5 Title to Real Property

In California, the basic principles followed governing title to real property were derived from England's Common Law generally implemented by case law known as stare decisis. This term is Latin for "to stand by a decision". Stare decisis is applied as a doctrine to bind a trial court by higher court decisions (appellate and supreme court) that become precedents on a legal question raised in the lower/trial court. Reliance on such precedents is required of lower/trial courts until a higher court changes the rule.

California has a 150-year history of development and evolution in the way its courts have applied legal principles regarding the title to real property and the conveyance/transfer of the title. These legal principles also apply to the encumbering of title to real property through mortgages or deeds of trust and to provide notice of and to evidence monetary claims against the title in the form of liens. This history is documented by the enactment of constitutional provisions and statutes and by a long line of case law. In the absence of some specifically applicable constitutional or statutory provisions, the Common Law/case law prevails.

CALIFORNIA ADOPTS A RECORDING SYSTEM

California was admitted to the Union by the United States on September 9, 1850. One of the first acts of the Legislature of the new state was to adopt a recording system by which evidence of title or interests in the title could be collected and maintained in a convenient and safe public place. The purpose of establishing a recording system was to inform persons planning to purchase or otherwise deal with land about the ownership and condition of the title. This system was designed to protect innocent lenders and purchasers against secret sales, transfers, or conveyances and from undisclosed encumbrances/liens. The purpose of this system is to allow the title to the real property to be freely transferable.

The California Legislature adopted a recording system modeled after the system established by the original American Colonies. It was strictly an American device for safeguarding the ownership of and the encumbering of land/property. Recording of sales, transfers, or conveyances and encumbrances/liens as part of a public record was established to impart *constructive* notice. This system of recording is known as the "Race Recording", or as the "Race-Notice Recording" statute/law.

Actual v. Constructive Notice
Actual notice consists of express information of a fact. *Constructive* notice means notice given by the public records. By means of *constructive* notice, people are presumed to know the contents of recorded instruments. Publicly recording instruments of transfer/conveyance or to encumber/lien the title to real property imparts *constructive* notice. For example, Civil Code Section 2934 enacted in 1872 states in part, "Any assignment of a mortgage and any assignment of the beneficial interest under a deed of trust may be recorded, and from the time the same is filed for record operates as *constructive* notice of the contents thereof to all persons…".

Which Instruments May Be Recorded
The Government Code of California provides that, after being acknowledged (executed in front of a Notary Public, or properly witnessed as provided by applicable law), any instrument or judgment affecting the title to or possession of real property may be recorded. <u>See</u> *Government Code Sections 27201, 27201.5, 27287, and 27288.*

The word "instrument" as defined in Section 27279(a) of the Government Code "…means a written paper signed by a person or persons transferring the title to, or giving a lien on real property, or giving a right to a debt or duty." A similar definition is set forth in a historic 19th century case. <u>See</u> *Hoag v Howard (1880) 55 Cal. 564-567*. The definition of an "instrument" does not necessarily include every writing purporting to affect real property. However, the term "instrument" does include, among others, deeds, mortgages, leases, land contracts, deeds of trust and agreements between or among landowners/property owners.

Purpose of Recording Statutes
The general purpose of recording statutes is to permit (rather than require) the recordation of any instrument which affects the title to or possession of real property, and to penalize the person who fails to take advantage of recording.

However, existing law includes examples where recording is required as a predicate to accomplish a defined public policy objective. One such example is Civil Code Section 2932.5 that provides, “Where a power to sell real property is given to a mortgagee, or other encumbrancer, in an instrument intended to secure the payment of money …[T]the power of sale may be exercised by the assignee of the assignment **if duly acknowledged and recorded** (emphasis added).”

Another example is in Business and Professions Code Section 10233.2 regarding perfecting ownership of promissory notes or interests therein. This Section states in part “…the delivery, transfer and perfection shall be deemed complete even if the broker retains possession of the note or collateral instruments and documents, provided that the deed of trust or assignment of the deed of trust or collateral documents in favor of the lender or purchaser **is recorded in the office of the county recorder in the county in which the security property is located, and the note is made payable to the lender or is endorsed or assigned to the purchaser** (emphasis added).”

Because of the recording of instruments of conveyance or encumbrance/lien, purchasers (and others dealing with title to property) may in good faith discover and rely upon the ownership of title or an interest therein. While the Government Code does not specify any particular time within which an instrument must be recorded, priority of recordation will ordinarily determine the rights of the parties if there are conflicting claims to the same parcel of land/property, i.e., the title thereto or an interest therein. The instrument recorded first in the chain of title would generally achieve priority over subsequently recorded instruments (fact issues such as subordination or *actual* notice may affect priority notwithstanding recording dates). The definition of the “Race Recording” or “Race-Notice Recording” statutes/laws is intended to describe the manner of achieving priority in the chain of title. Generally, the person winning the race gains priority.

The county recorder in the county within which the property is located must record instruments affecting real property. If the property lies in more than one county, the instrument, or certified copy of the record, must be recorded in each county in which the property is located in order to impart *constructive* notice in the respective counties.

If it is necessary to record a document written in a foreign language, the recorder will file the foreign language instrument with a certified translation. In those counties in which a photographic or electronic method of recording is employed, the foreign language instrument and the translation may be recorded and the original instrument returned to the party who requested recordation. See *Government Code Section 27293.*

When an Instrument is Deemed Recorded

Generally, an instrument is recorded when it is duly acknowledged or verified and deposited in the recorder’s office with the proper officer and marked “filed for record.” It is the duty of the recorder to number the instrument in the order in which it is deposited, including the year, month, day, hour, and minute of its reception, and indicate at whose request it was “filed for record.” The contents of the document are transferred to its appropriate book or image of records upon the page or pursuant to the number endorsed on the document, and the original document is returned to the party who left it for recording.

The recorder indexes all recorded documents in alphabetical order according to the names of the grantors and grantees or mortgagors or mortgagees, which terms include holders of beneficial interests in and trustors/borrowers of deeds of trusts, and the name or nature of the document. The documents are also indexed by date of recording and the recording reference. See *Government Code 27230 et seq.*

Effect of Recording as Imparting Notice

The courts have ruled that the benefits of a recording statute are not available to one who takes title with *actual* notice of a previously executed though unrecorded instrument. For example, possession of land/property by one other than the seller is *actual* notice to an intending buyer sufficient to impose a duty to inquire about the possession. Despite the recording statutes and the assurance they give about the status of title, a prudent purchaser should inspect the premises in person or through a trusted agent.

The obligation to inspect includes inquiring of persons in possession of the real property (e.g., a tenant or lessee), what claim such persons have to occupy and use the property, and is there a written agreement supporting the claim. The agreement may be a month-to-month tenancy, a leasehold or an estate for years, a land contract of sale, an option to purchase, a lease with a first right of refusal, etc. Such a claim would be imparted by *actual* notice because of the occupancy of the persons in possession. The agreement evidencing the claim need not be recorded to affect the title to the real property.

In addition to the foregoing, there are many types of unrecorded interests that a prospective purchaser may discover during a physical inspection of property. For example, a pathway or sewer line may mean adjoining owners have an unrecorded easement. Lumber or recent carpentry work may mean certain persons have a right to file mechanics' liens.

The recording laws do not protect the party "first to record" against what may be discovered through a physical inspection, nor do standard form title insurance policies cover the situations previously described. As previously mentioned, the inspection of a property to be purchased or encumbered is recommended and advice from a qualified professional is often required (e.g., lawyer, title officer, civil engineer, etc.) before proceeding to purchasing or encumbering the land/property. The intended title insurer should be asked about extended coverage to insure against the unrecorded interests that may be discovered by physical inspection as discussed in this section.

Priorities in Recording

The California recording statutes encourage prompt recording of conveyances and encumbrances and prohibits use of the *constructive* notice doctrine as an aid to proven fraud. The recording laws protect only innocent parties.

Certain priorities are affected by statutory provisions. For example and for the purposes of establishing priority, existing California Law distinguishes between a mortgage and deed of trust given for the price of real property (purchase money mortgage) from such instruments of encumbrance given to refinance or further encumber the property (non-purchase money mortgage). The former have priority over all other liens created against the purchaser, subject to the operation of the recording laws, and the later do not have priority over the defined liens. Further, the priority to be established for mortgagees or deeds of trust on an estate for years in real property (leasehold) shall be determined in the same manner as establishing the priorities of such liens against the title of real property. See *Civil Code Section 2898.*

Not all liens on real property rank in priority according to their respective dates of recording. For example, with respect to the same parcel of property, A executed a mortgage in favor of B dated June 1 and recorded June 20. A executed a mortgage in favor of C dated June 10 and recorded June 15. C's mortgage will be superior in priority to B's only if C did *not* have, on or prior to June 15, notice of B's mortgage.

Special Lien/Encumbrance Situations

Liens and encumbrances are discussed again later in this chapter. However, it will be helpful to note here the impact of the recording laws on liens and encumbrances. Liens are imposed for monetary claims against the title to real property or for the performance of an act in connection therewith. Liens are encumbrances, but there are encumbrances that are not monetary claims, e.g., an easement. These forms of encumbrances typically affect the condition or use of the property. It can be said that all liens are encumbrances, but not all encumbrances are liens.

California Law refers to mortgages and deeds of trust as functional equivalents. The historic distinctions between the two instruments include the application of the "lien" vs. "legal title" theories (to be discussed later in this chapter), and the use of a third party trustee with certain defined powers in a deed of trust but not in a classic mortgage instrument. The perceived limitation of the use of the trustee in a deed of trust was eliminated in 1986 through the enactment of Civil Code Section 2920. For the purposes of this chapter, the terms "mortgage" and "deed of trust" are used interchangeably and for each other as functional equivalents, as defined in current California Law.

A lender/encumbrancer will often agree in the deed of trust (the senior instrument) to make "future advances" as a part of a secured loan transaction. Another lien/encumbrance (for example, a junior deed of trust or a mechanic's lien) may intervene between the time of recordation of the lender's senior deed of trust and the time of a "future advance". A question of priority is then posed regarding the sums advanced by the senior lender.

When the terms of the senior deed of trust obligate the lender to make "future advances" (e.g., progress payments under a construction loan), these "obligatory advances" have the same priority as the loan secured by the senior deed of trust, regardless of intervening liens (monetary claims). See *Civil Code Section 2884.*

In other cases, the senior lender may have the option of making “future advances” of money to the borrower/trustor, but is not required to do so. These “optional advances” for priority purposes date from the time the advance is made, unless the lender can show no *actua*l or *constructive* notice of intervening liens. This does not mean lenders are excused from checking the public record.

The issue of “future advances” is of particular concern in loan products known as Home Equity Lines of Credit (“HELOC”). Such loan products have become popular in the last 15 to 20 years. The advances made as part of a HELOC loan transaction are generally “optional”, i.e., defined conditions must first be met prior to the lender extending to the borrower/trustor additional credit. To facilitate the use of these loan products, the title insurance industry has offered endorsements to the institutional lending community (financial depository institutions and certain licensed lenders) maintaining for the purposes of the coverage provided the priority of the “optional advances” to protect the interests of the lenders making HELOCs. <u>See</u> *Civil Code Section 2884.*

Mechanics’ liens generally relate back to the time of the commencement of the construction work as a whole. Thus, a deed of trust must be executed, delivered, accepted and recorded prior to commencement of any work regarding the security property to assure the priority of the construction loan secured by the deed of trust over the claims that may be made by contractors, laborers, material houses, suppliers, design professionals and the like in the form of mechanics liens. <u>See</u> *Civil Code Section 3134.*

Liens for real property taxes and other general taxes, as well as special county and municipal taxes and assessments are superior in priority to the lien of any mortgage or deed of trust regardless of the date of creation, including execution, delivery, acceptance, and recording. California Law provides that any tax or assessment declared a lien on real property should be given priority over all other liens, including judgments, deeds, mortgages, deeds of trust, etc. <u>See</u> *Revenue & Taxation Code Section 2192.1.*

Provided they are bona fide encumbrances/liens, deeds of trust and mortgages recorded prior to general federal tax liens or state tax liens are superior in priority to those liens. However, subsequent to the non-judicial foreclosure of the security property, the IRS has asserted the priority of its tax claims are altered to a senior position when the assets to which such claims attached become the cash available from the foreclosure proceeds.

Persons having priority may by agreement waive this priority in favor of others. An agreement to do this is called a “subordination agreement.” These agreements are often executed in connection with deeds of trust to subordinate a senior encumbrance/lien to a later recorded junior encumbrance/lien. An example is where a landowner’s/property owner’s “purchase-money” deed of trust (securing a debt in the form of a seller “carry-back” established at the time the security property was purchased) is subordinated by agreement to a construction loan to finance the improvements to be made to the property.

Without such priority of claim for payment against the real property, a construction lender would typically decline to extend credit and, therefore, funds would not be available for the building contractor to expend time and materials on the construction project.

In certain loan transactions, statutory requirements are imposed regarding the use of subordination clauses. These requirements include notice of the existence of a subordination clause, and a disclosure of the contents of the subordination agreement. While these requirements apply to loans in the amount of $25,000 or less, they represent good guidelines to be considered when engaging in the use of subordination clauses and agreements. <u>See</u> *Civil Code Section 2953.1 et seq.*

As previously mentioned, a mortgage or deed of trust given for the purchase price of real property at the time of the conveyance of the security property has priority over all other liens created against the purchaser, subject to operation of the recording laws. <u>See</u> *Civil Code Section 2898.*

Two or more deeds of trust recorded at the same time (concurrently) may contain on the face of each deed of trust (as part of an industry practice) a recital about which is intended by the parties to be first, second, or third in priority. The recitals can be effective subordination agreements with the informed knowledge and consent of the lenders and the trustors/borrowers (referred to as mortgagors).

OWNERSHIP OF REAL PROPERTY

All property has an owner, the government - federal, state, or local— or some private party or entity (typically referred to as persons). Very broadly, an estate in real property may be owned in the following ways:

1. Sole or several ownership;
2. Joint, common, or community ownership;
   a. Tenancy in common;
   b. Joint tenancy;
   c. Community property; or,
   d. Partnership interests.
3. Ownership by other lawfully created entities.

SOLE OR SEVERAL OWNERSHIP

Sole or several ownership is defined to mean ownership by one person. Being the sole owner, one person enjoys the benefits of the property and is subject to the accompanying burdens, such as the payment of taxes. Subject to applicable federal and state law, a sole owner is free to dispose of property at will. Typically, only the sole owner's signature is required on the instrument of transfer/deed of conveyance. See *Civil Code Section 681*.

JOINT, COMMON, OR COMMUNITY OWNERSHIP

Joint, common, or community ownership or co-ownership means simultaneous ownership of a given piece of property by several persons (two or more). See *Civil Code Section 682*. The types of such ownership interests include the following:

Tenancy in Common

Tenancy in common exists when several (two or more) persons are owners of undivided interests in the title to real property. It is created if an instrument conveying an interest in real property to two or more persons does not specify that the interest is acquired by them in joint tenancy, in partnership, or as community property. Some instruments of transfer/deeds of conveyance clearly state the intentions of the persons acquiring are to hold title as tenants in common. See *Civil Code Section 685.*

Example: Interests of such tenants in common may be any fraction of the whole. One party may own one-tenth, another three-tenths, and a third party may own the remaining six-tenths. If the deed to cotenants does not recite their respective interests, the interests will be presumed to be equal.

There is a unity of possession in tenancy in common. This means each owner has a right to possession and none can exclude the others nor claim any specific portion for him or herself alone. It follows that no tenant in common can be charged rent for the use of the land/property, unless otherwise agreed to by all the cotenants. On the other hand a tenant in common who receives rent for the premises/property from a third party, must divide such profits with the other tenants in common in proportion to the shares owned. Similarly, payments made by one tenant in common for the benefit of all may normally be recovered on a proportionate basis from each. These might include, among others, moneys spent for necessary repairs, taxes, and interest and principal payments under a deed of trust.

Subject to applicable federal and state law, a tenant in common is free to sell, transfer or otherwise convey, or mortgage the tenant's own interest as he or she sees fit. The new owner becomes a tenant in common with the others. Few lenders are willing to extend credit to be secured by a mortgage or deed of trust against only the interest of a single tenant in common. In the event of a foreclosure of their mortgage encumbrance/lien, lenders typically do not want to end up as co-owner with other tenants in common. Because of the practical difficulties involved in selling, transferring or otherwise conveying, or mortgaging the interest of a single tenant in common, the tenant may be limited in his/her effort to liquidate the single interest to forcing a sale of the entire property by filing an action before a court of competent jurisdiction known as a "partition action."

No right of survivorship exists for individual tenants when title is held as tenants in common. The undivided interest of a deceased tenant in common passes to the beneficiaries (heirs or devisees) of the estate subject to probate, pursuant to the last will and testament of the deceased or by intestate succession. The heirs or devisees of the deceased simply take the tenant's place among the other owners who continue to hold title to the property as tenants in common. See *Probate Code Section 6400 et seq.*

Joint Tenancy

Joint tenancy exists if two or more persons are joint and equal owners of the same undivided interest in real property. Generally, to establish a joint tenancy a fourfold unity must exist: interest, title, time, and possession. Joint tenants have the same interest, acquired by the same conveyance, commencing at the same time, and held by the same possession. See *Civil Code Section 683.*

The most important characteristic of a joint tenancy is the right of survivorship that flows from the unity of interest. If one joint tenant dies, the surviving joint tenant (or tenants) become(s) the owner(s) of the property to the exclusion of the heirs or devisees of the deceased. Thus, joint tenancy property cannot be disposed of by the last will and testament, is not subject to intestate succession, and typically does not become part of the estate of a joint tenant subject to probate.

Further, the surviving joint tenant(s) is/are not liable to creditors of the deceased who only hold existing encumbrances/liens on the joint tenancy property. The words "with the right of survivorship" are not necessary for a valid joint tenancy deed, although they are often inserted. To perfect the ownership interests of the surviving joint tenants, severance of the joint tenancy of the deceased is to be accomplished and evidenced in the public record.

The creditors of a living joint tenant (as distinct form a deceased joint tenant) may proceed against the interest of that tenant and force an execution sale. This would sever the joint tenancy and leave title in the execution purchaser and the other joint tenant as tenants in common.

Creating A Joint Tenancy. With limited exception, California appellate courts have accepted and enforced the common law rule that if any one of the four unities — time, title, interest or possession — is lacking, a tenancy in common, not a joint tenancy, exists. An exception to the general rule has been more recently applied in connection with the time of acquisition of the title to the property. Consultation with knowledgeable legal counsel is recommended to answer questions that may be posed by property owners regarding the establishment of joint tenancies and the legal, practical, tax, estate planning, and other considerations involved.

However, by statute a joint tenancy may be created:

1. By transfer from a sole owner to himself or herself and others as joint tenants.
2. By transfer from tenants in common to themselves or to themselves, or any of them, and others as joint tenants.
3. By transfer from joint tenants to themselves, or to any of them, or to others as joint tenants.
4. By transfer from a husband and wife (when holding title as community property or otherwise) to themselves, or to themselves and others, or to one of them and to another or others as joint tenants.
5. By transfer to executors of an estate or trustees of a trust as joint tenants.

See *Civil Code Section 683.*

Severance. A joint tenant may sever the joint tenancy as to his or her own interest by a conveyance to a third party, or to a cotenant. If there are three or more joint tenants, the joint tenancy is severed as to the interest conveyed but continues as between the other joint tenants as to the remaining interests. If title is in A, B and C as joint tenants, and A conveys to D, then B and C continue as joint tenants as to a two-thirds interest and D owns a one-third interest, as tenant in common. If A and B only are joint tenants and B conveys to C, then A and C would be in title as tenants in common. See *Civil Code Section 683.2*

Another method is a partition action by the joint tenants. If the partition cannot be made without prejudice to the owners, a court may order the property sold and the division of the proceeds of the sale distributed ratably to the owners. In some circumstances, a severance will not terminate the right of survivorship interest of the other joint tenants in the severing joint tenant's interest. Nor, under the circumstances set out in Civil Code

Section 683.2, may a severance contrary to a written agreement of the joint tenants defeat the rights of a purchaser or encumbrancer for value and in good faith and without knowledge of the written agreement.

On death of a joint tenant, the joint tenancy is automatically terminated. Nevertheless, for record title purposes, the following must be recorded in the county where the property is located:

- A certified copy of a court decree determining the fact of death and describing the property; or
- A certified copy of the death certificate or equivalent, or court decree determining the fact of death, or letters testamentary or of administration or a court decree of distribution in probate proceedings. With each of these alternatives, it is customary to attach an affidavit that identifies the deceased as one of the joint tenants of the property.

Some of the Pros and Cons of Joint Tenancy. On the plus side, the major advantage of joint tenancy is the comparative simplicity of vesting title in the surviving joint tenant (or joint tenants). The marketable title delay arising from probate proceedings in the form of a stay for as much as six months (or even longer) is avoided. Although certain legal costs are ultimately involved in terminating the joint tenancy, the customary commissions and fees payable to executors or administrators and to their attorneys may become unnecessary.

As previously mentioned, a further advantage of joint tenancy is that the survivor holds the property free from debts of the deceased tenant and from liens against the deceased tenant's interest. This can work an injustice to creditors, but a diligent creditor can usually take appropriate precautionary steps to avoid such loss, or may have access to other assets of the decedent. On the other hand, in many situations joint tenancy is a pitfall for the uniformed or unwary.

The supposed advantages may be imaginary. A joint tenant may not want the other (surviving) joint tenant to get the title free and clear; the likely saving of probate fees is at least partly offset by costs of terminating the joint tenancy, and may be completely offset by added taxes. The probate delay is not unreasonably long, and there may be no creditors of the estate. Moreover, the joint tenant gives up the right to dispose of his or her interest by a last will and testament.

Giving advice about the way to hold title to real property is ill advised and considered the unauthorized practice of law when offered by persons who are not members of the State Bar of California. As previously mentioned, significant legal, practical, tax, estate planning, and other issues and consequences may result from holding title in one form or another. The advice of knowledgeable legal counsel and other appropriate professionals is strongly recommended before selecting the form of ownership of the title to real property

Community Property

Community property generally consists of all property acquired by a husband and wife, or either, during a valid marriage, other than separate property acquired prior to the marriage, by gift, or as an individual heir or devisee of a deceased. Separate property may also include the fruits falling from the previously described tree of categories of separate property, as well as property designated as separate by the husband or wife or by court order. Separate property of either the husband or the wife is not community property.

Separate property of a married person includes:

1. All property owned before marriage.
2. All property acquired during marriage by gift or inheritance.
3. All rents, issues and profits of separate property, as well as other property acquired with the proceeds from sale of separate property. For instance, if a wife owned a duplex prior to marriage, the rents from the duplex would remain her separate property. If she sold the duplex and bought common stock, the stock and dividends would be her separate property. It would have to be clearly and unequivocally identifiable as separate property, and separate records should be maintained to make certain any separate property is not commingled in any way with the community property. Very often husband and wife deliberately may allow their separate property to merge with community property in keeping with their intentions or with their conduct and actions.
4. Earnings and accumulations of a spouse while living separate and apart from the other spouse.

5. Earnings and accumulations of each party after a court decree of separate maintenance.

6. Property conveyed by either spouse to the other with the intent of making it the grantee's separate property.

It should be recalled that a husband and wife often hold property as joint tenants. Yet, even when title is held in joint tenancy, it is possible (e.g., by separate written agreement) to own the assets as community property. The record title may not be controlling in light of off-record agreements showing other intentions of the parties. For example, joint tenancy property owned by married persons may, in fact, be considered separate property. See *Civil Code Sections 682.1 and 687* and the *Family Code under Part 1 and 2, Division 4, commencing with Section 720*.

Management and control. Each spouse has equal management and control of community property. An exception exists if one of the spouses manages a community personal property business. That spouse generally has sole management and control of that business. Community property is liable for the debts of either spouse contracted after marriage. Community property is liable for a debt contracted prior to marriage, except that portion of the community property comprised of the earnings of the other spouse.

Neither spouse may make a gift of community property without the consent of the other. Neither spouse may encumber personal property such as the furniture, furnishings, or fittings of the home, or the clothing of the other spouse or minor children without the written consent of the other spouse. However, each must join in the sale/transfer or conveyance, or the encumbrancing or leasing of community real property.

If real property is owned by several (two or more) persons, real estate licensees should obtain the necessary signatures of each person in title to listing agreements and to purchase and sale agreements, whether for the purpose of countering or accepting offers from the intended buyer/purchaser.

Each spouse has the right to dispose of his or her half of community property by will. Absent a will, title to the decedent's half of the community property passes to the surviving spouse. See *the Family Code under Part 4, Division 4, commencing with Section 1100.*

Joint tenancy and community property. Considerable confusion surrounds the status of some family homes in California, since the husband and wife may acquire their home with community funds but proceed (as previously mentioned) to take record title "as joint tenants." It is not generally understood that some of the consequences of holding title in joint tenancy are entirely different from the consequences of holding title as community property.

As previously mentioned, California courts are aware of this problem and have established the rule that the true intention of husband and wife as to the status of their property shall prevail over the record title. Ambiguity results from the specific circumstance of having the record title in joint tenancy while the true character of the property, as intended by the husband and wife, is community property. This transition might be accomplished by appropriate agreement in writing, or even by a deed from themselves "as joint tenants" to themselves "as community property."

Among themselves, the rights and duties of joint tenants are generally the same as among tenants in common, with the vital exception of the rule of survivorship. As previously discussed, a joint tenant may borrow money and, as security for the repayment of the debt, execute a mortgage or deed of trust on his/her interest just as a tenant in common may. This does not destroy the joint tenancy, but if the borrower should default, and the mortgage or deed of trust should be foreclosed while the borrower is still alive, the joint tenancy would be ended (a severance) and a tenancy in common created. As previously noted, most lenders would hesitate to make such a loan.

Should the borrower/trustor/mortgagor die before the mortgage is paid off or foreclosed, the surviving joint tenant gets title free and clear of the mortgage executed by the deceased joint tenant. When title is held as community property, no separate interest exists for the purpose of encumbering through a mortgage or a deed of trust. As previously mentioned, the signatures of both the husband and wife are required to sell, transfer, or otherwise convey or encumber the community property.

While a probate is typically required to dispose of the community property in the event of the death of either spouse, in certain fact situations a limited probate proceeding has been authorized by existing law. This limited probate proceeding is commonly known as a community property or small estate “set-aside”. For example, the court may find that the entire estate of the deceased spouse is property passing to the surviving spouse. In such event, the court may determine that no administration of the estate is required. See *Probate Code Section 6600 et seq. and Section 13656.*

TENANCY IN PARTNERSHIP

At the time of initial codification in California Law of the various forms of ownership of property interests, the recognized entity for ownership was a partnership. Tenancy in partnership exists if two or more persons, as partners, own property for partnership purposes. Under the Uniform Partnership Act, the incidents of tenancy in partnership are such that:

1. A partner has an equal right with all other partners to possession of specific partnership property for partnership purposes. Unless the other partners agree, however, no partner has a right to possession for any other purpose.
2. A partner’s right in specific partnership property is not assignable except in connection with the assignment of rights of all the partners in the same property.
3. A partner’s right in specific partnership property is not subject to attachment or execution, except on a claim against the partnership.
4. On death, a partner’s right in specific partnership property vests in the surviving partner (or partners). The rights in the property of the last surviving partner would vest in the decedent’s legal representative. In either case, the vesting creates a right to possess the partnership property only for partnership purposes.
5. A partner’s right in specific partnership property is not subject to dower or curtesy (both have been abolished in California by statute) nor allowance to widows, heirs, or next of kin. Even when married, a partner’s right is not community property. On the other hand, a partner’s interest in the partnership as such (that is, a partner’s share of profits and of surplus) is governed by community property rules for some purposes.

These incidents make sense because two or more persons are attempting to carry on a business for profit. Without these incidents, continuity and unified, efficient operation would be difficult. Partners are not, however, prevented from owning different fractional parts of the business. Thus, although each partner has unlimited liability to third parties for firm debts, each partner’s interest in profits and losses may be any percentage to which the parties agreed.

Partners may also structure the business relationship as a partnership in many different ways. By agreement, one partner may have greater authority than the other partners. An example that is often used is a limited partnership. The general partner or partners manage and control the partnership and the limited partners (in exchange for limited liability) give up management and control. In a partnership where all partners have equal rights of management and control, the partnership is commonly referred to as a general or co-partnership.

The Uniform Partnership Act set forth in 15001 et seq. of the Corporations Code and the Limited Uniform Partnership Act set forth in 15501 et seq. of the Corporations Code each have been or will be repealed effective January 1, 2010. The Uniform Partnership Act of 1994, commencing with Section 16100 of the Corporations Code, remains operative and describes, among other issues, the scope of and limitations imposed on general or co-partnerships in California. This law includes language describing the relationships between partners, the handling of charging orders and claims of creditors against the partnership or an individual partner, and how the partnership is to be wound-up and dissolved.

Limited Liability Partnerships are described in the Corporations Code, commencing with Section 16951. However, the Uniform Limited Partnership Act of 2008 (enacted subsequent to the previous sections of the Corporations Code describing Limited Liability Partnerships) is set forth in the Corporations Code, commencing with Section 15900.

The foregoing body of law is complex and comprehensive. Understanding what portions have been or will be repealed and what portions remain operative is essential. Furthermore, to establish partnership relationships requires an understanding of practical, legal, tax and other important issues. Accordingly, the advice of knowledgeable legal counsel is recommended before proceeding to form a partnership or determining to hold title to real property or interests therein in a partnership entity.

OTHER LAWFULLY CREATED ENTITIES

In the 19^{th} century when some of the applicable Civil Code Sections previously cited were enacted, the entity most commonly used to hold title or interests therein was a partnership. Corporations and trusts existed, and when they joined in a common economic enterprise, were often identified as “combinations”. Two additional entities have been more recently authorized by state legislative action. They are Limited Liability Companies (“LLCs”) and, as previously discussed, Limited Liability Partnerships (“LLPs”).

Each of the foregoing entities may and do hold title to real property or to interests therein. The body of law describing corporations and their organization, operation, and management is enormous. Three categories of corporations are recognized in California Law. Included are general corporations, nonprofit corporations, and corporations for a specific purpose.

The law applicable to corporations is set forth in federal and state statutes and regulations. For example, the State of Delaware publishes statutes and regulations regarding corporations, which are instructive as many corporations are organized under Delaware law. Organizing and operating a corporation under California Law requires review of California Corporations Code Sections 100 through 2319 (General Corporation Law), Sections 5000 through 10841 (Nonprofit Corporation Law), and Sections 12000 through 14451(Corporations for Specific Purposes).

Limited Liability Partnerships were discussed in the previous section entitled, “TENANCY IN PARTNERSHIP”. Limited Liability Companies are organized similar to a corporation, but taxed similar to a partnership. The legislation authorizing the use of such entitles was enacted in 1994 and is set forth in Corporations Code Sections 17000 through 17656. LLCs may hold title to real property and to interests therein. However, a real estate broker may **not** license an LLC entity to perform acts for which a real estate license is required. See *Corporations Code Section 17375.* Real estate brokers may license corporations as brokers and partnerships are able to perform acts for which a real estate license is required through licensed partners that are real estate brokers. See *Business and Professions Code Sections 10137.1, 10158, and 10211.*

The body of law describing the administration of trusts, the duties of trustees, the accounting of trust assets, federal and state tax issues, etc. is complex and appears in various state and federal statutes and regulations. The primary reference for trust administration is found in California Probate Code Sections 16000 through 16504. The use of trusts to hold title or interests therein occurs most often in family trusts or in other forms of inter vivos trusts.

Again, it is important to understand that the use of trusts, as well as other entities, to hold title or interests therein should occur only with the advice of knowledgeable legal counsel and of other appropriate professionals. A word of caution is necessary regarding the demands frequently made upon real estate and mortgage brokers by lenders and title insurers (or their underwritten companies), either directly or through escrow holders, regarding properties where the title is held in trusts by principals of the brokers.

Typically, the real estate or mortgage broker is directed to instruct his/her principals to transfer the title to the real property from an existing trust to the individual beneficiaries/settlers/trustors for purposes of encumbering the property with new financing; or to sell, transfer or convey title to the property to third parties. The practical, legal, estate planning, and tax consequences may be significant and should be reviewed, in advance, by legal counsel and appropriate professionals representing the principals for this purpose. Real estate and mortgage brokers may be engaging in the unauthorized practice of law to provide such instructions to their principals (even when directed to do so by representatives of the lending, title, or escrow industries) without making it perfectly clear the information required to make such a decision is beyond the scope of the practice of real estate and requires the advice of knowledgeable legal counsel and competent professionals.

ENCUMBRANCES/LIENS

In this section, the principal types of encumbrances/liens are examined that may be imposed on a given parcel of land/property without affecting the fee title to the owner’s real property as part of the owner’s estate. This discussion includes the distinctions between the "lien" vs. "legal title" theories, and the fact that the "lien" theory has been adopted by California and represents current law.

Definition- Encumbrance

An encumbrance may be defined very generally as any right or interest in land/property, possessed by a stranger to the title, which affects the value of the owner's estate, but does not prevent the owner from enjoying and selling, transferring, or otherwise conveying the fee title.

Two categories of encumbrances exist: those affecting title and those affecting condition or use of the property**.**

Encumbrances that affect title. Most notably, these are liens. A lien is defined as a charge imposed on property and made security for the payment of a monetary claim or the performance of an act in connection therewith. Typically, the lien is imposed for the payment of a debt evidenced by a promissory note. Liens may also be imposed solely for the performance of an act in the form of a performance deed of trust.

Liens may affect real or personal property and may be voluntary (e.g., a home mortgage to secure a loan) or involuntary (e.g., imposed by law for overdue taxes). A lien may be specific, affecting only a particular property (e.g., a trust deed, or a mechanic's lien on a given property) or may be a general lien, affecting all property of the owner not exempt by law (e.g., a money judgment, or a lien for overdue state or federal income taxes). As previously mentioned in this chapter, all liens are encumbrances, but not all encumbrances are liens.

Encumbrances that affect the physical condition or use of the property. Examples are easements, building restrictions and zoning requirements, and encroachments.

A buyer will commonly accept a deed to encumbered property, with the price adjusted accordingly. Often, the encumbrance may not be objectionable, e.g., an easement for utility purposes. But sometimes a buyer may insist that the encumbrance be removed or cleared from the public record before the transaction closes.

Cloud on the title. A "cloud on the title" is defined as any outstanding claim or encumbrance that would, if valid, affect or impair the owner's title to a particular property/estate. While the cloud remains, the owner is prevented from selling transferring, or conveying marketable title. The ability to further encumber the title may also be impaired by a "cloud on the title".

Examples are: a mortgage paid off but without official recordation of that fact (a reconveyance of a deed of trust); an apparent interest in the property which remains because one of a group of heirs fails to sign the deed on sale of the property; or a notice of action (a lis pendens) which remains on the public record even after the plaintiff and defendant have agreed to dismissal of the court action. Removal of a cloud may require time and patience. Meanwhile, closing will be postponed until the persons requesting coverage obtain a title insurance policy without reference to the cloud.

It is important to understand the distinction between the "lien" theory and the "legal title" theory and the impact of these theories on the use of mortgages and deeds of trust as security devices/instruments for the repayment of a monetary claim or the performance of an act.

LIEN THEORY VS. LEGAL TITLE THEORY

History. An essential concept of California Law is the ability to secure the repayment of monetary claims or the performance of an act typically in connection therewith by a "lien" that does not impair the owner's rights to freely enjoy the benefits of the use and ownership of the property. These benefits include the right to sell, transfer, or otherwise convey, or further encumber the title to the land/real property. It is settled law that California is a "lien" and not a "legal title" theory state when imposing encumbrances/liens against the title of real property.

California has a 150-year history of development and evolution in the way its courts have applied legal principles to mortgages and deeds of trust. As of 2009, this 150-year history is split approximately in half, creating two 75-year periods. The first 75-year period begins in 1859, ends in 1933, and is marked by the California Supreme Court's historic insistence that mortgages create "liens" and deeds of trust transfer "legal title". The Court held that the two instruments/security devices have no common features, and each are controlled by different bodies of real property law ("Title Period").

The second 75-year period begins in 1933, runs to the present, and is marked by the 180-degree reversal of position in which the California Supreme Court currently insists that a deed trust is the functional equivalent of a mortgage with power of sale. Therefore, both instruments (mortgages and deeds of trust) are governed by mortgage laws ("Lien Period"). In these two periods, dramatically differing opinions on the same legal issue were offered by California courts. These differing opinions evolved the law regarding deeds of trust over the last 75 years to reconcile the law applicable to mortgages with power of sale, and thus established the "lien theory" as the applicable California Law.

The most comprehensive analysis of distinctions in the legal status of deeds of trusts and mortgages during the Title Period is contained in two California Law Review articles. The first published in 1915 by Professor Kidd is *Trust Deeds and Mortgages in California*. See, *A. M. Kidd, Trust Deeds and Mortgages in California, 3 Cal. L. Rev 381 (1915).*

The second analysis, *Applications of the Distinction between Mortgages and Trust Deeds in California*, was published in 1938 and brings Professor Kidd's 1915 article current through the watershed Bank of Italy II decision in 1933. See, *Joseph M. Cormack and James B. Irsfeld Jr., Applications of the Distinction between Mortgages and Trust Deeds in California, 26 Cal. L. Rev. 206 (1938).*

In the 1915 article, Professor Kidd identifies the paradoxical character of California mortgage and deed of trust law, which applied the "lien" theory and "legal title" theory of real property security instruments in the same state at the same time. The Title Period begins with the California Supreme Court's decision in Koch v. Briggs, 14 Cal. 256 (1859.

The California Supreme Court held in the Koch v. Briggs case: "It [a deed of trust] has no feature in common with a mortgage, except that it was executed to secure an indebtedness." As the 1915 and 1938 articles detail, the legal effect of seeking to impose the "lien" theory for mortgages and the "legal title" theory for deeds of trust resulted in numerous distinctions that seemingly had no foundation in legal principle, since both instruments were clearly real property instruments/security devices. These distinctions were most prominent in substantive areas such as the right of redemption (none historically recognized for deeds of trust), the one form of action rule, limitations on deficiencies, and negotiability of a note secured by a mortgage versus deed of trust, the fiduciary duties imposed on foreclosure trustees, homestead exemptions, mechanics liens, and the impact of bankruptcy.

As noted by the leading treatise on California real estate: "Creditors began using the deed of trust as a real property security instrument during the 19th century because of the procedural inhibitions imposed on the mortgage by the courts and the impediments attendant with judicial foreclosure of the debtor's equity of redemption. The use of a conveyance to a trustee clothed with a power of sale offered the creditor several advantages over the mortgage so that, by the time the distinctions between the two security instruments were removed during the early part of the 20th century, the deed of trust had become the generally accepted and preferred security device in California."

"Except for some minor distinctions, for all practical purposes, a mortgage that contains a power of sale has a similar legal effect and economic function as the deed of trust. Each is subject to the same procedures and limitations on judicial and non-judicial foreclosure, each is subject to the same redemption provisions both prior to and after the foreclosure sale, and each is subject to the same anti-deficiency limitations. Both are intended by the parties to serve the same economic function of providing security for the performance of an obligation." See, *Miller & Starr, California Real Estate 3d, § 10:1.*

The depression era years of 1932 and 1933 were the turning point for beginning the process of reconciling California mortgage and deed of trust law. Two California Supreme Court opinions arising from the same case symbolize the fitful end of the "Legal Title" period and the beginning of the "Lien" period. Although Bank of Italy II is universally cited as the seminal decision reconciling mortgage and deed of trust law, little attention is paid to the fact that just six (6) months earlier, the California Supreme Court decided Bank of Italy Nat. Trust & Savings Ass'n v. Bentley, 14 P. 2d 85 (1932) – Bank of Italy I.

In Bank of Italy I, the California Supreme Court held: “It must be considered as thoroughly settled in California that a deed of trust is not a mortgage. Substantial differences between two types of security have been recognized, and statutes applicable to mortgages have generally been held inapplicable to deeds of trust…”.[citations omitted]…Stockwell v. Barnum, 7 Cal. App. 413, 94 P. 400 …Id., 14 P. 2d at 86.

This holding of Bank of Italy I makes even more remarkable the reversal of position contained in Bank of Italy II (only six months later in the same case before the same court): “This view, that deeds of trust, except for the passage of title for the purpose of the trust, are practically and substantially only mortgages with a power of sale…”. See, *Bank of Italy Nat’l Trust and Savings Ass’n v. Bentley, 217 Cal. 644, 657 (1933).*

Current Law. The California Supreme Court’s recognition in Bank of Italy II that deeds of trust are “practically and substantially only mortgages with power of sale” renders obsolete all pre-1933 case law that was built upon the legal foundation of Koch v. Briggs that holds a deed of trust “has no feature in common with a mortgage, except that it was executed to secure an indebtedness.” In case after case published over the last 75 years, the California courts have reconciled any remaining distinctions between a deed of trust and mortgage with power of sale. See, The 1989 California Supreme Court case of *Monterey S.P. Partnership v. W.L. Bingham, Inc., 261 Cal. 3d 454 (1989).* (“Monterey”) reveals just how far the unification of trust deeds and mortgages has come.

In Monterey, the court considered whether service of a complaint to the trustee of a deed of trust in a mechanic’s lien foreclosure action is sufficient to bind the beneficiary of the deed of trust. In its holding, the court makes it abundantly clear that a deed of trust creates a “lien” on the property and has the same legal effect as a mortgage with a power of sale: “Although Whitney, supra, 10 Cal. 547, involved the effect of a mechanic’s lien foreclosure on the rights of a mortgagee, the holding applies equally to a beneficiary under a deed of trust. As explained in describing “the anomalous nature of deeds of trust in this state” (Bank of Italy etc. Assn. v. Bentley (1933) 217 Cal. 644, 657, 20 P.2d 940), “deeds of trust, except for the passage of title for the purpose of the trust, are practically and substantially only mortgages with a power of sale...”.

In practical effect, if not in legal parlance, a deed of trust is a “lien” on the property and not a transfer of fee title to the trustee, i.e., establishing and adopting the “lien” theory vs. the “legal title” theory. It would be inconsistent with Bank of Italy, supra, 217 Cal. 644, 20 P.2d 940, to deny the beneficiaries the rights of mortgagees recognized in Whitney, supra, 10 Cal. 547, merely because the beneficiaries’ security interest took the form of a deed of trust, which conveys “title” to a trustee. The deed of trust conveys “title” to the trustee “only so far as may be necessary to the execution of the trust.” (Lupertino v. Carbahal (1973) 35 Cal.App.3d 742, 748, 111 Cal.Rptr. 112.)

The Court of Appeal also relied on Johnson v. Curley (1927) 83 Cal.App. 627, 257 P. 163, which held that beneficiaries under a deed of trust were not necessary parties to an action to have that deed declared void for fraud. However, as plaintiff Monterey and amici curiae on its behalf point out, the Court of Appeal’s reliance on Johnson was misplaced for several reasons. First, **Johnson was decided before the court clarified that a deed of trust is tantamount to a mortgage with a power of sale**. (Bank of Italy, supra, 217 Cal. at p. 657, 20 P.2d 940.) Id., at 590-591 (emphasis added).

As Monterey makes clear, pre-Bank of Italy II cases premised on the distinction between trust deeds and mortgages are no longer good law. The same result was recently reached in Aviel v. Ng, 161 Cal. App. 4th 809 (2008). In Aviel, the court considered whether a subordination agreement subordinating a lease to “mortgages” also subordinated the lease to a deed of trust beneficiary that had foreclosed on the lessor’s property. The lessee argued strenuously that the perceived distinctions between a mortgage and a deed of trust should result in the court finding that the subordination did not apply to the deed of trust. The court rejected the arguments as follows:

Here there was a subordination clause within the lease rendering the lease subordinate to “mortgages which may now or hereafter affect” the real property. The Ngs, however, emphasize distinctions between mortgages and deeds of trust that are either illusory or unimportant. For example, they underscore that a deed of trust conveys legal title, and, citing Anglo-California T. Co. v. Oakland Rys. (1924), 193 Cal. 451, 225 P. 452, urge that “the interest in the property [vests] as an estate and not as a lien.” Anglo-California T. Co. predates Bank of

Italy and is predicated on the obsolete "lien" versus "legal title" theory historically relied on to differentiate the two security devices/instruments. That theory has been discredited by the more contemporary jurisprudence discussed above which functionally equates the two instruments and recognizes that a deed of trust, for all practical purposes, is a "lien" on the property. Also See, *Domarad v. Fisher & Burke, Inc., 270 Cal.App.2d 543, 553 (1969).*

These authorities and many more since 1933 confirm that any pre-Bank of Italy II authorities are premised on the distinction between deeds of trust and mortgages with power of sale are no longer good law. These earlier decisions have been rendered obsolete based on the evolution of California Law and the consistently applied holding that mortgages and deeds of trust are functionally equivalent and trust deeds are evaluated under general mortgage law. Also See, *Cornelison v. Kornbluth, 15 Cal.3d 590 (1975).*

MECHANIC'S LIEN

California law expressly provides that persons furnishing labor or material for the improvement of real estate may file liens upon the property affected, if the persons furnishing labor or material are not timely paid. Thus, an unpaid contractor, or a craftsman employed by the contractor to work on a building project, but who has not been paid by the owner or contractor may protect their right as an unpaid contractor or craftsman employed by a contractor, to receive payment by filing a lien against the property in a manner prescribed by law. Any person who has furnished material such as lumber, plumbing, or roofing holds the same right, if the claim is not timely paid. It is because of the possibility of these liens being recorded that an owner employing a contractor often requires that a bond be furnished to guarantee payment of possible mechanics' lien claims.

DESIGN PROFESSIONAL'S LIEN

Effective January 1, 1991, California Civil Code Sections 3081.1 through 3081.10 provide for the filing of a design professional's lien.

For this purpose, a "design professional" is defined as a certificated architect, a registered professional engineer, or a licensed land surveyor who furnishes services, pursuant to a written contract with a landowner (property owner) for the design, engineering, or planning of a work of improvement.

If a landowner (property owner) defaults under a written contract with a design professional, a 10-day written demand for payment must be made on the landowner (property owner) prior to the recordation of a design professional's lien. Section 3081.3 requires the 10-day written demand for payment be mailed by first-class registered or certified mail, postage prepaid, addressed to the landowner (property owner), which notice of and demand for payment shall specify that a default has occurred (pursuant to the contract or agreement) and the amount of the default. Subsequently, the design professional may record a notice of lien against the real property on which a work of improvement is to be constructed, with the notice of lien describing the real property being improved, and further specifying the building permit or other governmental approval of the work as a condition of recording the notice of lien. See *Civil Code Section 3081.2 and 3081.3.*

The design professional's lien will not take priority over the interests of record of a purchaser/ buyer/lessee/encumbrancer, if the interests of the foregoing in question was duly recorded prior to the recording of the design professional's lien. See *Civil Code Section 3081.9.* The design professional's lien does not apply to the work of an improvement related to a single-family owner occupied residence where the construction costs are less than $100,000 in value. See *Civil Code Section 3081.10.*

Except as previously discussed, the statutes provide for enforcement of a design professional's lien in the same manner as a mechanic's lien.

Definition

A lien is a charge imposed in some way, other than by a transfer in trust upon specific property by which it is made security for the performance of an act. A mechanic's lien is a lien that secures payment to persons who have furnished material, performed labor, or expended skill in the improvement of real property belonging to another. See *Title 15 of the Civil Code, commencing with Section 3082*.

It is helpful to keep in mind while reading and thinking about this material on mechanics' liens that:

- The mechanic's lien claimant's fundamental objective is to get paid; and
- The claim of mechanic's lien is the claimant's security used to reach the objective of payment.

To convert the security for the lien into money requires:

1. Timely recordation of a notice and claim of lien (one document) in the county recorder's office in which the work of improvement is located;
2. Perfection of the recorded notice and claim of lien by the filing of an action (a lawsuit) in the right court;
3. Recordation of a lis pendens (a written notice that a lawsuit has been filed concerning real property, involving either the title to the property or a claimed ownership in the property);
4. Timely pursuit of the lawsuit to judgment; and
5. Enforcement of that judgment by a mechanic's lien foreclosure sale.

Origin

The basic lien rights of mechanics, materialmen, artisans and laborers is found at Article XIV, Section 3 of the California State Constitution:

"Sec. 3. Mechanics, persons furnishing materials, artisans, and laborers of every class, shall have a lien upon the property upon which they have bestowed labor or furnished material for the value of such labor done and material furnished; and the Legislature shall provide, by law, for the speedy and efficient enforcement of such liens."

The statutes enacted pursuant to this constitutional provision are, as previously mentioned found in Title 15, Division 3, Part 4, of the Civil Code, commencing with Section 3082. This Section of the law is entitled, "WORKS OF IMPROVEMENT".

The Theory

The mechanic's lien law is based on the theory that improvements to real property contribute additional value to land; therefore, it is only equitable to impose a charge on the land/property equal to such increase in value. This charge may exist in the absence of any direct contract relationship between the lien claimant and the landowner. The lien must, however, be founded upon a valid contract with the contractor, subcontractor, material house, supplier, lessee or vendee. Also, ordinarily the lien is valid only to the extent of labor and materials furnished for and actually used in the job.

Public Policy

The mechanics' lien statutes and the decisions of the courts interpreting and construing them reflect a strong public policy of providing extraordinary rights to unpaid contributors of services and material in the property they were instrumental in improving, and in the funds intended for payment for the improvements. The rights of these unpaid contributors accrue and may be enforced against the property, even though (in certain fact situations) the owner of the property has not contracted with the claimant and no personal liability exists to the claimant.

The mechanic's lien device is the traditional remedy giving security to people who improve the property of others. However, owners are given means within the California statutes to protect against the burdening of their land/property with improper liens. The basic elements of California's system of protection for mechanics' lienors and owners are:

1. Mechanic's lien;
2. Stop notice on private work;
3. Stop notice on public work;
4. Payment bond on private work;
5. Payment bond on public work;
6. Contractor's license bond; and
7. Notice of nonresponsibility.

Persons Entitled to a Mechanic's Lien

The constitutional guarantee of the right to a mechanic's lien upon the property is provided to mechanics, materialmen, contractors, subcontractors, lessors of equipment, artisans, design professionals, machinists, builders, teamsters, draymen, and all persons and laborers of every class performing labor upon or bestowing skill or other necessary services upon, or bestowing materials, or leasing equipment to be used or consumed in or furnishing appliances, teams, or power contributing to works of improvement. See *Section 3110 of the Civil Code*. Persons specifically entitled to mechanics' liens by virtue of the constitution and the statutes include the following:

Mechanics	Registered Engineers
Materialmen	Licensed Land Surveyors
Contractors	Machinists
Subcontractors	Builders
Lessors of Equipment	Teamsters
Artisans	Draymen
Architects	Union Trust Fund

See *Section 3111 of the Civil Code*

Property Subject to Mechanics' Liens

The land/property that may be subject to a claim of mechanic's lien should be the property described in a recorded claim of mechanic's lien. Perhaps the only safe exception to this is real property owned and used by the public. No lien for work or material attaches to a "public work." See *Los Angeles Stone Co. v. National Surety Co.*, 178 C 247, 173 P 79 (1918). In situations in which private enterprise undertakes improvement of public lands/properties, a claim of lien could be sustained against the improvements, although it would be invalid as to the land/property. See Western Electric Co. Inc. v. Colley, 79 CA 770, 251 P 331 (1926).

With every statutory increase in the designation of those contributors of services and material entitled to a claim of mechanic's lien, there has usually been a corresponding broadening of the land/property interests that may be subjected to a claim of mechanic's lien. Today, under appropriate circumstances, a claim of mechanic's lien may attach to only a building or structure; only to land/property beneath a building or structure; to both land/property and the building or structure; or, to a parcel of land upon/property for which there is no structure.

Public Works

This discussion of the mechanic's lien law applies only to private works of improvement. Sections 3179 through 3214 and Sections 3247 through 3252 of the Civil Code should be consulted in connection with any question or problem arising from the contribution of labor or material to a public work of improvement. A "public work of improvement" means any work of improvement contracted for by a public entity. "Public entity" means the state, Regents of the University of California, a county, a city, district, public authority, public agency, and any other political subdivision or public corporation in the state. See *Civil Code Sections 3099 and 3100.*

Work of Improvement

Mechanics' liens are triggered by the commencement of a work of improvement. A work of improvement is defined in Section 3106 of the Civil Code as including the construction, alteration, addition to, or repair of a building or structure. The structure could be a bridge, ditch, well, fence, etc. It may also include activities not directly associated with a building or structure such as seeding, sodding, planting, or grading. A work of improvement includes "site improvements" such as trees or other vegetation located on the land/property, the drilling of test holes, grading, filling, or otherwise improving the land/property as well as the street, highway, or sidewalk in front of adjoining the land/property. "Site improvements" also improve constructing or installing sewers or other public utilities, the construction of areas, vaults, cellars, or rooms under the land/property including sidewalks and demolishing or removing of any improvements on the land/property. See *Civil Code Section 3102.*

Lender's Priority

If commencement of work has occurred on a project prior to recordation of a mortgage or deed of trust, all mechanics' liens are prior to the recorded instrument of encumbrance. The lender's margin of security for repayment of a construction loan is jeopardized by the commencement of work on the project prior to recordation of the instrument of encumbrance. If any mechanic's lien claimant can show that commencement of work occurred prior to recordation of the lender's instrument of encumbrance, all mechanic's lienors will take priority over the lender if the real property/land subject to the work of improvement is sold at sheriff's sale. <u>See</u> *Civil Code Section 3134.*

Preliminary 20-Day Notice

The right to claim a lien and to assert the privileges of a mechanic's lien claimant is dependent on compliance with numerous statutory procedural requirements.

The initial step in the perfection of a claim of mechanic's lien for all claimants, except one under direct contract with the owner, one performing actual labor for wages or an express labor trust fund, as defined in Civil Code Section 3111, is to give the preliminary 20-day notice specified in Section 3097 of the Civil Code. That is, before recording a mechanic's lien, the lien claimant gives a written notice to certain persons, depending on the relationship of the lien claimant to the work of improvement and the owner of the real property/land on which the work has been done or will be done. The notice may be given any time after the contract has been entered into, but it must be given no later than 20 days after claimant has first furnished labor, services, equipment or materials to the job site. This 20-day notice is preliminary to the recording of a mechanic's lien. It is a prerequisite to the validity of a claim of mechanic's lien. The persons who are entitled to *receive* the notice depends on the relationship of the mechanic's lien claimant to the owner of the property. Thus:

1. If the claimant has a direct contract with the owner, the notice needs to be given only to the construction lender, if any, or to the reputed construction lender, if any. <u>See</u> *Section 3097(b) of the Civil Co*de.
2. If the claimant does not have a direct contract with the owner, the notice is required to be given to the following persons. <u>See</u> *Section 3097 (a) of the Civil Code:*
   a. The owner, or reputed owner;
   b. The original contractor, or reputed contractor; and
   c. The construction lender, or reputed construction lender.
   d. Any subcontractors with whom the claimant has contracted.

The purpose of the notice is to inform the owner, original contractor, and construction lender, if any, prior to the time of recording a claim of lien, that the improved property may be subject to liens arising out of a contract to which they are parties. <u>See</u> *Wand Corp. v. San Gabriel Valley Lumber Co. 236 CA2d 855, 46 Cal. Rptr. 486 (1965).*

The preliminary 20-day notice shall contain all of the following:

1. Name and address of the person furnishing the labor, service, equipment, or materials;
2. Name of the person who contracted for purchase of the labor, service, equipment, or materials;
3. A description of the job site sufficient for identification (e.g., common street address of the job site or legal description);
4. A general description of the labor, service, equipment, or materials furnished, or to be furnished and an estimate of the total price thereof; and
5. A Notice To Property Owner in bold face type as required by law.

<u>See</u> *Civil Code Section 3097.*

An up-to-date form should be used since a failure to use a current form that complies with the statute may cause the court to disregard the preliminary 20-day notice. <u>See</u> *Harold James Inc. v. Five Points Ranch, Inc., 158 CA3 1, 204 CR 494 (1984).*

Every written contract entered into between a land/property owner and an original contractor shall provide space for the owner to enter his name and address of residence and place of business. The original contractor must make available the name and address of residence of the owner and the name and address of the construction lender or lenders to any person seeking to serve a preliminary 20-day notice. See *Section 3097 (m) of the Civil Code*.

If one or more construction loans are obtained after commencement of construction, the property owner must provide the name and address of the construction lender or lenders to each person who has given to the property owner a preliminary 20-day notice. See *Section 3097 (n) of the Civil Code*.

Filing a Preliminary 20-day Notice

Each person serving a preliminary 20-day notice may file (not record) that notice with the county recorder in which any portion of the real property is located. The filed preliminary 20-day notice is not a recordable document and, hence, is not entered into the county recorder's indexes that impart *constructive* notice. The recorder is to maintain a separate and distinct index of the filings of the preliminary 20-day notice that does not impart *actual* or *constructive* notice to any person of the existence (or contents) of the filed 20-day notice. No duty of inquiry on the part of any party to determine the existence or contents of the preliminary 20-day notice is imposed by the filing. See *Civil Code Section 3079(o).*

The purpose of filing the preliminary 20-day notice is limited. It is intended to provide the necessary information for the county recorder to issue notices of recorded notices of completion and of cessation to those persons who filed the 20-day notice. Once the county recorder's office records either a notice of completion or cessation, it must mail to those persons who filed a preliminary 20-day notice, notification that a notice of completion or cessation has been recorded and the date of recording of the foregoing. See *Section 3097 (o) (2) of the Civil Code*.

Failure of the county recorder to mail the notices required by law to the person who filed the preliminary 20-day notice, or the failure of those persons to receive such notices shall not affect the period within which a claim of lien is required to be recorded. However, the county recorder is to make a good faith effort to mail within 5 days after the recording of a notice of completion or cessation notices thereof to those persons who filed the preliminary 20-day notice. See *Section 3079 (o)(3) of the Civil Code*.

Determination of Completion Time

Fixing the time of completion, to the exact day, is critical to establishing whether a given claim of lien (mechanic's or design professional's lien) has been recorded within the time limit fixed by law. The determination of completion of works of improvement can be complex under California law. Generally, any one of the following alternatives is recognized by the law as equivalent to completion:

l. Occupation or use by the owner or owner's agent, accompanied by cessation of labor on the work of improvement;

2. Acceptance by the owner or owner's agent of the work of improvement;

3. A cessation of labor on the work of improvement for a continuous period of 60 days; or

4. A cessation of labor on the work of improvement for a continuous period of 30 days or more, if the owner records in the county recorder's office a prescribed notice of cessation. See *Section 3092 of the Civil Code*.

If the work of improvement is subject to acceptance by any public entity, the completion date is considered as the date of acceptance or a cessation of labor for a continuous period of 30 days. See *Civil Code Section 3086*.

Thereafter, generally within 10-days the owner may file the notice of completion. If properly drawn, it will show the date of completion, the name and address of the owner, the nature of the interest or estate of the owner, a description of the land/property (which includes the official street address of the property, if it has one, or a sufficient legal description of the site), and the name of the original contractor, if any. If the notice is given only of completion of a contract for a particular portion of the total work of improvement, then the notice will also generally state the kind of work done or materials furnished.

As previously mentioned, the notice of completion should be filed with the recorder of the county where the property is situated within 10 days after completion of the work of improvement. See *Civil Code Sections 3093 and 3117.*

A mechanic's claim of lien may be filed:

1. By the *original contractor* within 60 days after the date of filing for record of the notice of completion or of cessation. An original contractor is one who contracts directly with the owner or owner's agent to do the work and furnish materials for the entire job, or for a particular portion of the work of construction. The owner may enter into different original contracts, for example, framing, plumbing, painting, or papering. A material supplier, as such, is not an original contractor. (It should be noted that contracting with more than one original contractor may be subject to applicable provisions of the Contractors State License Law. See *Business and Professions Code Section 7000 et seq).*

2. By *any claimant, other than the original contractor*, within 30 days after filing for record of the notice of completion or of cessation.

3. If the notice of completion or cessation is not recorded, the original contractor (as defined) or *any other claimant must file/record a claim of mechanic's lien* within 90 days after completion of the work of improvement. See *Civil Code Section 3106.*

If there are two or more original contractors, as defined, and a notice of completion or cessation is properly recorded as to one of them, the original contractor under the contract covered by the notice must, within 60 days after recording of such notice, file/record the claim of mechanic's lien. The claimant under the contract for which notice of completion or cessation has been recorded must, within 30 days after the recording of the notice, file/record the claim of a mechanic's lien. Each original contractor and any claimants under the contract with the original contractor are subject to their own notice of completion or cessation and the recording of a claim of mechanic's lien within the periods prescribed by applicable law. If no notice of completion or cessation has been recorded, the period of recording claims of mechanic's liens is the 90 days specified in Sections 3115 and 3116. See *Sections 3114, 3115, 3116, and 3117 of the Civil Code.*

Termination of the Lien

Voluntary release of a mechanic's lien, normally after payment of the underlying debt, will terminate the lien. But even in the absence of release, the lien does not endure indefinitely. If a mechanic's lien claimant fails to commence an action to foreclose the claim of lien within 90 days after recording the claim of lien and if within that time no extended credit is recorded, the lien is automatically null, void and of no further force and effect. (Section 3144(b), Civil Code) When credit is extended for purposes of this limitation, it may not extend for more than one year from the time of completion of the work. Moreover, a notice of the fact and terms of the credit must be filed for record within the 90-day lien period.

If the lien is foreclosed by court action, there may ultimately be a judicial sale of the property and payment to the lienholder out of the proceeds.

Notice of Nonresponsibility

The owner or any person having or claiming any interest in the land may, within 10 days after obtaining knowledge of construction, alteration, or repair, give notice that he or she will not be responsible for the work by posting a notice in some conspicuous place on the property and recording a verified copy thereof. The notice must contain a description of the property; the name of the person giving notice and the nature of his/her title or interest; the name of the purchaser under the contract, if any, or lessee if known; and a statement that the person giving the notice will not be responsible for any claims arising from the work of improvement. If such notice is posted, the owner of the interest in the land may not have his/her interest liened, provided the notice is recorded within the ten-day period.

The validity of a notice of nonresponsibility cannot be determined from the official county records since they will not disclose whether compliance has been made with the code requirements as to posting on the premises. If such posting has not been made, a recorded notice affords no protection from a mechanic's lien.

Release of Lien Bond

Owners and contractors disputing the correctness or the validity of a recorded claim of mechanic's lien may record, either before or after the commencement of an action to enforce the claim of lien, a lien release bond in accordance with the provisions of Civil Code Section 3143. A proper lien release bond, properly recorded, is effective to "lift" or release the claim of lien from the real property described in the lien release bond as well as any pending action brought to foreclose the claim of lien.

CONDITIONS REQUIRING OWNER TO PROVIDE CONTRACTOR WITH COPY OF RECORDED CONSTRUCTION LOAN INSTRUMENTS AND SECURITY FOR PAYMENT

Recent amendments to the law require (in those fact situations where a lending institution is extending credit in the form of a construction loan) the owner must provide the original contractor with a copy certified by the county recorder of the recorded construction mortgage or deed of trust. The recorded instrument is to disclose the amount of the construction loan. The trigger for the foregoing is when the contract for the work of improvement is more than $5,000,000 and the owner is the fee simple title holder of the property, or the contract for the work of improvement is more than $1,000,000 and the owner holds less than a fee simple title interest such as a leasehold interest.

In certain defined fact situations, the owner may be required to provide security for the payment obligations under the construction contract. The security may be in the form of a payment bond, an irrevocable letter of credit, or an escrow account with funds deposited therein subject to a security interest established in favor of the original contractor being determined sufficient by written opinion of legal counsel. This body of law is complex and should be reviewed by knowledgeable legal counsel. See *Civil Code Section 3110.5.*

ATTACHMENTS AND JUDGMENTS

Property Subject to Attachment

Attachment is the process by which real or personal property of a defendant in a lawsuit is seized and retained in the custody of the law as security for satisfaction of the judgment the plaintiff hopes to obtain in the pending litigation. The plaintiff gets the lien before entry of judgment, and is somewhat more assured of availability of the defendant's property for eventual execution in satisfaction of the claim (if the judgment is awarded to the plaintiff).

The purpose of an attachment is to protect a plaintiff who is a prospective judgment creditor against attempts by the defendant/debtor to transfer or dissipate the property subject to the attachment, and thus, in so dissipating the property, frustrate efforts to obtain satisfaction of a judgment subsequently obtained. The property seized and held under the attachment process constitutes an asset, or assets, which a judgment creditor may cause to be sold through execution proceedings in satisfaction of the judgment.

An attachment has always been referred to as a harsh remedy because it imposes a lien on the defendant's property and deprives him or her of absolute dominion and control over it for so long as it takes the court to adjudicate the plaintiff's claim. It is because of the deprivation of the defendant's right to dispose of defendant's attached property that the procedural framework of the attachment process has not been adopted to accommodate time consuming complex legal issues or disputes. Instead, the attachment process is based on the theory that the existence of a debt owed by the defendant to the plaintiff is conceded and that the principal function of the court is merely to ascertain the amount of that debt. This is why the right of a plaintiff to an attachment lien before trial (a prejudgment attachment lien) has been historically confined to actions arising out of contracts, express or implied, for the payment of money. Even in case of a claim arising out of a contract, the courts have been reticent to issues orders for prejudgment attachment liens.

Section 488.720 of the Code of Civil Procedure introduces a novel method of tempering the harsh consequences of an attachment lien and preventing its abuse. In noticed proceedings before the court, should the value of the defendant's interest in the property sought to be attached be shown to be clearly in excess of the amount necessary to satisfy plaintiff's claim, the court may order a release of as much of the property as it considers excess security.

Prejudgment attachments of the property of a natural person (individual) have been limited by case law and statute to claims arising out of the conduct of a business, trade, or profession. There are numerous other limitations on obtaining a prejudgment attachment.

Property Exempt from Attachment and Execution

As a matter of public policy, certain property is exempt from attachment or execution where the defendant is a natural person. The exemptions include, among others, property that is necessary for the support of the defendant or the family of the defendant; "earnings" as provided for and defined in Code of Civil Procedure Sections 706.010 and 706.011; interests in real property except leasehold estates with unexpired terms of less than a year; accounts receivable of a trade, business, or profession conducted by the defendant, as defined; equipment; farm products; inventory; money judgments arising out of the conduct of the defendant regarding a trade, business, or profession; money on the premises where a trade, business, or professions is conducted by the defendant, except the first $1000.00 located elsewhere, as defined; negotiable documents of title; instruments; securities; and minerals or the like. Community property interests of the defendant are subject to the attachment. A proper claim is to be made for the exemptions to apply. See *Code of Civil Procedure Sections 487.010, 487.020, 487.030 and 706.010, et seq.*

The most important exemption is the homestead, and the formalities of declaration of homestead by the owner are discussed later in this chapter. See *Code of Civil Procedures Section 487.025.*

Judgment

A final judgment is the final determination of the rights of the parties in an action or proceeding by a court of competent jurisdiction. Of course, the possibility exists that either party will appeal the judgment and, following the appeal, the judgment might subsequently be reversed or amended. Notwithstanding the foregoing, comparatively few judgments are appealed. Even for those judgments that are not appealed, the judgment is enforceable until the time to appeal or seek other procedural legal relief has elapsed.

A simple money judgment does not automatically create a lien. However, as soon as a properly certified abstract of the judgment is recorded with the recorder of any county, it becomes a lien upon all real property of the judgment debtor located in that county. It extends in that county to all real property the debtor may thereafter acquire before the lien expires. The lien of a lump sum money judgment normally continues for ten years from the date of entry of the judgment or decree. See Code *of Civil Procedure Section 664 et seq.* As with the lien on attachment, a judgment lien is discharged if enforcement of the judgment is stayed on appeal and the defendant executes a sufficient undertaking (promise or security) or deposits in court the requisite amount of money. See *Code of Civil Procedure Sections 489.010 et. seq. and 515.010 et seq.*

California Law has been amended to limit the inclusion of the social security number of the debtor on the abstract of judgment to the last four digits of the number. However, the listing of the social security number and the driver’s license number of the judgment debtor pursuant to Section 4506 of the Family Code applies to abstracts of judgment recorded after January 1, 1979, unless otherwise limited pursuant to the previously mentioned section of the Family Code.

The abstract of judgment is to contain the title of the court where the judgment is entered, the cause and number of the action, and the date of the entry of the judgment in the records of the court. In addition, the name and last know address of the judgment debtor and the name and address of the judgment creditor are to be included along with the date of the issuance of the abstract. Generally, the priority of an abstract of judgment is the date of recordation of the original abstract of judgment. Exceptions to this rule have been provided by law. See *Code of Civil Procedure Section 674.*

EASEMENTS

Generally

Having considered various types of liens which are encumbrances affecting the title to property, it is important to consider encumbrances which affect the physical condition or use of the property. Easements, probably the most common of this category, are ordinarily rights to enter and use another person’s land or a portion thereof within definable limits. Therefore, an easement is a right, privilege, or interest limited to a specific purpose which one party has in the land/property of another.

Easement rights are often created for the benefit of the owner of adjoining land. The benefitted land is called the “dominant tenement,” and the land subject to the easement is described as the “servient tenement.” Unless the easement is specifically described to be “exclusive,” its creation does not prevent the owner of the land from using the land/property and the portion covered by the easement in a way that does not interfere with the use of the easement.

Appurtenant Easements

Typical statutory easements (or land burdens or servitudes as they are also known) include, among others: a right of ingress and egress (a right to go on the land and to exit from the land); the right to use a wall as a party wall; or the right to receive more than natural support from adjacent land/property or things affixed thereto.

These easements, when attached to a ‘‘dominant tenement,” are considered “appurtenant” thereto, and pass automatically upon transfer of the dominant tenement without explicit mention in the instrument of transfer. “Appurtenant” means “belonging to.” Civil Code Section 801 lists a variety of easements commonly used in real property transactions. Civil Code Section 801.5 provides for a solar easement to ensure that solar collectors receive direct and unimpaired sunlight to facilitate the operation of the solar energy system.

Easements in Gross

It is possible to have an easement that is not appurtenant to particular land/property. Thus A, who owns no related land/property, may have a right-of-way over B’s land/property. Public utilities frequently enjoy easements to erect poles and string wires over private lands, yet own no related dominant tenement. Such easements are technically known as easements in gross, and are personal rights attached to the person of the easement holder and not attached to any specific land/property, yet in reality they encumber someone’s land/property and in effect constitute an interest therein.

If the instrument creating an easement is unclear, the following factors are useful in determining whether the easement is appurtenant or in gross: (1) if the easement can fairly be construed as being attached to the land/property, it will be so construed; (2) the intention of the parties and the right created are important considerations; and (3) outside evidence may be considered.

How Easements Are Created

Easements may be created in various ways, such as by express grant, express reservation, implied grant or implied reservation, agreement, prescription, necessity, dedication, condemnation, sale of land/property with reference to a plat, or estoppel.

Normally, easements arise in one of three ways. Either they are expressly set forth in some writing (such as a deed or a contract), or they arise by implication of law, or by virtue of long use. Those created by deed must comply with the usual requirements of any deed and may arise either by express grant to another or by express reservation to oneself.

While the most common method of creating an easement is by express grant or reservation in a grant deed, written agreements/contracts between adjoining landowners/property owners often are used. Generally, a deed or other recorded instrument to impart *constructive* notice of the easement established by the agreement/contract. The person who can grant a permanent easement is the fee owner of the servient tenement, or a person with the power to dispose of the fee.

Easements created by agreement/contract with a deed or other instrument of record to impart *constructive* notice must not violate applicable law, public policy implementing the law, or public policy even though not expressly applicable law. In a recent case, the agreement/contract between the dominant tenement and the servient tenement established an easement for maintaining horses on the land/property of the servient tenement. The applicable zoning ordinance prohibited the maintenance of horses on the land/property affected by the easement. Because of the violation of the zoning ordinance, the court held the easement unenforceable and the agreement/contract void. See Civil Code Section 1667 and Baccouche v. Blankenship (2007), Cal.App.4th [No. B192291. Second Dist., Div. Four. Sep. 11, 2007.]

Easement by Implication of Law

Civil Code Section 1104 contains the rule for implied grants. Certain conditions must exist at the time land/property is conveyed before an easement by implied grant will have effect. An easement by necessity is one example of an easement by implication, but an easement by necessity differs somewhat in its requirements from other easements by implication.

The “way of necessity” is generally recognized whenever a transfer occurs which truly “landlocks” a parcel of real estate (land/property) and no method of access exists, except over the servient tenement retained by the seller, or over the land/property of a stranger. The former is established by implication. The later would generally require a quit claim deed from the seller describing the road used by the seller and the seller’s predecessors in title to the parcel of land/property conveyed that otherwise is “landlocked”. To implement the claim to the access may require establishing the easement by perscription.

Another implied easement is recognized when land/property in one ownership is divided, and at the time of division, one portion is being used for the benefit of the other portion, e.g., a sewer lateral. See *Civil Code Section 801 and 1104.*

Easement by Prescription

Continuous and uninterrupted use for five years will create an easement by prescription where such use is hostile and adverse (without license or permission from the owner), open and notorious (the owner knows of the use or may be presumed to have notice of the use), exclusive (although use is not necessarily by one person only, it is such as to indicate to the landowner/property owner that a private right is being asserted), and under some claim of right. Generally, payment of ad valorem or other relevant real property taxes is not required to establish an easement by prescription, although it is among the requirements to establish adverse possession and ownership of the land/property. The obtaining of a quitclaim deed as discussed in the previous section may join the concept of easement by implication with easement by prescription. Should the stranger have been in chain of title to the subject land/property, an easement by implication with a quitclaim deed may be established. See *Civil Code Section 813 and 1008.*

Termination of Easements

Easements may be extinguished or terminated in several ways, including express release, legal proceedings, nonuse of a prescriptive easement for five years, abandonment, merger of the servient tenement and the easement in the same person, destruction of the servient tenement, and adverse possession by the owner of the servient tenement. An easement obtained by grant cannot be lost by nonuse. See *Civil Code Section 811.*

RESTRICTIONS

A very common type of encumbrance is the restriction, which, as the name suggests, in some way restricts the free use of the land by the owner. Commonly, restrictions are referred to as the covenants, conditions, and restrictions (CC&Rs) or the declaration.

Restrictions are generally created by private owners, typically by appropriate clauses in deeds, or in agreements, or in general plans of entire subdivisions. A restriction usually assumes the form of a *covenant*—a promise to do or not to do a certain thing—or a *condition*. Zoning is an example of a public use restriction on the use of land.

Distinction between Covenants and Conditions

A covenant is essentially a promise to do or not to do a certain thing. It is generally used in connection with instruments pertaining to real property, and is created by agreement. Typically it is embodied in deeds, but it may be found in any other writing. For example, a tenant might covenant in a lease to make certain repairs, or a buyer might covenant to use certain land/property only for a retail grocery store. A mere recital of fact, without anything more, is not a covenant.

A condition, on the other hand, is a qualification of an estate granted. Conditions, which can be imposed in conveyances, are classified as conditions precedent and conditions subsequent. A condition precedent requires certain action or the happening of a specified event before the estate granted can vest (i.e., take effect).

A familiar example is a requirement found in most of the installment contracts of sale of real estate (also known as a land contract of sale). All payments required under the agreement shall be made at the time specified before the buyer may demand transfer of title. It is important to understand that the use of such contracts are subject to legal issues where there is existing mortgages or deeds of trust encumbering the title of the land/property described therein. Accordingly, such contracts should not be used without the advice of knowledgeable legal counsel.

If there is a condition subsequent in a deed, the title vests immediately in the grantee, but upon breach of the condition, the grantor has the power to terminate the estate. This is termed a forfeiture, since the title may revert or be forfeited to the creator of the condition or to the heirs or successors in interest of the creator without payment of any consideration. An example is a condition subsequent in the deed stating that the property may not be used for the sale of liquor or other forms of alcoholic beverage. Should this condition subsequent be violated, title reverts to the grantor that created the condition or to the lawful heirs or successors in interest of the grantor.

Covenants and conditions are distinguishable in two further respects, in regard to the relief awarded and second, as to the persons by or against whom they may be enforced.

Relief awarded. As to the first, while a condition affects the estate created, and the failure to comply with it may result in a forfeiture of title, the only remedy to a breach of covenant is an action of damages or an injunction. Breach of a condition may prevent any right arising in favor of the breaching party, or destroy a right previously acquired, but does not subject the breaching party to liability and damages. While a breach of a covenant gives rise to a right of actual damages, does not necessarily excuse the other party from performance.

Enforcement. As to the second difference, a covenant normally does not bind successors of the promisor who may become owners of the affected land/property. However, some covenants "run with the land" (i.e., they bind the assigns of the covenantor or promisor and vest in and benefit the assigns of the covenantee or promisee), or they may be binding and effective by statute or in equity. Conditions, on the other hand, run with the restricted land into the indefinite future, unless abandoned or vacated by the grantor creating the condition or the lawful heirs or successors in interest of the grantor.

How construed. Whether a particular provision is a condition or covenant is a question of construction. Since the law abhors forfeitures, the courts ordinarily will construe restrictive provisions as covenants only, unless the intent to create a condition is plain. The use of the term "condition" or "covenant" is not always controlling. The real test is whether the intention is clearly expressed and the enjoyment of the estate conveyed was intended to depend upon the performance of a condition; otherwise, the provision will be construed as a covenant only.

For instance, the deed reciting that it is given upon the agreement of the grantee to do or not to do a certain thing implies a covenant and not a condition. So also with a recital that the land conveyed is or is not to be used for certain purposes.

Certain Covenants and Conditions Are Void

Covenants and conditions that are unlawful, impossible of performance, or in restraint of alienation, are void.

For example, a condition that a party shall not marry is void, but a condition to give use of property only *until* marriage is valid. A condition against conveying without the consent of the grantor, or for only a specified price, is void as in restraint of alienation. In such cases, title passes free of the condition subsequent. Recently, owner/developers of subdivision properties have sought to impose conditions subsequent upon the deeds conveying title to the individual parcels/properties within the subdivision requiring the payment of fees at the time of sale or transfer to an entity established for a community purpose (such as the maintenance of a commonly or publicly owned land/property functioning as a preserve).

Title does not pass at all if a condition precedent is impossible to perform or requires the performance of a wrongful act. However, if the act itself is not wrong, but is otherwise unlawful, the deed takes effect and the condition is void.

Covenants Implied in Grant Deed

When the word "grant" is used in any conveyance of an estate of inheritance or fee simple, it implies the following covenants on the part of the grantor (and grantor's heirs or successors in interest) to the grantee (and grantee's heirs, successors and assigns):

1. That the grantor has not already conveyed the same estate or any interest therein to any other person;
2. That the estate is free from undisclosed encumbrances made by the grantor, or any person claiming under grantor. As noted earlier, encumbrances include, among others, liens, taxes, easements, restrictions, conditions, mortgages and deeds of trust.

Thus, a grant deed by a private party is presumed by law to convey a fee simple title, unless it appears from the wording of the deed itself that a lesser estate was intended. Moreover, if a grantor subsequently acquires any title or claim of title to the real property that the grantor had purported to grant in fee simple, the after-acquired title usually passes by operation of law to the grantee or grantee's successors. When fee title to the land/property is being conveyed that is subject to encumbrances such as mortgages and deeds of trust, the practice in California is to rely on title insurance coverage (obtained at the time of the sale or transfer) listing the encumbrances as exceptions to the coverage in the order of their priority. The title insurance coverage issued to the purchaser is relied upon in lieu of describing these instruments of encumbrance on the face of the deed. Accordingly, it is important that title insurance coverage be obtained at the time of the sale or transfer of the land/property.

Deed Restrictions

Restrictions imposed by deeds, or in similar private contracts, may be drafted to restrict, for any legitimate purpose, the use or occupancy of land/property. The right to acquire and possess property includes the right to dispose of it or any part of it, and to impose upon the grant any legal restrictions the grantor deems appropriate. However, the right may not be exercised in a manner forbidden by law. Restrictions prohibiting the use of property on the basis of race, color, sex, religion, ancestry, national origin, age (generally), disability, sexual orientation, marital status, familial status, or source of income are unenforceable under state and federal law.

Declarations that impose restricted covenants that discriminate on the basis of race, color, religion or other prohibited basis included in a deed or grant in violation of Section 12955 of the Government Code are unlawful and unenforceable. Should historic restrictions include covenants that contain unlawful discriminatory prohibitions, the conditions, covenants and restrictions, or other governing documents must contain a cover page or stamp on the face thereof stating such restrictive covenants are unlawful and unenforceable. Further, a statutory procedure is provided through which the documents may be created and recorded by a person who holds an ownership record in the land/property that he or she believes is the subject of an unlawful restrictive covenant. The document is entitled, "Restrictive Covenant Modification". See *Government Code Sections 12956.1 and 12956.2*.

In addition, conditions restraining alienation, when "repugnant to the interest created", are void. However, federal law has been enacted that preempts state law in this regard to the extent mortgagees or beneficiaries of mortgage/deed of trust instruments have the right (pursuant to the provisions of these instruments) to accelerate all sums due thereunder irrespective of the majority date stated in such instruments of encumbrance in the event of the sale, transfer, further encumbrance, or other conveyance of the security property. See *Section 711 of the Civil Code* and *the Federal Depository Institutions Act of 1982*.

Restrictions may validly cover a multitude of matters: use for residential or business purposes; character of buildings (single family or multiple units); cost of buildings (e.g., a requirement that houses cost more than $100,000); location of buildings (e.g., side lines of five feet and 20-foot setbacks); and even requirements for architectural approval of proposed homes by a local group/committee established for that purpose.

Unless the language used in the deed clearly indicates that the grantor intended the conditions or restrictions to operate for the benefit of other lots or persons, the restrictions run to the grantor only, and a quitclaim deed from the grantor, or the grantor's heirs, successors in interest or assigns, is a sufficient release. However, if the language used in the deed shows that the conditions or restrictions were intended for the benefit of adjoining owners, or other lots or owners of separate interests in the tract/subdivision (such as a common interest development), quitclaim deeds may be required from each owner of separate interests having the benefit thereof, as well as from the grantor or the grantor's heirs, successors in interest or assigns, to release the conditions or restrictions. When the subdivision is a common interest development, the vote of the owners of separate interests is generally required. The requirements and conditions imposed by the political subdivision of jurisdiction (local government) to establish the common interest development may prevent the release of the covenants or restrictions without the concurrence of the governmental entity.

Notice of Discriminatory Restrictions

Effective January 2000, a county recorder, title insurance company, escrow company, or real estate licensee who provides a declaration, governing documents or deed to any person that contain an unlawful covenant or restriction must provide a specified statement about the illegality of discriminatory restrictions and the right of homeowners to have such language removed. As previously mentioned, the statement must be contained in either a cover page placed over the document or a stamp on the first page of the document. See *Government Code Sections 12956.1 and 12956.2*.

New Subdivisions

In contrast to zoning ordinances, private contract restrictions need not promote public health, general public welfare or safety. They may be intended to create a particular type of neighborhood deemed desirable by the tract/subdivision owner and may be based solely on aesthetic conditions. These tracts/subdivisions are typically know and described as common interest developments. As might be expected, the most common use of covenants and restrictions today is in new subdivisions. The original owner/developer/subdivider establishes uniform regulations as to occupancy, use, character, cost and location of buildings and records a “declaration of restrictions” when the subdivision is first created. Thereafter, all lot owners or owners of separate interests, as among themselves, may enforce the covenants and restrictions against any one or all of the others, provided the covenants and restrictions have been properly imposed and have not been otherwise waived.

In some cases, when land/property is originally subdivided, arrangement is made in the nature of a covenant whereby a perpetual property owners’ association is formed to be governed by rules and regulations set forth in an agreement signed by all new lot purchasers/owners of separate interests. Such associations (typically described as homeowner’s associations) are often given the power to amend tract/subdivision restrictions from time to time to correspond with community growth (provided the amendments are not inconsistent with the conditions imposed by the local government having jurisdiction over the land/property when the tract/subdivision was established and are not inconsistent with applicable law, including zoning ordinances and building codes. Homeowner’s associations may have the power to revise building restrictions pertaining to certain blocks of lots/parcels in the development/subdivision, impose architectural restrictions, and make other authorized requirements from time to time.

Termination

Restrictions may be terminated by

l. expiration of their terms;

2. voluntary cancellation;

3. merger of ownership;

4. act of government; or

5. changed conditions (i.e., a court finds that the restrictions should be terminated because the conditions which the restrictions addressed have changed).

Restrictions usually have either a fixed termination date or one which becomes effective on recordation of a cancellation notice by a given the appropriate percentage of the lot owners or owners of special interests.

Zoning Regulations

Restrictions on the use of land may be imposed by government regulation as well as by private contracts.

The governing authority of a city or county (local government) has the power to adopt ordinances establishing zones within which structures/improvements must conform to specified standards as to character (including aesthetic considerations) and location, and to limit buildings designed for business or trade to designated areas consistent with the general plan. Zoning ordinances apply to each form of use that may be contemplated by the owner of the land/property (agricultural, industrial, commercial retail, commercial office, research and development, multi-family residential, single family residential, among others),

However, zoning restrictions, to be valid, should be substantially related to the preservation or protection of public health, safety, morals, or general welfare. They must be uniform and cannot be discriminatory or created for the benefit of any particular group. Public authorities may enjoin or abate improvements or alterations that are in violation of a zoning ordinance, but only the use of the land/property, not the title, is affected.

ENCROACHMENTS

Adjoining owners of real property often find themselves involved with *encroachments* in the form of fences or walls and buildings extending over the boundary lines. The party encroaching on a neighbor may be doing so with legal justification. The person who encroached may have gained title to the strip encroached on by adverse possession, or may have acquired an easement by prescription or possibly by implication to the land/property upon which the encroachment has occurred.

On the other hand, the encroachment may be wrongful. If it is, the party encroached upon may sue for damages and a court may require removal of the encroachment.

Note: If the encroachment is slight (e.g., measurable in inches), the cost of removal great, and the cause an excusable mistake, a court may deny removal and award dollar damages to the owner of the land/property subject to the encroachment. In such an event, the local government would require either a boundary line adjustment or an appropriate variance to establish the minimum “setbacks” required by the applicable zoning ordinance. The determination whether the encroachment may remain and damages may be paid in lieu of removal requires exhausting administrative remedies with the local government prior to a court of competent jurisdiction being able to rule on the matter.

HOMESTEAD EXEMPTION

The principal purpose of the *homestead exemption* is to shield the home against creditors of certain types whose claims might be exercised through judgment lien enforcement. Few areas of California real property law are more misunderstood.

Obligations unaffected by the declaration. Over the years, the homestead exemption amount has been increased from time to time, with the type of homestead determining the actual amount of the exemption. However, the validity of a homestead depends not only upon the recordation of the homestead declaration but on certain off-record matters including, actual residency in the declared homestead dwelling at the time the declaration is recorded and an actual interest in the “dwelling”.

The homestead declaration does not protect the homestead from all forced sales. For example, it is subject to a forced sale if a judgment is obtained: (l) prior to the recording of the homestead declaration; (2) on debts secured by encumbrances on the premises executed by the owner before the declaration was filed for record; and (3) obligations secured by mechanics’, contractors’, subcontractors’, laborers’, materialmen’s, suppliers’ or vendors’ liens on the premises. Voluntary encumbrances by the owner of the homestead are not affected by a declaration of homestead. A mortgage or deed of trust is an example of a voluntary encumbrance.

Two Homestead Statutes

Articles 4 and 5 of Chapter 4, Division 2, Title 9, Part 2 of the California Code of Civil Procedure (commencing with Section 704.710) contain respectively the applicable law regarding the “Homestead Exemption” and ”Declared Homesteads”.

While both Articles deal with granting homeowners homestead protection from the claims of certain creditors, the Articles are in part mutually exclusive. Article 4 provides protection to homeowner debtors who meet the requirements but have not filed a declaration of homestead. Article 5 concerns homeowners who undertake the actual filing of a homestead declaration. In either case, there is protection against certain judgment liens to the amount of the exemption afforded by law.

The following discussion concerns primarily the “Declared Homestead” under Article 5.

(**NOTE:** A “Probate Homestead” also exists in California. See Probate Code Sections 60 and 6520 through 6528.)

Declared Homestead

A dwelling in which an owner or his or her spouse resides may be selected as a “Declared Homestead” by recording a homestead declaration in the office of the county recorder of the county where the dwelling is located. From and after the time of recording, the dwelling is a “Declared Homestead”. See *the Code of Civil Procedure Sections 704.710 and 704.910.*

Definitions for Declared Homestead

A “Declared Homestead” is the dwelling described in a homestead declaration and a “Declared Homestead Owner” includes both (1) the owner of an interest in the “Declared Homestead” who is named as a “Declared Homestead Owner” in a homestead declaration recorded pursuant to Code of Civil Procedure Section 704.920 and, (2) the declarant named in a declaration of homestead, including the spouse of the declarant, recorded prior to July 1, 1983, pursuant to the former Title 5 (commencing with Section 1237) of Part 4 of Division 2 of the Civil Code. See *the Code of Civil Procedure Section 704.910.*

“Dwelling” means any interest in real property (whether present or future, vested or contingent, legal or equitable) that is a “dwelling” as defined in Section 704.710 of Article 4 and Section 704.910 of Article 5 of the Code of Civil Procedure, but does not include a leasehold estate with an unexpired term of less than two years or the interest of the beneficiary of a trust. See *the Code of Civil Procedure Section 704.910.*

For the purpose of Article 4 and Article 5 of the Code of Civil Procedure, “Spouse” means a “spouse” as defined in Sections 704.710 and 704.910.

Definitions and Terminology
Some of the terminology for "Declared Homesteads" depends for their meaning on definitions from Article 4, which describes a residential exemption, even if there is no filing of a "Declared Homestead". These definitions are:

1. **"Dwelling"** means a place where a person actually resides and may include, but is not limited to, the following:
   a. A house together with the outbuildings and the land upon which they are situated;
   b. A mobilehome together with the outbuildings and the land upon which they are situated;
   c. A boat or other waterborne vessel;
   d. A condominium, as defined in Section 783 of the Civil Code;
   e. A Planned Development, as defined in Section 11003 of the Business and Professions Code;
   f. A stock cooperative, as defined in Section 11003.2 of the Business and Professions Code; and
   g. A community apartment project, as defined in Section 11004 of the Business and Professions Code.
2. **"Family unit"** means any of the following:
   a. The judgment debtor and the judgment debtor's spouse if the spouses reside together in the homestead.
   b. The judgment debtor and at least one of the following persons who the judgment debtor cares for or maintains in the homestead:
      (1) The minor child or minor grandchild of the judgment debtor or the judgment debtor's spouse or the minor child or grandchild of a deceased spouse or former spouse.
      (2) The minor brother or sister of the judgment debtor or judgment debtor's spouse or the minor child of a deceased brother or sister of either spouse.
      (3) The father, mother, grandfather, or grandmother of the judgment debtor or the judgment debtor's spouse or the father, mother, grandfather, or grandmother of a deceased spouse.
      (4) An unmarried relative described in this paragraph who has attained the age of majority and is unable to take care of or support himself or herself.
   c. The judgment debtor's spouse and at least one of the persons listed in paragraph (2) who the judgment debtor's spouse cares for or maintains in the homestead.

<u>See</u> *the Code of Civil Procedure Section 704.710.*

3. **"Homestead"** means the principal dwelling (l) in which the judgment debtor or the judgment debtor's spouse resided on the date the judgment creditor's lien attached to the dwelling, and (2) in which the judgment debtor or the judgment debtor's spouse resided continuously thereafter until the date of the court determination that the dwelling is a homestead. Where exempt proceeds from the sale or damage or destruction of a homestead are used toward the acquisition of a dwelling within the six-month period provided by Section 704.720, "homestead" also means the dwelling so acquired if it is the principal dwelling in which the judgment debtor or the judgment debtor's spouse resided continuously from the date of acquisition until the date of the court determination that the dwelling is a homestead, whether or not an abstract or certified copy of a judgment was recorded to create a judgment lien before the dwelling was acquired. <u>See</u> *the Code of Civil Procedure Section 704.710.*
4. **"Spouse"** does *not* include a married person following entry of a judgment decreeing legal separation of the parties, or an interlocutory judgment of dissolution of the marriage, unless such married persons reside together in the same dwelling. <u>See</u> *the Code of Civil Procedure Section 704.710.*

Amount of Homestead Exemption
The amount of the homestead exemption is the same under Articles 4 and 5 and is based upon the debtor's status at the time the creditor's lien is recorded. The current protected homestead exemption values and the required status of the debtor or spouse are as follows:

1. $50,000, unless the judgment debtor or spouse of the judgment debtor who resides in the homestead is the person described in paragraph (2) or (3);

2. $75,000, if the judgment debtor or the spouse of the judgment debtor who resides in the homestead at the time of the attempted sale of the homestead is a member of the family unit, and there is at least one member of the family unit who owns no interest in the homestead or whose only interest in the homestead is a community property interest with the judgment debtor;

3. $150,000, if the judgment debtor or spouse of the judgment debtor who resides in the homestead is at that time of the attempted sale of the homestead any one of the following:

   A. A person 65 years of age or older

   B. A person physically or mentally disabled and because of that disability is unable to engage in substantial gainful employment. There is a rebuttable presumption affecting the burden of proof that the person receiving disability insurance payments under Title II or supplemental security income payments under Title XVI of the Federal Social Security Act satisfies the requirement of this paragraph as to his or her inability to engage insubstantial gainful employment.

   C. A person 55 years of age or older with a gross annual income of not more than $15,000 or, if the judgment debtor is married, a gross annual income, including the gross annual income of the judgment debtor's spouse, of not more than $20,000 and the sale is an involuntary sale.

Regardless of any other provision of this law, the combined homestead exemptions of spouse on the same judgment shall not exceed the amount specified in paragraph (2) or (3) above, which ever is applicable, regardless of whether the spouses are jointly obligated on the judgment or whether the homestead consists of community or separate property or both. If both spouses are entitled to a homestead exemption, the exemption of proceeds of the homestead shall be apportioned between the spouses on the basis of their proportionate interests in the homestead. <u>See</u> *the Code of Civil Procedure Section 704.730.*

Contents of the Declaration of Homestead

1. A recorded homestead declaration will contain all of the following:

   a. The name of the "Declared Homestead" owner. A husband and wife both may be named as "Declared Homestead" owners in the same homestead declaration if each owns an interest in the dwelling selected as the "Declared Homestead".

   b. A description of the "Declared Homestead".

   c. A statement that the "Declared Homestead" is the principal dwelling of the "Declared Homestead" owner or such person's spouse, and that the "Declared Homestead" owner or such person's spouse resides in the "Declared Homestead" on the date the homestead declaration is recorded.

2. The homestead declaration shall be executed and acknowledged in the manner of an acknowledgment of a conveyance of real property by at least one of the following persons.

   a. The "Declared Homestead" owner.

   b. The spouse of the "Declared Homestead" owner.

   c. The guardian or conservator of the person or estate of either of the persons listed in (a) or (b) above. The guardian or conservator may execute, acknowledge, and record a homestead declaration without the need to obtain court authorization.

   d. A person acting under a power of attorney or otherwise authorized to act on behalf of a person listed in (a) or (b) above.

3. The homestead declaration shall include a statement that the facts stated in the homestead declaration are known to be true as of the personal knowledge of the person executing and acknowledging the homestead declaration. If the homestead declaration is executed and acknowledged by a person listed in (c) or (d) above, it shall also contain a statement that the person has authority to so act on behalf of the "Declared

Homestead" owner or the spouse of the "Declared Homestead" owner and the source of the person's authority.

See *the Code of Civil Procedure Section 704.930.*

The definition of "dwelling" for purposes of Article 5 means an interest in real property that is a dwelling as defined in Section 704.710 (Article 4), but excludes a leasehold estate with an unexpired term of less than two years at the time of the filing of the homestead declaration. A "dwelling" that is personal property (boat, waterborne vessel or mobilehome not affixed to land/property) appears to be excluded under Article 5. Prior to applying the definition of "dwelling", the advise of knowledgeable legal counsel should be obtained. See *the Code of Civil Procedure Section 704.910.*

The law does not set a limit on the amount of land/property that may be contained in the homestead "dwelling" property Ownership interests and occupancy by the owner or owner's spouse at the time of filing the declaration are the principal governing factors.

Where unmarried persons hold interests in the same "dwelling" in which they both reside, they must record separate homestead declarations, if each desires to have a valid homestead.

Under previous law, a person who was a "head of household" was entitled to qualify for the amount of the greater exemption. Under current law, the amount of the exemption will depend upon whether or not the judgment debtor qualifies as a "family unit."

See *Article 4 and 5 of the Code of Civil Procedure commencing with Section 704.710.*

Declarations recorded prior to July 1, 1983. Any declaration of homestead filed prior to July 1, 1983, remains valid, but the effect is limited to the effect given a homestead declaration under current statutes, i.e., the previously filed declaration must be qualified under present law. See *Article 5 of the Code of Civil Procedure commencing with Section 704.910.*

Effect of recording - how terminated. When a valid declaration of homestead has been filed in the office of the county recorder where the property is located, containing all of the statements and information required by law, the property becomes a homestead protected from execution and forced sale, except as otherwise provided by statute. The homestead remains operative until terminated by conveyance, abandoned by a recorded instrument of abandonment, or sold at execution sale.

A homestead declaration does not restrict or limit any right to convey or encumber the declared homestead.

To be effective, the declaration must be recorded; when properly recorded, the declaration is prima facie evidence of the facts contained therein; but off-record matters could prove otherwise.

See *the Code of Civil Procedure Sections 704.920, 704.940, 704.965, 704.970, 704.980, and 704.990.*

Rights of spouses. A married person who is not the owner of an interest in the dwelling may execute, acknowledge, and record a homestead declaration naming the other spouse who is an owner of an interest in the dwelling as the "Declared Homestead" owner but at least one of the spouses must reside in the dwelling as his or her principal dwelling at the time of recording. See *the Code of Civil Procedure Sections 704.920 and 704.930.*

Either spouse can declare a homestead on the community or quasi-community property, on property held as tenants in common, or held as joint tenants, but cannot declare a homestead on the separate property of the other spouse in which the declarant has no ownership interest. A homestead cannot be declared after the homeowner files a petition in bankruptcy. The phrase, "Quasi-community property", refers to real property situated in this state acquired in any of the following ways:(1) By either spouse while domiciled elsewhere which would have been community property if the spouse who acquired the property had been domiciled in this state at the time of its acquisition. (2) In exchange for real or personal property, wherever situated, which would have been community property if the spouse who acquired the property so exchanged had been domiciled in this state at the time of its acquisition.

If a husband and wife own separate interests as separate property, each spouse qualifies for his or her own exemption but the combined exemptions cannot exceed the amount that is due to a "family unit." A declaration intended to be for the "joint benefit" of both spouses, one or both spouses must qualify as a "family unit."

After a decree of legal separation or interlocutory judgment of dissolution of marriage, if a spouse no longer resides on the property, the spouse cannot declare a homestead on the property.

See the *Code of Civil Procedure Sections 704.710 and 704.910* and *Family Code Section 910 et seq.*

Levy and execution sale. When an execution for the enforcement of a judgment is levied on a homestead dwelling, the judgment creditor must follow specific procedures.

Within 20 days after a writ of execution is levied and the creditor is notified of this fact, the creditor must apply to the court where the judgment was rendered for an order to execute the sale of the property. See *the Code of Civil Procedure Sections 704.740, 704.750 and 704.760.*

The value of the property is determined by the court. The court may appoint an appraiser and will consider other evidences of value to set a minimum bid for the property. Creditors must prove sufficient value to receive the minimum bid or the court may not make a finding for the sale.

If the court makes an order for sale of the dwelling upon a hearing at which neither the judgment debtor's spouse nor attorney debtor or spouse appeared, then within 10 days after the order for sale, the creditor must serve a copy of the order and statutory notice of sale on the debtor. The property is not sold if no bid is received at least equal to the court's prescribed minimum bid (which is a sum at least equal to the amount needed to pay all liens and encumbrances on the property, the amount of the homestead exemption, and the lien of the judgment creditor enforcing the lien), and the creditor cannot subject the property to an additional order for sale for at least one year. See *the Code of Civil Procedure Sections 704.770, 704.780, 704.790, and 704.800.*

After the sale, the proceeds of sale are distributed as follows: (a) to discharge all liens and encumbrances on the property recorded prior to the judgment lien; (b) to the owner/debtor for the amount of the homestead exemption; (c) to costs of execution; (d) to the amount due the judgment creditor; and finally (e) balance to owner/debtor.

The proceeds from the execution sale are exempt for 6 months after the debtor receives the proceeds. If reinvested in a new "dwelling" and a new declaration of homestead is recorded within this 6-month period, the new filing has the same effect as though recorded on the date the prior declaration was recorded. See *the Code of Civil Procedure Section 704.960(b).*

Federal Homestead Act of 1862

The declared homestead discussed above has nothing to do with the term "homesteading" as applied to filings on federal lands whereby a person acquired title to acreage by establishing residence or making improvements upon the land.

The purpose of the Federal Homestead Act of 1862 was to encourage settlement of the nation. Except for Alaska, homesteading was discontinued on public lands in 1976. Because all the good agricultural land had already been homesteaded and deeded, Congress recognized that the Homestead Act had outlived its usefulness and passed the Federal Land Policy and Management Act of 1976that immediately repealed the old law (as to all states except Alaska).

ASSURING MARKETABILITY OF TITLE

Casual reflection on the nature of title to real property and its use and transfer must lead to the conclusion that establishing marketable title is often a complex and difficult undertaking. The term itself has no universally accepted meaning. It does not mean a perfect title, but rather one that is free from plausible or reasonable objections. In effect, the title is marketable (or merchantable) if there is reasonable assurance as to the extent of the rights involved. The title must be such that a proper court would compel the buyer to accept it, if asked to decree specific performance of the purchase and sale contract/agreement.

Establishing a marketable title is especially important whenever land/property is transferred for consideration, and when, in connection with such transfer or otherwise, money is loaned with land as security. The prospective buyer or lender would be reluctant to commit funds to the transaction without some assurance of getting what was bargained for. Buyers of real property expect some assurance that there are no hidden interests in the real property they propose to buy.

For example: One uses the surface, another extracts subsurface minerals, and a third controls the air space above the surface. Interests in land/real property may be divided, distributed, and distinguished in many different manners or ways. This occurs since much land/property is of comparatively high value, especially in urban areas where the growth and concentration of population have placed a premium on such parcels. Consequently, the land/property has been divided, subdivided and recombined into a patchwork measured in feet and sometimes even in inches.

Since the persons who own or deal with land/property are themselves subject to a variety of laws which determine the extent of their rights (e.g., probate, dissolution, guardianship, bankruptcy, business association laws, among others), an understanding of how these laws affect ownership rights is necessary. Since creditors and others may burden the real property with a variety of liens and encumbrances, an understanding of how applicable law affects the rights of mortgagees and mortgagors (beneficiaries and trustors) and creditors and debtors is also essential.

Who owns what? The issue is one of determining all the important facts with reference to who owns what interests or rights in the title to a particular parcel of land. Actual possession of the land/property has always been important and helpful in providing the answer. But possession may be by someone other than the owner, and transfers may be made without taking possession. Hence, the documentary record of ownership in the county recorder's office of the county in which the parcel is located assumes great significance. Reliance on recorded documents is encouraged by the official recording system under which deeds and other instruments affecting title may be recorded with the recorder of the county in which the land/property is situated.

Thus, a "chain of paper title" could be traced back to the original conveyance from the government. However, recordation is not generally compulsory, although there are fact situations were it is required. The "Race Recording" or "Race-Notice Recording" systems were created to accomplish a "chain of paper title" and to establish the priority of recorded instruments/documents. However, the record of the "chain of paper title" is not always properly achieved or maintained. Records may be erroneous, or sometimes may even reflect fraudulent and unenforceable transactions. When done thoroughly and conscientiously, the resulting records over the years become a complicated history in themselves, yet they may be woefully incomplete for purposes of determining the status of the title in question. This is so for a variety of reasons.

For example: In an intestate transfer, a qualified heir might have inadvertently been excluded; or a transfer, valid on its face may have been made by a person incompetent because of age or mental condition. Then too, other official records (e.g., tax records and records of court judgments) may profoundly affect the picture. In short, title to land/property and marketability of that title depends not only on recorded facts of title transfer, but also on a vast array of extraneous information outside of the documents recorded in the county recorder's office.

Abstract of Title

As might be expected under such complex circumstances, historically the individual buyer or lender was ill equipped to make the necessary *investigation* of the status of the title to property. They soon came to rely on the title specialist who made a business of studying the records and preparing summaries or abstracts of title of all pertinent documents discovered in the search. An abstract of title is a summary statement of the successive conveyances and other facts (appearing in the proper place in the public records) on which a person's title to real property rests. The abstract of title and a lawyer's opinion of the documents appearing in the abstractor's "chain of title" were the basis of our earliest attempts to establish marketable title. This method still exists today, with modern refinements.

Certificate of Title

In time, abstractors accumulated extensive files of abstracts and other useful data, including "lot books" wherein references to recorded documents were systematically arranged according to the particular property affected, and "general indices" wherein landowners were listed alphabetically together with information concerning them and affecting titles (e.g., probates and property settlements).

These files came to be known as "title plants" and provided classified and summarized histories of real estate transactions and of other activities that affect or might affect ownership of the land/property in the areas covered. With the growth and improvement of title plants and increased proficiency of examiners employed by the abstractors, the formal abstract of title for delivery to the customer and the related legal opinion were sometimes dispensed with completely. The abstract company would simply study its records and furnish the customer with a certificate of title in which it stated that it found the title properly vested in the present owner, subject to noted encumbrances. The certificate plan has strictly limited use today, for it was a transitional method of assuring not insuring titles.

Guarantee of Title

The next step was the guarantee of title under which the title insurance company did more than certify the correctness of its research and examination.

Thus, the company provided written *assurances* (not insurance) about the title to real property. The coverage was usually limited to a particular condition of title, a certain period of time, and a certain kind of information. This meant it was engaged in the insurance business and generally was subject to regulation as such.

Title Insurance

As already noted, the public records may be incomplete or erroneous and do not necessarily disclose shortcomings arising from forgery, incompetence, and failures to comply with legal requirements, among others. Accordingly, the policy of title insurance was developed as the culmination of the quest for a reliable and marketable title as well as compensation for incorrect assurances that cause a covered loss. Although still covering most risks that are a matter of public record, it alone extends protection against many nonrecorded types of risks, depending on the type of policy purchased. The title insurance company continues to utilize the “title plant” to conduct as accurate a search of the records as possible and seeks to interpret correctly what it finds in the records. Its unique contribution is the protection it affords against risks that lie outside the public records.

Preliminary report. In current practice, the title insurance industry typically issues a “preliminary report” rather than a “search” or “abstract” that are intended to assure the status of title and for which there would be liability, as defined in the document issued as a “search” or “abstract”. The Insurance Code defines “preliminary report” as a “commitment” or “binder” furnished in connection with an application for title insurance and such reports are offers to issue a title policy subject to the stated exceptions set forth therein and such other matters as may be incorporated by reference. Preliminary reports are not abstracts of title, nor are any of the rights, duties, or responsibilities applicable to the preparation and issuance of an abstract of title applicable to the issuance of such reports. Preliminary reports are not to be construed as nor constitute a representation as to the condition of title to real property (a “search” of the title). Preliminary reports are a statement of the terms and conditions upon which the issuer is willing to issue its title policy, if such offer is accepted. See *Insurance Code Section 1234.11.*

Standard policy. In addition to risks of record, the standard policy of title insurance protects against:

- off-record hazards such as forgery, impersonation, or lack of capacity of a party to any transaction involving title to the land (e.g., a deed of an incompetent or an agent whose authority has terminated, or of a corporation whose charter has expired);
- the possibility that a deed of record was not in fact delivered with intent to convey title (typically excluding a fraudulent conveyance);
- the loss which might arise from the lien of federal estate taxes, which is effective without notice upon death; and
- the expense, including attorneys’ fees, incurred in defending the title, whether the plaintiff prevails or not.

The standard policy of title insurance does *not* however protect the policyholder against defects in the title known to the holder or to the agent of the holder to exist at the date of the policy and not previously disclosed to the insurance company. Further, the standard policy neither protects against easements and liens which are not shown by the public records; nor against rights or claims of persons in physical possession of the land/property, yet which are not shown by the public records (since the insurer typically does not inspect the property when offering such coverage); nor against rights or claims not shown in public records, yet which could be ascertained by physical inspection of the land/property, or by appropriate inquiry of persons on the land/property, or by a correct survey; nor against mining claims, reservations in patents, or water rights; nor against zoning ordinances.

These limitations may not be as dangerous as they might appear to be. To a considerable degree, the limitations can or may be eliminated by careful inspection of the land/property by the purchaser/buyer or his or her agents (e.g., brokers/appraisers) and a routine inquiry as to the status of persons in possession. However, if desired, most of these risks can be covered by special endorsement or use of extended coverage policies at added premium cost.

ALTA Policy (for lenders). In California, many loans secured by real property have been made by out-of-state financial institutions/licensed lenders that were not in a position to make personal inspection of the properties involved except at disproportionate expense. For them and other nonresident lenders, the special ALTA (American Land Title Association) Policy was developed. This policy expands the risks normally insured against to include: rights of parties in physical possession, including tenants and buyers under unrecorded instruments; reservations in patents; and, most importantly, unmarketable title. The new ALTA Loan Policy (issued 10-17-92 and further revised 6-17-2006) also covers recorded notices of enforcement of excluded matters (like zoning), as well as recorded notices of defects, liens or encumbrances affecting title that result from a violation of matters excluded from policy coverage. A review by knowledgeable legal counsel of the provisions of ALTA Loan Policies is recommended before purchasing coverage, including specific endorsements.

Extended coverage. The American Land Title Association has adopted an owner's extended coverage policy (designated as ALTA Owner's Policy [10-17-92]) that provides to buyers or owners much the same protection that the ALTA policy gives lenders. The owner's policy has been recently revised and the coverage expanded. The California Land Title Association ("CLTA") has also provided expanded protection for the owner's policies it issues under standard coverage.

However, reliance on the owner's or the owner's agent notice or knowledge of defects affecting the title and not of record has also been expanded and enhanced. These policies offer no protection against defects or other matters concerning the title that are known to exist by the insured (the owner or the agents of the owner) as of the date of the policy that have not previously been communicated in writing to the insurer. These policies also offer no protection regarding governmental regulations concerning occupancy and use. The former limitation is self-explanatory; the latter exists because zoning regulations concern the condition of the land/property rather than the condition of title.

For homeowner's (1 to 4 residential units) a new CLTA/ALTA policy was developed in 1998; (ALTA Homeowner's Policy (10-17-98), and CLTA Homeowners Policy (6-2-98). As previously mentioned, these polices have been revised again. Generally, the policies are the same with the exception: the CLTA policy provides a form of Subdivision Map coverage, while the ALTA policy makes the Map Act coverage optional. The idea of the new and revised policies is to provide homeowners with a form of extended coverage. The new and revised policies contain maximums payable under certain categories of coverage and small deductibles payable by the insured. Both policies incorporate protection against certain risks that conventionally were available only to lenders and only by endorsement.

Domestic Title Insurance Companies in California

Section 12359 of the Insurance Code of California requires that a title insurance company organized under the laws of this State have at least $500,000 paid-in capital represented by shares of stock. Section 12350 requires that the insurer deposit with the Insurance Commissioner a "guarantee fund" of $100,000 in cash or approved securities to secure protection for title insurance policy holders. A title insurer must also set apart annually, as a title insurance surplus fund, a sum equal to 10 percent of its premiums collected during the year until this fund equals the lesser of 25 percent of the paid-in capital of the company or $1,000,000. This fund acts as further security to the holders and beneficiaries of policies of title insurance.

Policies of title insurance are now almost universally used in California, largely in the standardized forms prepared by the California Land Title Association ("CLTA"), the trade organization of the title companies in this State. Every title insurer must adopt and make available to the public a schedule of fees and charges for title policies. Today, it is the general practice in California for buyers, sellers and lenders, as well as the attorneys and real estate brokers who serve them, to rely on title insurance companies for title information, title reports and policies of title insurance.

Rebate Law

Title insurance companies are required to charge for preliminary reports under the terms of legislation adopted at the 1967 general session of the California Legislature. The rebate law requires title insurance companies to not only charge for reports, but also to make sincere efforts to collect for them except in certain defined circumstances.

Title insurance companies can still furnish "the name of the owner of record and the record description of any parcel or real property" without charge. Such information may be referred to as a "property profile" or "subject property history".

The statute extends the anti-commission provisions of Section 12404 of the Insurance Code to prohibit direct or indirect payments by a title insurance company to principals in a transaction as a consideration for title business.

Thus, the law prohibits a title insurance company from paying, either directly or indirectly, any commission, rebate, or other consideration as an inducement for or as compensation on any title insurance business, escrow or other title business in connection with which a title policy is issued. Rebates are also precluded in the Real Estate Law, as defined.

See *Business and Professions Code Section 10177.4.*