safety authorities.
2. Rights of eminent domain notice of the exercise of such rights appears in the public records at Date of Policy.
  3. Defects, liens, encumbrances, adverse claims, or other matters (a) created, suffered, assumed or agreed to by the insured claimant; (b) not known to the Company and not shown by the public records but known to the insured claimant either at Date of Policy or at the date such claimant acquired an estate or interest insured by this policy or acquired the insured mortgage and not disclosed in writing by the insured claimant to the Company prior to the date such insured claimant became an insured hereunder; (c) resulting in no loss or damage to the insured claimant; (d) attaching or created subsequent to Date of Policy (except to the extent insurance is afforded herein as to any statutory lien for labor or material).
  4. Unenforceability of the lien of the insured mortgage because of failure of the insured at Date of Policy or of any subsequent owner of the indebtedness to comply with applicable "doing business" laws of the state in which the land is situated.

**CHANGE IN DEFINITION OF "PUBLIC RECORDS"**

**1970 AND 1984 REVISION OF THE 1970 ALTA LOAN POLICIES:**

1. Definition of Terms  
The following terms when used in this policy mean:

\* \* \*

- (f) "public records": those records which by law impart constructive notice of matters relating to said land.

### **1987 ALTA LOAN POLICY:**

1. Definition of Terms

The following terms when used in this policy mean:

\* \* \*

- (f) "public records": records established under state statutes at Date of Policy for the purpose of imparting constructive notice of matters relating to real property to purchasers for value and without knowledge. With respect to Section 1 (a) (iv) of the Exclusions From Coverage, "public records" shall also include environmental protection liens filed in the records of the clerk of the United States district court for the district in which the land is located.

### **1987 ALTA POLICIES**

Many of the principal changes in the 1987 policies were designed to clarify the meaning or to put certain provisions where they properly belong. For instance, in the insuring provisions on the cover sheet of the policy, there had been exceptions from coverage for usury and consumer credit protection. These exceptions were deleted from the insuring provisions but were put under the Exclusions Section of the policy.

The insuring clause of both the ALTA Loan policy 1970 (Rev. 10-17-70, 10-17-84) and the 1987 ALTA Loan Policy (10-21-87), which appears on the facing page of the policy are virtually the same. Both forms insure against:

- loss from defects in the execution of the mortgage
- the invalidity or unenforceability of the lien of the mortgage
- the title being vested other than as shown
- the unmarketability of the title of the mortgagor
  
- defects in or liens or encumbrances on the title insured which are not excepted under Schedule B or by the Conditions and Stipulations of the policy

- the priority of the mortgage over any lien or encumbrance not excepted under Schedule B or by the Conditions and Stipulations of the policy

- any statutory lien for labor or materials
- lack of a right of access to and from the land

### **CHANGES IN INSURING PROVISIONS:**

In the 1970 policy, there had been an exception from coverage with respect to mechanic's liens for work contracted for and done after the date of the policy, for which the insured was not obligated to make an advance. This was deleted from the insuring provisions and was transferred to the Exclusion Section as Item No. 6. However, in transferring it to Item No. 6, not only did it exclude any statutory liens for services, labor or material, but it also excluded "the claim of priority of any statutory lien for services, labor and material over the lien of the insured mortgage" arising from work done, unless such work was financed in whole or in part by the proceeds of the indebtedness secured by the insured mortgage and the insured had an obligation to make such advances for such work. Thus, while changing the location of the exception the exception was expanded to include any claim of priority. This would relieve the title company of any defense obligation if the person is merely claiming a priority of lien over the insured mortgage.

Another change in the insuring provisions was to remove from the initial paragraph of the insuring provisions, the obligation to pay the costs, attorney's fees and expenses, which the company may be obligated to pay under the policy, and to add it as a last item in the insuring provisions. The new provision states that the company will pay costs, attorney's fees and expenses incurred in the defense of title or the lien of the insured mortgage, "but only to the extent provided in the Conditions and Stipulations". Thus, the title companies have limited the costs, attorney's fees and expenses with respect to any defense, since they have limited their obligation to defend in the various provisions in the policy.

In the Exclusions from Coverage, it is provided in the initial paragraph that the matters set forth in that Section are expressly excluded from coverage and, "the Company will not pay for loss or damage, costs, attorney's fees or expenses which arise by reason" thereof. Previously, there was no reference to the payment of loss, damage, costs, attorney's fees, or expenses in the Exclusions provision.

In Sections 1(a) and (b) of the Exclusions, a provision is added with respect to any violation of environmental laws but, the policy excepts from the exclusion any claim to the extent that notice of the enforcement would have been recorded in the public records as the date of the policy. This provision, as well as the provision dealing with governmental policy power in 1(b) of the Exclusions, was adopted and added to the 1970

policy in 1984.

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A new exclusion has been added in Section 3(e) of the Exclusions, providing that there is excluded any claim or loss which would not have been sustained if the insured claimant has paid "value" for the insured mortgage. This is the first time that payment of value is required as a basis for an insured maintaining an action under the policy. The question arises as to whether this will be expanded by the Courts to require fair value as we have seen in recent Court decisions, or whether any value would be adequate. The 1987 ALTA loan policy exclusions follow.

**1987 ALTA LOAN POLICY EXCLUSIONS:**

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 which arise by reason of:

1. (a) Any law, ordinance or governmental regulation (including but not limited to building and zoning laws, ordinances, or regulations) restricting, regulating, prohibiting or relating to (i) the occupancy, use, or enjoyment of the land; (ii) the character, dimensions or location of any improvement now or hereafter erected on the land; (iii) a separation in ownership or a change in the dimensions or area of the land or any parcel of which the land is or was a part; or (iv) environmental protection, or the effect of any violation of these laws, ordinances, or governmental regulations, except to the extent that a notice of the enforcement thereof or a notice of a defect, lien, or encumbrance resulting from a violation or alleged violation affecting the land has been recorded in the public records as Date of Policy.
- (b) Any governmental police power not excluded by (a) above, except to the extent that a notice of the exercise thereof or a notice of a defect, lien or encumbrance resulting from a violation or alleged violation affecting the land has been recorded in the public records as Date of Policy.
2. Rights of eminent domain unless notice of the exercise thereof has been recorded in the public records as Date of Policy, but not excluding from coverage any taking which has occurred prior to Date of Policy which would be binding on the rights of a purchaser for value without knowledge.

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3. Defects, liens, encumbrances, adverse claims or other matters;
  - (a) created, suffered, assumed or agreed to by the insured claimant:
  - (b) not known to the Company, not recorded in the public records at Date of Policy, but known to the insured claimant and not disclosed in writing to the Company by the insured claimant prior to the date the insured claimant became an insured under this policy;
  - (c) resulting in no loss or damage to the insured claimant;
  - (d) attaching or created subsequent to Date of Policy (except to the extent that this policy insures the priority of the lien of the insured mortgage over any statutory lien for services, labor or material); or
  - (e) resulting in loss or damage which would not have been sustained if the insured claimant had paid value for the insured mortgage.
4. Unenforceability of the lien of the insured mortgage because of the inability or failure of the insured at Date of Policy, or the inability or failure of any subsequent owner of the indebtedness, to comply with applicable doing business laws of the state in which the land is situated.
5. Invalidity or unenforceability of the lien of the insured mortgage, or claim thereof, which arises out of the transaction evidenced by the insured mortgage and is based upon usury or any consumer credit protection or trust in lending law.
6. Any statutory lien for services, labor or materials (or the claim of priority of any statutory lien for services, labor or materials over the lien of the insured mortgage) arising from an improvement or work related to the land which is contracted for and commenced subsequent to Date of Policy and is not financed in whole or in part by proceeds of the indebtedness secured by the insured mortgage which at Date of Policy the insured had advanced or is obligated to advance.

In Schedule A of the Policy, Item 3, the words "Title to" had been added to Item 3 so that it now reads, "Title to the estate or interest in the land is vested in:". The title companies wanted to be certain that the only estate that the policy is insuring is the estate set forth in the Schedule A, whether it be a leasehold estate or a fee estate, and the only item the title company is insuring with respect to that estate *is title*.

There is a revision in the initial paragraph of Schedule B, Part 1, which added to the policy, the provision that the "Company will not pay costs, attorney's fees or expenses" with respect to any item set forth in Schedule B, Part 1. If the title company excepts a matter from coverage, there will be no defense costs paid by the title company, even if some issue relative to title arises as a result of one of those matters. It is the position of the title company that this was always the intention and that it is just removing an ambiguity by inserting the provision in the initial paragraph of Schedule B.

There are many changes in the Conditions and Stipulations Section of the policy. The principal ones are as follows:

1. Section 1(a) contains the definition of insured and in subsection (i) it provides that the term "Insured" includes the owner of the indebtedness secured by the insured mortgage and each successor in ownership of the indebtedness except "a successor who is an obligor under the provisions of Section 12(c) of these Conditions of Stipulations". This effectively eliminated any guarantor or bonding company who has reimbursed the insured and has taken an assignment of the mortgage.

There is an exception to this Section 12(c) exception for the successor who acquired the indebtedness as a purchaser for value without knowledge of the asserted defect, lien, encumbrance or adverse claim, or other matter insured against by the policy as affecting title to the land.

2. Section 1(c) includes in the definition of "knowledge", the definition of "known" and provides that "knowledge" or "known" means actual knowledge, not constructive knowledge which may be imputed to the insured by reason of the public records or any other records which impart constructive notice. The question arises as to what is meant by actual knowledge. If there is a mortgage servicing clerk in a bank who is told of a defect in title, but the clerk never tells the manager of the Service Department or any officer of the bank of the defect, does

the bank have actual knowledge of such defect so as to void coverage under the title policy?

3. Section 1(f) contains the definition of "public records". This is much more restrictive than the prior definition in that it limits it to records "established under state statutes at the Date of Policy for the purpose of imparting constructive notice of matters relating to real property to purchasers for value and without notice". It is questionable whether all records presently searched by the title company before issuing a title commitment have been established by statute. Certain records, for instance, records in the Sheriff's office concerning foreign execution, in the Clerk of the Courts office concerning the judgments or pending suits, in the probate court's general index, or in bankruptcy court, are not specifically established under state statutes for the purpose of imparting notice of matters relating to real property. It is suggested that the insured obtain an endorsement to the policy, specifying the public records which must be searched and which should be included in the definition of public records.
4. The new form of policy now defines unmarketability of the title in Section 1(g) as an alleged or apparent matter affecting the title to the land which would entitle a purchaser, of an estate or interest described in Schedule A or the insured mortgage, to be released from the obligation to purchase, by reason of a contractual condition requiring the delivery of marketable title. The questions arise as to whether or not there must be litigation determining that a purchaser would be able to terminate the contract based on unmarketability, before the title company could be held liable under this provision, and whether the title company could be required to defend any unmarketability claim. Must the Court determine whether the purchaser should be released?
5. Section 2 deals with the continuation of insurance. It provides that the amount of insurance which shall be available to the insured, in the event the insured acquires title after foreclosure, or by deed in lieu of foreclosure, or any other legal manner which discharges the lien of the insured mortgage, shall be as set forth in Section 2(c). This provision is very similar to the provision contained in the 1970 policy, except that there is included in Subclause (2), in addition to the amount of the principal of the indebtedness, the interest thereon, expenses of foreclosure, amounts advanced to insure compliance with laws and to protect the lien of the mortgage, the "reasonable amounts expended

to prevent deterioration of improvements." This gives a benefit to the insured over the 1970 Policy provisions.

6. Sections 3 and 4 of the 1970 policy have been revised considerably and now appear as Sections 3, 4 and 5 in the 1986 policy. Section 3, provides that the insured must notify the company promptly of any litigation or any knowledge of any claim against the title or interest, which would be adverse to the title or interest being insured. If prompt notice is not given, the insurance shall terminate with regard to the matters for which the prompt notice was required unless the company was not prejudiced by the failure to give such notice.

In Section 4, the company agrees to provide for the defense of the insured in the litigation but limits its defense to only those "stated causes of action alleging a defect, lien or encumbrance or other matter insured against by this Policy". The company has the right to select counsel of its own choice, without any consultation with the insured, but it is subject to the right of the insured to object for reasonable cause. The company shall not be liable for, and will not pay, the fees of any other counsel, and will not pay for the defense of any matter which is not insured against by the policy. Previously, if there were some matters insured against and some matters not insured included in the litigation, the company would assume on the entire defense so as to avoid two counsels working at cross purposes. When requested by the company, the insured must furnish to the company, all reasonable and necessary witnesses and evidence, and take any other lawful actions which, in the opinion of the company, are necessary or desirable to establish the title to the estate, or interest, or the lien of the insured mortgage. If the company is prejudiced by the failure of the insured to cooperate, the company's obligation as to the insured under the policy shall terminate.

Section 5 provides that the insured must deliver to the company a proof of loss or damage signed and "sworn to by the insured claimant" within 90 days after the insured claimant shall ascertain the facts giving rise to the loss or damage. The proof of loss or damage shall describe the defect in, or lien or encumbrance on the title and other matters insured against by the policy which constitutes the basis of the loss and shall state to the extent possible, the basis for calculating the amount of the loss or damage. In addition, the insured is required to submit to examination under oath by representatives of the company, and is required to produce for examination, inspection and copying, at such reasonable times and places as may be designated by an authorized representative of the company, all records, books, ledgers, checks, correspondence or memorandums whether bearing a date before or after the effective date of the policy which pertain to the loss or damage. This could create problems for many insured in that there may be a confidential relationship between the insured lender and the borrower. For instance, a savings and

loan association is prohibited by law against furnishing any information about its customers unless it receives the authorization of its customer to do so. This would

terminate coverage under the policy if the insured fails to comply, or in the alternative it could cause a violation of law if the insured complies with the policy. Section 5 further provides that failure to disclose the information terminates the insurance. The Company agrees to keep the information confidential "unless, in the sole judgment of the Company, it is necessary for the administration of the claim".

7. Section 6 of the 1984 policy is substantially the same as Section 5 of the 1970 policy and provides that the company may tender the amount of the insurance and be released of any further obligation to defend. Some believe that the company should be obligated to clear up a title that it insured as marketable if unmarketability is claimed, or to take other action, rather than merely make a payment of the amount and walk away from the claim. In any event, the company had the right previously, so this is nothing new with respect to the policy.
8. Section 7 provides for the limit of liability of the company under the loan policy. Section 7(a) provides that the limit of liability is the least of (i) the amount of insurance, (ii) the amount of the unpaid principal indebtedness secured by the mortgage, (iii) the difference between the value of the estate as insured and the value of the estate with or subject to the defect. Section 2(c) also provides that the insurance would be the least of three amounts, but provides that one of the amounts would be the amount of the principal indebtedness remaining unpaid, plus the interest thereon, the expenses of foreclosure, the amount advanced to protect the lien of the mortgage or the security of the property, and reasonable amounts to prevent deterioration of the improvements. In Section 7(a)(ii), the amount is limited to the unpaid principal amount. It does not include interest, taxes which may be advanced or any other amounts advanced for the protection of the lien of the security of the property. Thus the company has again restricted its liability considerably. Section 7(c) provides that the company will only pay those costs, attorney's fees, and expenses incurred in accordance with Section 4 of the Conditions and Stipulation.
9. Section (B) provides that the amount of insurance decreases as payments are made on the principal of the indebtedness. The Section was expanded to provide that any voluntary partial satisfaction or release of the insured mortgage, whether by payment, satisfaction or release, shall reduce the insurance pro tanto. In many corporate financings today, you will have a substantial loan secured, not only by real estate, but also by equipment,

inventory, accounts receivable. For instance, a bank loans \$100,000 to a corporate entity which is secured by a lien on real estate valued at \$40,000

and a lien on machinery, inventory and accounts receivable valued at \$60,000. If \$40,000 of the \$100,000 loan is satisfied and assuming a \$40,000 loan policy was issued, is the insurance terminated even though \$60,000 is still owing on the loan? According to Section (B), the insurance would have terminated at that point, even though the lender would be relying upon the insurance for protection of its security until they paid. Any insured would be wise to obtain an indorsement clarifying the insurance coverage.

Section 12(b) permits an insured to release security, modify terms of payout or release collateral, provided the priority of the lien is not affected, but if done after insured has notice of claim, the Company is released to the extent its right of subrogation is impaired. This is similar to other forms of insurance.

10. Section 13, provides for compulsory arbitration. If either party requests arbitration, then both parties must submit to binding arbitration. At the March, 1987, Mid-Year Meeting of the ALTA, this was softened somewhat to provide that it shall be only binding arbitration for policies up to \$1,000,000 in amount. Beyond that, both parties must agree to arbitration in order to be subject to binding arbitration. The arbitration shall be in accordance with the Title Insurance Arbitration Rules. Arbitration is not covered by any rules of evidence and all types of evidentiary material may be submitted to the arbitrators. The arbitration is to be submitted to the arbitrators. The arbitration is to be secret so that there will be no published decisions relative to it and no guidance for future arbitration. It is the purpose of arbitration to achieve an equitable result, rather than determining whether any party has specific rights or liabilities under the contract. An insured should obtain an indorsement deleting the arbitration provision.
11. With respect to the Owner's Policy, a co-insurance clause has been added to Section 7(B) providing that, (i) if on the date of the policy the amount of insurance is less than 80% of the value of the land or the full consideration paid for the land, whichever is less, or (ii) if subsequent to the date of the policy an improvement is erected on the land which increases the value of the land by at least 20% over the amount of insurance stated in Schedule A, then the company shall only pay the loss pro rata in proportion to the amount of insurance on the date of the policy bears to the total value of the land on the date of the policy, or if improvements are made, the company will

only pay the loss pro rata in proportion to 120% of the amount of insurance

stated bears to the sum of the amount of insurance and the amount expended for the improvements.

**THE ALTA 1990 & 1992 POLICIES:** The ALTA 1990 policies are gradually replacing the 1987 policies. In each case, the text is exactly the same as the 1987 version, the only difference being that addition of an exclusion dealing with "creditors' rights". In the owner's policy, this exclusion is worded as follows:

*Any claim, which arises out of the transaction vesting in the insured the estate or interest insured by this policy, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws. [Emphasis added.]*

In the loan policy, the wording is slightly different:

*Any claim, which arises out of the transaction creating the interest of the mortgagee insured by this policy, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws. [Emphasis added.]*

The italicized language restricts the exclusion to the transaction which creates the estate or interest insured. In other words, if a *prior* transaction in the chain of title is attacked, the exclusion does not apply. The use of the 1990 policies will nevertheless vastly simplify the underwriting considerations present where a title may be vulnerable to this sort of challenge.

The ALTA 1992 policies were developed in response to objections of certain lenders to the broad wording of the "creditors' rights" exclusion found in the ALTA 1990 policies. They expressed concern that a literal reading of the exclusion could exculpate the title company from liability where (for example) a mortgage was not timely recorded (and thus was deemed "unperfected" under the Bankruptcy Code), even though the delay was caused by the title insurer.

The 1992 policies (formally dated 10/17/92) attempt to address such issues by modifying the exclusionary language. In the owner's policies, the exclusion is worded as follows:

"Any claim, which arises out of the transaction vesting in the insured the estate or interest insured by this policy, by reason of the operation of federal bankruptcy, state insolvency, or other similar creditors' rights laws, this is based on:

- (i) the *transaction creating the estate or interest insured* by this policy being deemed a fraudulent conveyance or fraudulent transfer; or
- (ii) the *transaction creating the estate or interest insured* by this policy being deemed a preferential transfer except where the preferential transfer results from the failure:
  - (a) to timely record the instrument of transfer; or
  - (b) of such recordation to impart constructive notice to a purchaser for value or a judgment or lien creditor." [Emphasis added.]

In the loan policies, the wording is slightly different:

"Any claim, *which arises out of the transaction creating the interest of the mortgagee insured* by this policy, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws, that is based on:

- (i) the *transaction creating the interest of the insured mortgagee* being deemed a fraudulent conveyance or fraudulent transfer; or
- (ii) the subordination of the interest of the insured mortgagee as the result of the application of the doctrine of equitable subordination; or
- (iii) the *transaction creating the interest of the insured mortgagee* being deemed a preferential transfer except where the preferential transfer results from the failure:
  - (a) of such recordation to impart notice to a purchaser for value or a judgment or lien creditor." [Emphasis added.]

As the italicized language suggests, the exclusion, like that used in the 1990 policies, is *transactional in nature*. In other words, its applicability is limited to circumstances where the estate or interest insured is subject to a flaw which renders it vulnerable to attack. The exclusion does not extend to situations where a prior transaction is the source of the problem. It is also note worthy that the loan policy exclusion makes specific reference to the *doctrine of equitable subordination*.

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**POLICIES AND  
ENDORSEMENTS  
Underwriting**

As a result of FannieMae Announcement 94-13, which amends Announcement M 07-91, effective November 1, 1991, FannieMae will not accept any ALTA Policy other than the 1992 Loan Policy.

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