TITLE CONSIDERATIONS IN CHAPTER 13 LIEN STRIPPING

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I. TITLE INSURANCE AND ALTERNATIVES

Several different methods of searching and examining the title to real estate are followed in the United States. These include a search of the public land records by the attorney, a search by an abstractor who compiles an abstract showing all recorded instruments affecting the land, and a search by the staff of title insurers or of title agencies that issue a commitment for title insurance. Paul E. Bayse, Clearing Land Titles §3, at 13-14 (2d ed. 1970 & Supp. 2004). In Wisconsin, there are three primary alternatives available to persons interested in obtaining information from a commercial title insurer or title agency: Title insurance, title reports (also known as "letter reports") and abstracts of title.

A. Abstracts of Title

"An abstract of title consists of a series of entries each of which contains a summary of the material parts of a recorded or filed instrument (including deeds, mortgages, easements, judgments and property taxes) affecting title to the property covered by the abstract. Altogether they furnish a history of the title beginning with the acquisition of the land involved from the United States Government and continuing through a series of transfers to the present record owner." Gary E. Sherman, I Wisconsin Practice §11.1 at 279 (1987).

B. Title Reports

Title reports vary considerably in format and content. Generally, a title report is a report prepared by a title company or title agency that reports information about the title that is limited to the information described in the title report. Typically, the title report states that the information compiled is limited to liens, defects and encumbrances filed since the date the latest deed was recorded, and no earlier. Title reports are used mainly be lenders, not purchasers, who for cost reasons are looking for a report that shows whether there are any mortgages or liens against the title since the date that the current owner acquired the title. The title report does not show the chain of title except for the period of time during which the current owner acquired the title. Thus, the title report would seldom show easements, covenants, conditions and restrictions that were recorded prior to the date that present owner acquired the title. The cost of a title report is often minimal. Title reports often contain disclaimers of liability. The title report is therefore unsuitable to most real estate sale transactions as evidence of the owner's title.

C. Title Insurance

Title insurance is a contract of indemnity that obligates the title insurer to pay loss as defined by the policy. Heyd v. Chicago Title Ins. Co., 218 Neb. 296; 354 N.W.2d 154 (1984). The purpose of title insurance "is to indemnify the insured for impairment of its interest due to failure of title as guaranteed in the title insurance report." Greenberg v. Stewart Title Guar. Co., 171 Wis. 2d 485, 493, 492 N.W.2d 147 (1992) [quoting Blackhawk Prod. v. Chicago Ins., 144 Wis. 2d 68, at 78, 423 N.W.2d 521 (1988)]. Title insurance consists of three documents: The commitment for title insurance, policy, and endorsements.

D. Why Title Insurance is Widely Accepted

Although earlier versions of the offer afforded the parties a choice of providing either an abstract of title or title insurance, the current standard offer to purchase, Form WB-11 Residential Offer to Purchase (7-1-11), requires that a commitment for title insurance be provided to the purchaser. Lines 340-342 provide:

> TITLE EVIDENCE: Seller shall give evidence of title in the form of an owner's policy of title insurance in the amount of the purchase price on a current ALTA form issued by an insurer licensed to write title insurance in Wisconsin. Seller shall pay all costs of providing title evidence to Buyer. Buyer shall pay all costs of providing title evidence required by Buyer's lender.

As a result, title insurance has become a standard requirement in the vast majority of Wisconsin real estate transactions. There are currently seven title insurers and several hundred title agents active in Wisconsin. However, all title insurers and title agents issue the same standard American Land Title Association ("ALTA") commitment and policy forms. Therefore, although there may be minor differences among companies, generally, the commitment's component parts will be the same regardless the company that issued it.

E. Component Parts of the Title Commitment

The commitment for title insurance or, as it was formerly known, binder or preliminary report, is prepared and issued for the purpose of apprising the proposed purchaser or lender of the status of the title before the transaction is closed and committing the title insurer, upon whose agreement to indemnify the transaction ultimately hinges, to issuing a policy. The commitment constitutes a detailed composite or profile of the subject matter, the underlying real estate title: The name of the owner, property description, a listing of mortgages, liens, taxes and matters ordinarily satisfied or released prior to a transfer of the title, and lastly, easements, restrictive covenants and other matters that usually survive the transfer of ownership. Seller and purchaser are advised to timely obtain a commitment so that they know for a certainty what liens and encumbrances affect the title and without delay make

arrangements or begin negotiations with the appropriate parties for their payment or release.

The commitment contains three distinct parts, known as schedules: Schedule A, Schedule B –Section I (or "Schedule B – Section 1"), and Schedule B – Section II (or "Schedule B – Section 2"). Each schedule is of indeterminate length, page or image numbers, and may be modified to incorporate by reference any number of attachments or documents. Depending upon the locale, title insurance providers may incorporate in the ALTA Commitment additional pages, exhibits or attachments, and provide copies of applicable easements, restrictive covenants, condominium declarations etc. Regardless the form or locale, the reader of the commitment must assure themselves that the commitment document that they possess is in fact the complete, not merely a portion of the, commitment, so that their examination of the commitment will in turn prove complete and accurate.

II. AVAILABILITY OF TITLE INSURANCE

A. How the Commitment Differs From the Underlying Title

The title commitment displays, at a minimum, the name of the current owner, the property description, and liens, defects and encumbrances that affect the title. From this information, the reader can ascertain what liens, defects and encumbrances affect the title. However, in contrast to abstracts of title, the chain of title is not revealed by the title commitment. Thus, by reading the commitment, it is not possible to know the names of former owners or mortgages that were satisfied. The title commitment is an encapsulated snapshot version, not a running history, of the title.

B. Who Does the Policy Insure?

The named insured party in the title insurance policy will almost invariably be the property's owner, a mortgagee or the owner of indebtedness secured thereby, or a lessee. With rare exceptions, insofar as owners are concerned, the title insurer will insure purchasers, and not individuals or entities that already own property, devisees or heirs, persons claiming title by adverse possession, transfer on death beneficiaries, non-titled spouses, shareholders of a corporation, LLC members, or individuals having acquired the title by operation of law. The proposed insured is not necessarily a specific individual or entity. For example, it is common practice in Wisconsin for counsel for the plaintiff that has commenced or will commence a mortgage foreclosure action to request issue a commitment naming as the proposed Insured a "purchaser to be named" or "qualified purchaser at sheriff's sale."

C. What is the Proposed Policy Amount?

The cost of title insurance is based upon the Policy Amount. The larger the Policy Amount, the larger the premium will be. The proposed Policy Amount is almost

always the sale price or, if the proposed insured is a prospective lender, the amount of indebtedness to be secured by a new mortgage. In the case of commitments issued at the request of counsel for a foreclosing loan servicer or bank, the proposed Policy Amount is a nominal amount, such as $15,000.00. It appears that from common practice, counsel for the bank is not dissuaded from requesting a nominal Policy Amount by the prospect of coverage insufficient to compensate the insured against an unsatisfied lien, defect or encumbrance during the pendency of the foreclosure suit.

D. Against What Types of Liens, Defects and Encumbrances Does the Policy Indemnify?

The standard owner's policy of title insurance of prevailing usage in most states, the American Land Title Association (ALTA) Owner's Policy (6-17-06), affords specific forms of coverage or Covered Risks. The Owner's Policy indemnifies the Insured against ten (10) identified matters or "Covered Risks." Among the risks is non-vesting of title:

> Subject to the Exclusions of Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions, the Company insures, as of Date of Policy and, to the extent stated in Covered Risks 9 and 10, after Date of Policy, against loss or damage, not exceeding the Amount of insurance, sustained or incurred by the Insured by reason of: 1. *Title being vested other than as stated in Schedule A* (emphasis added).

Title insurance also insures Smith against loss occasioned by the existence of *liens, defects or encumbrances* not excepted or excluded from coverage and that were, for any number of reasons, the result of non-payment or non-release, and not disclosed by the seller, Anderson.

E. Exceptions From Coverage

Schedule B-II of the commitment removes coverage for matters that may otherwise be covered by stating: "The policy or policies to be issued will contain exceptions to the following unless the same are disposed of to the satisfaction of the company." A list of numbered or lettered paragraphs that describe matters will then appear. These paragraphs describe matters against which the title insurer will not provide coverage, but which are subject to possible further discussion or negotiations.

F. Exclusions From Coverage

The Policy contains several exclusions from coverage from loss, including those occasioned by:

1. Any law, ordinance, permit, or governmental regulation (including those relating to building and zoning) restricting, regulating, prohibiting, or relating to the occupancy, use, or enjoyment of the Land;

2. Rights of eminent domain.

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 (however, this does not modify or limit the coverage provided under Covered Risk 9 and 10); or

   (e) resulting in loss or damage that would not have been sustained if the Insured Claimant had paid value for the Title.

4. Any claim, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws, that the transaction vesting the Title as shown in Schedule A, is

   (a) a fraudulent conveyance or fraudulent transfer; or

   (b) a preferential transfer for any reason not stated in Covered Risk 9 of this policy.

Exclusion 3(a) of the title insurance policy defendants issued provides: 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: (3) Defects, liens, encumbrances, adverse claims or other matters: (a) created, suffered, assumed or agreed to by the Insured Claimant. Does the Policy indemnify the Insured against a federal tax lien that was filed against the Insured Owner? All evidence and testimony regarding the matter established that plaintiff had no responsibility for the payment of taxes and in no way agreed to the placement of a lien. Archambo v. Lawyers Title Ins. Corp., No. 202289, 2002 WL 31013194 (Mich. Ct. App. Sept. 3, 2002) (unpublished).

G. The Difference Between Exceptions and Exclusions

Schedule B – Section 2 of the commitment ("Schedule B-2") contains *exceptions* that will appear in Schedule B of the policy. The policy jacket contains *exclusions* from coverage. Though both limit or remove coverage, exceptions are distinguishable from exclusions, which will appear elsewhere in the policy: *Exclusions* are direct limitations on coverage that exclude certain matters the policy was never designed to cover, such the insured's own acts or unenforceability of the mortgage caused by usury or failure to comply with truth in lending laws. *Exceptions* are matters for which coverage is not given though the policy would ordinarily insure and indemnify against a loss arising from the matter excepted. "Title insurance policies contain Exclusions from Coverage which limit the coverage clauses to make it clear that there

is no coverage for matters that are, by their nature, outside of the scope of a title insurance policy. In general, these exclusions relate to matters that cannot be insured against on other than a pure casualty basis…", Raymond J. Werner, The Basics of Title Insurance in Title Insurance: The Lawyer's Expanding Role 19 (James M. Pedowitz ed. 1985).

III. LIENS, DEFECTS AND ENCUMBRANCES

A. Construction Notice and the Recording System

Prospective purchasers and lenders that neglect to investigate the title and timely negotiate the release of encumbrances are exposed to a host of otherwise unknowable matters. Kordecki v. Rizzo, 106 Wis.2d 713, 317 N.W.2d 479 (1982). A basic premise of the recording system is that purchasers are charged with notice of liens against the title that were duly recorded, though the purchaser knew nothing about them at the time of purchase. In addition, statutory liens, tax liens and judgment liens constitute liens against real property regardless of the purchaser's actual knowledge.

B. What Public Land Records Impart Constructive Notice?

State law governs what records impart constructive notice to prospective purchasers. A search and examination of a title is incomplete unless it extends to all of the following offices of the county where the land is located:

1. Register of deeds
2. Clerk of circuit courts
3. County treasurer
4. Probate court
5. United States bankruptcy court (Dane, Eau Claire and Milwaukee Counties)
6. United States district court (Dane, Eau Claire and Milwaukee Counties)

C. Pitfalls of the Public Land Records

The public land records for all their benefits expose purchasers, lenders and investors to risks that cannot, though the title of the purchaser appears unequivocally vested in the seller or mortgagor at date of closing, be entirely eradicated. Though public land records of real estate ownership are largely static, they are nonetheless capable of being manipulated or altered in subtle ways that can prove injurious to the real estate's investor. The congenital weakness of the public land records system is occasional misfeasance concerning maintenance of the *indices*. Indices are books, card indexes or electronic search engines created and maintained by public

administrative personnel that guide the records user, professional and lay user alike, to the source of title by listing all deeds, mortgages, easements and other instruments that affect the title to specific parcels, or land owned by specific individuals or entities. "…Only a few of the statutes make the index an essential part of the record. Since the latter is the case in Iowa, North Carolina, Pennsylvania, Washington, and Wisconsin, a record in these states is ineffective for imparting constructive notice if it is not indexed or if there is a material defect in the indexing." 4 American Law of Property 603-605 (1952). Shove v. Larsen, 22 Wis. 142 (1867). An attorney who delivered the mortgage of his client to the register of deeds in proper form for recordation, but did not verify that the mortgage was properly indexed, was liable to the client when the mortgagor later died without have paid the note, and the real estate was sold to a bona fide purchaser who, because of the register's error in indexing, had no constructive notice of the unsatisfied mortgage. Antonis v. Liberati, 821 A.2d 666 (Pa. 2003). Indexing in the public tract index remains a prerequisite for constructive notice, though the county register of deeds may have adopted a better parallel computerized index that is used by administrative personnel and public users. Associates Financial Services v. Brown, 2002 WI App, 258 Wis. 2d 915, 656 N.W.2d 56 (Ct. App. 2002). Judgments that are rendered and entered by circuit court but not properly entered in the docket and of which the purchaser of the debtor did not when consideration was paid have actual knowledge do not constitute liens against real property.

> For such a judgment to become a lien upon the debtor's real property, other than the homestead, it must, under sec. 270.79, Stats., first be docketed in the county where such real property is found. To be so docketed it must, under sec. 270.74, be entered by the clerk in a book or books to be kept by him--that is, in a judgment docket which may be arranged alphabetically (which was not the case here), or, if the judgment docket is not so arranged, then also in an alphabetical index to accompany such docket.
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> Wisconsin Mortgage & Sec. Co. v. Kriesel, 191 Wis. 602; 211 N.W. 795 (1927)

Though all documents, conveyances and instruments recorded, filed or docketed are in fact safely protected from loss or alteration in the courthouse environs, if the indices themselves are incomplete or inaccurate, the purchaser's perception of the title will remain so as well.

IV. MORTGAGES

A. Mortgage as an Encumbrance

Where the contract for sale of real estate required the seller to deliver marketable title, specific performance by the vendor was denied. "(I)n the case at bar, this Court finds that the Contract at issue does not provide [the Gigantes] with the remedy of specific

performance. The unsatisfied mortgage is a defect in the title**."** Lopes v. Sappington, 958 So.2d 483, 485 (Fla. 4th DCA 2007). Marketable title is title that is free from encumbrances and is of such a character as to assure to the purchaser the quiet and peaceable enjoyment of the premises. Thus, the failure to discharge a mortgage is a cloud that renders title unmarketable**.** Thorpe v. Papadelis**,** Docket No's. 304499, 304922, 2013 WL 1689281 (Mich. Ct. App. April 18, 2013).

Not all recorded mortgages impair marketability For example, a mortgage granted by a party who never owned the property, though recorded, did not impair the marketability of the title. Flemetis v. McArthur, 119 Utah 268 (1951).

B. Effect of Mortgages Improperly Satisfied

Recordation of a satisfaction does not necessarily mean that the mortgage should be regarded as duly satisfied, as where the entity that satisfied the mortgage was not the mortgagee. Mortgages, assignments of mortgages, and satisfactions of mortgages require attention for accuracy of detail before it can be established that the mortgage does not impair the title. Thus, the existence of mortgages that though satisfactions were recorded, were improperly satisfied impair the marketability of the seller's title.

> Mortgages are defectively satisfied of record and discrepancies exist in the names of grantors and titleholders, illustrated as where one takes title as John J. Jones and conveys as J. J. Jones. Like discrepancies between the names of the one who should satisfy and the one who executes the satisfaction of mortgages constitutes the defect in most of the satisfactions. The mortgages defectively satisfied are eleven in number, ranging in date of execution from 1840 to 1870. In one of them, dated 1854, there is no similarity between the name of the mortgagee and the one who executed the satisfaction, and no assignment of the mortgage is shown. This leaves the mortgage unsatisfied of record.
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> Douglass v. Ransom, 205 Wis. 439, 237 N.W. 260 (1931).

C. Where Loan Was Paid but Mortgage Was Not Satisfied

What is the effect of a mortgage that secured a loan that was paid or repaid but for which no satisfaction was issued or recorded in the office of the register of deeds?

> Wisconsin courts have long recognized a strict rule that a mortgage is extinguished by payment of the underlying note. See Connor v. Connor, 218 Wis. 336, 343, 259 N.W. 729 (1935) (after underlying debt was satisfied, mortgage no longer existed); Marshall & Ilsley Bank v. Ewig, 230 Wis. 353, 356–57, 283 N.W. 795 (1939) (mortgage ceased to exist after the incident indebtedness was satisfied); see also In re Carley Capital Grp., 117 B.R. 951, 954 (Bankr.W.D.Wis.1990) (same). " '[A] mortgage is not property at all independent of the debt it secures. The extinguishment of the debt ... extinguishes the mortgage.' " Marshall & Ilsley Bank, 230 Wis. at 357, 283 N.W. 795 (quoted source omitted).

Schanon v. Studtmann, No. 12-8423, 2012 WL 1172169 (Wis. Ct. App. April 10, 2012) (unpublished).

D. Affidavit of Satisfaction, §708.15

Effective December 12, 2013, 2013 Wisconsin Act 66, created Section 708.15, Stats. The law was enacted with the support of the Wisconsin Land Title Association, a state association of title agents and title insurers. The law introduced a new method of satisfying mortgage of "residential property" (property that is used primarily for personal, family or household purposes and is improved by one to 4 dwelling units). The closing agent that paid a loan secured by a mortgage, if they provided a notification to the secured party that included the requisite information may after 30 days have elapsed from the date of the notification sign and submit for recording an affidavit of satisfaction of mortgage. The affidavit of satisfaction is effective only if it is signed by 2 persons who are employees of, and who have been authorized by, the title insurance company to sign the affidavit on behalf of the title insurance company. Upon recording, an affidavit of satisfaction that substantially complies with the statute, though not executed by the mortgagee, constitutes a satisfaction of the mortgage.

Sec. 708.15 also enables the recording of satisfactions for mortgages that were paid prior to the new law's effective date but never satisfied, of which there are multitudes. Thus, the statute authorizes the closing agent that paid a mortgage loan in 2004, where the mortgagee is a bank no longer in business, was taken over by the FDIC or was acquired by another bank, and therefore makes it possible to rid the public records of unsatisfied residential mortgages. In the event that neither the individual who handled the payment after the closing is locatable, nor is the title agency by which he was employed still in operation, is it possible for the title insurer to authorize a different agent to satisfy the mortgage? Yes. Sec. 708.15(8)(a) provides: "Only a title insurance company, acting directly or through an authorized agent, may serve as a satisfaction agent under this section." Sec. 708.15(8)(d) provides: "The satisfaction agent is presumed to be acting for, and with authority from, the entitled person if the satisfaction agent, directly or through an agent, assisted in completing full payment or performance of the secured obligation…" It is anticipated that title insurers will likely avail themselves of the statute as a basis for signing and recording, either by its employees or agents, affidavits of satisfaction of such mortgages. It is also anticipated that title insurers will continue to issue letters of indemnity.

V. LIEN STRIPPING IN CHAPTER 13

A. Title Insurer Criteria When Analyzing Liens, Defects and Encumbrances

Deletion from the commitment by the title insurer of a lien, defect or encumbrance of which it is aware usually signifies that the title insurer has elected to provide coverage against the lien, defect or encumbrance. When analyzing the title for the purpose of determining whether to delete an unsatisfied lien, defect or encumbrance ("Title Defect"), the title insurer generally bases its determination on state and federal law concerning validity, enforceability and marketability. Although the distinction is simplistic, there are three possibilities:

- The Title Defect is one that is enforceable and thus will not be deleted.
- The Title Defect is one that is unenforceable and time-barred by applicable law and thus will be deleted.
- The Title Defect is one that requires further information before a conclusive determination can be finalized over whether the Title Defect will be deleted.

In the case of some Title Defects that are revealed by a search of the title, the Title Defect will be initially raised as a requirement or exception in the commitment. The title insurer is uncertain based upon its analysis whether the Title Defect is enforceable. Thus, an unsatisfied mortgage that was granted by a predecessor in title will usually be shown as an exception in the commitment. When unequivocal evidence establishing that the loan was paid in full, or an indemnity issued by another title insurer that indemnifies against the unsatisfied mortgage is received, the title insurer may ultimately agree to delete the unsatisfied mortgage.

B. Order Stripping Lien or Avoiding Lien by Confirmed Plan

1. Can Chapter 13 Debtor utilize Section 506(d) to strip off wholly unsecured lien?

Title insurers are aware of the split of authorities and the conflicting decisions concerning whether a Chapter 13 debtor who is ineligible for a discharge may strip off wholly unsecured junior liens within four years of a Chapter 7. Congress did not intend to prevent lien stripping through § 1328(f)(1), and wholly unsecured junior lien could be stripped off. In re Fair, 450 B.R. 853 (E.D.Wis.2011). Debtor who, having recently obtained discharge in a prior Chapter 7 case, was statutorily ineligible for discharge in Chapter 13, could not use Chapter 13 plan to strip off a junior mortgage lien. Lindskog v. M&I Bank, 480 B.R. 916 (E.D.Wis. 2012). Debtor who, due to his receipt of discharge in prior Chapter 7 case, was ineligible to receive Chapter 13 discharge even if he successfully completed his payments under plan could not use his successive Chapter 13 filing to strip off a wholly unsecured junior mortgage lien. In re Jarvis, 390 B.R. 600 (Bankr.C.D.Ill.2008).

Unless the law is settled, it is not appropriate to project a future ruling that could retroactively validate mortgages that were stripped down by lower courts, resulting in enforcement and a loss under the policy issued to a subsequent purchaser of the property. See In re Jablonski**,** 139 B.R. 15 (Bankr.W.D.Pa.1992)**.** Generally, title insurers will evaluate each transaction, examine the Chapter 13 case to verify at a minimum that a discharge was entered, and then further review the facts and circumstances of the transaction before determining whether the mortgage will be deleted from the commitment.

2. Recordation of order

Assuming that the title insurer agrees that the order stripping off a mortgage is sufficient as a basis for issuing a title policy that omits the mortgage, what minimum information should the order contain? The order should contain a property description ("legal description") of the land subject to the mortgage. Property descriptions sometimes change over time. For example, land described by metes and bounds could conceivably become the subject of a new subdivision plat, certified survey map or condominium plat. Once the subdivision plat has been recorded, the "lots in that plat shall be described by the name of the plat and the lot and block in the plat for all purposes." §236.28, Stats. Similar, once a certified survey map is recorded, reference in subsequent conveyances shall be to the certified survey map. §236.34(3), Stats.

If in sequence, a certified survey map ("CSM") was recorded by which two lots in a previously recorded subdivision plat were combined, which is the correct description that should be used on a post-CSM conveyance: The CSM lot, or the two subdivision plat lots?

Example:

Alex acquired Lots 14 and 15, lots in the recorded plat of Pharaoh Subdivision. Alex later granted a first mortgage and second mortgage. Subsequently, he applied for approval of a new certified survey map so that he could combine both lots to make a larger site on which to construct a new home. The CSM was recorded. Alex then filed a Chapter 13 petition and now seeks to strip off the wholly unsecured second mortgage.

What should the order stripping off the mortgage use as the property description: "Lot 1 of CSM 836", or "Lots 14 and 15 of Pharaoh Subdivision?" Answer: "Lot 1 of CSM 836" should be used, so that the order is duly indexed by the register of deeds and is, when a future search made, shown in the chain of title for the description as it is now known, and not the subdivision plat as it was formerly known.

3. Appeal

In the event that the closing for the sale of real estate is to occur prior to the appeal period having elapsed, the title insurer will raise an exception for possible appeal:

> Consequences of any appeal from the Order entered in United States Bankruptcy Court for the Eastern District of Wisconsin in Case No. _____, _____, Debtor.