



## Non-imputation title insurance - by Thomas Kearns and Hyman Kindler



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Real estate investors often purchase ownership interests in existing entities that own commercial real estate rather than acquiring the property by deed. Reasons for this include more favorable transfer or income tax consequences. Sometimes, if the price is large enough, the purchaser would like to have title insurance coverage for their investment, which coverage, in New York, for an ownership purchase, can typically be obtained through what is commonly referred to as an “investor’s” title insurance policy. In an investor’s policy, the insured is the purchaser of the equity (and not the entity that owns the real estate). If there was a recovery under a claim made such a policy,

only the purchaser would receive the insurance proceeds (and not the entity that owns the real estate). However, in either a partial ownership purchase or a purchase of 100% of the ownership interests, title insurance policies typically have a big hole in these circumstances: all New York title policies have an exclusion for the knowledge of the insured.

This is resolved by the issuance of a non-imputation endorsement by the title insurer which removes the knowledge exclusion. The issuance of that endorsement is, however, heavily dependent on the facts and circumstances of the transfer and seller. The title insurer often insists on a detailed affidavit from

the seller and often insist on an indemnity to back up that affidavit from a credit-worthy individual or entity even to the extent of insisting on financial disclosure from the indemnitor.

We have handled numerous negotiations over non-imputation issues over the years. Here are some of the factors to consider:

1) Why is the transaction being structured as a membership interest purchase rather than a fee transfer by deed? The party asking for the transfer may have less leverage on the issue.

2) Usually the seller is making certain representations to the buyer. Consider including representations as to title matters to avoid the necessity of non-imputation coverage. Of course, the caps and survival periods must be negotiated on such representations.

3) Is there a credit-worthy indemnitor willing to give the indemnity? If so, should that indemnitor be back-stopped by others or should sale proceeds be reserved to cover unexpected post-closing claims?

4) Be sure to investigate recent work which might give rise to mechanics liens. In New York, deeds protect buyers against such claims. A membership interest transfer does not.

5) In the right circumstances, title insurers may waive or limit the indemnity, but those circumstances are rare and involve an analysis of the type of property, the level of professional management and the circumstances surrounding the transaction. Don’t count on a waiver and keep in mind even if an indemnity might be waived, an affidavit from a knowledgeable person stating that there are no known title issues will never be waived. A willfully false affidavit will subject the affiant to legal liability despite the lack of an express indemnity.

While navigating non-imputation issues requires diligence, non-imputation coverage can be key to successfully concluding a transaction.

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