

Title Insurance Coverage for “Unmarketability of the Title”

By John C. Murray
©2007

Introduction

The 1992 American Land Title Association (“ALTA”) Owner’s and Loan title-insurance policies provide coverage (subject to the policy exclusions and exceptions and the policy conditions and stipulations) “against loss or damage, not exceeding the Amount of Insurance stated in Schedule A, sustained or incurred by the insured by reason of: . . . 3. Unmarketability of the title.” “Unmarketability of the title,” in turn, is defined in Section 1. (g) of the Conditions and Stipulations section of the 1992 ALTA Owner’s Policy as “an alleged or apparent matter affecting the title to the land, not excluded or excepted from coverage, which would entitle a purchaser of the estate or interest described in Schedule A to be released from the obligation to purchase by virtue of a contractual condition requiring the delivery of marketable title.” In the 1992 ALTA Loan Policy, “Unmarketability of the title” is defined in Section 1. (g) of the Conditions and Stipulations as “an alleged or apparent matter affecting the title to the land, not excluded or excepted from coverage, which would entitle a purchaser of the estate or interest described in Schedule A or the insured mortgage to be released from the obligation to purchase by virtue of a contractual condition requiring the delivery of marketable title.”

The 2006 standard Owner’s and Loan Policy forms, adopted as of June 17, 2006, revised the definition of “unmarketable title” in the policies (new condition 1(k) in the Owner’s Policy and new condition 1(m) in the Loan

Policy). The 2006 policy definition in both the Owner's and Loan Policy has been expanded, resulting in (1) deletion of the phrase "not excluded or excepted from coverage," and (2) coverage for loss that occurs when grantees of the insured interest besides purchasers, including lessees or lenders, are released from their obligations due to a contractual condition requiring the delivery of marketable title. This additional coverage is not provided by the 1992 ALTA Policies.

But these policy definitions do not answer the question of what exactly is covered by the insuring provision for a claim based on "unmarketability of the title." This article will discuss the definitions, distinctions and guidelines developed by case law in making this determination.

Determination of "Unmarketability" Claim

The question of marketability may arise in many contexts, including the following:

1. An unreleased mortgage in the chain of title;
2. A missing signature in a document in the chain of title;
3. A transfer from a decedent without a proper probate proceedings or a right of survivorship;
4. A "wild" deed or mortgage; an apparent violation of restrictions or covenants affecting the property;
5. An encroachment, easement, or disputed boundary location;

6. A forgery or questionable signature on a document in the chain of title;
7. A deed recorded long after the death of the grantor;
8. A vesting in reliance on an off-record, defective, or illegible power of attorney;
9. A tax or judgment lien against a name matching a grantor's name;
10. Incorrect parcel descriptions;
11. A jurisdictional or other defect in a court action or proceeding (including defective notice or service of process) from which title to the insured property is derived;
12. Unresolved conflicts between two surveys;
13. A conveyance while a bankruptcy stay remains in effect; and
14. Ambiguous documents in the chain of title.
15. A right of reverter in the chain of title.

Unlike other types of claims, there need not be an "adverse claimant" in order to raise an unmarketability claim under the title policy. The mere possibility of a "cloud" on title, sufficient to justify a potential purchaser's or lender's refusal to buy or lend on the property, is enough to trigger coverage under the ALTA Owner's and Loan Policies. (But a perceived defect in title, which presents no potential claim for coverage under a title policy because it does not affect the status of title to the property, cannot

otherwise provide coverage under the insuring provision for unmarketability of the title.) The purpose of this particular insuring provision is to provide coverage, even when there may not be an adverse claim or present loss, in those cases where a question of title is significant enough to justify the refusal of a potential purchaser or lender to consummate the transaction. The provision has nothing to do with the physical condition of the real property, no matter how significantly the problem may affect the market value of the property or the ability of the insured party to sell or encumber it.

The insured may suffer a loss, when selling or mortgaging a property as a result of a title defect that was not discovered or disclosed in the original title search, that can't be adequately measured by (as stated in Section 7(a) of the Conditions and Stipulations of the ALTA Owner's and Loan Policies for calculation of loss) "the difference between the value of the insured estate or interest as insured and the value of the insured estate or interest subject to the defect, lien or encumbrance insured against by this policy." For example, if the buyer of a property refuses to purchase it because the seller is unable to deliver title in the condition specified in the purchase agreement, the loss to the insured triggered by the inability of the seller to convey the property in the condition agreed to may be different than a loss otherwise incurred by the insured after the closing. *See Native Sun Investment Group v. Ticor Title Ins. Co.*, 189 Cal. App. 3d 1265, 1274 (Cal. Ct. App. 1987) ("diminution in value is not the only means of drawing a causal connection between proven damages and a title defect").

Policy Coverage Limited to Title Defects

As noted above, unmarketability of the title is not necessarily the same as reduction in market value. Title to

real property can be marketable even if the land is unsalable or unusable. What makes a title unmarketable is a problem with “clean” ownership. In general, “[a] difference exists between economic lack of marketability, which relates to physical conditions affecting the use of the property, and title marketability, which relates to defects affecting legally recognized rights and incidents of ownership. One can hold perfect title to land that is valueless, and one can have marketable title to land while the land itself is unmarketable.” 43 AM. JUR. 2d, *Insurance*, § 528.

See. e.g., Chicago Title Ins. Co. v. Investguard, Ltd., 215 Ga. App. 121, 123 (Ga. Ct. App. 1994) (“a difference exists between economic lack of marketability, which relates to physical conditions affecting the use of the property, and title marketability, which relates to defects affecting legally recognized rights and incidents of ownership”); *Hocking v. Title Ins. & Trust Co.*, 37 Cal. 2d 644, 651 (1951) (“One can hold perfect title to land that is valueless: one can have marketable title to land while the land itself is unmarketable”); *Sec. Union Title Ins. Co. v. RC Acres, Inc.*, 269 Ga. App. 359, 362 (2004), *cert. denied*, *RC Acres, Inc. v. Sec. Union Title Ins. Co.*, 2004 Ga. LEXIS 1068 (Ga. Nov. 22, 2004) (“[the insured] had no economic loss from the recorded flowage easement, because the fair market value of the purchase price already reflected the encumbrance of the easement in the price willingly paid for it.”); *Denny’s Restaurants v. Security Union Title Ins. Co.*, 71 Wn. App. 194, 211 (1993) (“although resale value is almost always detrimentally affected by unmarketability, it does not necessarily follow that, when the resale value of property drops because of the physical condition of the land, the land is unmarketable. In other words, a distinction exists between marketability and merchantability”); *Riordan v. Lawyers Title Insurance Corp.*, 2005 U.S. Dist. LEXIS 6784 (D. New Mexico, March 3, 2005), at *12 (“A difference exists between economic lack of marketability, which

relates to physical conditions affecting the use of the property, and title marketability, which relates to defects affecting legally recognized rights and incidents of ownership”); *Division Eight Block v. Golden Eagle Ins. Corp.*, 121 Cal. App. 4th 186, 196 (Cal. App. 2d Dist. 2004) (denying coverage under title policies because “those policies do not insure against a reduction in the market value of the land”); *Sinks v. Karleskint*, 130 Ill. App. 3d 527, 530 (Ill. App. Ct. 1985) (“Merchantability does not equate with market value or marketability. Numerous factors may affect the market value of land and unquestionably access to a public way is such a factor; however, if the title is secure against defects in the statutory warranties, the title is merchantable. It is only defects in title affecting market value that result in unmerchantability”); *Haines v. Old Republic Nat’l Title Ins. Co.*, --- P.3d ---, 2008 WL 731397 (Wyo.), 2008 WY 31 (March 20, 2008) (ruling, in matter of first impression, that public road provided access and made title marketable, and therefore title policy did not require insurer to obtain recorded easement or right of access); *Riordan v. Lawyers Title Ins. Corp.*, 393 F.Supp. 2d 1100, 2005 U.S. Dist. LEXIS 6784 (March 3, 2005) at *12 (holding title policy did not cover loss due to lack of vehicular access to property, and stating that “[d]efects in the physical condition of the property do not constitute unmarketability of the title”); *House v. First Am. Title Co.*, 2006 Ind. App. LEXIS 2472 (Ind. Ct. App Dec. 8, 2006), at *5 (holding that injunction against using septic system and field on insured’s property was not covered by title insurance policy, because “the order of injunction may have affected the property’s market value, but never affected [the insured’s] title”); D. Barlow Burke, LAW OF TITLE INSURANCE *Law of Title Insurance* § 3.2.3 (2nd ed. 1993) (“An insured can have perfect legal title, worth nothing”).

As noted above, title-policy coverage for unmarketability of the title applies only to claims resulting

from title defects; unmarketability problems relating to the physical condition or use of the property, or its economic or market value, are not covered by the title policy. *See, e.g., Super Fitness of Malden v. Wig Realty Trust*, 2001 Mass. Super. LEXIS 663 (Mass. Super. Ct. 2001), at *24 (“[t]he physical state of the land does not affect title marketability”). For example, off-record environmental contamination or hazardous waste at the property, damage to improvements on the property, and the existence of zoning restrictions or regulation of the use of the property, are not risks covered by the insuring provisions of the ALTA Owner’s and Loan policies. Such matters do not constitute a “defect, lien or encumbrance,” and do not affect the marketability of title.

With respect to the disallowance of unmarketability claims based on environmental contamination at the insured property, *see McManus v. Rosewood Realty Trust*, 143 N.H. 78, 80 (1998) (presence of contamination did not affect marketable title; court stated that “there is a difference between economic lack of marketability, which relates to physical conditions affecting the use of property, [and] title marketability, which relates to defects affecting legally recognized rights and incidents of ownership. One can hold perfect title to land that is valueless; one can have marketable title to land while the land itself is unmarketable”); *Lick Mill Creek Apartments v. Chicago Title Ins. Co.*, 231 Cal. App. 3d 1654, 1663 (1991), *review denied*, 1991 Cal. LEXIS 4097 (Cal. Aug. 29, 1991) (possibility of imposition of lien for cleanup costs did not make hazardous waste an encumbrance on title or impair its marketability; insuring provisions of title policy did not provide coverage for physical condition of land); *Chicago Title Ins. Co. v. Kumar*, 24 Mass. App. Ct. 53, 56-57 (1987) (rejecting defendant insured’s argument that possibility that future lien might attach to property, and potential liability for cleanup of hazardous material, rendered title

unmarketable; court stated that “we perceive a difference between the condition of the title to land and the physical state of the land”); *Humphries v. Ables*, 789 N.E.2d 1025, 1033 (Ind. Ct. App. 2003) (“marketable title may be transferred even if there is contamination upon the property which is to be conveyed,” and stating further that, when addressing marketable title, “we are to concern ourselves with issues that affect the *possessory* title of the owner, such as covenants, easements, leases, liens, boundary disputes, gaps in the chain of title, and adverse possession” (emphasis in text)); *Rood v. Commonwealth Land Title Ins. Co.*, --- A.2d ---, 2007 WL 3026013 (Pa. Super.), 2007 PA Super 315 (Oct. 18, 2007) (duty of title company is only to search “public records” that affect title to the property; policy does not protect against existence of abandoned septic tank on insured property even though local township had notice of it in its “Record of Sanitary Drainage and Plumbing Fixtures”).

This same rule of law applies with respect to property insurance in general. *See, e.g., Block v. Golden Eagle Ins. Corp.*, 121 Cal. App. 4th 186, 196 (Cal. App. 2d Dist. 2004) (insured suffered no damage or loss under property insurance policy because she was not obligated to incur any cleanup expenses for environmental contamination on the property; court, finding support for its position in *Lick Mills, supra*, stated that “there is nothing in the language of the policies present here that would cause an insured reasonably to expect there was coverage against the simple diminution in the market value of its property resulting from the condition of that property, even if it were related to the environmental condition of the property”).

Matters relating to the condition (or regulation) of the land (other than environmental contamination) generally do not render title to the land unmarketable or give rise to a claim under a title insurance policy. *See, e.g., Elysian*

Investment Group v. Stewart Title Guaranty Co., 105 Cal. App. 4th 315, 321 (Cal. App. 2d Dist. 2002) (recorded notice of substandard improvements did not give rise to coverage under title insurance policy, as "defect, lien or encumbrance" or as matter resulting in "unmarketability of the title," where notice merely provided warning about physical condition of land and applicable building and zoning requirements; court stated that "[t]here is no coverage [under a title policy] for physical conditions of property that merely affect land value"); *Sperling v. Title Guarantee & Trust Co.*, 227 A.D. 5, 9 (N.Y. App. Div. 1929), *aff'd* 170 N.Y. 613 (1930) ("a change of grade which concerned the physical condition of the land abutting the plaintiff's parcel was a matter of the failure to report which did not constitute a breach of the policy of title insurance"); *Chicago Title Ins. Co. v. Investguard, Ltd.*, *supra*, 215 Ga. App. at 123 (fact that property's value is located within flood plain may affect its marketability, but does not bring it within title policy's coverage for unmarketable title); *Hanson Bus. Park, L.P. v. First Nat'l Title Ins. Co.*, 209 S.W. 3d 867, 870 (Tex. App.- Dallas 2006) (holding that "the flood-plain status of that property is a defect, if at all, only in the condition of the property. We refuse to equate a defect in the condition of the property with a defect in title to the property"); *Voorheesville Rod & Gun Club, Inc. v. E.W. Tompkins Co.*, 82 N.Y.2d 564, 571 (1993) (rejecting insured purchasers' argument that title was unmarketable because of zoning restrictions); *Whaley v. First Am. Title Co.*, 2004 Tenn. App. LEXIS 195 (March 30, 2004), at *11 ("the improper subdivision of [the insured's] property does not render title unmarketable. Instead, it constitutes a defect in the physical condition of the property that makes the property economically difficult to sell"); *Logan v. Barretto*, 251 A.D.2d 552, 553 (N.Y. App. Div. 1998), *appeal denied*, 92 N.Y.2d 815 (1998) (sanitary code violations did not constitute defect in title or render it unmarketable; court stated that "marketability of title is concerned with

impairments on title to a property, i.e., the right to unencumbered ownership and possession, not with legal public regulation of the use of the property"); *Haw River Land & Timber Co. v. Lawyers Title Ins. Corp.*, 152 F.3d 275, 281 (1998) (4th Cir. N.C. 1998) (holding that zoning ordinances fall within title policy exclusion unless notice of violation appears in the public records; court stated that "zoning or environmental laws of general application, which are not recorded against specific parcels of property, are generally excluded from standard form ALTA title insurance policies . . ."); *Lohmeyer v. Bower*, 227 P.2d 102 (Kan. 1951 (minimum side lot violation does not make title unmarketable)); *Notaro Homes, Inc. v. Chicago Title Ins. Co.*, 309 Ill. App. 3d 246, 253 (Il. App. Ct. 1999), *appeal denied*, 189 Ill. App. 3d 661 (2000) (describing "marketable title" as "title that is not perfect but is reasonably secure against litigation or flaws decreasing the market value," and holding that failure to disclose existence of recorded amendment to zoning ordinance was not "cloud" on title or flaw that would, on its face, decrease property's market value); *Sabbagh v. Pizzuro*, 5 Misc. 3d 1002A, 2004 N.Y. Misc. LEXIS 1691, 2004 NY Slip Op 51159U (2004) (dismissing action against title insurer based on undisclosed filled-in swimming pool; court stated that title company "only insured against the unmarketability of title to the subject premises and not against the Town's regulation of the property; the questionable legality of the hidden in-ground pool and the lack of a valid building permit pertain only to public regulation of the use of the property which are not impairments on the title that affect its marketability and are, thus, not within the scope of coverage afforded by the title policy"); *Kremer v. Lawyers Title Ins. Corp.*, 2004 Vt. LEXIS 91, 107 (Sept. 8, 2004) (prior owner's failure to secure septic permit is not title defect covered by the owner's policy); *First United, Inc., v Chicago Title Ins. Co.*, 2006 Ark. LEXIS 330 (June 1, 2006) (loss in real estate value as result of purchaser's potential liability as successor-

in-interest under Time Share Act does not constitute a “defect” in title; title is not “unmarketable” where plaintiff is free to possess and control the land, or to sell it to whatever purchaser desires to buy it); (*Minchew v. City of New York*, 6 Misc. 3d 1038A, N.Y. Misc. LEXIS 470, 2005 NY Slip Op 50344 (2005), at *5 (“title insurance companies indicate that the failure to have a Certificate of Occupancy is not an objection to title and will not render title to a premises uninsurable”).

See generally Joel E. Smith, Annot., *Defects Affecting Marketability of Title within Meaning of Title Insurance Policy*, 18 A.L.R. 4TH 1311 (1982); Michael A DiSabatino, Annot., *Application of Provision in Land Purchase Agreement that it shall be Null Unless Marketable Title is Delivered, Where Defect in Title is Created or Permitted by Vendor Subsequent to Execution of Agreement*, 13 A.L.R. 4TH 927 (1982); Jay M. Zitter, Annot., *Construction and Effect of “Marketable Title Record Statute” Statutes*, 31 A.L.R. 4TH 11 (1984).

Reasonableness of Claim

Title insurance policies do not provide coverage for “unmarketability” claims when the insured’s allegation of the threat of litigation is remote or unreasonable. *See Larson v. Thomas*, 51 S.D. 564, 570 (S.D. 1927 (“as a general rule, a purchaser is not bound to accept a conveyance, if the title is reasonably doubtful. Mere possibility or suspicion of defect is not sufficient, but, if there is a doubt or uncertainty sufficient to form the basis of litigation or color of an outstanding title which may prove substantial, the title cannot be said to be marketable”); *Teague v. Bisceglia*, 19 Mass. L. Rep. 63 (Mass. Super. Ct., 2005) (“a mere possibility of defect in title will not relieve the purchaser from liability under his contract”).

In *Stewart Title Guaranty Co. v. Greenlands Realty, L.L.C.*, 58 F.Supp. 2d 360 (D.N.J. 1999), *summary judgment granted by, in part, summary judgment denied by, in part*, 58 F.Supp 2d 370 (D.N.J. 1999), *aff'd without opinion*, 281 F.3d 224 (3d Cir. N.J. 2001) (“*Greenlands I*”), the court stated that, “[t]itle [however,] is not rendered unmarketable by an alleged defect which is not reasonably debatable or by the threat of litigation which has no reasonable justification” (citation omitted). *Id.* At 366. The court held that a break in the chain of title to a three-foot strip of land did not render the title unmarketable, because failure to include the strip in a prior conveyance was a “scrivener’s error” and none of grantor’s successors (i.e., heirs and creditors) could assert a viable claim to the disputed strip of land. Therefore, the court reasoned, there was no reasonable threat of litigation at the time of closing.

See also Booth v. Attorneys’ Title Guar. Fund., Inc., 2001 UT 13 (2001), P 35, where the court held that title to the hotel property was not rendered unmarketable by a conveyance of the property without bankruptcy court approval, even though the owner-debtor, a limited partnership, was in Chapter 11 bankruptcy and the managing general partner was in a separate Chapter 7 bankruptcy. The court ruled that the bankruptcy court’s confirmation order in the owner-debtor’s Chapter 11 proceeding authorized the managing general partner to sell the hotel without permission from the bankruptcy court. The court also ruled that the general partner’s separate bankruptcy estate did not include the hotel but only his share of profits generated by the sale of the hotel, and therefore consent by the bankruptcy court handling that action was unnecessary and had no effect on the marketability of title to the hotel property. The court further noted that the plaintiffs had not presented any evidence of damage or injury, but acknowledged that if they had presented written evidence of an actual sale of the property at a substantial discount or of

having been turned down for refinancing on reasonable terms because of the alleged unmarketability of the property, the result might have been different. *Cf. Green v. Sams*, 433 S.E.2d 678, 683 (Ga. App. 1993), *cert. denied*, 1993 Ga. LEXIS 986 (Ga. Oct. 8, 1993) (an “apparent and real” risk of litigation relating to title makes title unmarketable); *Myerber, Sawyer & Rue, P.A. v. Agee*, 51 Md. App. 711, 717 (Md. Ct. Spec. App. 1982) (plaintiffs were forced to judicially establish easement by necessity against neighbor; court held that title was not marketable where litigation was necessary to create a merchantable title, and stated that “[m]arketability is not concerned with the results of litigation, only the likelihood”).

But an insured may claim that a “defect” in title exists that provides coverage under another provision of the title policy, even when title is held to be marketable. For example, in a subsequent ruling involving the same parties and the same issues as in *Greenlands I, supra, Stewart Title Guaranty Co. v. Greenlands Realty, L.L.C.*, 58 F.Supp. 2d 370 (D. N.J. 1999) (“*Greenlands II*”), the court ruled that an insured that has marketable title may nonetheless have a valid claim for loss or damage against the title insurer for a title defect, based on policy coverage (on the first page of the Owner’s and Loan policies) for “[a]ny defect in or lien or encumbrance on the title.” The court noted that this language is to be construed in favor of the insured and strictly construed against the insurer, and that the policy definition of “defect” is something less than unmarketability, i.e., if “defect” were synonymous with “unmarketability,” there would be no reason for the policy to separately define these terms. The court reasoned, therefore, that there are some defects that render title unmarketable and some that do not. But in this case the court was only willing to go as far as to find that there was a genuine issue of material fact regarding whether or not the title company had removed the defect in a “reasonably

diligent manner.” (The title company had, in fact, subsequent to the scheduled closing date filed suit to quiet title to the disputed strip of land and obtained a confirmatory deed from the court to the strip of land.) *See also Vestin Mortg., Inc. v. First Am. Title Ins. Co.*, 101 P.3d 398, 403 (Utah App. 2004) (“we . . . recognize that ‘defect’ may be defined as something less than a ‘lien’ or ‘encumbrance’”).

Perfect Title vs. Marketable Title

"Perfect title" may be described as title without fault, defect or omission. *See Pearce v. Freeman*, 22 Okla. 285, 286 (Okla. 1927) (“A perfect title is one free from litigation, palpable defects, and grave doubts, and consists of both legal and equitable title fairly deducible of record”); *Howie v. Panola-Quitman Drainage Dist.* 168 Miss. 387, 398 (1933) (“the words ‘perfect title,’ unless used in a more restricted sense, to be gathered from the instrument in which they appear, embrace not only the right of property and of possession, but also freedom from liens and incumbrances”); *Linscott v. Moseman*, 84 Kan. 541 (Kan. 1911) (“A vendee who has contracted for perfect title can not be compelled to accept a title encumbered by a recorded oil-and-gas lease whose validity, if it be invalid, depends upon facts which, were the title impugned, the vendee would be obliged to establish by parol evidence”).

Perfect title is not the same as “marketable title” or “merchantable title.” For example, in *Geithman v. Eichler*, 265 Ill. 579, 583 (1914), the parties’ contract provided that the seller would convey title in fee simple, free of encumbrances, by warranty deed. The court stated that: “This did not necessarily mean a perfect title of record but meant a good merchantable title. A party may have such title to land notwithstanding apparent defects in the chain as shown by the records.” *Id.* at 583. *See also Christopher v.*

West, 345 Ill. App. 515, 529-30 (Ill. App. Ct. 1952) (“[merchantable] title [which Illinois courts equate with ‘marketable’ title] need not be a perfect record title without fault, defect or omission . . . A merchantable title does not necessarily mean or require a perfect title”); *Sinks v. Karleskint*, *supra*, 130 Ill. App. 3d at 529 (“[merchantable title] has . . . been defined as ‘not perfect title, but rather title reasonably secure against litigation or flaws decreasing market value’” (citations omitted)); *Nelson v. Anderson*, 286 Ill. App. 3d 706, 708 (Ill. App. Ct. 1997) (“merchantable title is not perfect title, but rather title reasonably secure against the hazard, annoyance and expense of future litigation”); *Voorheesville Rod & Gun Club*, *supra*, 82 N.Y.2d at 571 (“marketable title is not perfect title; rather . . . [a] marketable title is a title free from reasonable doubt, but not every doubt” (internal quotations and citation omitted)); *Dime Savings Bank and Trust Co. v. Knapp*, 313 Ill. 377, 383 (1924) (“[i]f it were necessary, in order to establish a good title, that an abstract show a perfect paper title, without fault, defect, or omission, although cured by existing facts or lapse of time, land could rarely, if ever, be sold”); *U.S. Bank v. Smith*, 7 Misc. 3d 1005A, 2005 N.Y. Misc. LEXIS 628, 2005 NY Slip Op 50456U (Feb. 15, 2005), at *5 (“To be marketable, a title need not be absolutely free from every technical or possible suspicion and the mere possibility of a defect that, according to ordinary experience, has no probable basis, does not show an unmarketable title”). Furthermore, providing coverage against loss by reason of reason of unmarketability of the title is different from that of certifying that the owner or the mortgagor "in fact" or "in law" is possessed of a marketable title. *See, e.g., Crown Enterprises, Inc. v. Trustco Bank N.A.*, 2001 NY Slip Op. 400779U, 2001 N.Y. Misc. LEXIS 452 (Sup. Ct. of N.Y., Rensselaer Co., July 16, 2001), at *8 ("a title company's unconditional approval to insure a particular title does not necessarily render that title marketable" (citation omitted)).

As noted earlier, essentially title is "unmarketable" if an "alleged" or "apparent" matter would permit a purchaser that has contracted to buy the real estate to cancel on grounds of unmarketability. Exactly what constitutes a marketable title is a matter of judicial interpretation. State courts have varying definitions of this term. For example, courts have defined marketable title as "free from reasonable doubt"; "free from defects and encumbrances"; "title a reasonable [or prudent] person would accept"; "not a perfect title but one which is not subject to reasonable doubt nor does it require litigation"; "title that may be freely made the subject of resale and that can be sold at a fair price to a reasonable purchaser or mortgaged to a person of reasonable prudence as security for the loan of money"; and title that is "free from reasonable doubt and such as reasonably well informed and intelligent purchasers, exercising ordinary business caution, would be willing to accept."

BLACK'S LAW DICTIONARY (7th ed. 1999) defines "unmarketable title" as:

A title that that a reasonable buyer would refuse to accept because of possible conflicting interests in or litigation over the property. --- Also termed *bad title*; *unmerchantable title*; *nonmerchantable title*.

Id. at 1494. (Emphasis in text.)

In Kayfirst Corp. v. Washington Terminal Co., supra, 813 F.Supp. at 77, the court set forth the following definition of "marketable title":

A marketable title is a title which is free from encumbrances and any reasonable doubt as to its validity, and such as a reasonably intelligent person, who is well informed as to the facts and their legal bearings, and ready and willing to perform his

contract, would be willing to accept in the exercise or ordinary business prudence. Accordingly a marketable title must be so far free from defects as to enable the purchaser not only to hold the land in peace but also, if he wishes to sell it, to be reasonably sure that no flaw will appear to disturb its market value. (Citations omitted.)

See also Humphries v. Ables, supra, 789 N.E. 2d at 1032-33 (“[t]itle which has no defects of a serious nature, and none which affect the possessory title of the owner, ought to be judged marketable. . . One who contracts for the purchase of real property is not bound to accept a doubtful title, or one that would likely be involved in litigation, even though it may ultimately be adjudged to be good”); *U.S. Bank v. Smith, supra*, 2005 N.Y. Misc. LEXIS, at *5 (“A marketable title is one that is free from serious doubt as to its validity and reasonably certain not to be called into question; in short, one that can be sold to a reasonably prudent purchaser or mortgaged to a person of reasonable prudence as security for the loan of money”); *Ardex, Ltd. v. Brighton Homes*, 206 Ga. App. 606, 608 (1992) (“A good title means not merely a title valid in fact, but a marketable title which can be sold to a reasonable purchaser or mortgaged to a person of reasonable prudence as a security for the loan of money” (citations omitted)); *Kelley v. Leucadia Fin. Corp.*, 846 P.2d 1238, 1243 (Utah 1992) (“Marketable title is one that may be ‘freely made the subject of resale’ and that can be sold at a ‘fair price’ to a reasonable purchaser or mortgaged to a person of reasonable prudence as security for the loan of money” (quoting 77 AM. JUR. 2d *Vendor and Purchaser* § 131, at 313-14 (1975))); *G/GM Real Estate Corp. v. Susse Chalet Motor Lodge of Ohio, Inc.*, 61 Ohio St.3d 375, 377 (“title need not be free of any possible claim of defect in order to be marketable, but it must be in a condition as would satisfy a buyer of ordinary prudence”); *NYCTL 1998-1 Trust v. Mayfield*, 841 N.Y.S.2d 199 (2007) (“[a] marketable title

has been defined as one that may be freely made the subject of resale. It is one which can be readily sold or mortgaged to a person of reasonable prudence, the test of marketability being whether there is an objection thereto such as would interfere with a sale or with the market value of the property” (internal quotations and citations omitted)); Joyce D. Palomar, *Liability of Title Insurers*, THE LAW OF DISTRESSED REAL ESTATE, Vol. 3, Ch. 42 (2005), at 42-13 (“The judicial definition of marketable title is a title ‘legally free from doubt,’ or free from potential litigation”). Cf. *Kohlbrand v. Ranieri*, 2005 Ohio 295 (Jan. 28, 2005), P24 (criticizing section of Ohio real estate treatise stating that, with respect to definition of “marketable title”: “Title that is ‘free and clear’ is not the same as ‘clear title.’ Rather, ‘free and clear title’ means that it is unencumbered by any lien and is marketable”); *House v. First Am. Title Co.*, supra, 2006 Ind. App. LEXIS at *13 (“‘title’ which has no defects of a serious nature, and none which affect the possessory title of the owner, ought to be adjudged marketable” (internal quotations and citation omitted)); Charles B. Sheppard, *Assurances of Titles to Real Property in the United States: Is a Person who Assures Quality of Title to Real Property Liable For a Defect in the Title Caused By Conduct of the Assured?* 79 N. DAK. L. REV. 311, 974 n. 354 (2003) (“What is a ‘marketable title’? Most definitions of a ‘marketable,’ ‘merchantable’ or ‘perfect’ title provide little guidance as to the essential ingredients of the concept, and some beg the question itself”).

Unmarketability: Case Law

The issue of whether title to real property is rendered unmarketable often arises in connection with encroachments and easements over or on the insured property or over or on adjacent property. For example, an encroachment may encumber title or render title unmarketable in certain circumstances, particularly if the encroachment is

substantial; if it interferes with the free development of the subject property; or if it forces the insured (and a subsequent purchaser) to “purchase a lawsuit” to protect its interest in the property. (But certain minor and insubstantial encroachments, such as roof cornices, awnings, bay windows, trim, shrubbery, fire escapes, and cellar doors, generally do not prevent purchasers from closing property purchases or give rise to a claim for unmarketability under a title policy.) In *Mellinger v. Ticor Title Ins. Co.*, 93 Cal. App. 4th 691 (2001), *reh’g denied* Nov. 28, 2001, *review denied*, 2002 Cal. LEXIS 647 (Cal. Feb. 13, 2002), the court stated that “[b]ased on the meaning of marketable title established by the Supreme Court, the question is whether a reasonable purchaser, knowing that a third party might claim an interest in the property, would nonetheless proceed with the transaction.” *Id.* at 695-96. The court held that whether an encroachment was evidenced in the real property records was a question of fact for the jury, and refused to concur with an Illinois decision that treated the issue as a question of law. The court acknowledged that the policy’s survey exception might later be found to be applicable to exclude coverage, but stated that it was first appropriate to decide whether coverage existed in the first place under the terms of the policy.

See also Kayfirst Corp. v. Washington Terminal Co., *supra*, 813 F.Supp. at 76-78 (seven-foot subterranean concrete footing encroachment rendered title unmarketable “both because of the encroachment’s substantial nature and because it has forced Kayfirst – and would force a subsequent buyer – to purchase a lawsuit to protect its interest . . .”); *Rodolitz v. Canto Fancy Foods, Ltd. (In re Rodolitz Holding Corp.)*, 232 B.R. 573, 577 (E.D.N.Y. 1999) (encroachment on navigable water way in violation of federal statute, necessitating expense to remove, rendered title unmarketable because of reasonable doubt as to marketability of title and likelihood of litigation to

determine the question); *Rackouski v. Dobson*, 261 Ill. App. 3d 315, 318 (Ill. App. Ct. 3d Dist. 1994) (11.9-foot encroachment of insured's barn on to adjoining property was "substantial and not trivial" and rendered title unmarketable; court stated that "reasonable persons would not purchase property which would require them to either remove a substantial portion of a building from the property or defend a lawsuit, or both"); *In re Meehan*, 30 Wis. 2d 428, 430-31 (1966) (ruling that warranty against encumbrances extended to structures originating on seller's property that encroached upon adjoining property): *Winters v. Polin*, 309 Ill. App. 458, 461-62 (Ill. App. Ct. 1941) (encroachments of bay windows, which were permanent part of building on insured's property, on to adjacent lot were "substantial and not trivial, and seriously affected the marketability of the title" because of risk of litigation, even though encroachments were only 9.32 inches and 4.08 inches, respectively). *Cf. Sec. Union Title Insurance Co. v. RC Acres, Inc.*, 269 Ga. App. 359, 362 (2004), *cert. denied*, 2004 Ga. LEXIS 1068 (Ga. Nov. 22, 2004) ("[the insured] had no economic loss from the recorded flowage easement, because the fair market value of the purchase price already reflected the encumbrance of the easement in the price willingly paid by it"). *See generally* L.S. Tellier, Annot., *Encroachment of Structure on or over Adjoining Property or Way as Rendering Title Unmarketable*, 47 A.L.R. 2D 331 (1956, updated 1997).

An unmarketability claim also can arise where the parcels constituting the land described on Schedule A of the title policy are not correctly described. *See, e.g., Burgess v. Stewart Title Guar. Co.*, 65 Va. Cir. 311, 2004 Va. Cir. LEXIS 271, at *5 (2004) ("the aggregate acreage was insured as two lots where only one existed. The difference in the number of parcels conveyed affects the legal rights of the parties and is not one of mere economic marketability. A statement of the number of lots to be conveyed is a core

issue relating to the legally recognized rights of the parties regardless of issues of value or physical properties of the parcels”).

Furthermore, an unmarketability claim also may arise where title to the property has been obtained through a defective or invalid court proceeding. *See, e.g., U.S. Bank v. Smith, supra*, 2005 N.Y. Misc. LEXIS 628, at *6-7 (“Where title is obtained through a court action or proceeding which was defective, the title may be unmarketable and, thus, where the validity of the service of process on a defendant in a foreclosure action involved doubtful questions of law and fact, title was not marketable” (citing *Thomas v. Loomis*, 80 N.Y. S. 2d 309 (1948))).

A reverter (or possibility of reverter) has also been held to render title unmarketable. *See, e.g., NYCTL 1998-1 Trust v. Mayfield, supra*, 841 N.Y.S.2d at 203 (holding that, as in this case, “the possibility of reverter has been held to render title unmarketable” (citation omitted)); *McAndrew v. Lanphear*, 111 N.Y.S.2d 238, 242 (2007) (holding that improbability of facts coming into existence sufficient to actually invoke right of reverter does not create marketability where it does not otherwise exist).

Marketable Title vs. Insurable Title

The parties to a real estate transaction should understand that there is a difference between marketable title and insurable title. An insurable title is “one which a reasonably prudent title insurance company would be willing to insure, free from exceptions (other than those normally excluded by the policy form) and at normal title insurance rates.” James M. Pedowitz, “*Marketable Titles*” in *Real Estate Titles* (2d ed. 1998), p. 24-21.

Title policies do not provide coverage for aggravation, inconvenience, frustration, unmet expectations, consequential damages, or similar matters. For recourse in these areas, the insured must look to other sources (such as deed warranties or the seller's warranties and representations contained in the purchase and sale contract executed by the insured party with respect to the property). See Spencer Compton, *The State of Marketable Title (With Sample Clauses)*, 19 THE PRACTICAL REAL ESTATE LAWYER 33, 37 (2003) (explaining difference between marketable title and insurable title). See also Joseph Shade, *Petroleum Land Titles: Title Examination & Title Opinions*, 46 BAYLOR L. REV. 1007, 1012 (1994):

When title insurance is used, "insurability" rather than "marketable title" becomes the test of a title's acceptability. Insurability is the insurance company's willingness to insure title. Because the insurer typically accepts a degree of business risk when it issues title insurance, insurability is a broader and more flexible standard than marketable title. For example, a title insurance company will typically insure title to property if, in the insurer's opinion, the property title is sufficiently free of defects to justify issuing a policy indemnifying the insured against loss arising from potential title defects, even though the title does not meet the legal standard of 'marketability.

A title insurer's refusal to insure title does not render title unmarketable, because a title insurer cannot be compelled to issue a title policy. In *Wilson v. Pacific Coast Title Ins. Co.*, 106 Cal. App. 2d 599 (Cal. Ct. App. 1951), the title company declined to insure the title to the property for reasons that it set forth in a written report. The plaintiffs did not obtain a title policy, and proceeded to sell the property. The reasons given by the title company for its refusal to

insure the plaintiffs' title (obtained via a foreclosure proceeding) were that there was no assignment then of record from the original beneficiary to the new beneficiaries; that the substitution of trustee under the trust deed contained neither the acknowledgment nor the affidavit of service required by California law, and that the trustee's deed indicated that the notice of default was never published or personally served as required by California law. The plaintiffs argued that their title under the trust deed and the foreclosure proceedings was defective. The court ruled, however that:

[T]he refusal of the title company to insure plaintiffs' title for its stated reasons is merely an expression of the opinion of the title company. Plaintiffs acquired title to the property involved by foreclosure proceedings and the trustee's deed issued thereafter. There is no substantial evidence in the record upon which the trial court could have found that the title to the land involved was vested otherwise than in plaintiffs. Whether such title was defective was a question of fact for the determination of the trial court, as was the question whether such title was 'unmarketable.

Id. at 602.

In general, court decisions in this area are careful to make a clear distinction between marketable title and insurable title. For example, in *Nelson v. Anderson, supra*, 286 Ill. App. 3d at 708-09, the court found that the existence of an encroachment rendered title "unmerchantable," which the court defined as "that which a reasonable person will accept as not subject to a doubt or cloud that would affect its market value." The court ruled that the availability of title insurance to provide coverage over the risk (which involved the violation of a setback covenant in a subdivision plat that amounted to only 4.7 feet) would not prevent the purchaser

from refusing to close for failure to deliver merchantable title (as required by the parties' purchase and sale contract). The court reasoned that the nature of the covenant involved would allow any other homeowner in the subdivision to enforce the restriction, and that a reasonable purchaser would justifiably be concerned that the existence of the encumbrance might pose a threat of future litigation and could adversely affect the market value of the property. The court stated that, "[t]he law has long recognized that a buyer cannot be compelled to buy a lawsuit"). *Id.* at 709.

See also U.S. Bank v. Smith, supra, 2005 N.Y. Misc. 628, at *6 ("An insurable title is not necessarily a marketable one . . . and a purchaser will not be compelled to take insurable title if title is unmarketable and the purchaser is entitled to marketable title (citation omitted"); *Patten of New York Corp. v. Geoffrion*, 598 N.Y.S.2d 355, 356 (A.D. 3 Dept. 1993), *appeal denied*, 82 N.Y.2d 654 (1993) (easement created no material defect to title, and therefore did not destroy marketability; because title insurer was unwilling to insure over easement, easement prevented title from qualifying as insurable, even though it had no impact on marketability of title); *Cuny v. Quinn*, 860 So.2d 232, 237 (La. App. 5 Cir. 2003) ("the availability of title insurance was but one factor . . . [to] consider in determining merchantability of title. It was not a single dispositive factor"). *Cf. Aouate v. Hotel Europe, Inc.*, 792 So. 2d 596, 598 (Fla. App. 3d Dist. 2001) ("because Endorsement No.1 [effectively removing a *lis pendens* filed against the property] was sent by [the title insurer] on the day of closing, it meant that title was insurable and therefore good and marketable"); *Stewart v. Gainesville Bank & Trust Co.*, 263 Ga. App. 93, 94-95 (2003) (where seller did not warrant that it had marketable title to property or promise to clear any title defects, but granted purchaser option to terminate if it discovered title objection that seller failed to correct within reasonable period of time, "the [seller] was

not obligated under the contract to convey marketable title and [the purchaser's] remedy was to rescind the contract if [the seller] failed to satisfy his title objections"); *Desantis v. Lenoci*, 2005 Ohio App. LEXIS 4209 (Ohio Ct. App., Lorain County Sept. 7, 2005), at P11-P13 (holding that because parties' contract required seller to "remove" any title defects and did not provide that title insurance was an appropriate remedy for curing alleged title defects, sole remedy provided in contract was limited to removing title defects, and stating that, "While the title insurance may alleviate any pecuniary loss resulting from the instant real estate transaction, it would not eliminate the 'hazard of litigation' that is inherent in the purchase of property").

The debate over "marketable" vs. "insurable" title can arise in connection with actions for specific performance of property purchase and sale contracts. In *White River Development Group, LLC v. Souhegan River Associates*, 2003 Mich. App. LEXIS 1286 (Mich. App. Ct., May 29, 2003), the purchase and sale agreement stated that the sale of the land was to be consummated by the sellers delivering a "warranty deed conveying a marketable title." Another provision provided that the sellers were to provide title insurance or, alternatively, an abstract of title as proof of marketable title. The sellers were unable to obtain title insurance. The purchasers, although clearly having the right to rescind the agreement, sought specific performance of it. The issue, as framed by the Michigan appellate court, was whether the purchasers were entitled to specific performance where the sellers could not or did not provide marketable title. According to the court, under Michigan law, "if a seller cannot convey marketable title as agreed, in this case a whole fee interest, the purchaser has a right to enforce the contract as to the seller's partial interest with a proportional abatement of the contract price so long as the purchaser was unaware of the seller's inability to convey the whole fee." *Id.* at *5. The court also stated that, "[f]ailure to convey

marketable title is considered a breach of covenant, not a condition precedent,” thereby not relieving the sellers of their obligation to perform under the purchase agreement.” *Id.* at *6.

Some courts hold that where nothing is mentioned in a real estate sales contract regarding the nature of the title, there is an implied covenant by the grantor to convey marketable title. *See, e.g., Oswald v. Oswald*, 2005 Wisc. App. LEXIS 597 (Wis. Ct. App. July 6, 2005) at *7 (“where no provision indicating the character of the title is made in a contract for the sale of real estate, the law implies that the vendor is to convey marketable title free from incumbrances” (internal quotations and citations omitted)). *See also* Alex Polonsky, *Tanks for the Memories: Abandoning Caveat Emptor For the Transfers of Residential Property Contaminated With Petroleum From Leaking Underground Storage Tanks*, 22 VT. L. REV. 979, 994 (“Marketable title is implied in every real estate contract. Therefore, a buyer may rescind the [purchase and sale] Agreement if the seller does not have marketable title to the property even if the [purchase and sale] Agreement is silent regarding marketable title”); Charles B. Sheppard, *Assurances of Titles to Real Property Available in the United States: Is a Person Who Assures a Quality of Title Liable For a Defect in the Title Caused By Conduct of the Insured?*, 79 DRAKE L. REV. 311, 314-15 (2003):

A contract for the sale of an interest in real property includes at least one covenant or warranty of title in the absence of a stipulation between the parties in the contract to the contrary. This covenant or warranty of title is a promise on the part of the seller to deliver to the buyer either a judicially, statutorily, or contractually defined marketable title. The law does not require a seller to deliver perfect title to a buyer. Some commentators suggest that even

if a contract for the sale of an interest in real property contains a promise by the seller to deliver perfect title--a title that is not burdened by any lien or encumbrance--to the buyer, it is probable that such a promise could be successfully challenged as being illusory and therefore unenforceable. Such a promise would be illusory if the property in question is nonexempt property that is subject to a lien for payment of real property taxes. The promise would be illusory because it is impossible for the seller to tender or deliver a title that is free and clear of all liens and encumbrances. Consequently, the best quality of title that could be tendered in that type of situation would not be a perfect title.

Whether a seller has or has not tendered or delivered a contractually, judicially, or statutorily defined marketable title to a buyer is determined on a transaction-by-transaction basis. Whether a title is free from reasonable doubt and is therefore marketable is tested from the standpoint of the prospective purchaser and not that of either the prospective seller or of the court. It follows that the quality of the title to an interest in real property that is accepted as being marketable by a purchaser might be regarded as unmarketable by a different purchaser.

The parties to a contract for the sale of an interest in real property may include an express covenant by the seller to transfer marketable title to the buyer in the contract. Some contracts for the sale of an interest in real property do not contain an express promise by the seller to transfer marketable title to the buyer. In that

type of situation, such a covenant is nevertheless regarded as being a condition by implication, in the absence of a specific contract provision to the contrary.

Public Records; Survey Matters

Although the ALTA Owner's and Loan Policy forms define the term "public records" (in Section 1(f) of the Conditions and Stipulations), they do not limit coverage to matters of record title only. But the title company's obligation is limited to searching to the public records as defined in the policy. *See, e.g., Haw River Land & Timber Co. v. Lawyers Title Ins. Co., supra*, 152 F.3d at 280 ("in order to be contained in the 'public records,' as used in the ALTA title policy, a notice of enforcement or of an encumbrance would have to be recorded in one of these public records designed to put purchasers of real property on constructive notice about matters affecting title to the property which they are purchasing "; court further stated that, with respect to claim of coverage under policy based on violation of zoning ordinances, "the adverse impact of zoning ordinances and regulations would be covered only if they somehow affected title to specific property as it appeared in state established records putting persons on legal notice about matters affecting that property"); *Ditmore v. Lochner*, 2005 Mich. App. LEXIS 806 (Mich. Ct. App., March 24, 2005), at *8-9 (title insurer had right to rely on "public records" policy exclusion because circuit court judgment was not recorded in county register of deeds office and did not impart constructive notice); *Podorsek v. Lawyers Title Ins. Corp.*, 203 Mich. App. LEXIS 3186 (Mich. App., Dec. 11, 2003) (finding no coverage under title policy because "a drain easement filed in a drain commissioner's office, rather than with the register of deeds, did not provide constructive or actual notice of the easement").

With respect to survey matters, if the defect is not of record, but could have been identified if a survey had been done and submitted to the title insurer, this should not cause the title insurer to be liable to the insured for a claim of unmarketability of title based on the undiscovered or undisclosed survey defect. Also, the fact that the insured has received a title policy with “extended coverage” (i.e., the deletion of certain regional exceptions, including the exception for matters of survey) generally does not result in affirmative coverage for matters that would be of concern to the insured (such as major encroachments on to or over adjacent land or the absence of improvements on the land) and that would have been disclosed on an accurate survey. Coverage under a title policy exists only under the specific contractual insuring provisions and is subject to the terms and conditions of the policy (such as the definition of “land”), and generally cannot arise by implication based on the removal of a specific policy exclusion.

See, e.g., Chicago Title Insurance Co. v. Citizens and Southern Nat'l Bank, 821 F. Supp. 1492, 14 (N.D. Ga. 1993), *aff'd sub nom Chicago Title Ins. Co. v. Nationsbank*, 20 F.3d 1175 (11th Cir. 1994) (title company's inclusion of creditors' rights exclusion in other title policies does not create an implication that creditor's rights issues are covered in policies that contain no such specific exclusion); *Ginger v. American Title Ins. Co.*, 29 Mich. App. 279, 282-84 (1970), *appeal denied*, 384 Mich. 808 (1971) (denying title policy coverage for alleged intentional fraudulent transfer because it involved material matters known to insured and not disclosed to title insurer); *Elysian Investment Group v. Stewart Title Co.*, *supra*, 105 Cal. App. 4th at 324 (“[the insured] cannot rely upon an exclusion to extend coverage”); *Ray v. Valley Forge Ins. Co.*, 77 Cal. 4th 1039, 1048 (1999) (“Insurance policy exclusions do not extend coverage”); *Stanford Ranch, Inc. v. Maryland Cas. Co.*, 89 F.3d 618, 626-27 (1996) (“It is well established in California that an

exclusion cannot act as an additional grant or extension of coverage”); *Vestin Mortg., Inc. v. First Am. Title Ins. Co.*, *supra*, 101 P.3d at 401 (“If [the insured’s] claims are not covered by the policies, then the exclusions are not relevant”); *Somerset Sav. Bank v. Chicago Title Ins. Co.*, 420 Mass. 422, 429 (Mass. 1995) (finding that, with respect to the “reasonable expectations” of the plaintiff as the insured under the title policy, and its argument that right-of-way statutes are normally listed as an exception to coverage, “[E]ven if such a practice was accepted, the failure to include such a statute as an exclusion does not mean that coverage is available, where the express policy terms do not provide for coverage”). *Cf. Denny’s Restaurants v. Security Union Title Ins. Co.*, *supra*, 71 Wn. App. at 207-08 (1993) (finding that purpose of legal description in title insurance policy is to identify subject of insurance, not to limit protection of policy, and stating that, “[l]ogically, a deleted exclusion indicates that the former exclusion is no longer applicable; any other result would undermine the rationale for paying additional consideration to obtain extended coverage”); *Rackouski v. Dobson*, *supra*, 261 Ill. App. 3d at 317 (“[a]lthough the deletion of an exclusion should not automatically be construed as providing coverage, when the [title insurer] waived such a specific exception, we believe that the logical conclusion is that the policy, as executed, does cover such ‘encroachments, overlaps . . . which would be disclosed by an accurate survey . . .’” (internal quotations and citation omitted)). *See also First Am. Title Ins. Co. v. Dahlmann*, 291 Wis. 2d 156 (Wis. 2006). In this case, the court first explained the difference between title exclusions and exceptions:

Title insurance policies contain two types of provisions that reduce coverage: exclusions and exceptions. “Exclusions and exceptions are similar in that each class of items limits the coverage of the policy. However,

exclusions refer to subjects beyond the ambit of the policy, while exceptions are matters generally within the scope of the insuring provisions.” Wunsch at § III-6 (quoting J. Nielsen, *Title Escrow Claims Guide*, § 12.1, at 354 (1996)). Exceptions, not exclusions, are at issue in this case.

Id. at 171. The court also stated the general rule that “ambiguous terms are to be construed in favor of coverage, and exclusions are to be narrowly construed against an insurer.” *Id.* at 177. The court held that the encroachment of a hotel's underground parking garage into the right-of-way for a city street was an “encumbrance on the title” and covered by the policy if it was substantial, and ruled in favor of the insured, explaining that:

We reverse the decision of the court of appeals. We hold that a substantial encroachment, created by an improvement onto adjacent land, constitutes an encumbrance on the title of the insured property for the purpose of the title insurance contract at issue in this case. We further hold that such a substantial encroachment, and thus an encumbrance, is covered under the terms of the title insurance policy at issue. However, the issue of whether the encroachment here is “substantial,” so as to constitute an encumbrance on the title of the insured property, for purposes of the title insurance contract, presents a question for the trier of fact to resolve. We, therefore, remand the case to the circuit court for such a determination.

Id. at 178.

If a survey is in fact submitted to the title insurer, it generally will take specific exception to the items shown on the survey. If the title insurer takes specific exceptions for items shown on the survey, but misses a matter that should have been excepted and does not show it as a specific exception (such as an encroachment), the title insurer could incur liability under the “unmarketability of title” coverage provision if the buyer repudiates the contract because it has discovered the defect and refuses to close the transaction. In *First Am. Title Ins. Co. v. Dahlmann, supra*, the court noted that:

In issuing the title insurance policy, First American relied upon a survey completed by Jeffrey Johnson in 1994 (Johnson survey), and an affidavit from the landowner who sold the Inn to Dahlmann. The Johnson survey depicted the encroachment of an exterior wall of the parking garage and a vent into a four-foot right-of-way. However, the survey did not depict the encroachment of the garage under Frances Street. The seller's affidavit stated that no changes had been made to the Inn to affect the structure's size or location since the Johnson survey was conducted. As a result, at the request of Dahlmann's attorney, First American agreed to omit from the title insurance policy two potentially relevant exceptions, which were included in the standard form title commitment: (1) “Any discrepancies or conflicts in boundary lines, any shortages in area, or any encroachment or overlapping of improvements.” (Encroachment exception); (2) “Any facts, rights, interests or claims

which are not shown by the public record but which could be ascertained by an accurate survey of the land.” (Survey exception). As a result of the policy amendments, Dahlmann paid an additional premium.

Id. at 161-162. The court further noted that:

Petitioner presents an alternate question of whether the encroachment here renders the title unmarketable, and therefore falls within the insurance coverage. Because we resolve the issue on the basis of an encumbrance on title, we need not reach the question of unmarketability, but note that such an issue also presents questions for the trier of fact.

Id. at 160.

An unmarketability claim also may arise where there are surveys that show different descriptions of the property to be insured. *See Wates v. Crandall*, 144 N.Y.S. 2d 211, 215-16 (N.Y. Sup. Ct. 1955), *aff'd* 152 N.Y.S. 2d 874 (N.Y. App. Div. 2d Dep’t 1956), *reh’g and appeal denied*, 154 N.Y.S.2d 847 (N.Y. App. Div. 2d Dep’t 1956) (“there is a conflict between the respective surveys [obtained by the seller and purchaser], each prepared by a competent, licensed surveyor . . . [] [and] such conflict, unresolved, ipso facto would make title to [the disputed parcel] unmarketable”).

Recent Developments

In an ALTA Loan Policy, the “unmarketability of title” insuring provision covers the lender against title-related claims that disable or prevent the lender from selling his or her (or its) mortgage to another investor, or that would

require the lender to repurchase a mortgage. As noted above, this language does not cover circumstances resulting from physical condition of the land, such as contamination from hazardous waste or damage to improvements. During the past few years, the ALTA Forms Committee has been preparing drafts of a new ALTA Loan Policy (to replace the existing 1992 ALTA Loan Policy). The most recent draft (as of the date of this article), dated June 8, 2005, revises the definition of “Unmarketable Title” (to be designated as new Condition 1(m)) to read as follows:

Title affected by an alleged or apparent matter that would permit a prospective purchaser of the Title or the Insured Mortgage to be released from the obligation to purchase if there is a contractual condition requiring the delivery of marketable title.

Under the newer expanded coverage available in the ALTA Homeowner’s Policy (10/17/98), additional coverage is provided for certain “marketability” claims. (The Homeowner’s Policy applies only with respect to one-to-four family residences and only if the insured named in Schedule A is a natural person.) Insuring provision no. 14 covers the insured against the risk that “[b]ecause of an existing violation of a subdivision law or regulation affecting the Land . . . You are unable to obtain a building permit . . .” Also, insuring provision no. 15 protects the owner against risk of “forced removal” of “existing structures” because any portion of the structure was built without “obtaining a building permit.” (These particular insuring provisions are subject to a deductible and a maximum dollar amount of liability, and are also subject to the other policy exclusions, including the exclusion for matters “created, suffered, assumed or agreed to” by the insured.) But the question remains: What action by a governmental agency (or a neighbor demanding removal) gives rise to coverage under

the (undefined) term “forced,” i.e., there may be no actual loss to the insured or payment due under the title policy until the insured becomes obligated to expend money or defend an action to force removal of the structure; mere notice of a violation generally would not be sufficient to trigger coverage under the policy.

See, e.g., Costello v. Casale, 281 A.D.2d 581, 585 (N.Y. App. Div. 2001 (“no building violations had been issued against the premises as of the date that title reports were prepared, and the alleged renovations did not render title unmarketable, or expose the purchaser to potential litigation” (citation omitted)); *Elysian Investment Group v. Stewart Title Guaranty Co.*, *supra*, 105 Cal. App. 4th at 321 (recorded notice of substandard improvements did not result in unmarketability of title where notice merely provided warning about physical condition of land and applicable building and zoning requirements); *Ableman v. Slader*, 80 Ill. App. 2d 94, 99 (Ill. App. Ct. 1967) (existence of building code violation did not of itself constitute cloud on title where purchase agreement required only delivery of “good title,” as opposed to delivery of title “free of violations,” which would have rendered title unmarketable). *But see In re Rodolitz Holding Corp.*, *supra*, 232 B.R. at 577 (“title otherwise unmarketable because of the encroachment on [government property] is not rendered marketable [under New York law] merely because the [government] has not [demanded], and may not in the immediate future, demand that such encroachments be removed” (citation omitted)).

Conclusion

The standard ALTA Owner’s and Loan Policies provide valuable coverage against claims of unmarketability of the interests being insured under the respective policies. (Although such coverage may not be available in certain

states, such as Texas.) But it is important for the insured, as well as counsel for the insured, to understand the nature and scope of this specific coverage and what is not covered. Unfortunately, there is no standard or precise definition of “unmarketability,” which is a term of art and subject to judicial interpretation based on the facts of each case. It is, however, clear that title coverage is not available under this insuring provision for claims based on the physical condition or use of the land that affects the property’s economic or market value (unless and to the extent that additional endorsements are available and obtained for specific matters such as environmental liens and zoning violations). Furthermore, it is clear that marketable title does not mean “perfect” title to the insured’s interest in the property, and that marketable title is not the same as insured title.