

## Mortgages and Real Estate Security Agreements

Q What is a real estate security agreement?

A A real estate security agreement ("RESA") is for all practical purposes a mortgage. It is recorded in the real estate records like a mortgage, it has the priority of a mortgage, it has been treated as a mortgage in foreclosure actions, it must be disclosed like a mortgage under Truth-in-Lending, it is rescindable under Truth-in-Lending like a mortgage, and it may trigger the applicability of various Wisconsin laws governing mortgages. Like a mortgage, it states that it grants the lender a lien on the property to secure the obligations described in the RESA.

Q What purpose does a RESA serve?

A Although a RESA is for all practical purposes a mortgage, it was not originally intended by the WBA to take the place of a mortgage in transactions where a mortgage is preferred by the bank. The original intent was that banks be able to avoid some of the state regulatory requirements applicable to normal real estate mortgages by using the RESA so as to offer customers greater convenience, faster service and lower costs. Examiners generally did not require all of the supporting documentation necessary under state law for mortgages. The RESA may have a certain appeal to banks because unlike the mortgage it does not identify a specific amount secured by the RESA. Banks using mortgages usually make certain that the outstanding balance plus future advances do not exceed the amount of the note described on the face of the mortgage. This same concern does not exist with respect to the RESA because it does not identify an amount. RESAs may also be used today to accommodate a customer request that a loan be secured by the home for tax purposes. However, the RESA was intended to be used in very limited situations where the bank was essentially willing to lend on an unsecured basis but wanted a little additional comfort.

Q Which is preferred, the RESA or a mortgage?

A The RESA was intended to be used by banks in transactions in which there were essentially willing to lend unsecured, but wanted a little more comfort in the transaction. The WBA continues to advise banks that the RESA is not intended to take the place of a mortgage. If the bank wants a mortgage on real estate to secure a loan, the WBA suggests that the bank use a mortgage to secure the loan. One important distinction between a mortgage and a RESA is that the RESA does not contain many of the covenants and warranties that are contained in the

mortgage. For example, the RESA does not contain a covenant regarding compliance with environmental laws and indemnification of the lender. Another problem with using the RESA where a mortgage is intended is that a few banks have had to persuade the courts in foreclosure actions on RESA that the RESA is the equivalent of a mortgage and therefore may be foreclosed by the bank. As far as the WBA is aware, banks using the RESAs have prevailed in the courts on this issue. However, it is expensive to litigate and it is always possible that a different trial court or an appellate court may one day conclude that a RESA is not the equivalent of a mortgage. The WBA continues to suggest that the use of RESAs be limited to their original intent, and that banks should use mortgages for those loans which they intend to be secured by mortgages.

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