

# SCHWARTZ | MANENTE

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## **Potential Title Issues Relating to “Pretended Sales” or Non-Arm’s Length Transactions**

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### **Background**

Under the Texas Constitution, all “pretended sales of the homestead involving any condition of defeasance shall be void.” *Tex. Const. art. XVI, Sec. 50(c)*. As such, in Texas, we routinely see “pretended sales” exceptions and requirements on the title commitment when the seller is related to the buyer and/or the seller does not vacate the Texas homestead property immediately and establish a new Texas homestead. These are sometimes referred to as non-arm’s length transactions.

These title exceptions and requirements eliminate important coverage provisions under the lender’s title insurance policy, which is not in the best interest of the lender or subsequent investors. As one of the key components of a title insurance policy is insuring the lien is valid, there is a high probability that proceeding with these exceptions would result in an unsalable loan on the secondary market.

If a transfer between these related persons is found not to be *bona fide*, it could potentially void (invalidate) the lender’s lien. If that occurs and there is a “pretended sales” title exception on the loan policy, then the lender has no coverage and cannot file a claim with the title insurance company to recover for the loss of the lien.

### **Examples**

Scenarios that *may* result in these exceptions and requirements appearing on the title commitment:

- Buyer and Seller are brothers. Buying brother is purchasing the property from the Selling brother.
- Buyer and Seller are sisters. Seller currently lives in the property and plans to continue living in the property after Buyer’s purchase.
- Buyer is purchasing property from her parents (Sellers). Sellers are constructing a new home, but construction will not be completed at time of Buyer’s purchase, and Sellers will occupy subject property until construction is complete on their new home.
- Daughter (Buyer) is purchasing property from her father (Seller). Buyer is the caregiver for Seller, and Seller wants Buyer to have the house. The home is being purchased with gift equity, and the Seller is not moving out.

Examples of pretended sales exceptions and requirements that may appear on Schedule B or C of the title commitment:

- “Any failure of title by reason of: (i) any claim, assertion, or determination that the vesting of title in [Buyer’s Name] by that deed recorded \_\_\_\_\_ in \_\_\_\_\_ County, Texas was not a bona fide sale, but was instead a pretended sale; or (ii) any claim, assertion, or determination that the above referenced deed vesting title in [Buyer’s Name] constitutes a mortgage or other security device.”

- “Any loss, claim, or damage arising from or relating to homestead rights of \_\_\_\_\_, if any, including any loss or claim arising from or relating to any assertion or determination that the insured lien is not a valid and enforceable lien against homestead property.”
- “Loss, cost, or damage arising out of any allegation that the insured transaction is a pretended sale of homestead property and void under the Texas Constitution.”
- “Since the proposed transaction appears to involve a buyer and seller whom may be related. Company requires evidence that the seller relinquishes any homestead claim on this property and does not reside there. Otherwise, we will except to any loss, damage, or claim that may arise from homestead laws of Texas.”

## **Conclusion**

Potential resolutions vary depending on the circumstances. If the sellers have purchased another property, or will be leasing/renting another property after the sale, and intend to vacate the subject property, the title company may be willing to remove the exception if the sellers execute a separate document or affidavit relinquishing their homestead rights. Alternatively, lenders may be able to find a title company willing to proceed with issuing a title policy without a pretended sale exception.