



**House
Legislative
Analysis
Section**

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**TITLE INSURANCE: ALLOW
TRANSFER INTO TRUST**

**House Bill 5096 (Substitute H-2)
First Analysis (5-28-02)**

**Sponsor: Rep. Tony Stamas
Committee: Insurance and Financial
Services**

THE APPARENT PROBLEM:

Title insurance is an insurance policy purchased as a safeguard against hazards or defects in the title to real estate property and is purchased at the time a homeowner or business owner secures a mortgage. Title insurance, which is generally a one-time purchase, protects against such scenarios as buying a home from a person who did not have the right to sell the property, property for which there is a lien, and property for which back taxes are owed.

A problem has recently surfaced in the case of individuals transferring ownership of property to trusts. As a means of avoiding lengthy or costly probate proceedings, many estate planners are recommending that their clients transfer ownership of real and personal property to trusts in which the client, his or her spouse, and his or her beneficiaries are named trustees. Many of these transfers of real property are done by quit claim deed.

According to information supplied by persons representing the Michigan Land Title Association, in *General Medicine v First American Title Insurance Company*, insurance coverage was denied to an individual who had conveyed his interest in the insured property to a corporation controlled exclusively by the insured. In this case, the individual had used a quit claim deed to effect the transfer. In the unpublished decision, the Michigan Court of Appeals held that since the conveyance was made by a quit claim deed, the insured no longer had an interest in the property; therefore, liability and coverage under the title insurance policy had ceased.

In light of this ruling, some attorneys who provide estate planning services have raised concern regarding their clients' insurance coverages being terminated when transferring real property into a trust for estate planning purposes. Legislation has been introduced to address this concern.

THE CONTENT OF THE BILL:

The bill would add a provision to Chapter 73, entitled "Title Insurance", of the Insurance Code. Under the bill, if a person who was an insured party under a title insurance policy transferred ownership of the property to a qualifying trust, following would have to apply:

- The qualifying trust would be considered an insured party under the policy.
- Coverage would extend to the qualifying trust.
- The title insurer would be subrogated, with respect to the property, to the rights of the insured party who transferred ownership of the property to the qualifying trust. All of the rights of the insured party that existed immediately prior to the transfer would be preserved and extended to the qualifying trust, regardless of the type of instrument used to effect the transfer.

"Qualifying trust" would mean a trust that met both of the following:

- The settlor of the trust was the insured party, his or her spouse, or both, under a title insurance policy covering property transferred to the trust.
- A present beneficiary of the trust was the insured party, his or her spouse, or both, under a title insurance policy covering property transferred to the trust.

MCL 500.2128 and 500.7307

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the bill would have no fiscal impact on state or local governments. (5-22-02)

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ARGUMENTS:

For:

The recent Michigan Court of Appeals ruling has some estate planners concerned regarding title insurance policies that their clients have transferred to trusts, or living trusts as some call them. The problem revolves around the types of deeds that can be used to transfer ownership of real property. A warranty deed carries a guarantee, into perpetuity, that there are no problems with the property such as liens or back taxes owed, or that the person selling the property is the person who has the legal interest – or authority – in the property and therefore the right to sell it. A quit claim deed, on the other hand, terminates a person's interest in the property; the appellate court held therefore that a quit claim deed would also terminate any subrogation rights.

Subrogation transfers the rights of one individual to another. Under a title insurance policy, the insurer has rights of subrogation. This means that the insurer can step in when clear title is contested and basically fight the battle for the insured person. The insurer can sue the person who falsely claimed to have the right to sell the property, or can sue to collect back taxes. Title insurance provides protection even when an individual later sells the property. If the new owner finds that the title is not clear, the individual who sold the property is protected from a lawsuit by his or her title insurance policy because the insurance company can go up the chain of past owners to find the person responsible for the defect in the title. If subrogation rights are not transferred to the trust along with the real property, the individual transferring the property to his or her trust loses the protection that title insurance is meant to provide. This is particularly important for estate planning, as the named beneficiaries are probably the heirs and would most likely sell the property after their parents' deaths. Also, according to industry representatives, many people transferring real property to trusts do so by means of a quit claim deed. The bill would correct this problem by allowing, for the purposes of estate planning only, title insurance – along with subrogation rights – to be transferred to a trust regardless of the type of deed that was used.

Against:

According to the Real Property Section of the State Bar of Michigan, real property cannot be transferred to a trust because according to real estate law, a trust is not considered to be a legal entity. Therefore, the bill is technically incorrect. Since real property can

only be transferred to a legal entity, such as a person, the bill could easily be corrected by specifying that the transfer of title insurance be made instead to the trustee of a validly created trust, or words to that effect. If this concern is not addressed, some believe that the continuance of clean title could be compromised.

POSITIONS:

The Michigan Land Title Association (MLTA) supports the bill. (5-23-02)

The Michigan Bankers Association does not oppose the bill. (5-24-02)

The Real Property Section of the Michigan State Bar opposes the bill. (5-24-02)

Analyst: S. Stutzky

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.