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Hidden Risks in Real Estate Title Transactions

*Sherman Hollander**

NO AMOUNT OF CARE can avoid certain of the title hazards which a real estate transaction may encounter. The most careful attorney can do little or nothing, in such situations, to sidestep the pitfalls. In at least some such cases the legislature could provide relief by reducing the risk to innocent parties. To do so requires perceptive review of some time-honored concepts.

A number of types of other problems exist where a careful attorney may reduce the risk faced by his client. Even here perhaps the legislature could consider statutory improvements. It would be more fair and equitable if extraordinary care were not required to prevent an unjust result.

Dower Interest

One vestige of English Common Law which still operates in Ohio and may be the source of increasing losses to innocent parties in the future is dower. Dower as a basic right of inheritance has been supplanted by the statute of Descent and Distribution.¹ In one area alone, that is in the realm of inchoate dower, do we find this right still exercising its medieval force and power.

The inchoate right of dower is not a present interest in the title to land. It has no market value as such and cannot be sold separately from the title and is not subject to partition. It is a possibility of right of a vested interest, should certain conditions arise. First, it pertains only to land which is sold or mortgaged or otherwise encumbered during coverture without a release by the spouse claiming the interest. Second, that spouse claiming dower must survive the spouse who conveyed. And third, the marital status must have continued to exist to the death of the spouse who conveyed or encumbered without obtaining the dower release. In Ohio, the right is strictly statutory and is defined in Ohio Rev. Code Section 2103.02. Historically, the wife alone received the privileges of dower, but Ohio grants the identical right to either spouse.

The problem with dower is not that it exists, but that its existence may be a secret. The person who is an innocent victim of a missing unreleased dower right generally has no way to know that he has such a problem until it is too late. How can an attorney determine that the person conveying to his client has provided the necessary release of dower? If the grantor claims that he is unmarried and the allegation

* President, Ohio Title Co., Inc., of Cleveland; member of the Ohio Bar.

¹ Ohio Rev. Code § 2105.05.

is not true, it would be difficult to disprove. A marriage might have occurred in any county in this state, or in any state of this nation, or even in any foreign country or on the high seas. It is utterly impossible for any single record to be maintained of all marriages which would certify with certainty whether a person with whom one may be dealing is married or not, and if married, to whom. In fact, the only thing that can be determined is whether the statement or assertion of the grantor is in accordance with the meager evidence appearing in the public records which would be available to the purchaser. Such data might do little more than raise questions in the event of a conflict between the assertion being made at the time of the sale and evidence from the record chain of title. Thus, if the present grantor signed a mortgage five years ago with a spouse releasing dower, he must now explain why he now signs his deed as "unmarried."

The difficulty of determining whether a dower problem exists is even greater where the defect occurred at the time of some previous title transfer and is not evident from the public records.

Another common risk of dower gap exists where the spouse is named, but the person executing the instrument to release dower is some other person whose sole purpose is to assist the grantor in perpetrating the fraud. In any event, if dower is not released, that inchoate right continues, and the innocent purchaser has no way of ascertaining or protecting himself against a fraud in this respect, except that he may purchase the monetary protection of title insurance.

Why is the dower gap a greater risk now than it was a few generations ago? Only a few decades ago most land deals were among people acquainted with each other, at least remotely. Most vendors of land had lived in the community for a period of years and sometimes all of their lives. It would be fair to say that the number of modern day transactions where the purchaser knows the grantor prior to the sale and knows his spouse, or even knows them by reputation, is a relatively tiny percentage. In fact, the title to many parcels of land today is held by people who are relatively new to the community. Once it might very well have been taken for a sign of permanence in the community for a person to own land in it. This is no longer the case. Transfers of ownership of land are much more frequent, and in some parts of the country, notably the west coast areas, the fluidity of transfer is almost as great as it is with personalty of equivalent worth. But dower does not exist in relation to personal property. It is only land which is subject to this particular peculiar historic right and the dower release gap may have occurred in any past transaction in the chain of title.

When the purchaser of land discovers that this new home is subject to an unreleased dower claim, what can he do about it? He cannot compel the holder of the inchoate claim to sell it, and he must either live

with the title subject to the undetermined inchoate right until one or the other of the spouses dies, or he must buy the right for whatever price he can negotiate. This could be a costly purchase.

Even in instances where both parties may desire to eliminate the claim of dower it is not done with ease. Thus, where a couple decides, normally in the case of a second marriage, to execute an ante-nuptial agreement, it often provides that neither party will claim a dower right in the property of the other. Unfortunately, the ante-nuptial agreement is not self operative, is not enforceable in court, nor can it even be construed in court until the death of one party or the other. Thus, unless dower is actually released by the party who presumably has no right to claim it under the agreement, no title company knowing of this may certify that the title is free of dower.

Another dower problem area is in the realm of legal separation. Even though a separation agreement has been executed by both parties and has been ratified and incorporated within a Journal Entry in a decree for alimony, so long as the decree does not represent a divorce, the marriage remains subject to the rights of the parties in relation to dower.

In a number of instances, bills have been drawn and thrown into the legislative hopper to modify or extinguish the right of dower or at least to provide some protection to an innocent purchaser who acquires in ignorance of a concealed right. I know of no instance in which any of these bills have come forth favorably from a legislative committee. The Ohio General Assembly is deeply concerned about the protection of the innocent sixteen year old from the octogenarian husband who will divest himself of all of his real estate if she doesn't retain the protection of dower. I do not know of any example of this happening. On the other hand, every title man has seen at least one or more instances in which the dower right has been concealed, and an innocent purchaser has been thereby damaged.

Hidden Liens

The Uniform Commercial Code, unlike the medieval right of dower, is not merely an outgrowth of ancient and historic precedents. It was developed by modern legal experts. Much of it is carefully conceived and useful law. Unfortunately, it contains also some humanly conceived imperfections.

One of these is that it creates and permits in some instances a lien which is secret.² Another is that it fails to clarify and in fact may further obscure the division between real property and chattels. When these two flaws both apply in the same situation their interaction may be most unfair and damaging to an innocent party.

The basic theory of the recording laws is that they make possible the

² U. C. C. § 9-302.

protection of the public by requiring that rights in land be evidenced in such a manner that a person dealing with those rights may protect himself by an examination of the county records and by inquiry of those who may be in possession of the land. As to most chattels, no public filing as to ownership or liens is required, but the historic artisans lien requires the retention of possession by its claimant.

Ohio Revised Code Section 1309.21 exempts from the necessity of filing in any public record "a purchase money security interest in consumer goods; but filing is required for a fixture. . . ." No attempt was made to develop a clear definition of the term "fixture." Thus, the secret purchase money security interest may continue to attach to a thing which has not become a fixture but it will not be a lien if fixture status is achieved. A recent instance which came to my attention involved the purchase of an air conditioned house. The public records disclosed no evidence of a lien on the air conditioning unit. Air conditioning was provided by a centrally installed unit in the plenum of the furnace with a cooling tower located outside of the building. Apparently no Ohio court has yet determined whether such an installation is a fixture. The utility company which claimed the lien insisted on its right despite the secrecy of the claim. Though a settlement was reached in this case, it illustrates the danger to real estate of a secret lien even when it may be chargeable against something which may possibly not be real estate.

Recent years which have further defined fixtures may have added more obscurity than clarity. In *Merchants and Mechanics Federal Savings & Loan Assn. v. Herald*,³ wall to wall carpeting was construed as a fixture in a situation where it was purchased by the builder for apartment suites whose sub-flooring required such an installation before they could be properly usable. This would imply that whether carpeting is a fixture might be determined by whether it was purchased by the building owner or by a tenant. If a purchaser is unable to know whether some of the improvements which he purchased might be the subject of a secret lien without knowing who purchased each of these kinds of items such as carpeting or central air conditioning or other such assets, then a crystal ball may be just as important as an examination of public records in determining what rights exist.

Why should anyone ever be permitted to obtain a secret lien when he has not retained possession and makes no public record of the claim? Here the mere fact that the commercial code is a uniform enactment should not justify the retention of a uniform segment of it which is inequitable. Any secret lien should be considered abhorrent to the rights of third parties and should not receive the protection of the law. Certainly a team of experts who design uniform laws should take no pride in this kind of an achievement. Ohio has already departed from the uni-

³ 120 Ohio App. 115, 201 N.E. 2d 237 (1964).

formity of the commercial code in order to protect rights in real property against the disassembling of real estate by detachment of a fixture by reason of a lien which is later in time than other record liens on the real estate. In the six years since Ohio has made this correction, the Permanent Editorial Board for the Uniform Commercial Code has not yet completed recommendations for a similar correction. Does it make sense to retain inequities merely because they are uniform inequities?

Disability of Minority

Another problem which may trap the unwary or even the careful purchaser of land is the disability of minority. The historic purpose of such a limitation was to protect a person too tender in years against abuse by persons of greater experience who take contractual advantage of the innocent infant. Some inroads in recent years have been made on limiting this disability. As to veterans purchasing property with mortgages insured by the Veterans Administration statutory relief has been provided. The veteran and his wife who acquire a residence with a mortgage being insured as a VA loan may sign the mortgage and may release dower and may even convey title to the mortgaged premises prior to achieving the age of majority. It should be obvious from the fact that the Ohio statute⁴ is regarded as a preferential bill to veterans that the retention of the disability is not generally considered protective or advantageous by young married couples. The right by law to enter into the solemn state of marriage and to start raising a family would seem to be a rather awesome responsibility for persons still designated legally as infants. Certainly the disability to enter into an enforceable contract could be relieved for all persons legally married with more advantage than risk to the youthful spouses.

When checking the county records, the signatures of persons who have not yet existed for twenty-one years do not flash illuminated warnings to the title examiner. Thus, a deed signed by an infant may prove to be a weak link in a title chain which may be fractured some years thereafter. The innocent purchaser has no protection and no attempt to give him any seems to have received serious consideration in the Ohio General Assembly in recent years. Yet it is practically speaking, impossible for a purchaser of land to ascertain that all of the persons who signed the documents in the chain of record title were adults at the time. Sometimes a clue may exist, such as a family estate which shows the age of the persons who convey at a later date. This is generally not the case, however, and the person hurt has no recourse or protection. Perhaps the right to disaffirm could be required by statutes to be employed within one or two years after reaching the age of majority. At least the length of time this risk remains hidden could be reduced by such an enactment.

⁴ Ohio Rev. Code § 3109.02.

Unknown Heirs

Can the law protect an innocent purchaser against unknown missing heirs? *Shackelford v. Alford*,⁵ illustrates dramatically such a risk. The plaintiff filed her action to claim an interest in a parcel of land which had been owned by her father at the time of his death. The estate was administered showing only a single daughter of the decedent. It appears clear that the known heir did not even realize that she had a half-sister born of a marriage dissolved in 1895. In this 1963 decision, it was held, correctly, that the half-interest inherited by the claimant remained hers through a land sale in which she had not been made a party and a second land sale in the estate of the purchaser in the first land sale. Interests of this kind which are sufficiently ancient in vesting might be extinguished under the marketable title act. In the present case, even if the marketable title act had then been fully operative, it would have had no effect because the rights of the plaintiff accrued only at the death of her father, which was comparatively recent.

I recently encountered a similar type problem where the purchaser at a land sale which contained no apparent deficiencies had obtained a guaranty of his record title at the time. Some years later when attempting to sell the same parcel, he discovered that a determination of heirship had commenced after the completion of the land sale and heirs were discovered who had not been a party to the proceedings in which he had purchased. This innocent purchaser is now required to proceed with a partition action so that he may seek to buy in the right of claimants who were unknown to him until he attempted to sell his land.

In situations such as these we have certain equities to be balanced. The purchaser is clearly innocent of any knowledge of an outstanding interest. Even those administering the estate which omitted the mention of heirs not then known to exist did so in complete innocence of their existence. It is also true that the missing heirs in most such cases are unaware of their own possible interest which to them represents a wind-fall. Could the legislature preserve the protection of such unknown heirs and still assist an innocent purchaser? If the administrator who conducted the land sale proceedings had made unknown heirs party to the proceedings, the purchaser would have been protected, and the unknown heirs would have had their interests in the land extinguished.

Had the unknown heir been known, she would have been a party to the land sale proceedings and would have been divested of the title to the land anyway. She would, therefore, have received only a distributive share of the net proceeds of the sale less the segment of it which was required to pay the obligations of the estate. Would it not be more equitable if legislation were to place an omitted party in the same posi-

⁵ 119 Ohio App. 63, 196 N.E. 2d 609 (1963).

tion which he would have enjoyed at the end of the distribution of proceeds if he had been made a party to the land sale? Thus, the injured person might be given a money damages claim as of the moment of the discovery of the omission as against those who had received funds to which he would have been entitled had he properly been made a party to the action.

Defective Service

Another area of extraordinary and often concealed risks lies in the purchase of land which had had title to it transferred through judicial proceedings. How can a person examining the record of a foreclosure action determine whether the service supposedly made at the "usual place of residence" of the defendant was made at a place where the defendant actually did reside? *Lenz v. Frank*⁶ created shockwaves in 1949 when the Supreme Court there held that a flaw of this kind was fatal to the title of the purchasers. Whenever any question of service of process is involved, it is likely to be of equally critical proportions. Where parties who are necessary to a transaction have not been personally served and have not entered their appearance this danger may rise up to extinguish an apparently valid record title.

It may not be possible in such situations for legislative protection to be developed for a purchaser without doing injustice to the land owner who would be deprived of his title without proper notice of the proceedings through which the title was terminated.

Statutory Protection

Some statutory protection is available to a purchaser at a judicial sale.⁷ There, a purchaser whose title is invalid by reason of a defect in the proceedings is subrogated to the right of the creditor in the proceedings to the extent of the money paid to him and applied to the debtor's benefit and is given a lien on the property sold at the defective sale. Thus, were the purchaser to discover the defect promptly he could himself foreclose his new lien as against the omitted party's.

Where the omitted parties are not holders of an interest in the title but merely of junior liens, the purchaser should be entitled to more protection. If the liens which were represented by proper service on their holders in the proceedings totalled the full value of the property or somewhat in excess of what it was sold for at the judicial sale, then all that the junior lien holders would have received had they been parties would have been the right to file an answer. Where such a right would be an empty exercise, for example where the proceeds of sale were insufficient to pay the cost of court and the first mortgage, then it would seem that

⁶ 152 Ohio St. 153, 87 N.E. 2d 578 (1949).

⁷ Ohio Rev. Code § 2329.46.

the injury to the omitted lien claimant would be nominal. Under such circumstances, the legislature would hurt no one by giving statutory protection to the purchaser against omitted lien claimants who would not have been paid had they been parties to the transaction anyway. The present statutory protection requires the innocent purchaser to pay the costs of an action to enforce his statutory lien if the omitted lien claimant makes an issue of his worthless right. In fact, so long as claimants of sufficient liens to consume the full value of the property are made parties to an action to marshal liens and sell the land by reason of them it would seem somewhat pointless to add further costs to the action by requiring junior lien claimants who are far down the list and have no chance of receiving payment to be included in the proceedings at all.

Many peculiarities of service of process have voided actions based on apparent technical imperfections. Service by publication has been repeatedly found wanting for such flaws as failing to send a copy of the publication promptly to the last known address of the defendant, stating that the defendant resides in another state instead of that he cannot be served in Ohio, and for other types of defects, without even inquiry as to whether actual injury to the defendant did occur by reason thereof. Where the title has been transmitted through a court action, it would seem to be wisdom on the part of the attorney to obtain title insurance for the purchaser, since no direct recourse exists.

Mechanic's Lien Law

One risk whose existence is well known to most attorneys but where the greatest of care may only reduce that risk rather than eliminate it is in the realm of the Mechanic's Lien. Here again the danger lies not in that the land may be charged with a lien but that the lien may be secret as far as a purchaser or mortgage lender is concerned or even in some cases an owner.

The Mechanic's Lien right⁸ arises with the first commencement of work under the contract on behalf of all those who may claim under that contract. Thus, in the erection of a typical structure the lien rights of suppliers of sub-trades who may not even have been contracted with by the general contractor until many months after construction has been underway date back to the breaking of ground for the structure. As among the lien claimants the equity of this is apparent. If lien rights were limited to the commencement of work or furnishing of materials by each individual trade or supplier, then the first priority would be to the excavator and each person thereafter would be paid only to the extent that funds were left after paying all of his predecessors. Under such circumstances it would be increasingly difficult to get tradesmen to extend credit for work to be done in the later phases of construction. Thus,

⁸ *Ibid.* § 1311.02.

as a matter of basic fairness, it is equitable for all liens on the same contract to commence together and have an equal priority.

The problem arises because nothing evidences of record that the lien right has arisen, and the determination of the moment of its commencement remains a matter to be established by evidence, or by litigation, or by agreement when it becomes an issue at a later time.

Some protection is provided by the Mechanic's Lien law⁹ for a person who has improvements built on his own land on contract. He can require affidavits in accordance with this statute and can limit his disbursements to those with whom he contracts and those listed on the affidavits as sub-trades and material men. If he does so, he will receive the protection of the act as against failures of disclosure or concealment of lien claimants not known to him. So too can a mortgagee who disburses in accordance with the act obtain the sets of affidavits provided for in it. This is a procedure which is so cumbersome that it is, practically speaking, almost never employed.

If your client is purchasing land on which new construction has recently been completed, you may make efforts to obtain affidavits, but you will not find that the act provides direct protection to you for reliance upon them in the event they are deficient. Thus, if your seller is himself the builder and owner of the premises, each of the trades with whom he deals directly is a general contractor and his failure to advise you of one of these would provide no defense against the omitted lien.

It is the secrecy of the lien, not the right to it, which creates the problem in the case of the Mechanic's Lien. Yet all Ohio real estate is not subjected to this same kind of a hidden lien risk. Registered land in Ohio is chargeable with a Mechanic's Lien only to the extent that a memorial of it has been "entered upon the registered certificate of title prior to . . . transfer of the land or mortgage, lease or encumbrance thereof. . . ." ¹⁰ Thus, as to Torrenized land titles, a purchaser or a mortgagee is assured of a right to rely on what is disclosed by the public record. Certain states such as Michigan and New Jersey have Mechanic's Lien Statutes which also provide for disclosure and protection of the innocent purchaser or lender. Some years ago the Ohio General Assembly did authorize a study of the Mechanic's Lien law but failed to provide any funds for the study and it was not made. Certainly legislation which would protect against undisclosed lien rights on all land in Ohio whether or not it be registered, would serve a useful purpose.

Attempts to modify the Mechanic's Lien law have been met by opposition practically as a conditioned reflex of the material men. Yet they too would be in far better position were their liens known about by any prospective purchaser or lender. Certainly the purpose of disclosure is

⁹ *Id.* § 1311.04.

¹⁰ *Id.* § 5310.02.

not to prevent payment but to assure that the obligations will be properly paid to the persons entitled to them.

Conclusions

A cautious attorney, provided he is also lucky, may occasionally discover one or more of the potential title flaws which have been here listed. Were proof needed sufficient to countervene the possibility of any of these risks before title could be transferred to a purchaser, the marketability of real estate title would be virtually extinguished. Thus, hidden dower interests will continue to plague innocent purchasers. Secret liens on chattels affixed to real estate but not certainly defined as fixtures will continue to be clouded with the threat of removal. Prior owners who have divested themselves of title before achieving the age of majority will continue to intrude on apparently good record titles years after their interests were believed to have been terminated. Missing heirs will pop up from the great unknown without warning. Parties omitted from judicial proceedings who had no equity subject to their claim will continue to seek to recover what they would not have received had they been made parties by pressing claims against innocent purchasers. Mechanic's lien claimants whose interests are secret and often are undeterminable will continue to threaten purchasers of improved land.

What can be done? Certainly all of these areas should be given legislative attention. A bonafide purchaser for value should not be subjected to risks which are kept secret. Liens and interests should be required to be disclosed within the public record within the chain of record ownership. Where fairness must result in injury to one party or another, at least the bonafide purchaser for value should get the protection of relatively shortened statutes of limitation to assert claims against him.

Certainly most of the above risks occur only rarely. They do occur however, and the victim finds no solace in the fact that his loss is relatively rare. It is also quite likely that many of these risks will be increasing in future years because of our more fluid and complex society and growing population.

In many instances an attorney can counsel the purchase of protection against hidden title risks through title insurance. Monetary compensation for title loss should help alleviate the pain. It does not eliminate the risk however, and only change of the law of Ohio by legislative action can provide true cures for any of these concealed threats.