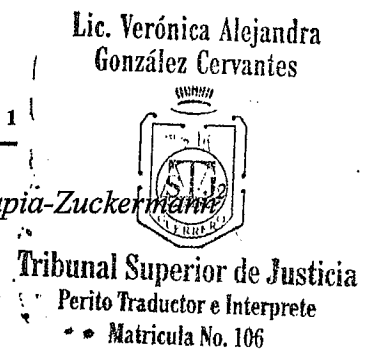


Title Insurance in Mexico and its Contribution to Legal Certainty¹

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Introduction



Title insurance is a figure only recently incorporated into our legal system and gradually, foreign investors' demands, among other elements, have made its use more frequent in operations involving real estate collateral.

As it stands, title insurance is a creation of common law given that in jurisdictions such as the United States and the United Kingdom the obligation to register transfers of real estate property in a centralized registry does not exist.³ Due to the slowness, disorderliness, and even corruption on the part of registry officials in the public property registries in Mexico, as well as the emergence of large real estate investments, Mexico, a country with an obligatory registry system and with Notary Publics as the only attorneys vested by the State with public faith and credit to formalize the transfer of real property⁴, has lately been forced to allow the exploration of new alternatives to assuage the situation of uncertainty which, at least in theory, should not prevail in the public registries or in our civil law.⁵

¹ "Title Insurance in Mexico and its Contribution towards the Rule of Law", originally published in Spanish in December of 2006 and edited by Themis and the Mexican Bar Association, First Edition, *Colección Foro de la Barra Mexicana*, within the compilation named "Rule of Law: Diagnostic and Proposals".

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³ In recent years the number of state jurisdictions in the United States that mandate the registration of deeds of property has increased (11 states approximately); however, the *Torrens* system or deed registration system is not very popular and its method is somewhat complex. Notwithstanding the obligation to register, said act does not constitute rights since the State assumes a passive role and acts as a receiver, in deposit, of the registered deed.

⁴ As stated in article 2,317 of the Federal Civil Code, all transfers of real estate with a value higher than \$17,765.55 Pesos must be recorded by way of public deed of property before a Notary Public. Article 730 of the same code exempts property which constitutes a family patrimony, in which case the value must not exceed \$177,645 Pesos. (These values were calculated on the basis of a \$48.67 Pesos minimum wage applicable in zone "A" and were published by the National Commission of Minimum Wages in the Official Gazette of the Federation (*Diario Oficial de la Federación*) on December 26, 2005).

⁵ As an example of this, there is only one company authorized by the National Insurance and Surety Commission (*Comisión Nacional de Seguros y Fianzas*) to directly issue title insurance policies. Stewart Title Guaranty de México, S.A. de C.V. with registration number S0070. There are other companies that resell these policies, such as First American Title Insurance Company, but under the registration of authorized insurance companies such as Grupo Nacional Provincial, S. A. with registration number S0043.



Real estate property insurance materializes by way of an indemnity contract which protects and guarantees the property rights of the purchaser of the policy against the eventualities contracted in the insurance agreement and which are listed in the policy and its endorsements on attachments. The convenience of not going before a state civil court in case of an eviction due to title defects in the title deed of the seller of the property or in case there was a defect in the consent granted or the representation powers or authority of one of the parties to the contract, among others we will explore, is a factor which, combined with the generalized slowness of those civil processes, has popularized the contracting of title insurance in Mexico.

Background

The question of the identity of the true owner of a property has been answered in as varying and dissimilar ways as there are legal communities in the world. Within the Roman-Canonic legal tradition, to follow the exact classification by John Henry Merryman, to which the Mexican legal system belongs, there exists a well-defined part in the civil codes of the entities which make up the United Mexican States and which regulate matters of publicity, precedence and opposition by creating public registries of real estate property in which the registration of the transfers of real property is mandatory and where the identity of the parties and of the Notary Public before whom the transfer was formalized is recorded.

Moreover, the registry-related provisions of the referenced civil codes establish the specific procedures and formalities that must be observed to register an executive title, as is the case of the first official copy of a public deed of title formalized before a Notary Public, or of an authentic document which was private when it was prepared and later was ratified before a Notary Public as to its content and the identities of the parties executing the same.

In common law legal systems, where title insurance was originated due to the fact that the obligation to record all transfers of real property in a central public property registry in order for them to be valid, and above all, to constitute a legal defense, did not and still does not exist in many jurisdictions. In common law jurisdictions, knowing who the true owner, with sufficient powers to transfer, was became an arduous exercise in research and because of this, the need arose for the



existence of an independent source of information regarding the identity of the contracting parties in, for example, a purchase and sale transaction. Thus arose the development of systems like the *pure race statute* or registry system whereby the first person who registers prevails and which is similar in its operation to that of the Mexican public property registries; however, this system represents a novelty vis-à-vis the system more widely used and known as *notice recording statute* where the relevant date is not that on which the document was registered, but that on which the document containing the transfer was signed. Emphasis was made on the good faith of the purchaser, understood as the lack of knowledge of another owner with a better right to transfer, given the fact that a property transfer that was not registered had no prevalence over his rights to the acquired property. Likewise, if a third-party purchaser had paid a price in good faith for the property, no matter how small the price, he would prevail in his rights to the property over a person who, having registered his title of ownership previously, laid claim to it.

In order to balance these two systems, a third one, known as the *race-notice recording statute* emerged in the United States, it combined the elements of the two previous systems; that is, a title had to be recorded in order to constitute a valid legal defense and notice against a subsequent third-party good faith purchaser, but the registration had to be recorded invariably in the chain of title. This is similar to what occurs in the chain of endorsements in commercial and negotiable instruments law.

Due to the complexity of Anglo-Saxon law, where the possibility exists of laying claim to titles that cannot be registered since they do not fall within the scope of application of the *recording acts* or registry acts, as is the case of claims not originated from an instrument recorded in writing, which include, but are not limited to matters relating to statutes of limitations, easement and access rights and verbal agreements regarding boundaries; the necessity arose to perfect a system which did not give certainty even when a written agreement had been subsequently signed and recorded to formalize the foregoing actions, as the defects were still alien to the written document and were not traceable by only examining such document.

Given the evident flaws in the common law system, which, in the contemporary world and due to the demand for legal certainty in commercial transactions was inadmissible, the services of a system that ensured the quality of title to real property were put to use.



This title assurance method, which is not official and has been sponsored by the private sector, was first used during the decade of the 1970's in the United States under the name of title insurance or property insurance to assume and diminish the risks that the American registry system posed. Notwithstanding its being a low-competitiveness and relatively high-cost market for consumers, it became popular due mainly to its precision, swiftness and efficient distribution of risks.

During 1976 and 1977 a legislation named *Uniform Simplification of Land Transfers Act* was enacted in the United States, which standardized the procedures for the transfer of real property. It materialized some of the most relevant aspects of those transfers and served as a model for multiple state jurisdictions in the United States to define the systems of registration of real estate transactions and announce the rise of private insurance carriers to assume in full the risks inherent to sellers' or transferors' property titles with regard to buyers or persons in whose favor the real property was transferred.

Title Insurance in Mexico

Still more recent is the incorporation and usage of title insurance in Mexico which, formally, was first commercialized in the year 2001. This insurance, contrary to what occurred in the United States and the United Kingdom, was first employed due to the multiple deficiencies that occur, whether they arose from the volume of documents to be recorded, the somewhat outdated technology used to record these documents, or to voluntary or involuntary errors in the public property registries, as well as the dichotomy that results, for example, from an independent National Agrarian Registry (*Registro Agrario Nacional*) in which the information does not necessarily coincide with the Civil Registry of Real Property.

In like manner, the presence of large-scale foreign and institutional investors who wish to invest in our country and who are accustomed to using title insurance which is normally required by their foreign creditors or lenders to grant the necessary financing, has made the employment of this type of insurance increasingly more common.



Contracting this type of insurance is practically identical to the hiring of any other insurance; however, the main difference is that while other kinds of insurance cover future eventualities, title insurance is an indemnity insurance which protects the rights of property which have been transferred to the new owner of the property and, therefore, the insurance company which issues the title insurance assumes the risks regarding past events⁶; that is, while the relevant claim is presented after the issuance of the respective insurance policy, such claim will have to do with facts or defects which existed prior to the date on which the policy was issued.

Logically, it is worth mentioning that this kind of policies exclude from their coverage defects, purchase preventive notices filed by Notary Publics or encumbrances that come up after the date of issuance of the policy or that were caused by acts of the insured.

The issuance of title insurance is preceded invariably by a so called Commitment Letter through which the insurance company, after reviewing the recorded history at the corresponding public property registry, informs the client that, due to the legal situation of the real property, it can issue the corresponding policy. There are two types of policies in the market, which are known by the identity of the insured party, whether it is the new owner (owner's policy) or his creditor or lender. The lender's or creditor's policy alone does not protect the new owner of the property.

The coverage extends, normally, to the payment of legal fees and the situations it covers are, amongst others, the following contingencies: (i) fraud, (ii) public documents issued or formalized by persons without legal capacity, (iii) invalid public documents provided after the demise of the person who granted them, (iv) forging of public documents and other authentic documents, (v) lack of authority of the rightful owner of the property on the part of the transferor or other persons with previous property rights, (vi) public documents granted by married persons who declared, at the moment of granting them, that they were single, (vii) non-registered easement rights and (viii) overdue taxes over inheritances or gratuitous transfers applicable to previous owners which are still outstanding in accordance with applicable tax law.

⁶ For example: an unknown probate proceeding or devise of a previous owner; forged public or private documents that were recorded or that were signed with forged or expired powers of attorney and errors, as mentioned earlier, in the public property registries.



Title insurance contained in the owner's policy continues to be valid while the insured or his heirs or assignees have interest in the insured property, and, consequently, will have an indefinite validity until such time as the property is transferred to a third party. As for a creditor's policy, it will continue to be valid in the same measure as the guaranty is outstanding, even when the rights to such guaranty are assigned to another lender.

Due to the lack of competition that exists in the market, the cost of title insurance is still high and fluctuates between 0.35% to 1.0% of the value of the real property, depending upon the commercial value of the insured real estate and the premium is payable, for one time only, at the moment of the issuance of the corresponding title insurance policy.

Notwithstanding its recent introduction into our legal and commercial systems, title insurance is becoming an instrument of additional legal certainty to the Notary Public and centralized public property registry systems that have operated in Mexico for many years.

Title insurance, a product, no doubt, of the recent commercial opening of Mexico to the world, will contribute to provide greater legal certainty, not only to foreign investors familiarized with its mechanism, but also to national investors who seek to confidently purchase real property in Mexico and its restricted zone.⁷

Conclusions

By means of brief and specific conclusions in the form of questions, I will advance a few general ideas which are intended to summarize my concerns and open the debate to discuss the virtues or flaws of title insurance in Mexico and its contribution to legal certainty.

1. Is title insurance necessary given the fact that the obligation to record every transfer of real property in a public property registry exists, as well as the presence of Notary Publics?

⁷ Real property located within 30 miles of the coastline or 50 miles from the border which is restricted from direct purchase, in fee simple, by foreigners, in accordance with the Mexican Constitution and the Foreign Investment Law.


2. In what measure does title insurance contribute to legal certainty regarding real estate investments? Will it be a determinant factor so that investment in this area will not become stagnant?

3. What other methods which provide legal certainty in real estate transactions exist or could be implemented and would help the Mexican Government in its endeavor to provide certainty in the purchase of real property? Could these alternate methods replace title insurance?

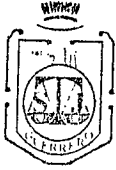
4. Since the cost of a title insurance policy is high, is it worth buying instead of presenting a civil claim before local courts to seek compensation for an eviction or damages suffered in connection with acquired real property? How can the operation of the current registry systems be improved through title insurance?

5. What virtues and flaws can be ascribed to title insurance? What solutions can be proposed to correct the defects? What legislative reforms can be enacted to enhance the regulation of this type of insurance?

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