

PENN ATTORNEYS

TITLE ALERT

DATE: 8/17/07

RE: Title Alert 2007-29

Deed In Lieu of Foreclosure

In today's market where adjustable interest rate changes may cause monthly mortgage payments to become unaffordable, we may see an increase in the number of transactions that involve a "Deed in Lieu of Foreclosure." A Deed in Lieu of Foreclosure is used by a mortgagor (i.e. the borrower) to convey all right, title and interest in the subject real property to the mortgagee (i.e. the lender) to satisfy borrower's obligation to repay a loan which is in default. This Deed affords the borrower immediate relief from the obligation to repay the defaulted loan, and precludes the borrower from being sued in a foreclosure action. The lender's advantages are a reduction in the time and cost usually associated with foreclosure, sheriff's sale and possible eviction. The disadvantage to the lender is that no liens are divested as a result of their accepting a Deed in Lieu of Foreclosure.

There are two common scenarios in which you may encounter a Deed In Lieu of Foreclosure:

1. Insuring a **purchaser from the lender** who acquired the property by a Deed in Lieu, or
2. Insuring **the lender grantee** receiving the Deed in Lieu from the defaulting borrower.

1. To insure a purchaser buying the property from the lender who is the vested Grantee pursuant to a Deed in Lieu of Foreclosure:

- If the mortgage is not satisfied of record, it must be satisfied at this time unless the new owner is expressly taking the property subject to the mortgage, and then the mortgage will be shown as an exception on Schedule B of the new Owner's Policy.
- Be cautious to confirm that the lender vested with title on the Deed in Lieu is the same as the Seller/grantor and the same as the named lender on the outstanding mortgage. If the name shown on the outstanding mortgage of record is different than the Seller/grantor, check for recorded Assignments of Mortgage. If you cannot so confirm, because there are no recorded Assignments, then production and recording of a satisfaction piece is required.
- As usual, a full search must be run for liens, judgments, outstanding taxes and municipal claims, paying particular attention to those in the name of the grantor who conveyed the property to the lender by Deed in Lieu, any and all of which must be paid, released or satisfied before Penn Attorneys can insure the new purchaser.

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2. To insure *the lender's fee simple interest* when accepting a Deed In Lieu of Foreclosure from its mortgagor in default, we will raise the following on the commitment:

- Deed in Lieu of Foreclosure as the instrument required to create the interest to be insured, to be signed by all record title holders.
- Agreement and Estoppel Affidavit must be executed by defaulting mortgagors/grantors, and by the lender/grantee.
- There is no requirement at this time that the defaulted mortgage be satisfied of record, **but if it is not so satisfied the Owner's Policy will contain a Schedule B exception for the subject mortgage** because the vesting of the fee simple interest in the lender does not necessarily create a merger with its mortgage obligation.
- If the lender to be insured requests creditor's rights coverage, Penn Attorneys will consider issuing such coverage upon specific review and underwriting.

The entitled “**Deed in Lieu of Foreclosure**” is usually a special warranty deed, and following the recital describes that grantor is making the conveyance voluntarily, and that grantor is receiving satisfaction of the mortgage obligation as recorded mortgage book X page Y. If there are any other liens, judgments, outstanding property taxes or municipal claims, all must be paid, released or otherwise discharged as usual before we insure the lender **unless** the lender agrees to take subject to these items, in which case they will remain as exceptions on the title policy being issued.

The **Agreement and Estoppel Affidavit** is an agreement between the parties that among other things, defines the terms of the agreement to provide the Deed, lists the amount owed, that the grantors will receive a discharge of their mortgage obligation, and the grantor's understanding that the Deed is an absolute conveyance of the full right, title and interest in the property. This document sometimes contains a statement of whether or not the lender intends for the mortgage obligation to merge with lender's fee simple interest. It is not recorded, but is further evidence that the transaction was voluntary, and that the grantor understands that he/she/they is/are giving up the property in exchange for a discharge of a loan obligation, when executing the Deed.

IMPORTANT NOTE re: Payment of Realty Transfer Tax: transfer tax is not required to record a Deed in Lieu of Foreclosure ***EXCEPT in Philadelphia***:

- **-PHILADELPHIA CITY TAX WAIVED IF:** The loan in default that is the subject of the Deed in Lieu is a purchase money mortgage **BUT ONLY IF** the borrower/grantor on the Deed & the lender/grantee on the Deed are both natural persons (i.e. the lender/grantee cannot be an institutional lender or bank).
- **-3% TAX DUE IF:** the loan is not a purchase money mortgage between two natural persons as described above, then you must pay to the City 3% of either:
 - - the fair market value of the property using the common level ratio, *if only nominal consideration* is shown on the Deed, or
 - - the amount of debt being forgiven by the lender *if that amount is being shown as the consideration* on the Deed.
- -In all areas, the 1% usually payable to the Commonwealth of Pennsylvania is always excluded.

This alert is designed to provide you with an overview of the usual factual scenarios surrounding Deed in Lieu of Foreclosure transactions. There are many variations and we welcome discussion of your particular transaction prior to requesting title insurance. As always, if you have any questions, please contact your servicing Penn Attorneys office.