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## My Client Wants to Take Title in a Trust

by Ruth A. Dillingham, Esq., Special Counsel

**I**n recent years many borrowers have requested that they be allowed to mortgage property held in a trust. Traditionally, the major investors (Fannie Mae and Freddie Mac) have denied the request. However, the agencies have relaxed their stance somewhat as more and more lenders and their borrowers have insisted that there be some opportunity for a trust to be a borrower. Reflective of that request, both Fannie Mae and Freddie Mac have devised guidelines that apply when the mortgagor is a trust. This is a review of these guidelines, however, any specific questions should be addressed to the appropriate person at the particular lender for review with that lender's specific investor. It should also be noted that the guidelines, while very similar, do contain inconsistencies, both in what they cover, and in what they don't.

### **Why is this a problem in the first case?**

When the borrower is an individual, there is clear liability for the outstanding mortgage debt. When the borrower is some other entity, that liability can be reduced, and in some instances eliminated. Thus, when the borrower executes a note and mortgage as "John Doe, Trustee of the Doe Family Trust," the only assets available to a lender in the event of a foreclosure and short-fall, are the assets of the Trust, which traditionally consists solely of the mortgaged real estate, which has insufficient value. For this reason, the guidelines require that whenever a trust is the borrower, the lender must warrant that the borrower's status as a trust does not diminish the investor's rights as a creditor.

### **Eligible Borrowers**

In general, in order for a trust to qualify as an eligible borrower, it must be:

An inter vivos trust, (created during the life of its creator, not under a will);

Created by a natural person (not a corporation, or similar entity); and  
Revocable (able to be changed or terminated) by the creator.



**In addition, the beneficiaries must:**

- Include the creator of the trust;
- Occupy the property as a principal residence or second home;
- Be the applicant for the loan, together with the Trustee;
- Be the individuals whose assets are used to underwrite the loan; and
- Not change over the life of the loan.

**And the Trustee must:**

- Be the creator of the Trust;
- Be the sole owner of the real estate;
- Have the power to borrow money; and
- Have the power to mortgage real estate.



**Documentation**

The guidelines provide particular requirements regarding the execution of the note and mortgage and the identity of the grantor on the deed.

The trustee(s) of the Trust and the individuals whose assets were used to qualify for the mortgage must sign the note. In addition the trustee(s) of the Trust must sign the mortgage. Moreover, the deed must name the Trustee of the Trust as the grantee.

**So why doesn't this work more often?**

For a couple of reasons. First, the criteria listed above are extensive and fairly specific. A particular transaction may not be able to fit all of the requirements. Second, the kind of trust that is allowed is not the only kind of trust which borrowers may wish to use. Trusts that facilitate estate planning do not fit into these guidelines and therefore do not qualify. Finally, the lender must warrant that the trust, as borrower, won't pose an unusual risk or impairment of the lender's or investor's rights in the event of default, and foreclosure. Clearly, most lenders would prefer not to assume that extra liability.

**What's the alternative?**

Wait until after the closing. Interestingly, this alternative is treated as the big secret, that can't be known by the lender. However, since the implementation of federal law to protect certain owners from losing their property because of the due on sale clause (12 USC

§ 1707-3(d)), this "post closing" alternative is not only a good idea, but also perfectly legal and acknowledged by Fannie Mae and Freddie Mac. In short, the 1995 amendments to the National Housing Act state that when mortgaged premises are occupied by a borrower, the due on sale clause can not be exercised in certain situations, including a transfer due to the death of a joint tenant or tenant by the entirety, a transfer to a relative due to death, a transfer pursuant to a divorce and a transfer into an inter vivos trust in which the Borrower remains the beneficiary of the trust and occupant of the property (12USC 1701j-3).

**What's the best course of action ?**

Borrowers should consider waiting until after the closing to make such a transfer, being careful not to trigger the due on transfer clause. In the event that the borrower wishes to put title to the property into an estate planning trust, the only solution may be to obtain permission from the lender to make the property owner the inter vivos trust and the beneficiary the estate planning trust.

**What is the impact on the Title Insurance Policy ?**

If the owner has an ALTA owner's policy and then transfers the property into a trust under which he or she is a beneficiary, they may request that the policy be endorsed to simply reflect the "new owner". This is accomplished through a Change Endorsement. A satisfactory review of the recorded trust and deed is necessary to issue this endorsement. The endorsement would make reference to Policy Number X insuring property at XYZ Street, XYZ Town, County etc. and Schedule A would be amended by changing the name of insured from XYZ to ABC trustee of XYZ trust. In some instances there may be a charge for this service.

If the policy is an Eagle Policy, no endorsement is necessary as the coverage under this form of policy automatically follows an owner who transfers the property to a nominee or estate planning trust under which he/she is a beneficiary.