

2 Rights in Real Estate

Real Estate as Property
Real Versus Personal Property
Regulation of Real Property Interests

REAL ESTATE AS PROPERTY

Land
Real estate
Property
Real property rights
Water rights

A simple definition of real estate is that it is air, water, land, and everything affixed to the land. Real estate in the United States may be owned privately by individuals and private entities or publicly by government entities. Private ownership rights in this country are not absolute. The government can impose taxes and restrictions on private ownership rights, and it can take private property away altogether. In addition, other private parties can exert their rights and interests on one's real property. A bank, for example, can take a property if the owner fails to pay a mortgage. A neighbor can claim the right to walk across one's property whether the owner likes it or not, provided he or she has done so for a certain number of years.

In attempting to define real estate, it is essential to understand *what rights and interests parties have in a parcel of real estate*. And to understand real estate rights and interests, one must first recognize the distinctions between:

- ▶ land and real estate
- ▶ real estate and property
- ▶ real property and personal property

Land

The legal concept of land encompasses

- ▶ the surface area of the earth
- ▶ everything beneath the surface of the earth extending downward to its center
- ▶ all *natural* things permanently attached to the earth
- ▶ the air above the surface of the earth extending outward to infinity.

Land, therefore, includes minerals beneath the earth's surface, water on or below the earth's surface, and the air above the surface. In addition, land includes all

plants attached to the ground or in the ground, such as trees and grass. A **parcel**, or **tract**, of land is a portion of land delineated by boundaries.

Physical characteristics. Land has three unique physical characteristics: *immobility, indestructibility, and heterogeneity*.

Land is immobile, since a parcel of land cannot be moved from one site to another. In other words, the geographical location of a tract of land is fixed and cannot be changed. One can transport portions of the land such as mined coal, dirt, or cut plants. However, as soon as such elements are detached from the land, they are no longer considered land.

Land is indestructible in the sense that one would have to remove a segment of the planet all the way to the core in order to destroy it. Even then, the portion extending upward to infinity would remain. For the same reason, land is considered to be permanent.

Land is non-homogeneous, since no two parcels of land are exactly the same. Admittedly, two adjacent parcels may be very similar and have the same economic value. However, they are inherently different because each parcel has a unique location.

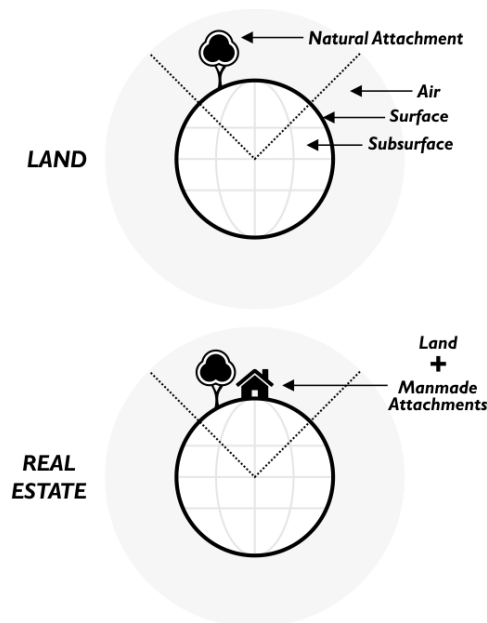
Real estate

The legal concept of real estate encompasses:

- ▶ land
- ▶ all *man-made structures* that are "permanently" attached to the land

Real estate therefore includes, in addition to land, such things as fences, streets, buildings, wells, sewers, sidewalks and piers. Such man-made structures attached to the land are called **improvements**. The phrase "permanently attached" refers primarily to one's intention in attaching the item. Obviously, very few if any manmade structures can be permanently attached to the land in the literal sense. But if a person constructs a house with the intention of creating a permanent dwelling, the house is considered real estate. By contrast, if a camper affixes a tent to the land with the intention of moving it to another camp in a week, the tent would not be considered real estate.

Exhibit 2.1 The Legal Concept of Land and Real Estate



Property

In common understanding, property is something that is owned by someone. A car is the property of Bill Brown if Bill Brown owns the car. If the item is not owned, it is not property. For example, if a car is abandoned and left to rust in the desert, the car is no longer property, since no one claims ownership. Similarly, the planet Jupiter is not property, since no one owns it.

From a more technical standpoint, property is not only the item that is owned but also a *set of rights to the item enjoyed by the owner*. These rights are commonly known as the "bundle of rights."

Exhibit 2.2 The Bundle of Rights



In owning property, one has the right to possess and use it as the law allows. The owner has the right to transfer ownership of the item (sell, rent, donate, assign, or bequeath). The owner may also encumber the item by mortgaging it as collateral for debt. Finally, the owner has the right to exclude others from use of the item. In the example of the car, when Bill Brown bought the car, the car became his

property: he owned the car itself. At the same time, he also acquired the legal rights to transfer, use, encumber, exclude, and possess the car.

Classifications of property. Our legal system recognizes two classifications of property: *real property* and *personal property*. **Real property** is ownership of real estate and the bundle of rights associated with owning the real estate. **Personal property** is ownership of anything which is not real estate, and the rights associated with owning the personal property item. Items of personal property are also called **chattels** or **personalty**.

Note: since all real estate in the United States is owned by some person, private organization, or government entity, all real estate in the country *is* real property. Given that fact, this text will follow the customary practice of using the two terms interchangeably and synonymously.

Tangible versus intangible property. Real and personal property may be further categorized as **tangible** or **intangible** property. Tangible property is physical, visible, and material. Intangible property is abstract, having no physical existence in itself, other than as evidence of one's ownership interest.

Exhibit 2.3 Tangible vs. Intangible Property

	Tangible	Intangible
Real Property	all types	
Personal Property	boat, car, jewelry	stock certificate, contract, patent

All real estate, by its physical nature, is tangible property. Personal property may be tangible or intangible. Boats, jewelry, coins, appliances, computers, and art work are examples of tangible personal property. Stocks, copyrights, bonds, trademarks, patents, franchises, and listing agreements are examples of intangible personal property.

Real property rights Real property rights consist of the bundle of rights associated with owning a parcel of real estate. Foremost of these rights is the right of possession.

The *right to use* a property refers to the right to use it in certain ways, such as mining, cultivating, landscaping, razing, and building on the property. The right is subject to the limitations of local zoning and the legality of the use. One's right to use may not infringe on the rights of others to use and enjoy their property. For example, an owner may be restricted from constructing a large pond on her property if in fact the pond would pose flooding and drainage hazards to the next door neighbor.

The *right to transfer* interests in the property includes the right to sell, bequeath, lease, donate, or assign ownership interests. An owner may transfer certain individual rights to the property without transferring total ownership. Also, one may transfer ownership while retaining individual interests. For example, a

person may sell mineral rights without selling the right of possession. On the other hand, the owner may convey all rights to the property except the mineral rights.

While all rights are transferrable, the owner can only transfer what the owner in fact possesses. A property seller, for example, cannot sell water rights if there are no water rights attached to the property.

The *right to encumber* the property essentially means the right to mortgage the property as collateral for debt. There may be restrictions to this right, such as a spouse's right to limit the degree to which a homestead may be mortgaged.

The *right to exclude* gives the property owner the legal right to keep others off the property and to prosecute trespassers.

The bundle of real property rights also applies separately to the individual components of real estate: the air, the surface, and the subsurface. An owner can, for example, transfer subsurface rights without transferring air rights. Similarly, an owner can rent air space without encumbering surface or subsurface rights. This might occur in a city where adjoining building owners want to construct a walkway over a third owner's lot. Such owners would have to acquire the air rights for the walkway. If the city wants to construct a subway through the owner's subsurface, the city has to obtain the subsurface rights to do so.

An ordinary lease is a common example of the transfer of a portion of one's bundle of rights. The owner relinquishes the right to possess portions of the surface, perhaps a building, in return for rent. The tenant enjoys the rights to possess and use the building over the term of the lease, after which these rights revert to the landlord. During the lease term, the tenant has no rights to the property's subsurface or airspace other than what the building occupies. Further, the tenant does not enjoy any of the other rights in the bundle of rights: he cannot encumber the property or transfer it. To a limited degree, the tenant may exclude persons from the property, but he may not exclude the legal owner.

Surface rights. Surface rights apply to the real estate contained within the surface boundaries of the parcel. This includes the ground, all natural things affixed to the ground, and all improvements. Surface rights also include water rights.

Air rights. Air rights apply to the space above the surface boundaries of the parcel, as delineated by imaginary vertical lines extended to infinity. Since the advent of aviation, air rights have been curtailed to allow aircraft to fly over one's property, provided the overflights do not interfere with the owner's use and enjoyment of the property. The issue of violation of air rights for the benefit of air transportation is an ongoing battle between airlines, airports, and nearby property owners.

Subsurface rights. Subsurface rights apply to land beneath the surface of the real estate parcel extending from its surface boundaries downward to the center

of the earth. Notable subsurface rights are the rights to extract mineral and gas deposits and subsurface water from the water table.

Water rights

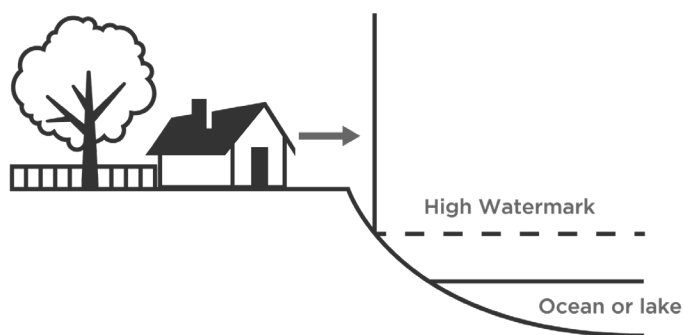
Water rights basically concern the rights to own and use water found in lakes, streams, rivers, and the ocean. In addition, they determine where parcel boundaries can be fixed with respect to adjoining bodies of water. What water rights does an owner of a property that contains or adjoins a body of water enjoy? The answer depends on three variables:

- ▶ whether the state controls the water
- ▶ whether the water is moving
- ▶ whether the water is navigable

Doctrine of Prior Appropriation. Since water is a resource necessary for survival, some states -- particularly those where water is scarce -- have taken the legal position that the state owns and controls all bodies of water. Called the Doctrine of Prior Appropriation, this position requires that property owners obtain permits for use of water. If a proposed usage is reasonable and beneficial, the state will grant a permit which, over time, can attach to the property of the permit holder. If a state does not operate under prior appropriation, it operates under the common law doctrines of *littoral rights* and *riparian rights*.

Littoral rights. Littoral rights concern properties abutting bodies of water that are not moving, such as lakes and seas. Owners of properties abutting a navigable, non-moving body of water enjoy the littoral right of use, but do not own the water nor the land beneath the water. Ownership extends to the high-water mark of the body of water.

Exhibit 2.4 Littoral Rights



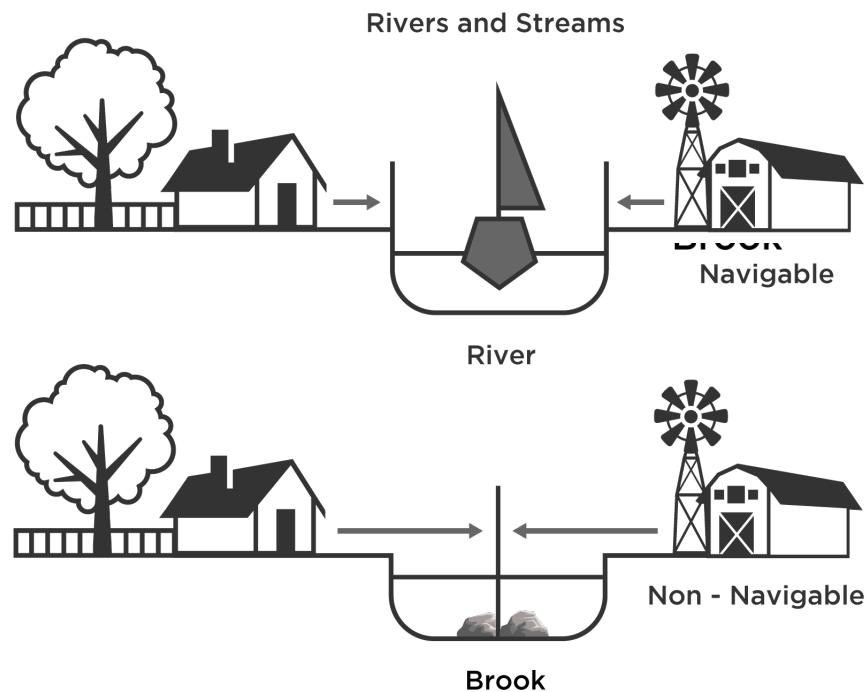
Oceans, Seas and Lakes

The legal premise underlying the definition of littoral rights is that a lake or sea is a *navigable body of water, therefore, public property* owned by the state. By contrast, a body of water entirely contained within the boundaries of an owner's property is not navigable. In such a case, the owner would own the water as well as unrestricted rights of usage.

Littoral rights attach to the property. When the property is sold, the littoral rights transfer with the property to the new owner.

Riparian rights. Riparian rights concern properties abutting moving water such as streams and rivers. If a property abuts a stream or river, the owner's riparian rights are determined by whether the water is *navigable or not navigable*. If the property abuts a non-navigable stream, the owner enjoys unrestricted use of the water and *owns the land beneath the stream to the stream's midpoint*. If the waterway in question is navigable, the waterway is considered to be a public easement. In such a case, the owner's property extends *to the water's edge* as opposed to the midpoint of the waterway. The state owns the land beneath the water.

Exhibit 2.5 Riparian Rights



One's riparian rights to use flowing water are subject to the conditions that:

- ▶ the usage is reasonable and does not infringe on the riparian rights of other owners downstream
- ▶ the usage does not pollute the water
- ▶ the usage does not impede or alter the course of the water flow.

Like littoral rights, riparian rights attach to the property.

REAL VERSUS PERSONAL PROPERTY

Fixtures

Differentiation criteria

Trade fixtures

Emblements

Factory-built housing

Conversion

In conveying real property, it is vitally important to recognize the distinctions between personal property and the real property that is to be conveyed. Confusion can arise because items of property *may be either personal property or real property, depending on circumstances.*

The primary criterion for distinguishing real from personal property is whether the item is permanently attached to the land or to structures attached to the land. For example, a tree growing in one's yard is an item of real property. However, when the owner cuts the tree down, it becomes personal property. Similarly, a swimming pool pump on a shelf in the owner's garage is personal property. When it is installed with the rest of the pool, it becomes real property.

While the "attachment" criterion is pivotal in distinguishing between real and personal property, there are other tests to be applied. In addition, the attachment rule is subject to exceptions.

Fixtures

A personal property item that has been converted to real property by attachment to real estate is called a fixture. Typical examples are chandeliers, toilets, water pumps, septic tanks, and window shutters.

The owner of real property inherently owns all fixtures belonging to the real property. When the owner sells the real property, the buyer acquires rights to all fixtures. Fixtures not included in the sale must be itemized and excluded in the sale contract.

Differentiation criteria

In the event that the attachment criterion is insufficient to determine whether an article of property is real or personal, a court may apply one or more of the following additional criteria.

Intention. One's original intention can override the test of movability in determining whether an item is a fixture or not. If someone attached an item to real property, yet intended to remove it after a period of time, the article may be deemed personal property. If a person intended an article to be a fixture, even though the item is easily removable, the article may be deemed a fixture.

For example, an apartment renter installs an alarm system, fully intending to remove the system upon lease expiration. Here, the alarm system would be considered personal property.

Adaptation. If an item is uniquely adapted to the property, or the property is custom-designed to accommodate the item, it may be deemed real property

whether the item is easily removable or not. House keys, a garbage compactor, and a removable door screen are examples.

Functionality. If an item is vital to the operation of the building, it may be deemed a fixture, even though perhaps easily removable. Window-unit air conditioners and detachable solar panels are possible examples.

Relationship of parties. If a tenant installs a fixture in order to conduct business, the fixture may be considered a trade fixture, which is the tenant's personal property.

Sale or lease contract provisions. In a sale or lease transaction, the listing of an item in the contract as a personal property item or a fixture overrides all other considerations. Unless otherwise stated as exceptions, all fixtures are included in the sale. For example, if a sale contract stipulates that the carpeting is not included in the sale, it becomes a personal property item. If the carpeting is not mentioned, it goes with the property, since it is attached to the floor of the building.

Trade fixtures

Trade fixtures, or **chattel fixtures**, are items of a tenant's *personal property* that the tenant has temporarily affixed to a landlord's real property in order to conduct business. Trade fixtures may be detached and removed before or upon surrender of the leased premises. Should the tenant fail to remove a trade fixture, it may become the property of the landlord through *accession*. Thereafter, the fixture is considered real property.

Examples of trade fixtures include a grocer's food freezers, a merchant's clothes racks, a tavern owner's bar, a dairy's milking machines, and a printer's printing press.

Emblements

Growing plants, including agricultural crops, may be either real property or personal property. Plants and crops that grow naturally without requiring anyone's labor or machinery are considered real property.

Plants and crops requiring human intervention and labor are called **emblements**. Emblements, despite their attachment to land, are considered personal property. If an emblemment is owned by a tenant farmer, the tenant has the right to the harvested crop whether the tenant's lease is active or expired. If the tenant grew the crop, it is his or her personal property, and the landlord cannot take it.

Factory-built housing

Factory-built housing consists of dwelling units constructed off-site and transported to and assembled on a building site. The category also includes readily moveable housing of the type that can be relocated from place to place, once known by the term **mobile home**. The National Manufactured Housing Construction and Safety Standards Act of 1976 defined the types of factory-built housing and retired the mobile home designation. **Manufactured housing** is factory-built housing that conforms to HUD standards. Factory-built housing may be considered real property or personal property, depending on whether it is permanently affixed to the ground, and according to state law. Real estate practitioners should understand the local laws before selling any kind of factory-built housing.

Conversion

The classification of an item of property as real or personal is not necessarily fixed. The classification may be changed by the process of conversion.

Severance is the conversion of real property to personal property by detaching it from the real estate, such as by cutting down a tree, detaching a door from a shed, or removing an antenna from a roof. **Affixing**, or attachment, is the act of converting personal property to real property by attaching it to the real estate, such as by assembling a pile of bricks into a barbecue pit, or constructing a boat dock from wood planks.

Exhibit 2.6 Real Property vs. Personal Property

Real Property	Personal Property
land fixtures attachments conversions by affixing	trade fixtures emblems conversions by severance

REGULATION OF REAL PROPERTY INTERESTS

Areas of regulation

Federal regulation

State regulation

Local regulation

Judicial regulation

Although the Constitution guarantees private ownership of real estate, laws and regulations at every level of government qualify and limit individual real property ownership and the bundle of rights associated with it.

Areas of regulation

Government entities regulate the following aspects of real property interests:

- ▶ the bundle of rights: possession, usage, transfer, encumbering and exclusion
- ▶ legal descriptions
- ▶ financing
- ▶ insurance
- ▶ inheritance
- ▶ taxation

Regulation takes the form of federal and state laws and regulations; county and local ordinances and codes; and court decisions in the judicial system.

Federal regulation

In regulating real property rights, the federal government is primarily concerned with broad standards of real property usage, natural disaster, land description, and discrimination.

Federal agencies such as the Federal Housing Administration promote and regulate home ownership. The Environmental Protection Agency establishes protective usage restrictions and guidelines for dealing with hazardous materials and other environmental concerns. Federal flood insurance legislation requires certain homeowners to obtain flood insurance policies. Federal laws such as the Federal Fair Housing Act of 1968 prohibit discrimination in housing based on race, religion, color, or national origin. Such laws as the Americans with Disabilities Act prescribe design and accessibility standards.

The federal government does not levy real estate taxes.

State regulation

State governments are the primary regulatory entities of the real estate business. State governments establish real estate license laws and qualifications. In addition, state governments have established real estate commissions to administer license laws and oversee activities of licensees.

State governments also exert regional influence in the usage and environmental control of real estate within the state. Relevant state laws might include laws relating to flood zones, waste disposal, drainage control, shore preservation, and pollution standards.

States also play a role in defining how real property may be owned, transferred, encumbered, and inherited. For example, in some states a mortgaged property becomes the legal property of the lender until the mortgage loan is paid.

States have the power to levy real estate taxes but generally pass this power to local government.

Local regulation

County and local government regulation focuses on land use control, control of improvements, and taxation. Land use regulations and ordinances control how all property within the jurisdiction may be developed, improved, demolished, and managed. County and local governments have the power to zone land, take over land for the public good, issue building permits, and establish the rules for all development projects.

County and local governments, along with school districts and other local jurisdictions, have the power to levy real estate taxes.

Judicial regulation

The judicial system exerts an influence on real estate ownership and use through decisions based on case law and common law, as distinguished from statutory law. Case law consists of decisions based on judicial precedent. Common law is the collective body of law deriving from custom and generally accepted practice in society.

Exhibit 2.7 Regulation of Real Property Interests

Federal	Constitution	Establishes absolute right of private ownership of real estate Prohibits federal government from levying real property taxes
	Laws	Create, regulate real estate-related agencies Prohibit discrimination Create standards for legal descriptions of real estate Establish environmental standards for all property Establish standards for protecting interests of handicapped people
	Agencies	Establish mortgage lending standards Establish housing construction standards Establish environmental standards
State	Constitution	May establish right to levy tax; or may delegate right to counties and municipalities
	Laws	Regulate real estate licensing Establish broad usage standards Define, qualify ownership rights
	Agencies	Regulate practitioners, administer real estate license laws
Local	Laws	Create and enforce real estate taxation Control land usage over specific parcels of land
Courts	Common law	Regulates real estate ownership and usage according to customary and accepted practices
	Case law	Regulates real estate ownership and usage according to prior court decisions

2 Rights and Interests in Real Estate Snapshot Review

REAL ESTATE AS PROPERTY

- Constitution guarantees private ownership of real estate; ownership rights not absolute; others may exert claims against one's property

Land

- surface, all natural things attached to it, subsurface, and air above the surface; unique aspects: immobile, indestructible, heterogeneous

Real estate

- land plus all permanently attached man-made structures, called improvements

Property

- something that is owned by someone and the associated rights of ownership
- the bundle of rights: possession, use, transfer, exclusion, and encumbrance
- property is real or personal, tangible or intangible

Real property rights

- any of the bundle of rights, applied to airspace (air rights), surface (surface rights), and subsurface (subsurface rights)

Water rights

- Doctrine of Prior Appropriation: state controls water usage; grants usage permits
- littoral rights: abutting property owners own land to high water mark; may use, but state owns underlying land
- riparian rights: if navigable, abutting property owners own land to water's edge; may use, but state owns underlying land; if not navigable, owner owns land to midpoint of waterway

REAL VS PERSONAL PROPERTY

- an item may be real or personal property depending on the "attachment" criterion and other circumstances

Fixtures

- real property converted from personal property by attachment to real estate

Differentiation criteria

- intention; adaptation; functionality; relationship of parties; contract provisions

Trade fixtures

- personal property items temporarily attached to real estate in order to conduct business; to be removed at some point

Emblements

- plants or crops considered personal property since human intervention is necessary for planting, harvesting

Factory-built housing

- housing pre-built off-site; includes mobile homes; real or personal depending on attachment to land

Conversion

- transforming real to personal property through severance, or personal to real property through affixing

REGULATION OF REAL PROPERTY INTERESTS

Federal regulation

- grants overall rights of ownership; controls broad usage standards, discrimination

State regulation

- governs the real estate business; sets regional usage standards

Local regulation

- levies real estate taxes; controls specific usage

Judicial regulation

- applies case law and common law to disputes