

Deeds in Lieu: Subsequent Foreclosure of Mortgage

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Introduction

Deeds in lieu of foreclosure are often heavily negotiated. However, in many instances the lender is actually doing the borrower a favor by agreeing to accept a deed-in-lieu. The lender rarely is actively seeking to acquire a property with a value less than the outstanding debt, which may require major repairs, renovation and rehabilitation. Lenders may even refuse to accept a deed-in-lieu, for reasons including environmental contamination, the belief that there is equity in the property, and excessive or monetarily significant subordinate liens. On the other hand, the lender may agree to accommodate a cooperative borrower by delaying the delivery of the conveyance to postpone the tax consequences to the borrower.

There is certainly a benefit to taking title immediately and avoiding the foreclosure process, but this benefit inures to both the lender and the borrower. It is also costly to structure a deed-in-lieu transaction, and the lender will customarily bear virtually all of the transactional expenses, including title and recording costs, and environmental inspections.

In any event, a deed in lieu of foreclosure does not “wipe out” any subordinate liens, and the grantee-mortgagee takes subject to all existing liens, whether known or unknown. To attempt to eliminate these liens, the lender still must foreclose the mortgage or otherwise deal with each of the existing encumbrances. The lender actually may have an incentive to pay something on lien claims to avoid a contested foreclosure proceeding; after all, the primary purpose of a deed-in-lieu transaction usually is to avoid foreclosure.

Case Law Permitting Subsequent Foreclosure

Recent case law generally supports the ability of a mortgagee to foreclose its mortgage after acceptance of a deed in lieu of foreclosure, at least where the deed contains an anti-merger provision. See, e.g., *PNC Bank v. Philben, Inc.*, 1997 Del. Super. LEXIS 467 (Del. Super. Ct. 1997) (not reported in A.2d) at *9-10 (holding that where the deed-in-lieu documents contained an anti-merger provision, the owner-mortgagee could subsequently commence foreclosure proceedings; the court noted that “where the mortgage includes an anti-merger provision to protect an existing mortgage balance, the deed is merely additional security for the mortgage debt,” and that “[the mortgagee] preserved its right to foreclose”); *GBJ, Inc., II v. First Ave. Inv. Corp.*, 520 N.W.2d 508, 511 (Minn.

App. 1994) (ruling that “[the mortgagee] did not forfeit its rights as mortgagee when it took the deed in lieu of foreclosure. To the contrary, the doctrine of merger presumes that the mortgagee retains all rights”; the court further stated that “[the mortgagee] therefore retained the right to foreclose”); *Runge v. Runge*, 1999 Minn. App. LEXIS 1187 (Ct. of Appeals of Minnesota) (unpublished) at *6 (stating that “[the mortgagee] did not forfeit his rights as mortgage when he took the deed in deed in lieu of foreclosure. To the contrary, the doctrine of merger presumes that the mortgagee retains all rights; and noting that deed contained “an unambiguous anti-merger clause evidencing [the mortgagee’s] intent not to merge his interests”); *Olney Trust Bank v. Pitts*, 200 Ill.App.3d 917, 926-27, 558 N.E.2d 398, 403-04 (5th Dist. 1990) (holding that “because there is no merger, the mortgage debt is not satisfied or extinguished”; the court permitted the lender, who had obtained a deed-in-lieu, to foreclose but prohibited it from pursuing an action for a deficiency judgment); *Zurich Ins. Co. v. Principal Mut. Life. Ins. Co.*, 1992 U.S. Dist. LEXIS 16029 (D. Ill. 1992) (“The Illinois Appellate Court has construed P 15-1401 [Ill. Rev. Stat. ch. 110, P 15-1401], which makes clear that a deed in lieu of foreclosure does not merge the mortgagee’s mortgage interest with its new interest as holder of title to the property] as containing an express disavowal of merger such that a deed in lieu of foreclosure, when executed, does not necessarily satisfy or extinguish a mortgage debt” (citing the *Olney* case, *supra*)); *In re Estate of Ozier*, 225 Ill.App.3d 33, 36, 587 N.E.2d 77, 80 (4th Dist. 1992) (“In the absence of evidence to the contrary, the law presumes that a mortgagee intended to keep his mortgage alive, when such course was essential to his protection against an intervening title or for other purposes of security”); *Zubrys v. Harbor Country Banking Co.*, Docket No. 192822 (unpublished opinion per curiam of the Michigan Court of Appeals, December 19, 1997) (holding that where the first mortgagee took a deed in lieu of foreclosure and subsequently foreclosed its mortgage after discovering the existence of a second mortgage, there was sufficient language in the deed-in-lieu documents to prevent a merger of the security interest and ownership interest; the court also held that the second mortgagee did not have standing to challenge the adequacy of the consideration given to the mortgagor for the deed in lieu); *Union Bank & Trust Co. v. Farmwald Development Corp.*, 181 Mich.App.538, 547, 450 N.W.2d 274, 278 (1989) (ruling that junior mortgagee’s objection to entry of foreclosure of mortgages of first mortgagee was unfounded, because first mortgagee’s interest was not extinguished and discharged by mortgagor’s conveyance of the secured property to the first mortgagee); *Clark v. Federal Land Bank*, 167 Mich. App. 439, 444-45, 423 N.W.2d 220, 222 (1988) (refusing to permit a subordinate judgment lienholder to have bank’s foreclosure on property subject to lien declared invalid; and stating that “the quitclaim deed executed by the [mortgagors] to the bank manifested unequivocally an intention that the mortgage not merge with the fee. Additionally, plaintiff’s rights were not affected by the intention to keep the mortgage alive, for she knew her judgment lien was subject to a first mortgage pursuant to the judgment of divorce”); *Miller v. Martineau*, 983 P.2d 1107 (Utah App.1999) (holding that, where it appears that the parties did not intend merger,

a third party who obtains both the mortgagee's and mortgagor's interests may avoid merger and proceed with foreclosure to eliminate a subordinate lessee); *Aetna Life Ins. Co. v. Hager*, Case No. 84-CI-41, Common Pleas Court of Ross County, Ohio (1984) (deed-in-lieu contained specific anti-merger language; lender subsequently elected to foreclose on the property, and two subordinate lienholders objected to foreclosure on the basis that it would be "improper and highly prejudicial to their interests," and that title had merged and therefore the lender – or, more properly, the related entity created by the lender to take title -- had no standing to bring the foreclosure action; the court ruled that the merger language was enforceable and that the first mortgage was not extinguished by the foreclosure, and stated that "Aetna elected to keep the mortgages separate and distinct and such an election is clearly an available option"); *Ennis v. Finanz Und Kommerz-Union Etabl*, 565 So. 2nd 374, 375 (Fla. App. 2 Dist. 1990) (holding that conveyance to mortgagee of fee simple title to mortgaged property does not give rise to merger so as to extinguish mortgage; mortgage lien can remain superior to competing creditor's judgment lien, so long as there is evidence that parties did not intend there to be such a merger).

See also Nancy Young, *Deed in Lieu of Foreclosure and Subsequent Foreclosure – A Case Study in Ohio*, RPPT E-REPORT (ABA Section of Real Property, Probate and Trust Law, April 2007) (stating, in connection with the *Aetna Life Ins. Co. v. Hager* case, *supra*, in which the author's law firm represented the lender, that "Obviously the best protection for a lender in accepting a deed in lieu of foreclosure with the intention of reserving the right to foreclose its mortgage is appropriate documentation at the time of the deed in lieu transaction"). *See generally* 55 AM. JUR. 2D MORTGAGES § 1345, *Intervening or Junior Claims or Liens*; 3 PATTON AND PALOMAR ON LAND TITLES § 564, *Constructive Releases; Termination of Lien by Merger* (2007).

But see RESTAT. 3D OF PROPERTY: MORTGAGES § 8.5, Reporter's Notes, Comment E.:

Under this section, however . . . the mortgagee who takes a deed in lieu with actual knowledge of a junior lien will lose the right to foreclose irrespective of whether there is merger intent. As Professor Burkhart emphasizes:

By focusing on merger, the courts have defined this second type of case too narrowly. In tune with the usual merger analysis, courts have defined this group of cases to include only mortgagees that express an intent to merge However, the senior mortgagee should be prohibited from exercising its lien in this situation regardless of whether it has manifested any intent concerning merger. Each time a deed in lieu transaction is negotiated with the understanding that

the mortgagee will acquire title subject to junior liens, the senior mortgagee has waived its right to eliminate those liens. Courts' focus on merger diverts them from focusing on the substance of the transaction.

Burkhart, *Freeing Mortgages of Merger*, 40 VAND. L. REV. 283, 348-49 (1987).

The Merger Doctrine: Statutory and Case Law

The section of the Illinois mortgage foreclosure statute that deals specifically with deeds in lieu of foreclosure, 735 ILCS 5/15-1401, states (with respect to the issue of merger) that “A deed in lieu of foreclosure, whether to the mortgagee or mortgagee’s nominee, shall not effect a merger of the mortgagee’s interest as mortgagee and the mortgagee’s interest derived from the deed in lieu of foreclosure.”

Most other states rely (at least in part) on the intention of the parties, either express or implied, to determine whether a merger occurred as the result of a deed-in-lieu transaction. In *Tidwell v. Dasher*, 152 Mich. App. 379, 393 N.W.2d 644 (1986), the court dealt with the issue of whether a deed in lieu of foreclosure created a merger that would affect the priority of an intervening lien. The court stated that “[t]he question of intention of a mortgagee or vendor is a question of fact which must be developed from evidence produced to show what the intention was at the time the acts were done.” *Id.*, 152 Mich. App. at 385, 393 N.W.2d at 647. In *Weitzki v. Weitzki*, 437 N.W.2d 449 (Neb. 1989), the court noted that the intention of the mortgagee is controlling as to whether the mortgage is kept alive. The court held that when the mortgagee becomes the owner of the fee, and there is no expression of intention as to whether the mortgagee wished to keep the mortgage alive, it will be presumed that the mortgagee intended to do what would prove most advantageous to himself in the absence of circumstances indicating a contrary purpose. The court then found that in this case no merger of title and lien occurred in light of the mortgagee’s intent to retain the priority of his lien against the subordinate lien. *See also FDIC v. Lee*, 988 F.2d 838, 843 (8th Cir. 1993) (“[t]he doctrine of merger is not favored and will not be applied in the absence of an intent on the part of the mortgagee, or unless the application of the doctrine is require by equities of a particular case” [quoting *Construction Machinery v. Roberts*, 307 Ark. 252, 819 S.W.2d 268, 270 (1991)]); *Sylvania Savings Bank v. Turner*, 27 Mich. App. 640, 645, 183 N.W.2d 894, 896-97 (1970) (“whether [merger] occurs depends fundamentally on the mortgagee’s intention. If it is in his interest to preserve his lien separately from the fee, it will ordinarily be concluded that he did not intend to merge the lien into the fee”); *Long Island Lighting Co. v. Commissioner of Taxation and Finance*, 652 N.Y.S.2d 640, 641, 235 A.D.2d 637, 638 (N.Y.A.D., 3rd Dept. 1997), *leave to appeal denied*, 90 N.Y.2d 801, 660 N.Y.S.2d 554, 683 N.E.2d 19 (1997) (noting that “the doctrine of merger is disfavored,” the court stated that “the determinative issue is whether the owner intended there be a merger, which must be discerned

from all the circumstances”); Nancy J. Appleby, *Negotiating and Structuring a Friendly Foreclosure or Deed in Lieu of Foreclosure: A Lender’s Perspective*, American Bar Association Section of Real Property, Probate and Trust Law, New York, NY (August 10, 1993), Tab 8.

In Texas, TEX. PROP. CODE § 51.006 permits the mortgagee to void a previously accepted deed in lieu of foreclosure in certain circumstances and foreclose the deed of trust. Also, the statute authorizes the mortgagee to foreclose its deed of trust after accepting the deed in lieu of foreclosure. In both cases the statute provides that the priority of the deed of trust is not affected or impaired by the deed in lieu of foreclosure. See Bill Locke, *Texas Deed in Lieu of Foreclosure*, posted to DIRT listserv, DIRT – Real Estate Lawyers Listserv [DIRT@LISTSERV.UMKC.EDU], Jan. 10, 2009, and attachment thereto (*Deeds in Lieu of Foreclosure*), for a discussion of the advantages and disadvantages of taking a deed in lieu of foreclosure in Texas.

See **Exhibit A** attached hereto for various forms of non-merger language for insertion in deeds in lieu of foreclosure and settlement agreements. There is really no need to “over-lawyer” these types of provisions; they all are sufficient to attain the desired goal. These types of clauses are enforceable in the vast majority of states.

Unenforceable Non-Merger Provisions: *United States Leather, Inc. v. Mitchell Manufacturing Group, Inc.*

However, courts generally will not enforce a non-merger provision in a deed in lieu of foreclosure where the rights of innocent third parties may be affected – or even lost – because of fraud or inequitable conduct by the parties to the deed. For example, in *United States Leather, Inc. v. Mitchell Mfg. Group, Inc.*, 276 F.3d 782 (6th Cir. 2002), the Sixth Circuit held that under the facts of the case, allowing an exception to the merger rule (based on the intention of the parties stated in the quitclaim deed in lieu of foreclosure that no merger of the mortgage and fee would occur) would not be enforced because it would inequitably permit the mortgagor to void its obligations to an intervening judgment creditor to the sole advantage of the mortgagor’s corporate parent.

This decision involved a very complicated factual situation. The case arose out of the efforts of the plaintiff, United States Leather, Inc. (“USL”), to enforce a judgment of approximately \$1.5 million against Mitchell Automotive, Inc. (“Mitchell Automotive”), which owned personal property and a manufacturing facility in Clare, Michigan. Mitchell Automotive was in the business of manufacturing and selling leather products for use in automobile interiors.

Over time, Mitchell Automotive built up a substantial debt to USL (as a supplier of finished leather), as well as to its parent corporation, Mitchell Corporation of Owosso (“Mitchell Corp.”). Mitchell Automotive eventually succeeded in finding a buyer, Lamont Group, Inc., and Lamont Group Acquisition

Corp. (collectively, “Lamont Group”) to purchase Mitchell Automotive’s real and personal property. Lamont Group paid \$6.5 million in cash to Mitchell Automotive and gave two promissory notes for the balance of the purchase price of \$27.5 million. To secure the indebtedness, Lamont Group granted Mitchell Automotive a security interest in the purchased assets and a mortgage on the real property. Shortly thereafter, Mitchell Automotive granted its parent, Mitchell Corp., a security interest in all its personal and intangible property (including all “instruments”) to secure any and all existing and future indebtedness to Mitchell Corp. According to the court, “It is undisputed that Mitchell Corp. obtained a security interest in the Lamont Group’s mortgage and promissory notes through their agreement.” *Id.* at 785.

The Lamont Group subsequently defaulted, and agreed to surrender all the personal property collateral and deliver a deed in lieu of foreclosure to the secured real property to Mitchell Automotive. The quitclaim deed to the real property contained language stating that it was the intention of the parties that the deed did not constitute “a merger with or extinguishment of the indebtedness secured thereby.” (The deed also provided that the recourse obligation of Lamont under the Asset Purchase Agreement for the purchase of Mitchell Automotive’s assets would be reduced by \$6 million). As a result of the conveyance, Mitchell Automotive held title to both the mortgage and the fee interest in the real property.

Shortly thereafter, USL obtained a consent judgment against Mitchell Automotive and Lamont Group in the amount of approximately \$1.5 million, and levied on the personal property of Mitchell Automotive at its offices in Owosso, Michigan. The levy officer did not take actual possession of the property, based on the agreement of Mitchell Automotive’s attorney that the property would not be moved, sold, or disposed of and that Mitchell Automotive’s remaining personal property was not sufficient to satisfy the judgment.

Mitchell Corp. then advised USL that it claimed priority against the assets of Mitchell Automotive by virtue of its prior security agreement and that it had “peaceably repossessed” the personal property of Mitchell Automotive in accordance with its rights under that agreement. USL responded to this development by filing a formal Notice of Levy against the manufacturing facility owned by Mitchell Automotive (which was the property previously conveyed by the deed-in-lieu from Lamont Group to Mitchell Automotive), and served a garnishment on the tenant of the property – eventually collecting \$46,000 in lease payments before the lease was terminated.

USL then filed a “motion for determination of interests in the property of Mitchell Automotive,” arguing that “Mitchell Corp.’s security interest was extinguished by merger, was not perfected, was fraudulent, and that the corporate form should be disregarded.” *Id.* at 786. The district court adopted the findings of the magistrate judge, who held that the mortgage was extinguished by

merger notwithstanding the non-merger language contained in the deed in lieu of foreclosure. The district court further ruled that the question of whether Mitchell Corp. had to perfect its security interest until after USL's garnishment and levy of Mitchell Automotive's personal property was irrelevant.

In upholding the ruling of the district court, the Sixth Circuit first stated the general rule in Michigan regarding the merger doctrine:

The general rule in Michigan is that when a holder of a real estate mortgage becomes the owner of the fee, the mortgage and fee are merged and the mortgage is extinguished. *Byerlien v. Shipp*, 451 N.W. 565, 569 (Mich. App. 1990). "This rule is, however, subject to the exception that when it is to the interest of the mortgagee and is his intention to keep the mortgage alive, there is no merger, *unless the rights of the mortgagor or third persons are affected thereby.*" *Id.* (emphasis added) (quoting *Anderson v. Thompson*, 225 Mich. 155, 195 N.W. 689 (Mich. 1923). *Id.* at 786-87.

The Sixth Circuit rejected Mitchell Automotive's argument that there was no merger because it did not hold both the title to the real property and the mortgage. The court reasoned that although Mitchell Automotive had granted a security interest in the Lamont Group's mortgage and promissory notes to Mitchell Corp., it "did not assign, transfer, or convey Lamont's mortgage to anyone." *Id.* at 787.

The court then ruled that because of equitable considerations involving the conflicting rights of USL as an intervening third party, it would not enforce the express non-merger intent of the parties as set forth in the deed in lieu of foreclosure from Lamont Group to Mitchell Automotive. According to the court:

Allowing an exception to [the] merger rule in this instance would do grave injustice. Such a finding would permit Defendant [Mitchell Automotive] to avoid paying an uncontested \$1.5 million debt to [USL] in favor of its parent corporation, Defendant [Mitchell Corp.]. The fact that these two corporations share the same office space, computers, employees, and are run by the same President who originally incurred the debt to [USL] only highlights the inequity of applying the exception."

Id. at 787.

The court found that this case was distinguishable from other Michigan cases where non-merger language contained in a deed in lieu of foreclosure had been enforced, as this was not a situation where the mortgagee was trying to

protect itself from the claims of junior lienholders of the mortgagor. As the court stated:

[Mitchell Automotive] is not in the position of a mortgagee trying to protect itself from junior lienholders of the Lamont Defendants; it is attempting to protect itself from having to pay a debt it acknowledges owing to Plaintiff. We agree that equitable considerations preclude Mitchell Automotive from avoiding merger when the effect is not to protect its own interests from the creditors of the Lamont Group (the mortgagor), but rather to prefer the debt of its parent corporation over the debt owed to USL as a third party.

Id. at 787-88.

The Sixth Circuit further noted that unlike the Michigan cases cited by Mitchell Corp., USL did not expressly acknowledge the priority of Mitchell Corp.'s mortgage and its judgment was not expressly made subject to Mitchell Corp.'s mortgage. The court also rejected Mitchell Corp.'s argument that it was itself a third party whose rights were "most affected by merger or non-merger." *Id.* at 788. The court held that USL was equally affected by the merger issue. The court further denied Mitchell Corp.'s claim that it was unfair to "lump" Mitchell Corp. and Mitchell Automotive together without first determining whether the corporate veil could be pierced. The court was greatly influenced by its finding (as stated earlier) that both corporations shared the same office space, computers, employees, and officers. The court reasoned that because USL had abandoned any claim against Mitchell Corp. for the indebtedness owed to it by Mitchell Automotive, it was not necessary to make a determination as to whether the facts of the case justified piercing the corporate veil. The court noted that the district court had instead been "called upon to weigh the equities between USL and Mitchell Corp. as secured creditors competing for the sole asset of the debtor," and in this regard "it was proper to consider the relationship between Mitchell Automotive and its respective creditors." *Id.* The court found that the equities of the case prevented Mitchell Automotive from relying on the exception to the merger rule "to favor the debt owed to the parent company over USL's judgment lien." *Id.* at 789.

See also *Bylerin v. Shipp*, 182 Mich. App. 39, 48 (1990) (stating that "When the holder of a real estate mortgage becomes the owner of the fee, the former estate is merged in the latter," but noting that the rule "is subject to the exception that when it is to the interest of the mortgagee and is his intention to keep the mortgage alive, there is no merger, unless the rights of the mortgagor or third persons are affected thereby"). Cf. *Alden State Bank v. Borton*, 2005 Mich. App. LEXIS 2859 (Nov. 17, 2005), at *9 (quitclaim deed in lieu of foreclosure contained explicit non-merger language; court ruled that plaintiffs were mere judgment creditors of property owners and "as Michigan courts have explained, the purpose of declining to find a merger is to allow a mortgagee/lender to protect

itself from the claims of junior lienholders of the mortgagor/borrower” (citing *United States Leather, supra*); court stated that “The [lender] Bank is not obligated to the [judgment creditors], but is attempting to protect itself from junior lienholders (citation omitted). Thus, there is no merger.”)

Title Insurance

The mortgagee-grantee may be able to obtain a non-merger endorsement (see **EXHIBIT B** attached hereto for a sample form) from the title insurer in connection with a deed-in-lieu transaction where there is appropriate non-merger language in the deed and settlement agreement, unless (a) the applicable facts and circumstances of the particular proposed transaction (including the law or regulations of the applicable jurisdiction) would cause the underwriter to believe the risk was unacceptable (e.g., there were many junior liens and, notwithstanding proper exceptions for them in Schedule B (b) the underwriter was concerned about the likelihood of a challenge by one or more of such junior lienors based on a merger argument and, therefore, and therefore the defense costs the title insurer would have to incur if it provided the non-merger coverage); or (c) a non-merger endorsement is not permissible as a regulatory or statutory matter in the governing jurisdiction. The anti-merger endorsement attached hereto as **EXHIBIT B** insures the lender (referred to in Schedule A of the existing Loan Policy) against loss sustained by reason of the invalidity or unenforceability of the lien of the insured mortgage as a result of the title to the estate being vested as shown in Schedule A (i.e., the same party). This endorsement, together with a date-down of the existing Loan Policy, should be issued at the time the new Owner’s Policy is issued.

The author has been informed that in New York a title insurer may not issue a non-merger endorsement. The author also has been informed that the (unwritten) position of the New York State Tax Commission is that the mortgage can be foreclosed (if there is non-merger language in the deed from the mortgagor to the mortgagee-grantee), but it cannot thereafter be kept alive for the purpose of a future transaction; e.g., the mortgagee-grantee cannot re-sell the property and modify the mortgage with its purchaser and retain a valid mortgage lien.

But as a general proposition, and assuming no regulatory prohibition and proper alignment of the title insurer’s and its customer’s interests so that the title insurer can deem it an acceptable risk in the context of the particular situation -- and absent the caveats stated in the prior paragraph -- the title insurer often will be able to provide the non-merger coverage requested.

Conclusion

The Sixth Circuit's ruling in *United States Leather, Inc. v. Mitchell Mfg. Group, Inc.*, *supra*, effectively employed the "balancing of the equities" doctrine to thwart what appeared to be an attempted preferential transfer or fraudulent conveyance of mortgaged property by a deed in lieu of foreclosure (although the court never decided this precise issue) to avoid an obligation to an innocent third-party judgment creditor. This case has complicated and unusual facts, and the Sixth Circuit was careful in its opinion to limit its holding to the facts presented. The court expressly acknowledged and confirmed that the generally permitted exception to the merger rule – i.e., that the mortgage would not be extinguished if the parties expressed their intention in the deed not to terminate the mortgage – would be valid and enforceable in those situations where the mortgagee's reason for keeping the mortgage alive was for the purpose of preserving its rights (including foreclosure) against subordinate lienholders of the mortgagor. As evidenced by the other cases and statutes discussed in this article, the unique facts of this case should not prevent the parties to a more conventional deed-in-lieu transaction from entering into a deed containing specific non-merger language, or prevent the owner-mortgagee from subsequently enforcing its rights under the preserved mortgage against subordinate lienholders.

EXHIBIT A

(Non-Merger Provisions)

1) Trust Deed:

Party of the first part and party of the second part acknowledge and agree, notwithstanding the transaction contemplated hereby, that (i) that certain First Mortgage and Security Agreement, dated _____, _____, from the party of the first part in favor of the party of the second part, and recorded on _____, _____ in the Recorder's Office of _____ County, Illinois, as Document No. _____ [and as modified and amended by that certain Amendment to First Mortgage and Security Agreement, dated as of _____, _____, by and among party of the first part and party of the second part, and recorded in the Recorder's Office of _____, County, Illinois, as Document No. _____] (the Mortgage), (ii) that certain Assignment of Leases and Rents, dated _____, _____, executed by party of the first part and party of the second part in favor of party of the second part and recorded on _____, _____ in the Office of the Recorder in _____ County, Illinois, as Document No. _____, and (v) all of the other documents executed in connection with such Mortgage or any amended, successor, or otherwise restated versions thereof, or of any of the foregoing (collectively, the Loan Documents) shall remain in full force and effect, now and hereafter, and the interest of the party of the first part in the within-described real estate by virtue of this deed shall not merge with the interests of party of the second part or its successors and assigns under the Loan Documents. The acceptance by party of the second part of this deed shall not prejudice, limit, restrict, or affect party of the second part's or its successors' and assigns' claim of priority under the Loan Documents over any other liens, claims, or encumbrances of any kind whatsoever. It is the express intention of party of the first part and party of the second part that party of the second part's interest in the within-described real estate shall not merge with the interest or rights of party of the second party's or its successors and assigns under the Loan Documents, but will be and remain at all times separate and distinct, and party of the second part may hereafter sell or otherwise transfer the within-described real estate.

2) Quit Claim Deed:

Grantor acknowledges that it expressly intended and agreed that the lien and security interest granted by Grantor to Grantee pursuant to that certain First Mortgage and Security Agreement dated _____ recorded on _____, _____ in the records of _____ County, Illinois as Document No. _____ shall remain in full force and effect and shall not merge with the interest acquired

hereunder, but shall remain a separate, distinct and continuing lien and security interest as therein provided.

Alternate (Quit Claim Deed):

SUBJECT to unpaid taxes, easements, zoning ordinances, and restrictions of record, the interests of tenants in possession, and that certain Mortgage (the Mortgage) dated _____, 20____, executed by Grantor in favor of Grantee, and recorded _____, 20____, in Book _____, Page _____, _____ County, _____ Records. Notwithstanding anything to the contrary herein, said Mortgage shall not be merged in the fee title hereby granted, but the premises herein described shall be and remain subject to said Mortgage until the same shall be sold at foreclosure sale or discharged by Grantee through a recorded written instrument.

3) Trustee's Deed (Bankruptcy Plan):

Party of the first part and party of the second part acknowledge and agree that notwithstanding the transaction contemplated hereby, (i) that certain First Mortgage and Security Agreement, dated _____, _____, from the party of the first part in favor of the party of the second part, and recorded on _____, _____ in the Office of the Recorder of Deeds of _____ County, Illinois as Document No. _____ and as modified and amended by that certain Amendment to First Mortgage and Security Agreement, dated as of _____, _____, by and among party of the first part, and party of the second part, and recorded in the Office of the Recorder of Deeds of _____ County, Illinois as Document No. _____ (the "Mortgage"), (ii) that certain Assignment of Rents, dated _____, _____, executed by party of the first part and the Partnership (defined below) in favor of party of the second part and recorded on _____, _____, in the Office of the Recorder of Deeds in _____ County, Illinois as Document No. _____, (iii) that certain Specific Assignment of Leases and Rents executed by party of the first part and the Partnership (defined below) in favor of party of the second part and recorded on _____, _____ in the Office of the Recorder of Deeds of _____ County, Illinois as Document No. _____, and (v) all of the other documents executed in connection with such Mortgage or any amended, successor, or otherwise restated versions thereof or of any of the foregoing, including, without limitation, the Restated Loan and Mortgage Documents (as defined in that certain Joint Plan of Reorganization, dated _____ (the "Plan"), proposed by _____, an Illinois limited partnership (the "Partnership"), and party of the second part in the Chapter 11 Case of the Partnership, Case No. _____, United States Bankruptcy Court for the _____ District of Illinois, _____ Division) (collectively, the "Loan Documents") shall remain in full force and effect, now and hereafter, and the interest of the party of the second part in the within-described real estate by virtue of this deed shall not merge with the interests of party of the

second part or its successors' and assigns' under the Loan Documents. The acceptance by party of the second part of this deed shall not prejudice, limit, restrict or effect party of the second part's or its successors' and assigns' claim of priority under the Loan Documents over any other liens, claims, or encumbrances of any kind whatsoever. It is the express intention of party of the first part and party of the second part that party of the second part's interest in the within described real estate shall not merge with the interest or rights of party of the second part's or its successors' and assigns' under the Loan Documents, but will be and remain at all times separate and distinct, and party of the second part may hereafter sell or otherwise transfer the within-described real estate.

3) Special Warranty Deed:

Nothing contained herein, or in any other document executed and delivered in relation hereto, shall be deemed to constitute any merger of title with respect to any assignment, assignment as security, deed of trust, mortgage or security interest held by GRANTEE, or its successors or assigns, with respect to such property, and GRANTEE expressly retains the right to proceed under foreclosure of its said assignments, assignments as security, deeds of trust, mortgages, and security interests so as to perfect title free and clear of any junior liens and encumbrances.

GRANTOR hereby waives any and all redemption rights to which it might otherwise be entitled.

Special Warranty Deed (Alternative):

Notwithstanding the fact that Grantor may be indebted to Grantee or an affiliate of Grantee, or that Grantee or an affiliate of Grantee may have or acquire, directly or indirectly, an interest in one or more liens or encumbrances affecting title to the property conveyed herein, (A) this deed is intended as an absolute conveyance rather than as security for any obligation, and Grantor expressly waives any statutory, equitable or other right to redeem any interest in the property conveyed herein, and (B) this deed shall not result in the merger of any such lien or encumbrance with the title conveyed hereby, or in the subordination or extinguishment of any such lien or encumbrance in favor of any other lien or encumbrance.

4) Special Deed:

This deed is an absolute conveyance of title in effect as well as form and is not intended as a mortgage, deed of trust, trust conveyance of title in effect as well as form and is not intended as a mortgage, deed of trust, trust conveyance or security of any kind. By acceptance of this deed, the party of the second part acknowledges that (i) this conveyance is made subject to that certain mortgage more particularly described on Exhibit ___ attached hereto (the "Existing Mortgage"), (ii) the Existing Mortgage continues to serve as security for a bona

vide debt and remains a subsisting lien on the premises hereby conveyed, and (iii) the Existing Mortgage (and lien created thereunder) shall not merge with the fee title of the premises hereby conveyed.

5) Warranty Deed:

This Warranty Deed is an absolute conveyance and grant of all of Grantor's right, title, and interest in the above-described real property and improvements thereon and easements and appurtenances thereto and is not intended as a mortgage, trust conveyance, or security of any kind, Grantor having sold, granted, and conveyed the above-described real property and all improvements thereon and easements and appurtenances thereto to Grantee for a fair and adequate consideration.

Grantor further declares that (a) this conveyance is freely and fairly made, executed, and delivered pursuant to the terms of the Settlement Agreement and with the advice, or opportunity for advice, of legal counsel of Grantor's selection; (b) that there are no agreements, oral or written, other than this Warranty Deed and the Settlement Agreement (and all documents referred to therein and executed in connection therewith) with respect to the above-described real property and all improvements thereon and easements and appurtenances thereto described above; and (c) that fair and adequate consideration has been given for Grantor's waiver of all redemption and cure rights permitted by law as more fully set forth in the Settlement Agreement.

Grantor and Grantee state that it is their express intention that the fee interest herein granted in the above-described real property and all improvements thereon and easements and appurtenances thereto conveyed pursuant to this Warranty Deed shall not merge with or extinguish the lien of Grantee's Loan Documents, or the interests of Grantee or its successors or assigns thereunder, but will be and remain at all times separate and distinct, and that the above-described real property conveyed and all improvements thereon and easements and appurtenances thereto conveyed pursuant hereto shall remain subject to Grantee's Loan Documents, and Grantee's Loan Documents shall remain in full force and effect now and hereafter until and unless the above-described real property and all improvements thereon and easements and appurtenances thereto shall be sold at a foreclosure sale or the lien of Grantee's Loan Documents shall be discharged by Grantee through a recorded written instrument.

6) Provision in Settlement Agreement:

ABSOLUTE CONVEYANCE

Owner and Beneficiary acknowledge and agree that the conveyance and transfer of the Property to Mortgagee in accordance with the terms of this Agreement is

an absolute conveyance and transfer of all of their right, title, and interest therein, in fact as well as form, and was not and is not now intended as a mortgage, trust conveyance, deed of trust, or security instrument of any kind; that the consideration for such conveyance and transfer is exactly as recited herein; and that Owner and Beneficiary have no further interest (including rights of possession, repurchase, cure or redemption) or claim in and to the Property or to the proceeds and profits, if any, which may be derived therefrom, during the period of ownership of or upon subsequent resale or conveyance by Mortgagee, of any kind whatsoever.

NO MERGER OF INTERESTS

Owner, Beneficiary, and Mortgagee acknowledge and agree that:

- A. the release of Owner and Beneficiary (but not Beneficiary [and Partners] pursuant to the Liability Agreement) from personal liability under or related to the Note and Security Documents shall not affect the status of the Note and Security Documents; and
- B. the interest of Mortgagee in the Property, as evidenced by the conveyance and transfer provided for herein, shall not merge with the interest of Mortgagee in the Property pursuant to Note and Security Documents.

It is the express intention of Owner, Beneficiary, and Mortgagee (and the Transfer Documents shall so recite) that such interest of Mortgagee in Property shall not merge, but shall be and remain at all times separate and distinct, notwithstanding any union of said interest in Mortgagee now or at any time subsequent by purchase, termination, or otherwise, and that the lien of Mortgagee on the Property established by the Note and Security Documents shall be and shall remain at all times a valid and continuous lien upon the Property until and unless such lien is released of record by Mortgagee.

Provision in Settlement Agreement (Alternative):

Debt and Mortgage Not Extinguished. Borrower's indebtedness under the Note, and the lien of the Mortgage shall not be extinguished as a result of the Closing on the transactions contemplated by this Agreement. The lien of the Mortgage is not intended to be, and shall not be, released or relinquished in any manner or respect whatsoever on account of this Agreement, the transaction contemplated hereby, or delivery of the Transfer Documents to Lender, which Mortgage shall remain valid and continuous and in full force and effect for the benefit of Lender, and its successors and assigns, and the priority of such Mortgage shall be maintained, until the Mortgage is expressly released by written instrument (a "Release Instrument") executed by Lender, or its successors and assigns, and clearly expressing (and not merely implying) an intent to release and relinquish

the Mortgage, which Release Instrument shall be recorded in the Office of the Recorder of Deeds of _____ County, _____. Lender, or its successors and assigns, shall have the right and option, but not the obligation, to execute a Release Instrument as, if and when Lender, or its successors and assigns, shall determine to do so in the exercise of its or their sole discretion.

7) Covenant Deed:

It is expressly understood and agreed that the execution and delivery of this instrument and conveyance shall not in any manner be deemed to be a merger with or the extinguishment of the Mortgage hereinbefore described, wherein Grantor is the Mortgagor and Grantee is the Mortgagee, which said Mortgage and the underlying indebtedness shall be and remain in full force and effect according to the respective tenors of said instruments; provided, however, it is expressly understood and agreed that the execution and delivery of this instrument and conveyance is a release of Grantor from enforcement of personal liability to Grantee under the said instruments.

Covenant Deed (Alternative):

It is expressly understood and agreed that the interests of the Grantee as mortgagee under the mortgage described below (the "Mortgage"), shall not be deemed to be merged into the fee acquired by Grantee under this Deed, nor shall the lien of the Mortgage be extinguished:

Mortgage dated _____, 20__ and recorded _____, 20__ in Book _____, Page _____, _____ County Records, which Mortgage was assigned to _____, as trustee for the registered holders of _____, Mortgage Pass-Through Certificates, Series _____, by virtue of a certain Assignment of Mortgage and Security Agreement and Assignment of Assignment of Leases and Rents and other collateral documents dated _____, 20__ and recorded _____, 20__ in Book _____, Page _____, _____ County Records, _____.

It is further expressly understood and agreed that the Mortgage constitutes a first lien on the Property, and that the indebtedness and obligations secured by the Mortgage shall be and remain in full force and effect.

8) Trustee's Deed – Foreclosure:

Grantor and Grantee declare that it is their intention that the interest of Grantee in the above described real estate as Grantee under this deed and as mortgagee under the following described mortgage:

which mortgage was merged into decree of foreclosure entered _____, 20____, shall not merge and that the lien of said mortgage and decree of foreclosure shall remain in full force and effect until specifically released.

EXHIBIT B

ENDORSEMENT

ATTACHED TO AND FORMING A PART OF
POLICY NO. NCS

ISSUED BY

FIRST AMERICAN TITLE INSURANCE COMPANY

NON-MERGER ENDORSEMENT

The company hereby insures the owner of the indebtedness secured by the mortgage referred to in Schedule A against loss sustained by reason of the invalidity or unenforceability of the lien of the Insured mortgage upon said estate occasioned by the title to said estate being vested as shown in Schedule A.

This endorsement is made a part of the Policy. It is subject to all the terms of the Policy and prior endorsements. Except as expressly stated on this endorsement, the terms, dates and amount of the Policy and prior endorsements are not changed.

First American Title Insurance Company

Dated: _____

By: _____

Its: _____