The owner of a tract of land mortgaged the tract to a bank to secure his preexisting obligation to the bank. The mortgage was promptly and properly recorded. The owner and a buyer then entered into a valid written contract for the purchase and sale of the tract, which provided for the transfer of "a marketable title, free of encumbrances." The contract did not expressly refer to the mortgage.

Shortly after entering into the contract, the buyer found another property that much better suited her needs and decided to try to avoid her contract with the owner. When the buyer discovered the existence of the mortgage, she asserted that the title was encumbered and that she would not close. The owner responded by offering to provide for payment and discharge of the mortgage at the closing from the proceeds of the closing. The buyer refused to go forward, and the owner brought an appropriate action against her for specific performance.

If the court holds for the owner in this action, what would be the likely reason?

A. The doctrine of equitable conversion supports the result.

B. The existence of the mortgage was not the buyer's real reason for refusing to close.

C. The mortgage is not entitled to priority because it was granted for preexisting obligations.

D. The owner's arrangements for the payment of the mortgage fully satisfied his obligation to deliver marketable title.

Explanation:

"Red flags" for marketable title

Covenants
Easements
Leases
Liens
Gaps in chain of title
Boundary disputes
Existing zoning violations
Adverse possession

All contracts for the sale of land have an **implied warranty** that the seller will convey **marketable title** to the buyer **upon closing** unless otherwise stated. Title need not be perfect to be marketable. However, it must be reasonably free from doubt and under no threat of litigation such that a reasonable person would accept and pay for it. If the seller cannot convey marketable title by the time of closing, the buyer can rescind (ie, cancel) the contract.

Title can be **rendered unmarketable** by **encumbrances** (eg, easements, mortgages, other liens). Although a mortgage is an encumbrance, the seller has the right to **satisfy the mortgage** up to the **time of closing** and will often use the sale proceeds to do so—as the owner has made arrangements to do here. As a result, the court will hold for the owner because the closing itself will likely render title marketable.

(Choice A) The doctrine of equitable conversion relates to the ownership of the property and the risk of loss in the period between contract formation and closing. It does not affect the parties' performance under the land-sale contract.

(Choice B) The buyer could have refused to close if she had an *actual* basis for doing so—even if that was not the buyer's actual reason for the refusal.

(Choice C) Priority refers to the order in which creditors receive sale proceeds from a foreclosure; whether a mortgage was granted for preexisting obligations does not affect its priority. Regardless, this will not affect the owner's success because (1) there is no indication that there are other encumbrances on the property, and (2) the mortgage will likely be satisfied and thereby extinguished upon closing.

Educational objective:

A mortgage is an encumbrance that can render title unmarketable. However, the seller has the right to satisfy the mortgage up to the time of closing and will often use the sale proceeds to do so.