Insuring Investor Transactions in Texas

Texas Land Title Institute
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PROFESSIONAL

Bruce Goldston was in private practice for 15 years, where he concentrated on real estate, probate and commercial matters. He subsequently handled bank closings and commercial and real estate litigation for the Federal Deposit Insurance Corporation for 3 years. In 1996 he joined Alamo Title Insurance as Claims Counsel where he supervised the administration and resolution of all claims which arose from policies issued by Alamo Title in Texas and New Mexico. In July, 1998, he became Underwriting Counsel for Fidelity National and Alamo Title, and in 2009 he was named by Fidelity as State Counsel for Texas and Oklahoma. He joined WFG National Title Insurance Company as Vice President and Regional Counsel of the Southwestern Region in March, 2010, where he supervises underwriting for Texas and Oklahoma.

EDUCATION

Austin College
Sherman, Texas
BA, 1972

St. Mary’s University School of Law
San Antonio, Texas
JD, 1975

TRAINING/SPEAKING EXPERIENCE

Mr. Goldston has spoken over 260 times on real estate, title insurance, underwriting, claims and legal issues. Some of the topics he has covered include:

- Introduction to Title Insurance
- Avoiding and Administering Claims
- Manufactured Housing
- Insuring Construction Transactions
- Examining
- Insuring Around
- Probate
- Current Underwriting Issues
- Legislative Updates
- Bankruptcy
- Foreclosures
- Home Equity Lending
- Ethics for Title Company Employees
- Homesteads
- Intestate Succession
- Voluntary and Involuntary Liens
- Easements
- Reverse Mortgages
- Escrow and Indemnity Agreements
- Marital Rights
- Taxes and Title Insurance
- Business Entities
- Minerals and Title Insurance
- Title Policy Endorsements
- Surveys
- Regulatory Issues
- Easements
- Minerals and Title Insurance
- Surveys
- Title Policy Endorsements
- Surveys
The objective of this presentation is to examine closing procedures, policy coverages, and procedural and rate rules which affect investor transactions.

I. WHAT IS AN INVESTOR TRANSACTION?

For purposes of this presentation, we will consider an investor transaction to be one or more of the following:

- A purchase in which the buyer/borrower does not intend to occupy the property and/or intends to re-sell the property in the short term.
- A purchase of a note and lien secured by a deed of trust, usually a seller carry note and usually on residential property.
- Pass through transactions;
- Wrap transactions;
- A purchase following a short sale;
- A closing which involves an assignment of the earnest money contract;
- Option contracts; and,
- Purchases at tax sales, execution sales and HOA sales

II. FLIP TRANSACTIONS

A. A flip transaction is one in which a purchaser acquires title and re-sells to a third party immediately. The first purchaser usually has already contracted with his buyer and has agreed upon the sale terms prior to his acquisition of title. There is nothing inherently illegal about a flip; there is nothing illegal about making a profit through the process of buying and selling.
B. Most Texas title underwriters have established guidelines for flips that are similar to the following. Always verify guidelines with your own underwriter.

C. You will have (at least) two earnest money contracts. A contracts to sell to B and B contracts to sell to C. A to B will usually be a cash sale; B to C may be cash or with third party financing.

D. The first sale will close into escrow, meaning that filing of documents and funding of A to B is generally dependent on closing the second sale.

E. If C has a lender the lender’s closing instructions may prohibit the closing of a transaction if there has been a conveyance of the property within the past 6 months (or some other specified period) prior to closing. Read your instructions thoroughly.

F. If the proposed transaction does not comply with the lender’s requirements, you must require the lender to revise their requirements in writing so that your transaction is permitted. Disclose all facts to the lender. Ask for a written acknowledgement of the facts and further authorization to proceed with the closing.

G. The commitments for both transactions must show title vested in A. For the B to C transaction make a schedule C requirement that A must convey to B.

H. You must set up each transaction as a separate GF file.

I. Most underwriters have thresholds so that if the increase in sale price between the 2 sales is in excess of the greater of a stated percentage or a dollar amount you must call Underwriting.

J. Verify that the deed into A or the deed from A to B does not contain any restrictions regarding re-sales within a specific period of time. Be especially careful if A is HUD or if there is a deed from HUD in your recent chain. HUD’s prohibition on property flipping provides:

“Re-sales occurring 90 days or less following acquisition will not be eligible for a mortgage to be insured by FHA. Re-sales occurring between 90 and 180 days will be eligible provided that the lender obtains an additional appraisal from an independent appraiser based on a re-sale percentage threshold established by FHA; this threshold would be relatively high so as to not adversely affect legitimate rehabilitation efforts but still deter unscrupulous sellers, lenders, and appraisers from attempting to flip properties and defraud homebuyers. Lenders may also prove that the increased value is the result of rehabilitation of the property. Re-sales occurring between 90 days and one year will be subject to a requirement that the lender obtain additional documentation to support the value to address circumstances or locations where HUD identifies property flipping as a problem. This authority would supersede the higher expected threshold established for the above-mention 90 to 180 day period and will be invoked when FHA determines that substantial abuse may be occurring in a particular locality.”
K. Short sales and flips go together like oil and water. Be very careful. There is an inconsistency between having to sell property for less than the existing debt followed by a flip of the property for a profit.

L. Those of you who have handled short sales know that it is common for the seller’s lender to require that the short sale deed contain a restriction regarding subsequent sales.

M. The Federal Housing Finance Agency (FHFA) and Freddie Mac and Fannie Mae have implemented deed restrictions such as the following:

“Grantee herein is prohibited from conveying captioned property for any sales price for a period of **30 days** from the date of this deed. After this 30 day period, Grantee is further prohibited from conveying the property for a sales price greater than [insert 120% of short sale price] until **90 days** from the date of this deed. These restrictions shall run with the land and are not personal to the Grantee.”


Fannie Mae Servicing Guide Announcement SVC-2012-19 can be found at: [https://www.fanniemae.com/content/announcement/svc1219.pdf](https://www.fanniemae.com/content/announcement/svc1219.pdf)

N. When a short sale deed contains a restriction similar to the above, most underwriters require an exception in any title commitment or policy issued within the relevant period:

“Deed restriction, prohibiting certain subsequent resale transactions for up to ____ days, contained in the deed from ______________________ to ______________________, dated ______________, and recorded in Vol. ____, Page ____, of the Official Records of Real Property of _____ County, Texas.”

O. Some private lenders are adopting similar requirements; the language of the deed restriction and the time periods may vary. Every deed in a short sale transaction should be carefully reviewed, and an exception must be inserted in commitments and policies where such a restriction exists. You should of course adjust the time period to fit the actual restriction.

P. Some lenders present title agents with “short sale affidavits” which require the title agent to confirm or warrant certain off record facts which are simply outside your knowledge. Examples include vouching for the market value of the property or whether there are any agreements regarding a re-sale of the property.

Commissioner’s Order 12-0217
March 19, 2012
2012 Texas Title Insurance Periodic Hearing
Docket No. 2732
(9) Item 2012-91, to consider amending Procedural Rule P-35, Prohibition Against Guaranties, Affirmations, Indemnifications, and Certifications, to expressly allow or disallow affidavits from settlement agents in short sales beyond the coverage in our promulgated forms, is disapproved. Requiring title agents to execute short sale affidavits violates P-35, as written. Short sale affidavits seek assurances beyond the expected scope of title agents’ knowledge.

Q. It is suggested you can reply to a lender request that you sign a short sale affidavit by providing them a copy of the Commissioner’s Order.

R. Agents have received closing instructions asking them to agree they will not close another transaction regarding the property within the next 12 months.

III. NOTE PURCHASES BY INVESTORS

A. Anyone who holds a note secured by a mortgage, whether a large commercial lender or an individual, may assign or transfer the note and mortgage to a third party.

In a Note Sale – Transfer of Lien situation, the agent must obtain:

1. The original note which must be endorsed by the payee (either the original payee or the last payee to whom the note was endorsed) with the legend “Pay to the order of ___________”; the name of the note purchaser will be placed in the blank. Retain a photocopy of the endorsed note in your file;

2. An estoppel agreement from the current noteholder; and

3. An assignment or transfer of lien, signed by the person who is the current holder of the lien of record.

B. An assignee of a note can either purchase a LP showing the assignee as the named insured, or receive an Assignment of Lien Endorsement to the original loan policy. The Assignment of Lien form is located in Section III of the Endorsement Instructions of the Basic Manual and the general T-3 form is used.

C. According to P 9b(1), if the property is 1 to 4 family residential, the assignee must be one of the named agencies of the federal government in order to issue the Assignment Endorsement (T-3). On all other types of property, the assignee may be anyone.

“Said Loan Policy is hereby amended to name as the Insured: _________________. The lien described in Schedule A of said policy has been assigned to said named Insured by assignment dated _________ and recorded in the Office of the County Clerk of ___________ County, Texas (here insert clerk’s file number or book and page of recording),
and Schedule A of said policy is hereby amended to cover said assignment, and it is expressly stated that the effective date of said policy is changed to the date of this Endorsement."

... "This endorsement shall be effective provided that, at Date of Endorsement:
The note or notes secured by the lien of the Insured Mortgage have been properly endorsed and delivered to the Assignee, or if the note or notes are transferable records, the Assignee has "control" of the single authoritative copy of each "transferable record" as these terms are defined by applicable electronic transaction laws." (January 3, 2014)

D. If a loan policy is being issued, the Schedule C requirement for a Note Sale – Transfer of Lien is:

Requirement is made that the closer obtain an estoppel letter signed by the Borrower and Note Holder verifying that the lien is valid; stating the current amount of unpaid principal and accrued interest; penalties, costs, etc., if any; stating that payment on the Note is not currently in default, or if it is that it has not been accelerated, or if it has been accelerated that it has been reinstated (obtain copy of written reinstatement); and stating the description of the property securing the lien.

The original note must be presented and endorsed by the current note holder to the note purchaser.

E. The LP will be issued for the balance on the note and the premium will be computed from the Basic Rate table. However, if there was an LP previously insuring the lien, the premium for the new LP will be computed under R-6B.

R-6B Subsequent to Mortgagee Policy – When a Mortgagee Policy(ies) is requested, for any reason whatsoever, on a lien already covered by an existing Mortgagee Policy(ies), but not on a renewal or extension thereof, the new policy being in the amount of the current unpaid balance of the indebtedness, the premium for the new policy shall be at the Basic Rate, but a credit for three-tenths (3/10) of said premium may be allowed.

IV. PASS THROUGH TRANSACTIONS

A. The term “pass through” describes the situation where a premium is collected in one transaction and no policy is issued; the premium is “passed through” to another transaction and used to purchase a policy in the second transaction.

R-2. Rebates and Discounts
No Company shall charge for a policy in one transaction and withhold issuance of a policy thereon, nor shall any Company charge a premium for a policy in one transaction
and apply the charged premium in a subsequent transaction, except when same covers identical land to that contained in the initial conveyance, and when same shall have been consented to by the parties to all conveyances involved, which consent may be provided for in the contract(s) on which the transaction is based, or may be given in a separate written instrument, or may be evidenced by the acceptance and signing of a closing statement clearly setting forth application of the premium charge as agreed by the parties to the transaction(s).

B. All parties should sign a simple pass though letter setting out their agreement to the collection of the premium in one transaction and the application of the premium in another transaction; retain the original letter in your file.

V. WRAP CONTRACTS AND MORTGAGES

A. A wrap transaction is one where a buyer (1) takes title subject to (not assuming) an existing deed of trust and (2) grants to the seller a new deed of trust that will wrap or wraparound the existing deed of trust. The buyer makes payments to the seller, with the seller continuing to make payments on the underlying loan. The underlying loan will not be paid off at closing and the lien will not be released. The existing lien will remain the first lien unless the prior lender agrees to subordinate its lien to the new lender’s lien.

B. A wrap is often used as a method of avoiding the consequence of a due on sale clause. If the deed of trust being wrapped contains a due on sale clause, some underwriters require that a separate Schedule B exception be inserted specifically taking exception to the clause, and not just to the deed of trust in general.

C. The risk to the buyer is that the seller will receive the buyer’s payment but will not make the payment on the wrapped note.

D. When issuing the title policy to the new lender, be sure that the existing, wrapped lien is shown on Schedule B as a superior lien. This is true regardless of whether a new lien is made by a third party or is a seller carry back.

E. Be careful if the mortgage being wrapped is FHA insured. The FHA position is that if property encumbered by an FHA insured lien is sold, the loan must be paid off or it must be assumed (with FHA approval) by the purchaser.

VI. ASSIGNMENTS OF EARNEST MONEY CONTRACTS

A. This type of investor strategy can be characterized as sort of a flip but where the middleman is never in title. It is sometimes called a “poor man’s flip” since the investor can reap a profit from the transaction without having to come up with purchase money.
B. The contract must be assignable. This is generally accomplished by showing the buyer as “. . . and/or assigns.” If the contract is not assignable and the buyer wants to assign it, you should require that it be amended so as to make it an assignable contract.

C. The assignment fee. Must it be reasonable? What is reasonable? Check with your underwriter and ask if there are any guidelines on this subject.

D. Must the assignment fee be shown on the settlement statement or CD?

E. Is the assignment fee included in the final buyer’s owner policy coverage? Loan policy coverage?

VII. HARD MONEY LENDERS

A. The term “hard money loans” is difficult to define but they usually share the characteristics of being relatively short term, having higher than prevailing commercial mortgage interest rates, and having low loan to value ratios.

B. Often times an investor who does not have good credit will borrow from a hard money lender on the expectation that he will quickly sell the property and pay off the loan from his profit. The hard money lender makes the loan on the basis of the equity cushion in the land instead of on the borrower’s credit.

VIII. LAND TRUSTS

A. A ‘land trust’ is a trust in which there is no duty imposed on the trustee other than to hold title to the land. Frequently the title of such a trust will be the street address of the property, such as “The 506 Willow Trust.” A land trust may not be a valid trust if the trustee has no duties. The Texas Property Code (Sect. 112.032) provides that property held in trust vests in the beneficiary if the trustee has neither a power nor a duty related to the administration of the trust; such is generally the case with a land trust.

B. When dealing with a land trust you should treat title as being held by the beneficiary and require the beneficiary to sign any deed to convey. Be sure to search the beneficiary’s name in your plant the same as if the beneficiary had taken title in his/her own name to begin with.

C. Also search the trustee’s name, as trustee, and require the joinder of the trustee on any conveyance. Although the trustee may not really hold legal title, nevertheless requiring joinder of the trustee will help create a searchable chain of title.

D. Many underwriters will not insure a purchase by a land trust.

IX. CONTRACTS FOR DEED
A. Although not as common as it used to be, investors will sometimes try to sell land under a contract for deed.

B. The Texas Legislature has enacted several pro consumer statutes over the last 15 years that have substantially leveled the playing field for buyers under contracts for deed. Conversely, these changes have made selling land under a contract for deed less attractive for a seller.

Effective September 1, 2015, HB 311 amended Sect. 5.064 of the Texas Property Code regarding contracts for deed as follows:

Sect. 5.064 Seller’s Remedies on Default

A seller may enforce the remedy of rescission or of forfeiture and acceleration against a purchaser in default under an executory contract for conveyance of real property only if:

(4) the contract has not been recorded in the county in which the property is located.

(Emphasis supplied)

Amendments to Sect. 5.066 reiterate the principle stated above.

C. If the contract for deed has been recorded the seller’s only remedy upon default is to pursue a non-judicial or judicial foreclosure. The remedies of rescission and forfeiture are not available.

X. OPTIONS TO PURCHASE

A. If an investor has identified a property that he believes can be re-sold for a profit but he does not yet have a buyer he can tie up that property and take it off the market by obtaining an option to purchase from the owner.

B. If the investor already has a buyer he may flip the property or assign the contract.

C. There is no established time limit for an option to purchase but most are usually in the 45 to 90 day range.

D. Few Texas underwriters are interested in insuring an option to purchase. Even if they did, the coverage would be only for the amount paid for the option which would probably be a small amount.

XI. AD VALOREM TAX SALES

A. Many investors purchase property at ad valorem tax sales. Consult your underwriters’ bulletins for the relevant guidelines. Most underwriters will not insure the purchaser at a tax sale.
B. If the mineral rights have not been severed, is the redemption period 2 years even if the property was not the homestead of the taxpayer?

Sec. 34.21. RIGHT OF REDEMPTION.

(a) The owner of real property . . . that was used as the residence homestead of the owner or that was land designated for agricultural use when the suit or the application for the warrant was filed, or the owner of a mineral interest . . . may redeem the property on or before the second anniversary . . .

(e) The owner of real property . . . other than property that was used as the residence homestead of the owner or that was land designated for agricultural use when the suit or the application for the warrant was filed, or that is a mineral interest, may redeem the property in the same manner . . .

XII. EXECUTION SALES

A. There are two ways to execute on a judgment in Texas. The judgment creditor can obtain a writ of execution against the property and direct the officer to seize and sell the property. The other way is for the creditor to file a new suit to foreclose its judgment lien.

B. If a separate suit to foreclose the judgment lien is not filed, few if any underwriters will consider that intervening third party liens are wiped out by the execution sale. This is largely because the notice required to be given to intervening creditors is public notice of published in a newspaper or by posting.

C. If a suit to foreclose is filed and intervening lienholders are joined as parties and properly served, and if the judgment recites that their liens are inferior to the judgment lien, the underwriter may be willing to insure around those liens.

D. Some underwriters will not insure after an execution sale unless the vested party obtains a deed from the prior owner whose title was foreclosed on.
PREMIUM PASS THROUGH LETTER

DATE: 
GF: 
SELLER: 
INTERMEDIATE BUYER: 
ULTIMATE BUYER: 
TITLE AGENT: 
UNDERWRITER: WFG National Title Insurance Company

TO: TITLE AGENT AND TITLE UNDERWRITER
We, the undersigned, being the SELLER, INTERMEDIATE BUYER, and the ULTIMATE BUYER described above, hereby give you written instructions to apply the premium collected in the transaction between the SELLER and the INTERMEDIATE BUYER ("first transaction") to the transaction between the INTERMEDIATE BUYER and the ULTIMATE BUYER ("second transaction").

The premium paid by the SELLER in the first transaction shall be applied to the benefit of the ULTIMATE BUYER in the second transaction.

This Pass Through Letter is given to the Title Agent and Underwriter for the purpose of complying with Rate Rule R-2, entitled “Rebates and Discounts.”

SELLER: 

________________________________________

INTERMEDIATE BUYER: 

________________________________________

ULTIMATE BUYER: 

________________________________________

ESTOPPEL CERTIFICATE FOR NOTE SALE

Affiant is the Maker/Holder of a Note executed by Maker dated , 20___, in the original principal amount of ____________. The Note is secured by a Deed of Trust ("Deed of Trust") of even date therewith, recorded in ____________County, Texas, covering the property described in said Deed of Trust.

Affiant states the following upon oath:

1. As of the ___ day of ________, 20___, the outstanding principal balance of the Note is $______________________________.

2. As of the ___ day of ________, 20___, the outstanding accrued interest on the Note is $______________________________.

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3. The terms of the Note and the Deed of Trust have not been modified unless an instrument evidencing such modification has been recorded in the real property records of the county in which the Property is located.

4. The Deed of Trust is a valid lien against the Property.

5. The Maker is not in default under the Note or the Deed of Trust.

6. The maturity of the Note has not been accelerated, or, if it has, the Note has been reinstated.

7. There are no defenses to the enforcement or the validity of the Note or Deed of Trust.

8. Affiant acknowledges that it is aware that the title agent and the title agent’s underwriter are relying upon the truth of the statements made herein, and said agent and underwriter would not proceed with issuing a title policy but for the giving of this Estoppel Certificate.

[Add signature blocks and jurat for Maker and Holder]
Know Your Underwriting Guidelines

- The areas we will discuss are treated differently by different underwriters so be sure you are aware of the particular guidelines applicable to your transaction.
I. What is an Investor Transaction

- A purchase where the buyer does not intend to occupy the property
- Pass through
- Flips
- Wrap
- Short sale purchase
- Assignments of earnest money contracts
II. Flip transactions

- Purchaser acquires land with the intent to re-sell immediately. A to B to C
- Identity of second buyer is known to the first buyer before the land is acquired.
- Flips are not illegal.
- What could go wrong?
You will have 2 earnest money contracts.
A to B will close into escrow. It’s usually “no deal” unless B can close on the sale to C.

If C has a third party lender read those instructions carefully. Is there a prohibition on other transfers of title in recent past?
Both commitments must vest in A. On the B to C commitment require a conveyance from A to B.
This provides notice to C’s lender.
- Thresholds. Know your underwriter. How large of a profit is ok?
- Be careful if HUD is involved. Restrictions on title transfers.

- Wet flips and dry flips.
- Dry flip = B needs the funds from the sale to C to acquire the land from A.
- Dry flips may not be insurable.
- **Short sales and FLIPs?**
- Beware of deed restrictions following short sales.
- Limitations placed on title company?

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**Bad Divorce**

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Nice purse!

Thanks. It's my ex-husband.
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III. Note Purchases

- A note and lien may be transferred to a third party.
- Usual requirements: (1) Original note must be **endorsed** by the original or current holder to the note purchaser; (2) an **estoppel** agreement should be obtained from the borrower and noteholder; and (3) the current lienholder must execute an **assignment or transfer** of lien.

- The purchaser/assignee can either purchase (1) an Assignment of Lien Endorsement [see P-9b(1)] or (2) a new Loan Policy.
- Limit on endorsement if property is 1-4.
- New Loan Policy. Premium reduced under R-6B? 30% reduction.
IV. Pass Through Transactions

- A premium cannot be collected in one transaction and applied in another transaction. R-2.
- Unless . . .
- All parties must sign a Pass Through Letter.

V. Wrap Contracts and Wrap Mortgages

- A wrap is not an assumption.
- The existing lien goes on Sch B of the commitment, not Sch C.
- Often used to avoid the consequence of a due on sale clause.
- Specific Sch B exception
- for the due on sale clause?
What is the property has an FHA insured mortgage on title?
Can you wrap an FHA mortgage?
FHA requires assumption or payment.

VI. Assignments of Earnest Money Contracts

- Investor can make a profit from a transaction without fronting any money.
- The contract must be assignable. “Buyer and/or assigns.”
- What is the contract is not assignable?
What is a reasonable fee?
Show the fee on the settlement statement?
1099?

Policy coverages.
$50,000.00 sale with a $5,000.00 assignment fee. What is buyer’s coverage?
The assignment fee is merely an expense of acquiring the land.
What is lender’s coverage?
VII. Hard Money Lenders

- Hard money loans are usually short term, have higher than prevailing commercial interest rates and origination fees and have low loan to value ratios.
- Often the borrower is not a good credit risk or the transaction is too speculative for a commercial lender to approve.
- Loan will be re-paid through a sale.

What is the concern?
- Just a red flag?
VIII. Land Trusts

- Investors sometimes put title to property they acquire into a Land Trust; the name of the trust is the street address.
- A property held in trust vests in the beneficiary if the trustee has neither a power nor a duty related to the administration of the trust. Sect. 112.032, Texas Property Code.
- Require joinder by all trustees and all beneficiaries.

IX. Contracts for Deed

- Once upon a time, investors sold land under contracts for deed.
- Why were they popular?
- Consumer oriented changes in the law.
Recording a contract for deed eliminates the power to cancel or forfeit the contract; requires a judicial or non judicial foreclosure.

Same rule if it is 1-4 and 40% of the purchase price has been paid or the equivalent of 48 monthly payments.

If you choose to close a sale by contract for deed your underwriter will probably require that the contract be recorded.

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**X. Options to Purchase**

- Investor wants to purchase but has not identified a buyer.
- Can flip or assign if he has a buyer.
- 45-90 days.
- Probably hard to find an underwriter.
- Low coverage amount.
XI. Ad Valorem Tax Sales

- Check your underwriting bulletins.
- Tax sales right of redemption and mineral interests.
- What kind of clouds are wiped out by the foreclosure?

XII. Execution Sales

- 2 ways to execute on a judgment.
- Underwriter more willing to insure if separate suit is filed.
- Third parties wiped out?
- Require deed from prior owner?
The end.