Title 101

(Revision 3)

An Updated Primer for Attorneys and Paralegals
in Real Estate Practice

Chicago Title Insurance Company

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About Title Insurance

A title insurance policy provides coverage to an insured owner for unknown or undisclosed title matters that occurred prior to the effective date of the policy. The owner's coverage under the policy lasts for as long as he or she owns the property or has liability under warranties given in a later deed.

A title insurance policy is not a sufficient substitute for "good" title, especially in circumstances where the title problem is caused by failing to make sure that all important matters are taken care of at or before closing. Title insurance is not a guarantee that the title is good. Its coverages are in the nature of an indemnity (and potential defense costs) if the insured lien or title is defective. Many purchases, refinances and foreclosures are delayed because of title matters, even though covered by the policy.

The Nature of Title Insurance

A title insurance policy provides an owner of an interest in real property or a lender with a security interest (lien) in real property with protection against loss resulting from a defect in title to the real property. The protection is provided by affirmative assurances regarding the following items:

- Vested ownership
- Access to the land
- No pre-existing undisclosed liens or encumbrances
- Unmarketable title

- For a loan policy: Insured lender's deed of trust is valid, enforceable, recorded in the public records and, therefore, has priority over any other deeds of trust, judgments, claims of ownership or other matters except as shown on the policy.

Title insurance, by its nature, is a "risk elimination" form of insurance in contrast to the "assumption of risk" involved in virtually all other lines of insurance. A policy of title insurance looks backwards from a specific moment in time. It insures an owner or lender against loss or damages arising out of defects to or liens on title which are not excepted or excluded in the title policy and that occurred prior to the issuance of the policy. At or before the closing, the attorney will perform a search of the public records and either handle issues at closing or discuss coverage options with the title insurance company for any known risks found by the search (such as outstanding deeds of trust or judgments), -- thus the term "risk elimination."

By way of contrast, casualty insurance (i.e., car, homeowner, life) covers matters which occur after the policy is issued and during a more limited coverage period (typically, one year). Casualty insurers assess the potential risks an insured presents based on their past history and statistics on the type of losses, so they can calculate the probability of future occurrences for the current insured's policy. Casualty insurance also typically requires payments made on a routine basis while there is only a one-time premium for title insurance.

The Approved Attorney System

In North Carolina, the "approved attorney" and the title company work together for the purpose of furnishing the purchaser or lender the protection of title insurance. The North Carolina legislature sanctioned the existence of title insurance companies "for the purpose of furnishing information in relation to titles to real estate and insuring owners and others interested therein against loss by reason of encumbrances and defective title." NCGS §58-26-1(a). However, a title company cannot issue a title insurance policy "unless and until the title insurance company has obtained the opinion of an attorney, licensed to practice law in North Carolina and not an employee or agent of the company who has conducted or caused to be conducted under the attorney's direct supervision a reasonable examination of the title." NCGS §58-26-1(a). In some states, the title insurance companies perform the title work and close the transaction or the attorneys act as agents for the title companies and issue title policies themselves. In North Carolina, however, since the approved attorney

cannot be an agent of the title insurer, title work must be conducted by an independent attorney.

In order to become an approved attorney for a title insurance company, the new attorney needs to contact the title insurer and request an approved attorney application. The application is usually a 4-5 page document which asks, among other things, for references, real estate experience and the evidence of malpractice insurance. The addition of an attorney to the list of approved attorneys is based upon the recommendations of the local bar and fellow citizens as to the attorney's moral integrity, legal ability and experience. Attorneys who fail to make efforts to provide quality legal representation to their clients and to the title insurer may be removed from the company's list of approved attorneys. Removal of the attorney may impair the ability of the attorney to practice real estate law due to the typical lender requirement of insured closing protection (below).

Closing Protection Letter (sometimes called "insured closing letter")

Once the attorney is approved, the title insurance company can issue a closing protection letter (a "CPL"). Closing Protection is an additional assurance to the lender and the owner that the named licensed North Carolina attorney is approved by the title insurer as of the date of the letter, and that the title insurance company stands behind the attorney's promise to comply with written closing instructions regarding title, gathering of required documents and collection and disbursement of lender funds.

However, the lender may not be protected against actions taken by or at the request of the lender contrary to official closing instructions. Lenders and attorneys should be very careful about documenting authorizations given to attorneys, assuring that attorneys agree to comply with both written closing instructions and the requirements of the commitment and that funds to be collected and disbursed are adequately itemized in written closing instructions or memoranda signed by all parties.

Helpful Hints:

1. Take all requests from lenders seriously.
2. Read and carefully follow the closing instructions.
3. Do not make changes to the closing instructions without WRITTEN authorization from the lender.

Many closing protection claims are denied because of failure of the lender to follow its own instructions or because the closing attorney received permission

to do less than a fully responsible job "as long as the title company will cover it" – when the title company is never advised of the deviation!! In addition, many claims occur simply because the closing attorney failed to obtain written confirmation of a change by the lender in the closing instructions.

Many closing protection claims result from failure of the attorney to respond to document requests *after* closing. The most common of these claims are for: 1) failure to obtain the final title policy in a timely fashion; or 2) failure to perform post-closing follow-up such as submitting complete closing packages in a timely fashion or failure to assure paid deeds of trust are canceled of record. The attorney must be certain to comply with requests for documentation from the lender after the closing to prevent claims from arising.

Title Search Basics

Before We Begin…
We offer this guide as an introduction to the process of searching title and that anyone desiring to become an effective title searcher do so under the direct supervision of a licensed North Carolina attorney.

The Purpose of a Title Search

When discussing why we conduct a title search, there really are two answers that should be considered. The first answer is that a client, whether an individual, a lender or possibly both, has asked the attorney for information on the title to a piece of real property. The client has the reasonable expectation that the search performed by her attorney will provide that accurate information the client needs to make reasoned decisions to buy, to convey, or to accept real property as collateral. An attorney, who has been retained to conduct a title search must, in fact, conduct a title search and must inform the client of any limitations on the search performed by the attorney (*See* Rules of Professional Conduct "RPC" 99). The searching attorney is the one with ultimate responsibility for the quality of the title search. Accordingly, attorneys and their paralegal staffs must understand the difference between a full search and a limited search and always make certain that the search conducted meets the client's expectations.

More pragmatically, we conduct a title search to determine the owner of the property and what impediments there may be on the title to the property. In this manuscript, we will try to describe many of the steps necessary to conduct a proper search.

Preliminary Information

Before beginning a title search, it is important to verify that you have the correct legal description or property address and current owner's name. Whenever possible, try to gather the following information and verify it with the buyer/borrower, seller, and/or the lender:

1. The full name(s) of the owner(s).
2. The property address.
3. County
4. Copies of unrecorded maps or surveys
5. Legal description
6. Deed Book reference to deed into current owner
7. Map/Plat book references

Before heading off to the Registry to do the search, also check within your office to see if the office has previously searched the tract. This can save you a great deal of time at the deed vault if you only need to update from a prior search. You are encouraged to begin a system of "master files" if you are on your own or to learn the system already in place at your firm.

If the transaction for which the search is to be conducted is a purchase, the lawyer should also be certain to collect an executed copy of the purchase contract. It is important that the closing attorney examine the contract in its entirety not only for matters pertaining to ownership (and therefore the beginning point for establishing a chain of title), but also to determine any other conditions there may be to closing.

If the transaction for which you have been retained is a refinance, be certain to obtain documented evidence from your client and his or her lender regarding the property they intend to use as security for the loan so that you are clearly searching the correct property and encumbering the correct property which all parties intend to secure the lender's loan.

The Search Period

While the State Bar ethics rules permit tacking to prior title policies in the context of real estate conveyances and refinance closings and the practice of tacking is presumably within the standard of care required of closing attorneys, it should not be confused with searching a title. Obviously, much of the process otherwise required is eliminated if you tack onto an existing policy. As the closing attorney, you are charged with the responsibility for the quality of the search that is committed. Accordingly, you should not only make certain that you understand the difference between a full title search and a limited title search, but that you also make your staff and clients aware of the differences.

Title searches can be broadly categorized into four groups. A discussion of each follows.

Full Search

Generally, a "full" search is considered to be for a period of 40-60 years. By conducting a full search, the attorney is most likely to discover matters that may affect title. Absent disclosure to the client of a lesser search, a full search is probably the standard. A full search seeks to cover the 30 year period under the Marketable Title Act (NCGS Chapter 47B) as discussed below and also to locate record matters that may affect title under the numerous exceptions to the act.

Marketable Title Act Search

A search of at least the period of the Marketable Title Act, NCGS Chapter 47B (i.e., back to a deed recorded at least 30 years prior and any instrument referenced in that deed) is the second category. An effective real property practitioner must be aware of the Marketable Title Act, its exceptions, and its implications in order to complete an effective title search. That act and its exceptions are beyond the scope of this manuscript, as a proper discussion would be lengthy.

It is noteworthy that most title insurers will consider a 30+ year search to be a full search. The Marketable Title Act reduces the risk of certain claims but does not eliminate all risks. **The decision of a title insurer to insure is**

frequently based on risk and market advantage and should not be confused with a full search or with the lawyer's obligation to the client.

Tacking

Tacking was not generally accepted as a valid practice until very recently and within the last fifteen or twenty years following the widespread use of title insurance to protect against risk. The practice of tacking to a prior policy has been sanctioned by the North Carolina State Bar (RPC 99) so long as the lawyer discloses the limited search to the client. The disclosure is not required to be in writing but you are encouraged to give the disclosure in writing and in adequate time prior to closing to perform a full search if requested by the client.

When tacking to a prior policy, one should always review the prior title policy carefully. The prior policy should be an owner's policy, not a loan policy. RPC 99 notes that "since title insurers frequently omit exceptions in mortgagees' policies that would [otherwise] appear in owners' policies, tacking should be limited to owners' policies." Furthermore, the prior policy should be reviewed carefully to ascertain that the exceptions contained in the prior are acceptable as the title insurer will very likely include them in any new commitment or policy. Some such items may need to be addressed at or before closing to have them removed.

Ethical Requirement:

When tacking, the lawyer is obligated to disclose to the client the "precise nature of the service being rendered" – RPC 99

When tacking, always try to be certain that you are not tacking to a policy issued based on a "limited search" or "shortened search." Be very wary of exceptions to "matters of record prior to _____" or other broad exceptions to "easements or servitudes of record" as they may indicate that the policy was issued by the insurer based on a very limited search. One should not tack to such a policy.

Shortened Searches

It is difficult to simply define a shortened search other than to say that it is something less than a full search and not a tack to a prior policy. In order to employ shortened searches one must clearly abide by the disclosure requirements of the Bar and disclose the fact that a shortened search was performed. Shortened searches may include searches to the deed into a developer for a subdivision tract or one-owner searches. Title insurers may

agree to insure based on these shortened searches but one should be very aware of the exceptions that the insurer may choose to take…particularly if an owner's policy is sought. Be certain, should you adopt this practice, to clearly understand the needs of the client and the effect on the policy that may be issued by the insurer.

One must also be very careful when tacking to a "prior title letter" ("PTL") issued by a title insurer. PTL's frequently mean that the insurer does not have a policy on the particular lot that is being searched. Very often, the title insurer will compile exceptions from other lots for which it has title policies and allow an attorney to "tack" to its PTL. One should always inquire of the title company to determine if there is a policy behind the PTL. Where there is not, the attorney's ethical obligations to his or her client may dictate not using the PTL.

Tacking for Rate

Notwithstanding the ethical obligation of the attorney with regard to the search period, it is important to consider that although one may choose not the tack to a policy for title, any prior policy may provide the basis for a reissue rate from the insurer. Reissue rates offer a significant savings to the client and should be considered whenever possible.

The Search

A typical title search is actually composed of searches of at least three different sources of information. Title history is found at the Register of Deeds for the county in which the property is located. Judgments, liens, estates, lis pendens and special proceedings must be searched at the office of the Clerk of Superior Court in the county. Taxes and assessments should be checked at the tax assessor's or collector's office in the city (when applicable) AND the county in which the property lies. Only by searching each of these records can you be certain to ascertain all of the possible title issues that must be reviewed by the attorney in giving a title opinion.

At the Register of Deeds

The Indexes

There are two separate indexes kept at the Register of Deeds, the Grantor Index and the Grantee Index.

The **Grantor Index** is an alphabetical listing of parties named as grantors in deeds, deeds of trust, easements, restrictions, etc. The grantor is the party making a conveyance or an "out" as they are commonly called. Sellers, borrowers and declarants are common examples of grantors.

Conversely, the **Grantee Index** is an alphabetical listing of the party/parties named as *grantees* in deeds, deed of trust and other documents of conveyance. The grantee is the party receiving the conveyance from the grantor.

Note also that registries may also have other books that provide useful if not vital information. These sources may include corporation books, map or plat books, lot/block books and Department of Transportation rights-of-way records. These additional indexes can be both informative and important to a complete title search, so be familiar with the registry in each county where you will search titles.

Creating the Chain of Title

The first step in the actual search is to establish what is commonly called the chain of title. The chain is a list of all of the owners of the real property over a span of time. Obviously, a chain of title could be very long indeed. The necessary length of the chain of title should be established by policy in your office and is discussed hereinabove.

Sample Chain of Title

Molly Ringwald to Fred Sanford
Deed Book 1190, Page 1011
♦
Al Pacino to Molly Ringwald
Deed Book 1008, Page 865
♦
Joe Dimaggio to Al Pacino
Deed Book 909, Page 401
♦
Al Capone to Joe Dimaggio
Deed Book 666, Page 666

The chain of title is established by a search in the Grantee index in most counties in North Carolina. It begins with the name of the present owner of the property and looks backward in time. By entering the name of the current owner in the Grantee index, you will usually find the name of the Grantor that conveyed the property to the current owner

and you have established the first "link" in the chain.

Thus, if your current owner is named Fred Sanford, you would search his name in the grantee index to find the deed into Fred from Molly Ringwald.

Then, to find the next link, you would search Molly Ringwald in the grantee index to find the deed into her from Al Pacino.

Repeat this process until you reach a transaction that occurred at a point in time far enough back to establish the necessary length of your chain (ie. 30, 40 or 60 years).

Gaps and Missing Links

When establishing a chain of title you will too frequently encounter gaps or missing links. You are not free to ignore these missing links in the chain of title, but rather you should proceed to other sources of information that may help you locate the missing link. There should be some evidence in the public record creating a continuous chain of title or that in and of itself constitutes a defect in title that must be addressed.

There are a number of potential sources of information for you to review that may provide you with the missing link in your chain of title.

A. Estate Files – One way real property is transferred other than by deed is through transfers occasioned by death. Pursuant to NCGS 28A-15-2, title to real property passes to the heirs of a decedent upon the death of the decedent subject to being reclaimed by the personal representative of the estate for the payment of claims of creditors of the decedent. Specifically, NCGS 28A-15-2(b) provides:

> "Real Property. The title to real property of a decedent is vested in his heirs as of the time of his death, but the title to real property of a decedent devised under a valid probated will becomes vested in the devisees and shall relate back to the decedent's death, subject to the provisions of NCGS 31-39."

Accordingly you may need to locate the estate file for a grantee in your chain of title if there is no evidence that the grantee transferred the property to his successor by way of deed or other recorded instrument. If

the decedent did not die in the county in which you are searching title to the property, there may or may not be an estate file located there. Therefore, it may require additional research on your part to ascertain whether a particular individual is in fact dead and if so, where his or her estate was probated. There should be some record evidence of his or her death in any jurisdiction where he or she owned real property. Ancillary administrations are frequently overlooked by personal representatives.

For a more thorough discussion of decedent's estates, see the Decedent's Estates segment of this manuscript below.

There are procedures provided for by statute to establish ancillary estate administrations. However, those procedures are a topic for another time and are not addressed by this manuscript. Just be mindful that additional work may be necessary on your part or the part of the seller's attorney to eliminate any gaps in your chain of title that result from the death of an individual previously having owned the property for which you are searching title. Accordingly, if you encounter this situation you should review the estate's administration procedures set for in the general statutes to make sure that your title is clear. In the appendix you will find a rather simple abstract for estate administrations that will assist you in determining that compliance with the statutory requirements occurred.

B. Special Proceedings – It may be that a gap in your chain of title can be eliminated by examining the Special Proceedings files. The appointment of a guardian for an incompetent, a partition proceeding, and name changes are examples of special proceedings that may affect title.

C. Foreclosure – If title to a particular property was not transferred by a previous owner by deed, it may have been the subject of a foreclosure action. Evidence of a foreclosure proceeding will may appear in the Special Proceedings files but may also appear at the registry. You must have a good working knowledge of Chapter 45 of the General Statutes such that you are able to determine if any link in your chain of title located through a foreclosure is valid. Like estate administration, foreclosure is a topic in and of itself and is not within the scope of this manuscript. You will find a Foreclosure Abstract in the appendix to this manuscript that you may find helpful in determining the effectiveness of the foreclosure action for transferring title.

D. Civil Actions – Occasionally title to real property has been transferred through some form of civil action. Examples include judicial foreclosures, execution sales, and conveyances pursuant to Rule 70 of the North Carolina Rules of Civil Procedure. Accordingly, if you cannot otherwise locate a link in a chain of title you should examine civil actions involving a particular predecessor in title to see if title passed through court action.

Always take note of pending civil actions. While civil actions do not typically affect title except where a lis pendens has been filed, they do occasionally result in judgments that will attach to all property of the judgment debtor. If you note pending civil actions be careful when updating judgments prior to recording!!!

E. Tax Office Records – In many counties, the local tax office will keep limited (sometimes detailed) title information. This is frequently an invaluable shortcut to locate a missing link. Inquire in your local tax office to see what information they may have. However, also remember that the information at the tax office is NOT sufficiently reliable for the basis of a title opinion.

Searching "Outs"

After completing the chain of title, the search is finished by searching forward in the Grantor Index from the earliest grantor named in the deed which is the starting point of the chain of title (above), searching until they conveyed to the next person in the chain of title, then searching the Grantor Index in that person's name, etc. In the search forward, you will be looking for so-called "outs" or "out conveyances" by each grantor in the chain. In this portion of the title search, you may find some of the following:

- Deeds of Trust
- Satisfactions
- Restrictions
- Easements
- Rights of way
- Foreclosures
- Sheriff's Sales
- Boundary Agreements
- Plats
- Timber / Mineral conveyances
- Powers of Attorney

When searching outs, it is very important to keep an accurate record of all outs discovered between the deed into an owner and the deed out of the owner. Note the book and page of each out conveyance so that you may use that information later. Also, be very wary of brief legal descriptions as shown on

the index. With some frequency, those brief descriptions are inaccurate in that they often incorrectly describe the property or the interest conveyed, and generally omit references to easements and restrictions that may have been reserved. The only way to be certain that an "out" does not apply to property that you are searching is to look at and read the document itself.

This process should be performed for each grantor in the chain of title and all of the outs should be noted. If you have concerns as to whether or not an "out" affects the subject property, report it so that it can be brought to the attention of the supervising attorney and possibly discussed with the title insurance company.

About Outs

An effective title searcher should be able to interpret the meaning of the various documents that one may encounter when running outs at the Registry. The following sections will cover the more common documents that one may find. The list is not exhaustive as there is no end to the permutations one can discover in the Registry.

- **Deeds** – Simply defined, a deed is an instrument that conveys an interest in real property. To be valid as between the parties, a deed must be in writing, contain language of conveyance, be signed by the grantor (seller) and must sufficiently identify the interest to be conveyed. To be valid and enforceable against the rest of the world, the deed must also be properly acknowledged before a notary, certified by the Register of Deeds and recorded in the Registry of the county in which the property lies. Each deed in a chain of title should be reviewed for these important components. It is also important to review each deed with a number of other considerations in mind:

  NOTE – North Carolina is a "**pure race**" state, meaning that the first party to record with the Register of Deeds a validly executed and probated deed from the record title holder(s) has the superior title, regardless of the date of execution.

  1. What type of deed is it?

     Warranty Deed – should contain language that the Grantor owns the property in fee simple, that the premises are free from encumbrances (except as may be shown on the deed) and that the grantor will

WARRANT and DEFEND the title against the lawful claims of all persons whomsoever.

Special Warranty Deed – should contain language of limited warranty by which the Grantor warrants that the Grantor (only) has done nothing to impair title.

Quitclaim or Non-Warranty Deed – generally contains no warranty. Here, the Grantor conveys only whatever interest he has and has no liability to the Grantee if he owns nothing. Quitclaim deeds are frequently used as corrective devices to fix title problems. They can be used to convey land for which the title is questionable and they should be reviewed carefully.

Correction Deed - When errors are located in deeds in the chain of title, practitioners have utilized the deed of correction to remedy past mistakes. It is advisable to have the Grantor of a deed of correction release all claims to the property as well as explain carefully the error correction. Also, deeds of correction are best when running to the present owner rather than to a former owner to alleviate any question of whether or not a subsequent deed from a former to a present owner is necessary. It is a wise practice for the examiner to check all out conveyances from all owners in the chain up to and through the recording of the deed of correction to make certain that there are no adverse conveyances that may disrupt the chain prior to the correction of the erroneous deed.

Corporate Deed - While a deed by a corporation may be either a general warranty, special warranty or a non-warranty, one must be cautious when reviewing its execution. In order to be binding on the corporation, the conveyance must be authorized by the Board of Directors of the corporation, the corporation must be validly existing (not suspended or dissolved) at the time of conveyance or deed should indicate that it is executed for the purpose of winding up corporate affairs. For a North Carolina entity, the examiner can review the standing of the corporation on the website of the North Carolina Secretary of State (www.sosnc.com). A corporate deed must be signed by an "executing officer" (as defined by NCGS §47-41.01 and including Chairman, CEO, President, Vice President, Treasurer and others) of the corporation or some person authorized to sign on behalf of the corporation. If a party other than one of the officers specified in the

statute executes a corporate deed, the examiner may have to look for evidence of corporate authority, commonly granted by Resolution of the Board, with which the signer can bind the corporation.

Please note also that deeds from partnerships, limited liability companies, and other such entities will also require close attention and adherence to the statute and to their structure.

Deeds Between Husband and Wife - The real estate attorney must be prepared to discuss domestic law on occasion. A deed from one spouse to the other should lead to questions regarding the marital status of both spouses. NCGS Chapter 39 provides assistance in this area and cannot be re-read too often. The real estate practitioner must be familiar with the advantages and disadvantages of tenancy by the entireties. In particular one must not fall into the trap of assuming that a recorded separation agreement will necessarily eliminate future troubles regarding real property between spouses.

There has been some debate considering a deed between a husband and wife and its legal effect. The debate concerns not whether such a deed conveys title but whether such a deed conveys title, including the statutory marital interest provided for in NCGS 30-3.1 and NCGS 29-14. A conservative practitioner will consider the import of NCGS 52-10 which requires that agreements between spouses be executed by both husband and wife. Many feel therefore that in order to sever the marital interest, a deed must comply with NCGS 52-10 and be signed by both husband and wife as grantors. Attached in the appendix is some recommended language for inclusion in a deed where the intent is to convey title and sever the marital interest.

2. What interest does the deed convey?

One must always be very careful to review a deed to verify that it does not convey an interest of less than fee simple title or less than all of the property. For example, a deed conveying only an easement, a life estate or a fractional interest (i.e. 1/2).

3. Is it a Gift Deed?

   Any deed which conveys title to property for no consideration is considered a gift deed. By statute in North Carolina, a gift deed must be recorded within 2 years of execution in order to be valid. Often, a gift deed will not state that it is a Deed of Gift. Gift Deeds can be identified by a recital of no consideration, or "in consideration of love and affection." Another indicator is the payment of zero deed stamps. When you see these indicators, it is important to verify that the deed was recorded within 2 years of execution.

   IMPORTANT – A gift deed MUST be recorded within 2 years of execution to be valid.

4. Is the deed properly executed?

   Did the Grantor sign the deed or did the Grantor's proper representative sign the deed? Consider the case of a deed signed by an attorney-in-fact. There must a power of attorney filed in the county where the property lies and the power of attorney must give specific authority to the attorney-in-fact to convey real property. Consider also a corporate deed that must be signed by an "executing officer" (as defined by NCGS §47-41.01) of the corporation or some person authorized to sign on behalf of the corporation. Remember also that a corporation must be validly existing (not suspended or dissolved) at the time of conveyance or deed should indicate that it is executed for the purpose of winding up corporate affairs. The status of a corporation can be verified on the Secretary of State's website at www.sosnc.com.

5. Is the deed properly notarized?

   Was it signed by the notary, with a seal and a commission expiration date? Had the commission expired at the time of signing? Did *all* signers appear before a notary and acknowledge their execution of the deed?

6. Is there a sufficient description of the property?

   The Legal Description contained in the deed, deed of trust, lease or other documents of closing determines exactly which piece of "ground" the title to which is to be insured and shown in Schedule A of the title

insurance policy. The legal descriptions contained in easements, restrictions, plats or other documents found in the chain of title may include the property to be insured, so those descriptions determine whether such items should appear as exceptions we must take in Schedule B of the policy. Therefore, the ability to read, map and understand legal descriptions is very critical. Descriptions come in various styles, contain different types of references and are of differing levels of quality. So, in construing them, courts have established preferences ("rules of construction") about which information is the most reliable, if they contain ambiguities. Be sure to review the appendix entitled "How Good is the Legal Description" so you'll know and understand these levels of reliability.

- **Deed of Trust and Satisfactions** - A deed of trust is used to encumber real property as security for repayment of a promissory note (loan) by a borrower. Under a deed of trust, the borrower (called the "grantor") conveys legal title to the real estate to a third party (called the "trustee") to hold for the benefit of the lender (called the "beneficiary") until the loan is repaid. Upon repayment of the loan, the lender must cancel the deed of trust and thereby restore title to the borrower without the necessity of a reconveyance. When the deed of trust is cancelled, a "satisfaction" is recorded at the registry as evidence of the release of the lien of the deed of trust. The following methods are the most commonly used in North Carolina to cancel a deed of trust of record or release the particular property from the lien of the deed of trust.

DEED OF TRUST – An instrument by which the property is transferred to a Trustee by the Borrower for the benefit of the Lender (Beneficiary). Deeds of trust are given to secure a debt that is represented by a promissory note.

1. Presentation of the *original* Deed of Trust and the *original* Promissory Note. Both must be (1) endorsed "Paid and Satisfied," (2) signed by the beneficiary (or appropriate officer of beneficiary) and (3) dated by the beneficiary (or appropriate officer) for the date being marked as paid. No recording fee. NCGS §45-37(a)(2)
2. *Trustee's Satisfaction*. NCGS §45-37(a)(7)c. Form is provided at NCGS §45-36.20 and §45-36.21. but previous form in NCGS §47-46.1 will also comply. No recording fee. (*Substitution of Trustee* form can be used if original trustee is unavailable. Recording fee same as for deeds.)

3. *Satisfaction by Secured Creditor,* NCGS §45-37(a)(7)a. Form is provided under NCGS §45-36.10 and §45-36.11, but the prior Certificate of Satisfaction by Note holder authorized by NCGS §47-46.2 will also suffice. (NOTE: The Affidavit of Lost Note is no longer required.) No recording fee.
4. *Affidavit of Satisfaction by Satisfaction Agent.* NCGS §45-37(a)(7)b. If a North Carolina licensed attorney provides the requisite notice to the appropriate secured creditor and complies with the procedures under NCGS §45-36.13 *et seq.*, and the secured creditor does not object timely, the attorney can file an Affidavit of Satisfaction, releasing the property from the lien of the deed of trust, though the debtor would still be liable for any outstanding balance and costs on the underlying obligation. Form is provided under NCGS §45-36.16.
5. *Release Deed* executed by trustee, with written approval by note holder. Usually the note holder will join in the execution of the release deed. Standard recording fees for deed required, but no transfer tax. (*Substitution of Trustee* form will be required if original trustee is unavailable. Recording fees same as for deeds.)

These forms are available at the Chicago Title Website:
http://www.northcarolina.ctt.com/chicagobulls.asp

- **Restrictions** – Restrictions are provisions contained in real property documents that prohibit, limit or regulate the use and development of land, or provide for maintenance assessments or dues to maintain common areas or private roads. Restrictions are generally found in three places:
  - Separate Instruments. They may be in a separate instrument, such as restrictive covenants or a declaration that may affect only the subject property for the benefit of other adjoining or neighboring property, or restrict a particular tract or subdivision to assure a common development scheme, as in a subdivision;
  - Prior Deeds. They may appear in a deed in the chain of title; or
  - Plats. They may be incorporated in the recorded plat of a parcel or subdivision.

  A Declaration of Covenants, Conditions and Restrictions may also dedicate easements and may contain covenants providing for assessments, obligations to maintain certain facilities or other conditions or obligations.

They may be a part of Planned Unit Development, Planned Community or Condominium documents as well. Chicago Title relies upon the certifying attorney to report the existence of restrictions, whether or not they contain a forfeiture or reversionary clause, building set back lines, limitations on the type of building, assessment obligations, easements, and whether they are use restricted, such as a "residential only" restriction, and to assure that assessments are paid current at closing and any other issues are appropriately addressed at or before closing, such as rights of first refusal or violations of the restrictions.

- **Plats** – Subdivision plats are recorded maps, usually dividing a tract into smaller ("subdivided") parcels, usually identified by "Lot", "Parcel" or "Tract" number. Usually they are drawn as part of a development of residential or commercial land for sale by a developer. However, they may be drawn and recorded in partitions among co-tenants. The plat is usually referenced as recorded in a Plat Book, a Book of Maps, or other similar indication of the name of these records in the particular county.

  Plats usually determine boundary lines (with a metes and bounds description) as between the lots and are relied upon for drafting the legal description of the property to be insured, such as "Being all of Lot 15 of Windy Oaks Subdivision, as shown on plat recorded in Plat Book 5, Page 15, Moore County Registry." However, in most cases, they are *not* actual *surveys* of the property since they typically do not reflect actual improvements, encroachments, parties in possession or other matters physically located on the land. Therefore, plats should not be relied on in the same way that you would rely upon an actual survey of the property.

  Plats often show roads, common areas and other matters affecting the subdivision, including but not limited to water (ditches, creeks, lakes, and oceans), easements for utilities, access roads (public or private), wetlands, and setbacks. They may show private roads and common areas dedicated to the use of property owners in the subdivision only, or they may actually provide for dedication of roads, parks and utility easements to become public upon completion of construction.

Plat vs. Survey
A plat is typically NOT a survey. Plats typically do not depict existing improvements, encroachments, parties in possession. While plats may create easements, they typically do not depict existing easements or usage by others to cross the land.

- **Easements** – An easement is a right of use over the land of another. Easements can be granted for the benefit of an adjoining tract of land (an appurtenant easement) or for the benefit of an individual person or entity (an easement in gross). There are also easements which restrict the use of land for the benefit of others. These are called negative easements.

  Appurtenant easements are commonly granted for things such as access, utilities, wells, and septic fields. An appurtenant easement always burdens one tract for the benefit of another tract of real property. An example would be an access easement from a public road across one tract (the servient tract) to another tract (the dominant tract). Although the appurtenant easement rights pass to subsequent owners of the dominant tract ("run with the land"), the better practice is to include appurtenant easements in the legal description of the property to be conveyed to the new owner.

  Appurtenant Easement – a right in the lands of another that benefits (is appurtenant to) lands of the easement holder. An example of an appurtenant easement is an access easement across the servient tract to the benefited tract.

  Easements in gross are personal in nature, meaning that there is not generally a dominant tract of land that is benefited by the easement (as is the case with an appurtenant easement) An example of an easement in gross would be where a power company secures permission to run electric transmission wires across owner's land. Historically, easements in gross have ended with the death of the grantee but there are cases in which it has been determined that easements in gross were both perpetual and assignable.

  Easement in Gross – a right in the lands of another for the benefit of a person or entity. An easement in gross is personal in nature and there is no "benefited" land as with an appurtenant easement. An example of an easement in gross would be a utility easement for electric transmission lines.

  A negative easement prohibits an owner of land from doing something on his land that he would otherwise be able to do. A good example is a restriction limiting the size or type of structure that can be erected on the land. Under this sort of easement, the benefited owner can maintain a civil action to prevent the owner of the land from violating the restrictive provision.

  Easements are created in several ways. They can be reserved and/or conveyed in a deed, in restrictive covenants or on a plat map, or granted in a

deed of easement. Easements created by these means will generally be found in documents recorded at the registry.

Easements can also be created by prescription. An easement by prescription is taken in much the same way that land is acquired by adverse possession. To acquire an easement by prescription, the party claiming the easement must show that 1) its use is adverse, hostile or under a claim of right; 2) the use was open and notorious such that the owner of the land would have notice of the use; 3) that the use has been continuous and uninterrupted for at least 20 years; and 4) that the easement can be substantially identified. The possibility of a prescriptive easement might be shown on a survey (e.g. "old dirt road" or "old foot path") and should always be noted on the title abstract and preliminary opinion. Prescriptive easements should be discussed with the title insurance company prior to assuming that they are insurable. These are frequently litigated, a significant inconvenience to the client-insured, and cases are often lost because of failure to prove the necessary adversity of interest.

NOTE: See our *Quick Tips for Title Searching* in the Appendix!

At the Tax Office

City and county governments collect much of their operating revenue in the form of property taxes or ad valorem taxes. Ad valorem taxes create a lien on real property and therefore close attention must be given to making certain that they are up to date for a period of 10 years. Such liens have "super-priority," meaning that they are first in priority over all other liens and are not extinguished by the foreclosure of a deed of trust. Never assume that taxes are paid . . . always verify it.

Ad Valorem Tax – a tax on the estimated value of real or personal property.

Ad valorem taxes are determined by applying a "tax rate" that is established by the county or city to a "valuation" or "assessed value" of the property being taxed. The tax rate is typically determined in the middle part of the year (generally not later than June

Ad Valorem Tax Calculation:
(Tax Rate) X (Assessed Value) = Taxes Owed

30th). Tax bills are created and released, usually around the first of September of each year. The bills will then be due and payable by the first Monday in January of the following year. Once tax bills have been released, lenders will typically require (and title insurers will generally require on a title commitment) that taxes for that year be paid at closing. Thus, the title policy can be issued without exception for taxes for that year. Earlier in the year, the title insurer will generally take exception to taxes for the year.

Beware of city taxes. City taxes may or may not be collected by the county tax office, or may be or have been collected by the county for some years and by the city government for others. If your tract is within the limits of a city or town or within their extraterritorial jurisdiction, be sure to contact the city or town tax collector to verify how their taxes are collected and for what time periods. Similarly, be sure to remain aware of annexation, which can add property to the city tax base resulting in both a city and county tax bill.

If you are searching in a county with which you are not well familiar, be sure to enlist the assistance of the staff at the tax collections office. Ask them to verify that taxes are current.

The tax office may also be responsible for collecting assessments for various improvements made by the city or county. Assessments are issued for things like water and sewer improvements, sidewalk construction, streets, streetlights, and curb and gutter improvements. Be sure to check for both current *and pending* assessments.

Also remember that certain properties may be subject to exemption from taxation. Property held by non-profit or religious organizations may be totally exempt from property taxes, so long as the qualified person or entity owns the property. Elderly owners of property might receive a senior citizen exemption that reduces their property tax liability (*See* NCGS Chapter 105). This can be critically important if the property is conveyed to a person or entity that does not qualify for the exemption. Farm or timber lands may be taxed on the "present-use value" rather than the "fair market value" which is usually the basis for the assessed value. Thus, the farmer gains the benefit of a lower assessed value and, therefore, lower taxes. However, the difference between the taxes due on the present use value and the taxes which otherwise would have been due if the property were taxed at the fair market value remains a lien on the property. The lien includes interest

BEWARE!
Be careful to look for property tax exemptions and deferred taxes which may have to be paid at closing.

and penalties. When the property is sold to a party or entity that does not qualify for the deferral, taxes that had been deferred for the previous three years become due and payable (*See* NCGS §105-277).

At the Office of the Clerk of Superior Court

Helpful Definitions

- **Judgment** – a decision of a court of law. Money judgments become a lien against all real property of the defendant in the county in which the judgment is docketed.
- **Lien** – an encumbrance against property for money, either voluntary or involuntary.
- **Claim of Lien** – (CLOL) Claims of lien are filed with the clerk's office by those claiming that they are entitled to money from a property owner. They are most commonly filed by workmen, contractors, construction materials providers and by state and federal tax authorities. You may also find claims of lien filed for homeowner's dues and for attorneys' fees of indigents.
- **Lis Pendens** – a legal notice docketed to show pending litigation relating to real property, and giving notice to anyone acquiring an interest in the property subsequent to the date of the notice that they may be bound by the outcome of the litigation.
- **Civil Proceeding** – any proceeding that is not a criminal proceeding. The significance to real property is the possibility that a judgment might arise from the civil action. Note that some counties do not file lis pendens separately so you may have to review the court file to determine whether the matter involves real property. In addition, current litigation may become a judgment attaching to the property prior to closing if a closing is not immediate or is delayed. So, a cautious title searcher will note the pending litigation in order to verify at the time of closing that it is still outstanding and has not gone to judgment prior to closing.
- **Special Proceedings** – include foreclosure and partition proceedings as well as incompetency and guardianship proceeding.

The Judgment Search

Once you have established your chain of title and satisfied yourself that there are no adverse consequences resulting from out conveyances as hereinabove discussed, you should proceed to the judgment, liens and lis pendens docket in the Clerk of Court's office in the county where your property is situated. In that docket, you will be looking for any judgments, liens or lis pendens that affect the title to your property.[1]

1. Judgments. Ordinarily a judgment is good for ten (10) years; however, if a civil action is commenced to renew a judgment before the initial ten year period has expired, your judgment may exist for a total of twenty (20) years. Accordingly, it is important that you determine that any judgment that otherwise appears to have expired has not been extended for an additional ten years by way of a separate civil action and/or new judgment.

   One should also be aware that a judgment in favor of the United States is valid for a period of 20 years. This rule is not applicable to federal tax liens which are enforceable according to state law. Judgments in favor of the United States are frequently associated with environmental liens, defaulted student loans or awards for restitution granted in federal courts, among others.

2. Lis Pendens. A lis pendens is a process by which you provide record notice of the pendency of a civil action affecting title to real property. Without going into the specifics of the effect of a lis pendens, I would simply refer you to Article 11 of NCGS Chapter 1. You should familiarize yourself with and refer to that statute when you find a lis pendens in the chain of title.

3. Liens. As for claims of lien and other types of liens, you may find references to them in this docket as well. Be reminded that the typical materialmen and mechanic's lien is governed by NCGS Chapter 44-A. Accordingly if you find a materialmen and mechanic's lien governed by that chapter in the chain of title, you should refer to that statute for guidance in ascertaining the validity and/or enforceability of the lien.

[1] In this fiscal climate, it is prudent for clients to consider all information available at the Clerk's office. For example, a history of lien filings against a builder, whether or not paid and released, may indicate that the builder is suffering financial hardship.

Even if you feel the lien is not valid or enforceable, the prudent practice would be to report this to the title company and let them decide how it should be handled. This shifts the burden of the decision to the title company that will surely be involved if enforcement of the lien is attempted at some future point. It is often the case that a claim of lien will be filed against property and never be properly and fully perfected. While that lien may still appear of record, it may have expired by operation of law. You will want to review the claim of lien carefully, review any civil action carefully that has been filed to enforce the same, and report your findings to the title company. You should be aware that Chapter 44-A allows for the filing of a claim of lien and a lis pendens in the county in which the property is situated with the lawsuit being filed to perfect and enforce that claim of lien being filed in another county. Ridge Community Investors, Inc. vs. Berry, 293 NC 688, 239 S.E.2d 566 (1977). Accordingly, if you should find a claim of lien that has not yet expired, or should you find a claim of lien that on its face has expired but a lis pendens is also filed in the county in which your property is situated, read that lis pendens carefully as it should identify for you the county in which the lien enforcement action is pending. Once that suit is filed, the necessary steps for perfection have taken place, and the lien is an encumbrance against title that must be dealt with through one of the release and/or discharge provisions contained in NCGS Chapter 44A-1 6, or such other process as is approved by your title insurance company.

4. Tax Liens. Be careful with tax liens you find in your chain of title. Depending upon the type of tax lien it may have priority over deeds of trust. Accordingly, if your property has been through a foreclosure and a tax lien is or has been an encumbrance on the property you need to be sure the proceeding actually extinguished the tax lien. Similarly, you need to be mindful of the extended redemption period and notice requirements afforded the IRS when attempting to extinguish a tax lien by foreclosure. Otherwise your client's title may be subject to a claim by the Internal Revenue Service.

Judgments, liens, lis pendens, civil proceedings and special proceedings are checked by using the index at the Clerk of Court in the County where the real property is located. Judgments may attach as liens on the property if entered against an individual and/or entity that has owned the subject property within the previous ten (10) years. In addition, judgments of the United States which are transcribed to the local Clerk's judgment index, attach for a period of 20

years. Each owner's name must be checked beginning on the date 10 years prior to closing (and should be checked for the 20 years' prior period to catch judgments in favor of the United States which are valid for 20 years), no matter when they took title, through the date that they conveyed away all interest to the next person in the chain of title. The judgments index will reveal judgments, liens and lis pendens. Civil proceedings and special proceedings have a separate index that must be searched. All three can be checked from the "judgments computer" (the Administrative Office of the Courts computer) at your clerk's office. The clerk will most often be glad to show you how to find each.

Did you know?
Judgments in favor of the United States (not federal tax liens) remain enforceable for 20 years while other judgments are valid for only 10 (unless renewed).

For an increasingly nominal fee, the AOC system may be accessed via the internet through certain private providers. This may be a good option for a large volume practice. However, internet systems should not replace a trip to the clerk's office prior to recording to check the most recent filings which may or may not have been docketed to the AOC computer system.

As with any computerized indexing system, many errors are made when entering information into the computer. A good rule of thumb while checking judgments is to enter as little information as necessary to get the desired result. The objective is to narrow the search but not exclude any applicable judgments.

If you are searching an unusual name such as Julius Bergman, you may wish to enter "Berg" or "Bergman." By entering the shortened version, you are certain to get all of the Bergmans listed in the index. On the other hand, if you are searching a popular name such as Terrence Smith and you entered "Smith" you would likely get thousands of judgments to search. Try entering "Smith,T" and see how it limits the number of hits. If there are still too many, try "Smith,Ter" and so on. Other examples include:

Robert A. Stone	try "Stone", "Stone,R" or "Stone,Ro"
Julius Bergman	try "Berg", "Bergman" or "Bergman,J"
John A. Smith	try "Smith,J", "Smith,John" or "Smith, John A."

Consider also that judgments can be docketed under a nickname. So you might find a judgment against "Rob Stone" or "Bob Stone" and not "Robert Stone" though they are the same person. Try common variations for names as in the following examples:

Elizabeth Perkins	try "E", "Liz", and "Bet"(to catch Beth, Betty and Bette)
Joseph Simms	try "J", "Jo", and "Joe"
Richard Simmons	try "Ric" (would catch Rick, Rich and Richard) and don't forget "Dick"

After completing the search of the computerized index, it is most important to verify that no new filings have been made that would not show up on the system. Ask your clerk to show you where and how new files are stored so that you can check those as well.

The prudent lawyer should also search the judgments index for the buyer. Clearly, if the buyer has a judgment that will attach to the property upon purchase, the lawyer may advise the buyer to take certain simple steps to avoid the attachment of the existing lien. A simple example would be where a husband has a judgment filed against him alone. He and his wife are buying a home. The attorney, aware of the lien, might advise that the property be placed in the wife's name alone to avoid attachment of the judgment lien to the property.

Title Insurance Commitments & Policies

The Concept of Title Insurance

Why is there Title Insurance?

In the parlance of legal scholars, the best and most absolute type of real property title is the "fee simple" or "fee simple absolute." An owner of real property in fee simple owns the property without condition or limitation. He can freely convey the property or leave it to his heirs without limitation. A fee simple estate without any exceptions or encumbrances (if such a thing existed) would represent "perfect" title.

It is clear today that there probably are no "perfect" titles. Governmental restrictions, utility easements, claims of adverse possession, tax liens and all manner of other limitations can arise by agreement or operation of law and diminish fee simple title. Certainly, a title search will disclose many of the limitations or defects in title. However, there are defects that may not be discovered in the most diligent title search. Examples of such defects include undisclosed heirs, forgeries, deeds by minors or incompetents or deeds executed under duress just to name a few.

Prior to the advent of title insurance, owners and lenders relied on opinions of title given by attorneys. Reliance solely on the attorney's opinions had its risks:

1. The title opinion and title abstract on which the title opinion was based were limited to matters found on the public records and consequently, did not cover "hidden risks";
2. The liability of the lawyer was limited to losses arising from the failure to exercise a reasonable degree of care and professional skill, and the basis for recovery was an action in negligence;
3. Many lawyers did not have the financial resources to respond to losses if liability was found;
4. The statute of limitations barred many cases (in many states such as North Carolina, the statute of limitations is surprisingly short); and
5. If the lawyer died no one was accountable to the purchaser to whom the lawyer provided title assurances.

It would be unsettling to most people to make what is often the largest purchase of their lives and buy real property without some protection against undisclosed or undiscoverable title problems. That is precisely where title insurance meets a need. Title insurance addresses the deficiencies of the existing system as follows:

1. Title companies have assumed liability for "hidden risks" which may not be revealed by a search of the public records like forgery, the incompetence of the grantor or mortgagor, undisclosed heirs, spouses or co-tenants, fraud and easements or interests by prescription.
2. Liability to the insured owner or lender under a title insurance policy is based on contract theory rather than tort/negligence and, thus, is easier to prove. Title insurance liability comes in two flavors:
    a. liability for loss or damage resulting from a matter insured against by the title policy (the duty to indemnify); and
    b. liability for costs, attorney's fees and expenses incurred in the defense of title (the duty to defend).
3. Title companies have the financial resources to cover losses that were absent in the attorney/abstractor system. Title insurance is regulated by state insurance agencies and the title companies must retain statutory reserves for claims.
4. The owner's title insurance policy has no term or term limitations as long as the insured owner or lender retains an interest or estate in the insured property. The protection

afforded an insured owner can continue for the duration of the insured owner's liability for covenants of warranty in their deed to a subsequent purchaser.

What is Title Insurance?

Simply stated, title insurance reduces the risk of the insured owner or lender by insuring one or both against loss or damage arising out of defects to or liens on title which are not excepted or excluded in the policy. These risks for which coverage may be provided by title insurance can be grouped into three very general categories:

1. ***Unknown*** title defects. This includes all of those things that cannot be found in the most diligent search by the most diligent attorney.
2. ***Undiscovered*** title defects. Undiscovered defects might include things that are missed by the attorney in the search of title.
3. ***Known risks*** which have been disclosed to the insurer. Known risks would include things like encroachments onto setbacks. The insurer may decide the risk of a claim is so slight that it is willing to accept the risk and "insure over" the defect.

So, title insurance is simply an indemnity form of insurance. The insurer promises to reimburse certain types of losses suffered by the policy holder as a result of a defective title.

What Title Insurance is NOT!

Title insurance is neither a guarantee that the title will be as reported in the policy, nor a statement that the title is "good" or "marketable", even though the policy provides some coverage for unmarketable title. It is a contract to indemnify against loss caused by defects in the title or encumbrances on the title. In many cases, the coverage may include "cure" of the defect. But policy cannot guarantee this as, in many cases, the defect cannot be cured and the policy simply provides reimbursement of the actual loss, typically based on a calculation of "diminution in value" of the insured property, or the change in value of the property with versus without the defect.

Remember that title insurance only promises to compensate the policyholder for an actual loss and only up to the face amount of the policy. So, for example, the mere fact that an easement for a utility line, which was not shown as an exception on the policy, is discovered after closing does not necessarily create a compensable claim. The owner must show that he has been damaged and suffered an actual loss. The actual loss could be in the form of diminished property value or damage resulting from the maintenance of the undisclosed easement.

The Title Insurance Commitment

The title insurance commitment is the title insurer's method of committing or promising to issue its policy of title insurance in favor of the proposed insured once the requirements made by the title insurer are met. The commitment is not effective until the proposed insured is identified, the amount of the policy is determined and the commitment is signed by an authorized officer or agent of the title insurance company. Title insurance commitments have a term of six (6) months from the date of issuance and terminate after this time if a title policy has not been issued, unless the failure to issue the policy is the title insurance company's fault. The time period can be extended for good cause but any such extension must be confirmed with the insurer prior to expiration.

NOTE: As you read this section, it may be helpful to look at the "Sample Commitment" in the Appendix.

The Body of the Title Commitment

Schedule A

Schedule A of the title commitment establishes a number of important details that should be reviewed carefully for correctness. Failure to review the commitment for accuracy can result in extra effort later when the policy is issued with incorrect or inaccurate information. Included in Schedule A are the following details:

1. The "effective date" which is the date, hour and minute through which the title attorney has searched the public records and certified title.
2. The proposed insured owner and/or lender are identified in items 2(a) and (b).
3. The type of policy each proposed insured will receive once the requirements in Schedule B - Section 1 are satisfied.
4. The amount of the policy is also inserted in item 2.
5. The interest of the proposed insured (i.e., fee simple, leasehold, or fee simple & easement).
6. The current owner.
7. The legal description of the property to be insured.

If appurtenant easements, such as an access easement, benefit the insured property and are to be insured, they should be clearly identified below the legal description as "together with . . . ." If such easements are not included within the legal description shown on the commitment, then they will not be insured in the policy. The title attorney must search the title to the insured easement area to determine if the party which granted the easement appurtenant to the insured property was legally entitled to do so. Any and all exceptions appearing of record prior to the recorded easement must be reported to the title insurance company, as well as those of the easement owner since the creation of the easement. For example: A deed of trust placed on the servient easement tract prior to recording of the easement has priority over the easement and a foreclosure of the deed of trust can therefore extinguish the subordinate easement interest.

Schedule B

Schedule B of the title commitment is divided into Schedule B - Section 1 (Requirements) and Schedule B - Section 2 (Exceptions).

Schedule B - Section 1 lists the specific requirements with which the certifying attorney must comply for the title insurer to issue its policy. Every commitment has two **standard requirements** which are (a) that payment be made to the grantors or mortgagors of the full consideration for the estate to be insured (in most cases, this is the purchase price); and (b) the proper instruments must be executed and recorded in order to create the estate to be insured. The remaining requirements depend on the type of transaction (purchase, sale, construction, refinance) and what the title attorney found

during his/her search. Typical requirements include but are not limited to the following:

- Deed(s) of Trust to be paid off and/or released.
- Other Lien(s) to be released.
- Payment of property taxes or assessments due or payable.
- Judgment(s) to be paid and released.
- Properly executed and recorded Deed or Deed of Trust to and from proper parties.
- For insurance regarding priority of conveyance by seller to proposed insured owner over potential liens for labor, services or materials, including surveyors, architects, engineers and rental equipment (herein "liens") of seller, or priority of proposed insured lender's deed of trust (once recorded) over said liens of seller and/or construction borrower, receipt of applicable NCLTA form (or substantially similar form approved by Company counsel prior to closing), completed and executed by all required parties in compliance with the form's instructions regarding same, to wit:
    - NCLTA Form 1, if no recent construction or addition of improvements on land and no construction loan by signing owner or borrower is contemplated;
    - NCLTA Form 2, if construction on the land was recently completed; or
    - NCLTA Form 3, if construction is in process or immediately contemplated (for loan including construction financing).

  In addition, if the proposed purchaser will be obtaining combined purchase and construction financing from proposed insured lender as a part of the transaction to be insured, proposed purchaser (construction loan borrower) must also provide duly completed and executed NCLTA Form 3 in order to obtain insurance of priority of the construction loan over such liens against the proposed purchaser (construction borrower).

- Requirements for issuance of special endorsements such as mobile home endorsements, zoning endorsements, etc.

Schedule B - Section 2 lists the exceptions which will appear on the policy of title insurance once issued. The exceptions are items that will NOT be insured

by the title insurance policy. Common exceptions include taxes not yet billed, restrictions, easements, encroachments, survey matters and leases. Again, the exceptions will reflect many of the things that the title attorney finds during his/her search of the public records.

One standard exception, known as the "gap" exception, will appear in the exceptions section in every commitment: "Defects, liens, encumbrances, adverse claims or other matters, if any, created first appearing in the public records or attaching subsequent to the effective date hereof but prior to the date the proposed Insured acquires for value of record the estate or interest or mortgage thereon covered by this Commitment." This exception addresses things that may appear of record during the "gap" between the end of the search period stated on the attorney's preliminary opinion and the recording of documents in the new transaction. These are matters which should be revealed in the update of title at the time of recording. So, if a judgment is docketed the day after the preliminary search was completed, that would not be covered in the policy unless paid and released by the attorney at or prior to closing.

Policy Language Incorporated by Reference

The commitment incorporates by reference the Covered Risks, the Conditions, and the Exclusions from Coverage from the applicable policy form to be issued. Similar to the title policy, the commitment contains a section for Conditions and Stipulations which, among other things, states that if the proposed insured has knowledge or acquires knowledge of a title defect or lien or other matter affecting title covered by the commitment, the title insurer is not liable for any loss or damages to the insured arising from its failure to disclose the matter. If the title insurer hears about the undisclosed title defect on its own or through the proposed insured the title insurer may amend the commitment accordingly, possibly to take exception the newly discovered issue.

The Title Policy

In the section entitled "About Title Insurance" the purpose of title insurance was discussed. It is with the policy that the protections are established. The policy provides the owners or lenders with title protection related to the real estate that they have purchased or used to secure a lien. We will see that there

are differences between the policies issued for owners and for lenders. However, in this initial discussion, we will review the basic contents.

The policy is indeed a complex legal document but it can be simplified by breaking it down into the following component parts:

1. A policy jacket which contains:
    a. Covered Risks;
    b. Exclusions from Coverage; and
    c. Conditions.
2. Insert Pages which are segregated into two parts:
    a. Schedule A
    b. Schedule B

The ALTA Policy Forms

The policy jacket is a uniform instrument that has been approved by the American Land Title Association or "ALTA." Therefore, policy jackets generally do not vary from one insurer to another. Policy forms have evolved over the years but changes to the jackets are infrequent. The most recent revision was a significant overhaul of the existing policies. In June of 2006 ALTA adopted new owner's and lender's policy forms. The ALTA Owner's Policy (06-17-06) is the industry standard and was intended to replace the aging ALTA Owner's Policy (10-17-92) which, as the name implies, had not been revised since 1992.

Similarly, the adopted ALTA Loan Policy (06-17-06) replaces the 1992 loan policy and the ALTA Short Form Residential Loan Policy (10-21-2000) both of which have been de-certified by ALTA.

For your reference as you read this section, we have provided copies of the policy jackets for each of the following new policy types in the Appendix:

New Policies:

1. ALTA Owner's Policy (06-17- 06)
2. ALTA Loan Policy (06-17-06)
3. ALTA Short Form Residential Loan Policy (06-16-07)

Old Policies

4. ALTA Owner's Policy (10-17-92)
5. ALTA Loan Policy (10-17-92)
6. ALTA Short Form Residential Loan Policy (10-21-2000)

For ease of discussion, we will review and consider the contents of the ALTA 2006 Owner's and Lender's policies.

Covered Risks

The covered risks in the policy are stated on the front cover of the policy. As you might assume, these provisions identify the specific matters that ARE COVERED or insured by the policy. They are surprisingly brief given their importance to the insured. The core coverages provided by the ALTA Owner's Policy (6-17-06) are:

1) Title to the estate or interest described in Schedule A being vested other than as stated in the policy;
2) Any defect in or lien or encumbrance on the title including, but not limited to:
   a) Fraud, forgery, incompetence;
   b) lack of authorization to transfer
   c) defective execution, acknowledgment;
   d) defective powers of attorney;
   e) defective administrative or judicial proceeding
   f) the lien of real estate taxes or assessments; and
   g) certain encroachments either onto the insured land or onto adjoining land;
3) Unmarketability of the title which allows another person to refuse to perform a contract to purchase, lease or to make a mortgage;
4) Lack of a right of access to and from the land;
5) Where notice of a violation is recorded in the public records, violation or enforcement of ordinances, permits or regulations regarding:
   a) Occupancy or use of the land;
   b) Character or location of improvements;
   c) Subdivision;
   d) Environmental protection
6) Enforcement of governmental police power if evidenced by a notice on the public record;
7) A governmental taking (eminent domain) if notice is on the public record;

8) Any taking that has occurred and is binding on the rights of a purchaser without Knowledge;
9) Title being defective because of a preference or fraudulent transfer under federal bankruptcy or other creditor's rights laws;
10) Defects, liens and encumbrances arising of record after closing but prior to recording of vesting instrument (Note: this so-called "gap" coverage is not typically applicable in North Carolina, a pure race state).

The core coverages above are common to both an owner's policy and a lender's policy. However, there are certain additional coverages which lenders require. In addition to the title matters that would concern the lender and owner, the lender seeks assurances regarding the validity and priority of its lien. The following are added to a lender's policy but are not included in an owner's policy:

1) The invalidity or unenforceability of the lien of the insured mortgage;
2) The lack of priority of the insured lien over any other lien or encumbrance;
3) Lack of priority of the lien of the insured mortgage:
   a) As security for the advance of proceeds of the loan over certain statutory liens for services, labor or material (mechanic's and materialmen's liens);
   b) Over the lien of any assessments for street improvements underway or completed at Date of Policy;
4) The invalidity or unenforceability of any assignment of the insured mortgage provided the assignment is shown in Schedule A, or the failure of the assignment shown in Schedule A to vest title to the insured mortgage in the named insured assignee free and clear of all liens.

Exclusions from Coverage

The insuring clauses in any ALTA form policy are subject to Exclusions from Coverage. If a matter arises which is excluded from coverage under the exclusions section, the title insurer is not obligated to pay for loss or damages suffered by the insured owner or lender, or for any costs, attorney's fees or expenses which the title insurer is ordinarily obligated to pay because of its duty to defend the insured.

The exclusions from coverage include the following:

1. Laws, ordinances and governmental regulations. This exclusion includes zoning ordinances, building codes, and other regulations that regulate the use, occupancy or enjoyment of land and may include environmental regulations. Also included in this exclusion is the governmental police power which allows any branch of government to implement an array of laws and regulations that benefit the health, safety and welfare of the general public. Issues that would be excluded by this paragraph include, zoning violations, failure to secure a certificate of occupancy, or failure of a subdivision to meet the local government's subdivision requirements (other than the limited coverages of the residential and homeowner's policies above mentioned).
2. Eminent Domain. Of course the power of eminent domain is the power of government to acquire private property for some public use, typically by condemnation. The power of eminent domain is excluded from coverage so long as no notice of its exercise has been recorded in public records as of the effective date of the policy. Such notice would, of course, be found in a diligent title search.
3. Defects, liens, encumbrances, adverse claims or other matters:
   a. Created, suffered, assumed, or agreed to by the insured;
   b. Not known to the company, not recorded in the public records at the date of policy, BUT KNOWN TO THE INSURED and not disclosed to the company;
   c. Resulting in no loss or damage to the insured;
   d. Attaching or created subsequent to Date of Policy; or
   e. Resulting in loss or damage which would not have been sustained if the insured claimant had paid value for the estate or interest insured by this policy.
4. Creditors' Rights Exclusion. This exclusion eliminates coverage for any claim arising under federal bankruptcy law or other so-called creditors' rights laws. A Bankruptcy court has the authority to void transactions made in advance of a bankruptcy if the transaction is deemed to be fraudulent to creditors of the bankrupt. So, if property is sold by X for less than fair market value and just prior to X's filing bankruptcy, the court could deem X's sale to be fraudulent against X's creditors, who, but for the sale, may have been able to have the property sold to satisfy X's debts.

On a lender's policy, there are again some additional concerns that must be excluded given that the lender's interest in the property is as a lien holder.

As with the insuring provisions, these exclusions deal with the validity and priority of the lender's lien. The following do not appear in the owner's policy:

5. Unenforceability of the lien as a result of lender's failure to be properly registered to conduct business in the state in which the insured property lies.
6. Unenforceability of the lien as a result of lender's failure to comply with usury, consumer credit protection or truth in lending laws.

Conditions and Stipulations

While the Covered Risks and the Exclusions from Coverage define what is and is not insured under the policy, the Conditions disclose the details of the coverage. More specifically, the Conditions address how and when to file a claim, what the responsibility of the insurer shall be in response to the claim, and the rights of the insurer with regard to the insured in handling a claim matter.

It is sufficient for this manuscript to briefly describe what is contained in the Conditions section of the Policy.

1. Definitions of frequently used terms.
   a. Insured. The party named in Schedule A. Includes those who succeed the named insured by operation of law (not a purchase) including heirs, devisees in a will, personal representatives, corporate or fiduciary successors. The ALTA 2006 Owner's Policy significantly expands the definition of the Insured to include grantees of the original insured who take title by deed without payment of actual valuable consideration. Examples of such insured grantees include an estate planning trust (trustee) and a successor entity (under certain conditions).
   b. Land. The land described in Schedule A and improvements affixed thereto which by law constitute real property, not including any property beyond the bounds of the description in Schedule A (easements or interests in abutting street, roads, alleys or waterways). This does *not* include personal property such as fixtures or mobile homes that have not been converted to real estate pursuant to statutory requirements.

2. Period of time policy remains in effect. The policy will continue in favor of the insured owner as long as:
   a. the insured owner retains an estate or interest in the land (owner does not sell the property);
   b. the insured owner sells the property and retains a purchase money deed of trust; or
   c. the insured owner sells the property and remains liable to the purchaser under covenants of warranty in the deed.
3. Notice. Requirements for the insured to give notice of claims to the title insurer.
4. Affirmative duty of insurer to defend a law suit. Without this provision, there would not be a compensable loss until the insured lost the lawsuit. This provision allows the insurer to intervene for the purpose of fighting the suit and "curing" the title defect. However, note that the determination whether to litigate is in the sole discretion of the title insurance company, which may instead elect to simply pay policy limits (See #6 below).
5. Requirements for proof of loss or damages to support a claim.
6. Option of the insurer to pay the policy amount rather than defend a claim.
7. All payments made by insurer under the policy reduce the amount of coverage.
8. Requirement that, in the event of a dispute between the insured and the insurer, the matter must be submitted to arbitration.

Schedule A

Much like Schedule A of the Commitment which is discussed above, Schedule A of the policy contains basic information applicable to the policy.

1. Policy Number.
2. Effective Date of Policy.
3. Amount of Insurance.
4. Name of the Insured. Either the owner or the lender.
5. The estate or interest in the land which is covered by the policy. This section identifies whether the interest is fee simple, leasehold or other type in interest.

6. Information on the insured deed of trust (Loan Policy) or the simultaneously insured mortgage or deed of trust encumbering the property (Owner's Policy)
7. The legal description of the land insured

Schedule B

Schedule B on the Policy includes exceptions shown in the Commitment as well as exceptions for any matters for which Requirements of the Commitment were not met. So, if all the requirements in Schedule B-1 of the commitment are not met, they will be listed in Schedule B of the Policy as exceptions. For example, if the commitment required payoff and release of a deed of trust to Big Bank, and the attorney does not report the deed of trust as paid and to be canceled, then it will appear as an exception in Schedule B of the policy. In addition, all of the exceptions appearing in Schedule B-2 of the Commitment will appear in Schedule B of the Policy (other than the exception for title matters between the attorney's Preliminary Opinion and the recording, the "gap" exception discussed above).

Short Form Residential Loan Policy

You will occasionally see a request for an ALTA Short Form Residential Loan Policy (06-16-07)) in your lender's instructions. The Short Form Policy is different from the typical Loan Policy in several ways. First, the Covered Risks, the Exclusions from Coverage and the Conditions that are contained in the standard policy are incorporated only by reference in the Short Form Policy. Thus, while those items are not physically included, they continue to apply.

Secondly, Schedule B of the Short Form Policy omits specific reference to exceptions for certain typical matters (below) on the insured property as you would have in the typical lender's policy. The policy contains certain blanket exceptions combined with certain affirmative coverages including the following:

1. Taxes and Assessments due and payable subsequent to the Policy date.

2. Covenants, conditions and restrictions of record, but with assurances that the covenants will not result in a reversion or forfeiture of title.
3. Easements and servitudes of record, but with assurances that improvements do not encroach onto the easements and that the use of the easements will not interfere with or damage improvements.
4. Mineral rights and reservations, but with assurance that use of the mineral reservation will not damage improvements.
5. Provides affirmative assurance against loss or damage by reason of matters affecting title that would have been disclosed by a survey.

The policy also includes an Addendum, which can be used to set forth additional exceptions or to limit the affirmative assurances. The policy is designed so that certain ALTA endorsement forms may be specified, and thus incorporated, by checking appropriate boxes.

Thirdly, the Short Form Policy is only available for transactions involving residential property with 1-4 family structures or condominium units.

Title Endorsements

Endorsements are added to title policies typically to expand the coverage of the policy to address special circumstances. They alter the Insuring Provisions and/or the Exclusions from Coverage.

Endorsements are typically requested by the lender in its closing instructions. The attorney must review the lender's written closing instructions carefully to determine which endorsements, if any, are requested and appropriate. We have provided a list of Common Residential Endorsements with descriptions of their purpose in the Appendix.

Most endorsements will have requirements that must be met before they can be issued. If the endorsement is requested in the preliminary opinion, the Commitment should include any specific requirements in Schedule B-1 for issuance of the endorsement. If you are not aware of the requirements to have

a particular endorsement issued, please call you local Chicago Title office and a list of requirements can be provided to you.

Various Other Issues

Decedent's Estates

Title companies receive numerous questions regarding the proper method to convey real property following the death of the record owner. In North Carolina, all real property interests owned by a person at the time of their death vest immediately in the decedent's heirs at law, subject to potential divestment by the various estate matters, including probate of a valid Last Will and Testament and Right of Survivorship. If the estate is still open, the interests, or potential interests, of all heirs, devisees, their spouses and the executor or administrator of the estate must be addressed prior to any conveyance of property. Among other things, the certifying attorney must determine to whom the title passes, the risk of dissent from a will or a caveat proceeding, whether all known creditors have been paid and the right of any additional creditors to file a claim, and whether federal and/or estate taxes have been paid or will be due. The title company relies upon the attorney to certify that all matters involving administration of the estate are satisfactorily addressed. (*See* Appendix for the various estate documents).

Terminology

Administrator(trix) - A personal representative appointed by the Clerk of Superior Court for the purpose of managing, settling and distributing the estate of an intestate decedent, usually where either no will is probated or the executor(s) under the will are unable or unwilling to serve.

Decedent - The person who died.

Devisee - A person who receives property under the decedent's will.

Executor(trix) - A person appointed by a testator (now the decedent) to carry out the directions and requests contained in the will and to dispose of the property according to provisions contained in the will.

Heir - A person who has a right to a share of a decedent's estate because of his or her relationship to the decedent. (Please note that the word "heir" is commonly used to describe persons that acquire property from a decedent whether by will or intestate succession. When used herein, the word heir is a reference solely to those persons that are entitled to a share of decedent's property had the decedent died without a will, i.e., through intestate succession. The word "devisee" is a reference solely to those persons entitled to a share of decedent's property under a valid will).

Intestate - A person who dies without having made a valid will or without having disposed of property or part thereof by a valid will.

Intestate Succession – The devolution of the decedent's property to his heir(s) at law pursuant to a statutory scheme when the decedent has died without having made a valid will or without having disposed of property or part thereof by a valid will.

Personal Representative - The executor(trix) or administrator(trix) of the decedent's estate.

Probate – Court procedure (usually done at the clerk's level) by which a will is proved to be valid or invalid.

Testate – Description of an estate where the decedent died leaving a valid, now probated will.

Testator(trix) – The decedent who died leaving a will.

Will – Usually the "Last Will and Testament" of the decedent. In order to qualify, it must comply with strict rules in North Carolina and be probated both in the county and state where the decedent was a resident at death, and in the county where the property to be insured is located.

Title to a decedent's real property transfers at death and is vested into the successor owner pursuant to one of four potential methods:

1. Passed by Intestacy to the Decedent's Heirs – Title is vested in the decedent's heirs at the time of death. NCGS § 28A-15-2(b). If no will is found and successfully probated, then title will remain with the intestate heirs.

2. Devised to a Devisee – If the will of the decedent is probated and found to be valid, then title is vested in the devisees. NCGS § 28A-15-2(b). The vesting relates back to the decedent's death, subject to the provisions of NCGS § 31-39.

3. Devised to an Executor – The will may devise the property specifically to the executor of the estate. This devise is usually accompanied with an instruction on how the executor should dispose of the property. For example, the will may instruct the executor to sell the decedent's real property and divide the proceeds among the decedent's children.

4. By Operation of Law – Prior to the decedent's death, the real property may have been titled in such a manner that it does not pass through the estate. This would include property held by the decedent under a life estate, a joint tenancy with right of survivorship, or under a tenancy by the entirety. In each of these cases, the decedent's interest in the property ends at death and does NOT pass through the estate.

Title companies rely upon the certifying attorney to review the decedent's estate file to determine the following:

1. Will Probated – Probating a will and having it found to be valid establishes the decedent's devisees, thereby naming the owners of the property who will be required to sign the conveyance. No will shall be effectual to pass real property unless it has been probated in the court of the proper county, and a certified copy thereof is recorded in the office of the clerk of superior court of the county wherein the land is located. NCGS § 31-39. Please note that conveyances made two years after the death of the testator or after the filing and approval of the final account to innocent purchasers from the heirs at law of the testator shall not be affected by the probate and registration of any will. NCGS § 31-39.

2. Intestate Succession – Intestate succession is a statutory scheme under which the decedent's property devolves to his heir(s) at law. It applies when the decedent has died without having made a valid will or without having

disposed of property or part thereof by a valid will. To whom the property passes depends upon the number of relatives the decedent had and their exact relation to the decedent. NCGS §§ 29-14, 29-15 and 29-16 describe the scheme. The most problematic aspect of title to real property which passes under intestacy is accounting for all heirs of the decedent. Title companies may be willing to rely upon affidavits from parties familiar with the decedent, but uninterested in the current transaction. Frequently, the insurer will also require indemnities from the heirs against claims of unknown or undisclosed heirs in order to insure such a transaction. These situations are handled on a case-by-case basis. (*See* Appendix - Intestate Heirs Affidavit and Indemnity).

3. Estate Tax Release/Certification - The estate may be required to pay federal and/or state estate taxes depending upon the total value of all estate property. If estate taxes are due, the personal representative may petition the clerk to sell property, including real property which has passed to the decedent's heirs or devisees, to pay the tax amount. This acts as defeasance of the heirs' or devisees' ownership interests in the property, and therefore anyone taking title solely through the heirs or devisees. If this occurs after a conveyance of the property, then the new owner may suffer a loss of title. If the personal representative fails to pay the tax amount, then the IRS or the NC Department of Revenue has a lien on the property. Once again, this could result in a loss of title for the new owner. The Estate Tax Release/Certification establishes that taxes either have been paid or that no taxes are due.

4. Notice to Creditors and Final Accounting - An unsecured creditor (any party owed money by the decedent) is entitled to have his claim paid from the assets of the estate. If a creditor files a claim against the estate, the personal representative may petition the clerk to sell property, including real property which has passed to the decedent's heirs or devisees, to pay the amount claimed. This acts as defeasance of the heirs'/devisees' ownership interests in the property, and anyone claiming through them. If this occurs after a conveyance of the property, then the new owner may suffer a loss of title. The time in which creditors can file a claim which affects title to real property is limited under NC statutes. Under NCGS § 28A-14-1, the personal representative may file a Notice to Creditors which establishes the time in which creditors may file a claim. If the personal representative has published a Notice to Creditors and the time for filing claims has passed with no claims being filed, then the property may be conveyed and insured without exception for the claims of creditors.

Real property is commonly sold under one of three situations while the estate is still open. These situations are as follows:

1. By the Personal Representative with Court Authority - The personal representative of an estate has authority to petition the clerk of court to sell property, including real property which has passed to the decedent's heirs, only to satisfy debts and taxes of the estate and *not* to liquidate the estate for the purported convenience of the heirs or devisees in dividing it up. NCGS § 28A-15-1 and NCGS § 28A-17-1. The Petition must include (1) a description of the real property to be sold; (2) the names, ages and addresses, if known, of the devisees and heirs of the decedent; and statement that the personal representative has determined that it is in the best interest of the administration of the estate to sell the real property. NCGS § 28A-17-2. The heirs and devisees are necessary parties to the proceeding and the petition must be served on the heirs or devisees and the sale approved by the clerk of court. NCGS § 28A-17-4. If these matters are satisfied, the property may be conveyed by a deed executed only by the personal representative.

2. By the Executor without Court Authority - The certifying attorney may report that property is being sold by the executor under authority contained in the will. The heirs of the decedent will not execute the conveyance. This is permissible only in two situations:

a. If the will specifically conveys the property to the Executor *or* only devises *proceeds* to the devisees, *and* the will instructs the executor to sell this real property; *or*
b. The will gives the executor the power to sell **and** the will devises the real property to the estate and not to a devisee.

NOTE: An argument exists in North Carolina as to whether or not NCGS 28A-15-1(c) alleviates the need to require the joinder of heirs in certain situations. This statute provides as follows

> If it shall be determined by the personal representative that it is in the best interest of the administration of the estate to sell, lease, or mortgage any real estate or interest therein to obtain money for the payment of debts and other claims against the decedent's estate, the personal representative shall institute a special proceeding before the clerk of superior court for such purpose pursuant to Article 17 of this Chapter, **except that no such proceeding shall be required for a sale made pursuant to authority given by will**. A general provision granting authority to the personal representative to sell the testator's real property, or incorporation by reference of the provisions of NCGS 32-27(2) shall be sufficient to eliminate the necessity for a proceeding under Article 17.

Where a will gives the executor the power to sell and the will devises the property to devisees other than the estate, this statute appears to give the executor the authority to convey the property without the joinder of the devisees or by obtaining court authority. As a result of the controversy,

practicing attorneys differ in their opinions on this statute. This creates a marketability risk. A later potential buyer may question to the seller's title to property acquired from a sale by the executor without court authority.

3. By the Heirs - Real property that passes to the heirs may be conveyed by the heirs if the following requirements are met:

a. Status of the estate is acceptable, or if decedent dies intestate, heirs have been conclusively identified. Title companies may require Indemnities in order to insure over open estate issues. (*See* Appendix - Open Estate Affidavit and Indemnity).
b. All spouses of heirs have joined in the execution of the conveyance.
c. If an heir is incompetent or a minor, then a guardian must be appointed, and the guardian must obtain a court order approving the sale. Please note that the sale of a minor's interest in real property must be approved by a Superior Court Judge. NCGS § 35A–1301.

Mortgage Loan Payoffs

Ordering and verifying a loan payoff statement is a crucial part of the lawyer's responsibility at closing. It can also be an exasperating experience with long hold times on the phone.

Under North Carolina's Mortgage Satisfaction Act, the requesting attorney is entitled to a reliable, enforceable, unconditional **written** payoff (*See* NCGS §45-36.7 and NCGS §45-36.8). The **written** payoff statement must be unconditional or, if containing conditions (such as equity lines or revolving lines of credit), the lender must provide a contact from whom the closing attorney may obtain current valid final payoff information within 24 hours prior to closing. Though the request for the payoff should be in writing, if the payoff is provided based on an oral or electronic request, it is still enforceable. Once payment is made in reliance on that **written** payoff statement, third parties relying upon the statement are entitled to a record satisfaction of the deed of trust, even if amounts are still owed by the borrower (who does remain personally liable). It must be a full payoff amount for the security interest (specific deed of trust) requested, not just an account number. A lender may correct an erroneous payoff statement, but if not delivered to the closing attorney - requestor prior to closing, the lender cannot claim the notice of correction as a basis for refusing to cancel the deed of trust. A borrower is entitled to one payoff statement without charge every 6 months and cannot be charged for correction of any previous error by the lender. A lender may, however, charge a fee of up to $25 for subsequent statements requested within the 6-month period as well as reasonable costs for expedited delivery.

NEVER, NEVER, NEVER…

RELY ON A *VERBAL* PAYOFF STATEMENT

Here are some suggestions that may make it easier to acquire a payoff.

Quick Tips for Loan Payoff Requests

- Gather the necessary information. You will most often need the full name of the borrower, an account number and, frequently, a social security number, as well as the deed of trust information from the public records. Occasionally, you may need written authorization from the borrower to get a payoff.
- Order payoffs as early as possible. Some lenders will take 5-10 business days to get a payoff out to you.
- Be aware that many lenders charge a fee for issuing a payoff statement so do not order repeatedly.
- ALWAYS require a written payoff statement with a per diem interest amount (the amount of interest that accrues each day).
- NEVER make a payoff pursuant to a borrower's statement or from a verbal payoff or simply from a regularly periodic notice to the borrower that is not clearly intended to be a payoff balance.
- Review the statement carefully for any "hidden" conditions such as prepayment penalties or requirement of an "audit" or notation that the statement cannot be relied upon for payment of the loan.
- NEVER accept a payoff statement from anyone other than the lender.
- When possible, ask for a signed payoff statement.
- Always verify that the payoff is for the correct property and (all) correct deed(s) of trust. Remember that the borrower may have more than one loan secured by the intended property, more than one loan secured by various properties, or loan(s) secured by multiple properties.
- When calculating payoffs for the settlement statement, remember to add extra days of interest for weekends and holidays as well as the time it may take for the payoff to be delivered to the lender.
- Always remember to consider whether a draw on the borrower's escrow account is imminent. If taxes or insurance are due, be sure that the lender has not made a payment from escrow after providing a payoff statement.
- Compare the payoff to the original loan amount. Great differences may indicate a need to verify that you have a correct payoff statement, especially with loans that are only a few years old.

The Payoff Cover Letter

Always include a cover letter when making a mortgage loan payoff. The account number should appear both in the letter and on the face of the check. The cover letter should also provide instructions to the lender for handling the payoff. **Most important** is the instruction to send the release documents to the attorney and not to the borrower ("obligor"). A proper cover letter will also inform the lender that, pursuant to NCGS §45-36.9, they have 30 days to secure the record satisfaction of the deed of trust and that failure to do so,

especially after a follow-up 30-day notice from the attorney after that 30 day period, may result in an automatic liability of $1,000 plus actual loss, court costs and attorneys' fees to enforce the satisfaction.

In the event that the loan payoff is not sufficient to pay the loan in full, the instruction letter should direct the lender to process the check as an immediate payment to the principal of the note, in order to prevent interest and penalties from continuing to accrue during the time it takes to sort out where and whether a mistake was made. Otherwise, if such instruction is omitted (and sometimes even when the instruction is included), many lenders will simply return the check by first class mail allowing interest to accrue for days before you are aware that the payoff was insufficient! So the instruction is important to assure that the lender has liability for failure to timely apply the payment, even if inadequate to satisfy the debt in its entirety.

A sample payoff cover letter is available at the Chicago Title website: www.northcarolina.ctt.com.

Paying Off Revolving Loans

Equity lines and Lines of Credit ("HELOC's") are so-called "revolving" loans meaning that the debt can fluctuate between zero and the maximum principal amount stated on the deed of trust through draws, payments, re-draws and repayments. The borrower can access the principal at his convenience by making draws. The significance for a closing attorney is that the borrower could make a draw after the payoff statement is requested and before the account is "frozen" (terminated) with the lender.

Therefore, it is critical that these types of accounts be "frozen" after the payoff statement is generated to prevent additional draws. Lenders will sometimes agree to freeze an account at the request of the attorney. But, the applicable statutory provision, NCGS §45-81, requires the written authorization of the **borrower** and many lenders will not terminate or freeze the loan without receipt of this signed authorization.

The termination ("freezing") of the account is critical; a simple check to payoff the balance does NOT terminate the loan. Instead, the borrower can make additional draws, sometimes years after your closing! Therefore, it is also critical to instruct the lender to close the loan upon payoff. The best method is to have the borrower sign an authorization to close the loan and enclose the original signed copy with the payoff statement.

Mobile Homes

The great challenge in dealing with mobile homes as a part of a real property transaction is that, unlike stick-built homes, a mobile home is titled like a motor vehicle until someone (usually the lawyer) "de-titles" the mobile home or, in the case of a new mobile home, prevents the motor vehicle title from being issued. The practical result of failure to de-title is that the mobile home is not necessarily conveyed by a deed conveying the real property beneath it. A mobile home with a DMV title is considered to be personal property and must be conveyed by a transfer of that title. . . just like a car. In addition, title insurance only applies to real property, so that a mobile home with an active DMV title cannot be insured.

The Chicago Title North Carolina website www.northcarolina.ctt.com contains the necessary forms and information for dealing with mobile homes. We have also created the following flowchart to assist in determining which forms and processes to use to when transferring and de-titling mobile homes.

MOBILE HOME FLOWCHART

(color version available from your ChicagoTitle marketing representative)

START HERE

Is ALTA 7 required or does Lender intend Mobile Home to be secured by DT?

YES → Verify that TONGUE, WHEELS and AXLES have been / will be removed and that Mobile Home is or will be installed on a PERMANENT FOUNDATION.

NO → Verify that attorney obligation does not include provision of security for lender and close accordingly.

If not → Mobile Home cannot be secured with a DT. Must be secured on DMV Title.

If so → Is the Mobile Home currently installed on the Property?

YES → SINCE JANUARY 1, 2002 HAS:
1. Affidavit for Removal of Manufactured Home from Vehicle Registration Been Filed? OR
2. Declaration of Intent to Affix been recorded?
3. Motor vehicle title NOT reinstated by DMV? AND
4. Is Home listed as Real Property for Ad Valorem Taxes?

YES → Close Normally

NO → Contact DMV to see if Motor Vehicle Title on file. Check by serial number, Vehicle Identification Number (VIN) or all owners names since home was built.

YES → Must cancel DMV Title

Prepare the following for closing:
1. Letter to DMV to cancel title.
2. MVR-46G Affidavit
3. Cover Sheet for MVR-46G.
4. MVR-63 Power of Attorney
5. Duplicate Power of Attorney for Recording

[Get forms @ www.northcarolina.ctt.com]

After Closing, Send Letter and MVR-46G to DMV for Cancellation

Record affidavit after return from DMV

Verify Ad Valorem Tax listing as Real Property

NO → Check UCC Filings for Financing Statement

Obtain Certificate of Origin to Consumer/Purchaser

NO → Give instruction to Dealer to provide certificate of origin (if new) or title (if used) to attorney

Construction or Installation completed prior to closing?

YES → Obtain lien affidavits-waivers-subordinations
- (NCLTA Form Nos. 1, 2 and/or 3)
- Refer to NCLTA forms for instructions

[Get forms @ www.northcarolina.ctt.com]

NO → Deed of Trust must include Future Advance provisions.

Prepare and Record the Following:
Declaration of Intent to Affix
-- Must be recorded
-- Must describe mobile home (make, model, serial number)
-- Contain statement of Owner's intent to affix & to be treated as real property
-- Attach Certificate of Origin marked "VOID" or "CANCELLED" if possible.

[Get forms @ www.northcarolina.ctt.com]

NCDMV CONTACT INFORMATION

NCDMV
Vehicle Registration Section
Mail & Distribution Unit
3148 Mail Service Center
Raleigh, NC 27699

Overnight Courier Address:
NCDMV
1100 New Bern Avenue
Raleigh, NC 27697

(919) 715-7000 or (919) 861-3639
www.dmv.dot.state.nc.us

Chicago Title Insurance Company

www.northcarolina.ctt.com

Mortgage Fraud

Mortgage fraud is a growing problem and has gotten the attention of the lending community, title insurers and even the FBI. Five years ago fraud was not even in the top ten causes and costs of claims for the title insurance industry. Today it is among the leading causes and the most expensive. Mortgage fraud is widespread and becoming more so in the State of North Carolina. Attorneys (and their clients) have recently been blind-sided, suffered significant losses, even had to serve prison time, by not recognizing some key recurring *fraudulent* schemes.

Like it or not, most everyone, lenders, title insurers, buyers, borrowers and even the Secretary of HUD and the FBI believe that the closing attorney is the "gatekeeper." As such, the attorney is considered to be the party in the transaction with the responsibility or perhaps even the duty to prevent bad things from happening on their watch…including mortgage fraud. Several North Carolina attorneys are now in federal penitentiaries serving time for their role in mortgage fraud schemes. The fact that they are in prison does not necessarily mean that these lawyers are bad actors. **The lawyer is often an unwitting participant in mortgage fraud.**

For help in spotting mortgage fraud in your practice, see our **Mortgage Fraud Tip Sheet** in the appendix to this manuscript

The purpose of this portion of Title 101 is to try and describe some of the schemes used to commit mortgage fraud with which every closing attorney should be familiar. Remember the axiom that if something looks like a duck and quacks like a duck…it probably is a duck. This manuscript will also describe the many indicia of fraudulent transactions with the goal being that

you'll know when you're looking at a duck! Also see the Mortgage Fraud Tip Sheet in the Appendix for quick list of suspicious activities that frequently indicate a fraud.

The Fraud Schemes

Those that would choose to attempt mortgage fraud are frequently smart and industrious people. They often go to elaborate lengths to defraud lenders because the payday can be quite large and the schemes that they use continue to evolve. However, there are a number of identified schemes that anyone involved in closing real estate transactions must be aware of.

Scheme #1 - Straw Borrower Scheme:

In this form there is no "real" buyer/borrower. In many of these situations the borrower is paid to purchase the property for a third party. This is because in many cases the straw-buyers' credit is normally sufficient to qualify for the loan while the third party cannot qualify. In other cases even the straw-buyer also could not qualify so there is "phantom income/employment" to create a qualified borrower.

Often the straw-buyer buys the property with a high loan to value ratio new loan. This cashes the seller out. The third party who actually takes the property will not make any payments on the loan. In really aggressive scams they may make a few initial payments while accumulating rental funds from a tenant they have placed in the property. The straw-buyer may not be aware that the third party will not make payments and not realize that his/her credit will be affected adversely. However, they usually find out they have been duped when they are contacted by a collection agency.

There are some keys to discovering a straw-buyer scheme. The following lists some of the more common red flags to avoid being taken in by this fraud:

- Down payment check is drawn on an account that differs from that shown on the loan application
- Names are added to purchase contract
- HUD-1 indicates transfers or payments to brokers or third parties
- Quit Claim Deed is used either right before or soon after closing
- The sale is to a relative or related party
- There is little or no credit for borrower

- There is usually lack of substantiated down payment through the closing
- There may be no real estate agent

The other good protection against fraud is making sure that the parties executing the documents are who they claim to be. The easiest ways to accomplish this is through excellent notary practices**.**

The first step is to confirm that the notary has a current and legitimate notary commission. In the state of North Carolina the notary is ***personally*** liable for negligence or fraud in the performance of the duties as a Notary Public. It is a Class 1 misdemeanor for a notary to sign an acknowledgement when the principal does not in fact appear before them. It is a Class 1 felony if they do so with the intent to commit a fraud.

The notary must be sure to meet the basic requirements of the acknowledgement. These are the **personal appearance of the party**, on given date, and **whose identity is proven by either personal knowledge or satisfactory evidence shown by either federal or state government identification**. A notary should always maintain and use a notary log or journal. They should also keep this journal and their seal locked in a safe place. Many frauds have been accomplished with the use of a "borrowed" notary seal.

Flips or Double Escrows

The most common recent real estate fraud and largest real estate scam in terms of the extent of damage it can cause are illegal flips. They can either be a single transactions or a series of transactions. In order for flips to occur, especially on a large scale, there must be two components; 1) An inflated appraisal; and 2) a closer who "looks the other way" or participates in the scam. The intended victim is the lender so therefore the true nature of the transaction is normally hidden from the ultimate lender. The elements that make up the flip are:

1) Purchase at or below market value
2) Inflated appraisal
3) Second sales contract (flip) at the inflated value and within a short time of the first transaction (in a fraudulent flip, there have been no improvements or only cosmetic improvements that do not add to the value…the value is artificially inflated)
4) Loan based upon inflated value

Disclosure is the key to avoiding a flip. Many lenders are now requesting a 12 or 24 month chain of title with the title commitment. They are looking for recent transactions that may be indicative of a flip. There are some basic things that real estate professionals can do to combat these scams.

1. Use the title commitment to make a flip disclosure
2. Use escrow flip disclosure forms
3. Make certain the new lender signs approval of flip
4. Make sure all monies deposited are disclosed properly
5. Read your lenders instructions

The following is actual language in a lender's instructions dealing with potential flip transactions affecting their collateral:

> STRICT COMPLIANCE WITH THESE INSTRUCTIONS IS REQUIRED.
>
> Sales Contract
>
> 2. The Seller(s) on the sales contract and the Seller(s) on the Commitment must be identical. *Any deviation will require WRITTEN approval prior to request for disbursement.*
>
> 4. *Earnest money credited on the HUD-1 Settlement Statement & earnest money reflected on the Sales Contract must not vary. Any discrepancies will require PRIOR approval from the disbursing office.*
>
> 5. *No cash allowances may be provided for borrower on the Sales Contract and no cash allowance may be credited to Borrower n the HUD-1 settlement statement.*
>
> Title Policy/Title Commitment/Restrictions/Endorsements
>
> *If you have information that this is a simultaneous transaction, contact Lender's office immediately. Written approval to proceed with the loan closing must be received to continue.*
>
> Property Requirements – Underwriting/Closing Requirements
>
> *Borrowers occupying property – NO SECONDARY FINANCING WITHOUT PRIOR APPROVAL FROM LENDER* …

These types of requirements have become fairly commonplace in lenders' instructions. Such instructions represent an effort by the lender to seek out an illegal flip **before it is closed**. It is crucial to read and comply with the lender's instructions to avoid liability to the lender for an undisclosed flip transaction.

Builder Bailout

Second only to large flip scams in terms of the extent of damage it can cause are builder bailouts. Often in these scams the basic elements are the entire development is made up of partially built homes that are sold to straw buyers, based on falsified financial information and based on inflated appraisals. The proceeds of these sales are used to bail builders out of their short-term construction loans. Builder bailouts occur when the builder or developer is

motivated to move property quickly in a depressed real estate market. The potential indicators of builder bailouts include:

- Repetitive use of the same escrow or settlement agent
- Repetitive use of same appraisers
- Repetitive use of employers
- Borrower is barely qualified or unqualified
- Sales price and appraisals are inflated
- No money down sales are included
- "Silent" second mortgages

Mechanics' Lien Fraud

Another closely related scam involves mechanics' liens. In this scam the closing agent will receive a refinance transaction. There will either be a recently recorded mechanics' lien on the property or one will appear after the order has opened. Most likely the loan broker will ask for an updated commitment that reflects the lien. Most times, the lien will be backdated even though it has been recently recorded. This will be the first clue that there *may be a fraud* occurring.

The mechanics' lien scam is usually run as follows. A contract is made on the suspect property. Many times, a typed "invoice" of work to be done is attached to the document to be recorded. Then, the unscrupulous "transaction arranger" seems to have a justified increase of value on the property as a matter of public record. Actual scams have used a couple of the following scenarios.

The closing agent receives a sale on the property for an inflated value, based on the filing of this mechanics' lien. The property may receive a higher appraisal based on inaccurate information that major improvements have been completed. If this is investigated it would be discovered that no work has been done. Usually, someone will appear with a release prior to close of escrow – stating that the lien has been paid in full**.**

Appraisal Fraud

Without falsely inflated property values, the scammer cannot generate the excess cash to create the necessary gain or down payment needed to accomplish the scam. These are most often brokered loans and not direct lender loans. By careful and calculated omissions or misrepresentations of information, the lender may be influenced in their decision-making process.

Initially appraisal fraud required a cooperative appraiser, but now any enterprising thief can create a very real looking appraisal on his home computer.

Closing attorneys should be at least somewhat familiar with the values of property in certain neighborhoods and regions within the county or counties where they practice. If there is an appraisal showing a $300,000 home in a neighborhood of $100,000 homes, perhaps a closer look is merited.

Signatures & Acknowledgments

Acknowledgment is defined as a notarial act in which the notary certifies that a signer, whose identity is personally known to the notary or proven on the basis of satisfactory evidence, has admitted, in the notary's presence, having signed a document voluntarily (NCGS Chapter 10B).

An acknowledgment of an instrument is not essential to the instrument's validity as between the parties, in most cases. However, a valid acknowledgment is required in order for the instrument to be validly recorded for priority purposes. A common mistake is to assume that, because a Registrar accepts an instrument for recording, it is properly acknowledged and valid record conveyance with priority over later documents. This is a poor assumption even though many registrars are excellent at catching defective acknowledgments. The best practice is to review each acknowledgment to verify that it meets the standards set forth in NCGS §10B-40 *et seq.* or in Chapter 47 of the North Carolina General Statutes. When drafting an acknowledgment, it is also advisable to use forms. The forms are also available at the Chicago Title website www.northcarolina.ctt.com for download in Word™ format.

Notarial Certificate Forms

For **ALL** Acknowledgments:

The notary can create an acknowledgment certificate that complies with the provisions of G.S. 10B-40(b) which is the "safe harbor" provision of the statute. For example:

State of _____
County of _____

I certify that the following person(s) personally appeared before me this day, each acknowledging to me that he or she signed the foregoing document: [name(s) of principal(s).]

Date: _____ _____ *Official Signature of Notary*

[Notary's printed / typed name], Notary Public

(Official Seal) My commission expires: _____

Forms for Specific Uses (*aka* "**NCGS Chapter 47 Forms**")

The notary can use forms in specific sections of Chapter 47, which include only those outlined below specifically, i.e.

• **Individual** *	G.S. 47-38
• **Husband & wife** *	G.S. 47-40
• **Corporation** *	G.S. 47-41.01
	G.S. 47-41.02
• **Attorney in fact for principal**	G.S. 47-43
• **Subscribing Witness**	G.S. 47-13.1
	G.S. 47-12.2
	G.S. 47-43.2
• **Proof of signature**	G.S. 47-43.3
• **Officer proof of signature**	G.S. 47-43.4

The above forms marked by an asterisk (" * ") can be used for fiduciary or representative capacities as well, such as partner of a partnership, member or manager of a limited liability companies, trustee, guardian, or executor. Each of these statutorily created acknowledgment forms are available on the Chicago Title website (www.northcarolina.ctt.com) for download in Word™ format.

Other Forms

For power of attorney (G.S. Chapter 32A):

State of _____
County of _____

On this ____ day of _____, 20__,, personally appeared before me, the said named [name of person executing power of attorney] to me known and known to me to be the person described in and who executed the foregoing instrument and he (or she) acknowledged that he (or she) executed the same and being duly sworn by me, made oath that the statements in the foregoing instrument are true.

Official Signature of Notary
[Notary's printed/typed name], Notary Public
(Official Seal) My commission expires:____

For attorney-in-fact signing on behalf of principal of a power of attorney (G.S. 47-43). The "Safe Harbor" form of G.S. 10B-41(a) can be used but many prefer the form below which provides the next searcher important details such as the location of the recorded power of attorney:

State of _____
County of _____

I, [notary's printed or typed name], a Notary Public of [county of notary's commission] County, North Carolina, do hereby certify that [name of attorney-in-fact], attorney-in-fact for [names of parties who executed the instrument through attorney-in-fact], personally appeared before me this day, and being by me duly sworn, says that he/she executed the foregoing and annexed instrument for and in behalf of [names of parties who executed the instrument through attorney-in-fact], and that his/her authority to execute and acknowledge said instrument is contained in an instrument duly executed, acknowledged, and recorded in the office of [name of official in whose office power of attorney is recorded, and the county and state of recordation], on the [day of month, month, and year of recordation], and that this instrument was executed under and by virtue of the authority given by said instrument granting him power of attorney; that the said [name of attorney-in-fact] acknowledged the due execution of the foregoing and annexed instrument for the purposes therein expressed for and in behalf of the said [names of parties who executed the instrument through attorney-in-fact].

Witness my hand and official seal this the ____ day of _____, 20___.

Official Signature of Notary
[Notary's printed/typed name], Notary Public
(Official Seal) My commission expires:____

For oaths or affirmations (jurat) (G.S. 10B-43(a):

1) The notary can create a notarial certificate that complies with the provisions of G.S. 10B-40(d); or

2) G.S. 10B-43(a) forms can be used:

State of _____
County of _____

Signed and sworn to (or affirmed) before me this day by [name of principal*, which can be eliminated if signature is near jurat and therefore principal is clear from the record].*

Date:_____ *Official Signature of Notary*

[Notary's printed/typed name], Notary Public

(Official Seal) My commission expires:____

Acknowledgment of armed forces personnel under Federal Statute

Military acknowledgments are also allowed under Title 10, United States Code, Section 1044a and 1044b.

10 USCS § 1044a. Authority to act as notary

(a) The persons named in subsection (b) have the general powers of a notary public and of a consul of the United States in the performance of all notarial acts to be executed by any of the following:

(1) Members of any of the armed forces.
(2) Other persons eligible for legal assistance under the provisions of section 1044 of this title [10 USCS § 1044] or regulations of the Department of Defense.
(3) Persons serving with, employed by, or accompanying the armed forces outside the United States and outside the Commonwealth of Puerto Rico, Guam, and the Virgin Islands.
(4) Other persons subject to the Uniform Code of Military Justice (chapter 47 of this title [10 USCS §§ 801 et seq.]) outside the United States.

(b) Persons with the powers described in subsection (a) are the following:

(1) All judge advocates, including reserve judge advocates when not in a duty status.
(2) All civilian attorneys serving as legal assistance attorneys.
(3) All adjutants, assistant adjutants, and personnel adjutants, including reserve members when not in a duty status.
(4) All other members of the armed forces, including reserve members when not in a duty status, who are designated by regulations of the armed forces or by statute to have those powers.
(5) For the performance of notarial acts at locations outside the United States, all employees of a military department or the Coast Guard who are designated by regulations of the Secretary concerned or by statute to have those powers for exercise outside the United States.

(c) No fee may be paid to or received by any person for the performance of a notarial act authorized in this section.

(d) The signature of any such person acting as notary, together with the title of that person's offices, is prima facie evidence that the signature is genuine, that the person holds the designated title, and that the person is authorized to perform a notarial act.

10 USCS § 1044b. Military powers of attorney: requirement for recognition by States

(a) Instruments to be given legal effect without regard to State law. A military power of attorney--

(1) is exempt from any requirement of form, substance, formality, or recording that is provided for powers of attorney under the laws of a State; and
(2) shall be given the same legal effect as a power of attorney prepared and executed in accordance with the laws of the State concerned.

(b) Military power of attorney. For purposes of this section, a military power of attorney is any general or special power of attorney that is notarized in accordance with section 1044a of this title [10 USCS § 1044a] or other applicable State or Federal law.

(c) Statement to be included.

(1) Under regulations prescribed by the Secretary concerned, each military power of attorney shall contain a statement that sets forth the provisions of subsection (a).
(2) Paragraph (1) shall not be construed to make inapplicable the provisions of subsection (a) to a military power of attorney that does not include a statement described in that paragraph.

(d) State defined. In this section, the term "State" includes the District of Columbia, the Commonwealth of Puerto Rico, and a possession of the United States.

Out of state, foreign or military acknowledgments and notarial certificates under State Statute:

Acknowledgments taken out of state (i.e. by notaries of other states) can be in the form authorized by that state. The attorney should assure they have verification of the requirements of that state and compliance with its terms. N.C.G.S. § 47-2 authorizes any of the following officials to execute acknowledgments of signatories to documents to be recorded. The forms above with respect to the particular type of signatory should be used. NCGS 47-2 reads as follows

The execution of all such instruments and writings as are permitted or required by law to be registered may be proved or acknowledged before any one of the following officials of the United States, of the District of Columbia, of the several states and territories of the United States, of countries under the dominion of the

United States and of foreign countries*: **Any judge of a court of record, any clerk of a court of record, any notary public, any commissioner of deeds, any commissioner of oaths, any mayor or chief magistrate of an incorporated town or city, any ambassador, minister, consul, vice-consul, consul general, vice-consul general, or commercial agent of the United States, any justice of the peace of any state or territory of the United States, any officer of the army or air force of the United States or United States marine corps having the rank of warrant officer or higher, any officer of the United States navy or coast guard having the rank of warrant officer, or higher, or any officer of the United States merchant marine having the rank of warrant officer, or higher.*** [emphasis added] No official seal shall be required of said military, naval or merchant marine official, but he shall sign his name, designate his rank, and give the name of his ship or military organization and the date, and for the purpose of certifying said acknowledgment, he shall use a form in substance as follows:

On this the ____ day of _____, 20__, before me [name of officer executing this acknowledgment], the undersigned officer, personally appeared [name of principal], known to me (or satisfactorily proven) to be accompanying or serving in or with the armed forces of the United States (or to be the spouse of a person accompanying or serving in or with the armed forces of the United States) and to be the person whose name is subscribed to the within instruments and acknowledged that he executed the same for the purposes therein contained. And the undersigned does further certify that he is at the date of this certificate a commissioned officer of the rank stated below and is in the active service of the armed forces of the United States.

Official Signature of Officer
[Rank of Officer & command to which attached]

If the proof or acknowledgment of the execution of an instrument is had before a justice of the peace of any state of the United States other than this State or of any territory of the United States, the certificate of such justice of the peace shall be accompanied by a certificate of the clerk of some court of record of the county in which such justice of the peace resides, which certificate of the clerk shall be under his hand and official seal, to the effect that such justice of the peace was at the time the certificate of such justice bears date an acting justice of the peace of such county and state or territory and that the genuine signature of such justice of the peace is set to such certificate.

The Seal

The seal of the signatory, as a requirement for a valid conveyance of real property, has been statutorily abolished in North Carolina (see NCGS 39-6.5). This change became effective October 1, 1999.

Note regarding corporate seal: However, for corporations, a formally adopted official seal of the corporation should be clearly affixed near the execution by the officers, in order to have the statutory presumption of authority of the signing officers, though its absence will not alone invalidate the conveyance.

G.S. 47-18.3(b). If an embossed or imprinted seal with the corporation's name in it is not available, providing a certified copy of the resolution of the board of directors of the corporation adopting the seal form to appear on the recorded documents is strongly recommended to avoid future marketability problems. The name of the corporation should appear in the seal. If a seal is not affixed, the particular notary acknowledgment should be conformed to delete reference to the corporate seal. (The notary seal requirement is, however, still mandatory.)

QUICK TIPS FOR ACKNOWLEDGEMENTS

- Create an acknowledgment for EACH signature and avoid grouping signers.
- Provide out of state notaries with instructions to clearly affix notarial seal inside the ½ margin, commission expiration date, and to complete all blanks in the acknowledgement.
- Always leave sufficient space in blanks and mark through any extra space after the blank is completed.
- Understand the effect of attestation in the corporate acknowledgment and the use of the corporate seal. Does your supervising attorney require attestation by the corporate Secretary?
- Whenever possible, find out which party will execute the instrument on the behalf of a partnership, LLC or corporation, and assure that they have proper authority under the entity's governing documents.
- Know that certain commissioned officers on active duty in the U.S. Armed Forces may be able to notarize documents for persons serving in the Armed Forces (*See* 10 U.S.C. §936).
- Be certain that the notary signature conforms to the name in the seal.
- If you have reason to doubt the validity of an acknowledgment, call Chicago Title before recording!

Marital Status

We must know the marital status of the record owner. If the title to the property according to the last record conveyance is in both spouses' names, even if they have separated or divorced, they both must sign any deed, deed of trust or other title instrument, in order to convey *both* of their title interests. Any purported conveyance of a title interest from one spouse to another by court order or property settlement or separation agreement should be closely reviewed for *current actual conveyance* language, not just an order or agreement *to convey*.

Even if title is only in one spouse's name, North Carolina statutes provide various marital interests for the spouse of the record owner. The two marital interests that have the greatest effect on title to real property are: 1) the right of a surviving spouse of an intestate decedent to elect a life estate in the family home (NCGS §29-30); and 2) the right of a surviving spouse to elect an intestate share of the estate and dissent from the will of a spouse (NCGS §30-3.1). Never assume that individuals with the same last name are married. They may be siblings or parent and child. The spouse of any individual owner has a marital interest in the property.

North Carolina Statutes also provide that this "marital interest" can be severed. NCGS §52-10 indicates that one spouse can release and quitclaim rights in real property which a spouse may acquire by marriage. Frequently this is accomplished by a non-warranty deed including language which specifically waives marital interests from one spouse to the other. Execution and notary acknowledgment of **BOTH** spouses are required pursuant to NCGS §52-10. A sample of appropriate language in a deed releasing the marital interest is as follows:

> This conveyance is made pursuant to NCGS §39-13.3, NCGS §52-10 and NCGS §52-10.1 in order to vest title to the within described property solely in the Grantee herein, free and clear of any right, title and interest of the Grantor herein. (For purposes of this provision, the "Grantor" shall mean any Grantor other than the individual Grantee spouse in whom title is to remain vested herein). This conveyance is made after fair and reasonable disclosure of the property and financial obligations, both real and personal, of each spouse to the other, as between Grantee and Grantee's spouse.
>
> For this purpose and with regard to the property and any interests and rights described herein or related thereto, by execution of this deed, the Grantor hereby waives, releases and quitclaims forever unto the Grantee (1) any and all right to share in the estate of the Grantee upon the Grantee's death as provided in NCGS §29-14, or pursuant to a Last Will and Testament or codicil thereto of the Grantee, (2) all and every right to elect to take a life estate in said real estate upon the death of the Grantee, (3) all and every right to an elective share in the estate of the Grantee pursuant to NCGS §30-3.1 *et seq*, (4) any and all rights arising out of any action for equitable distribution under NCGS §50-20, (5) any and all community property laws of any state, and (6) any and all other rights and interests in said real estate which the Grantor now has or may hereafter have or acquire arising out of or accruing to said Grantor by reason of past, current or future marital relationship with the Grantee.

There are numerous versions of provisions which waive marital interests. Please note that references to NCGS §39-13.3 alone are not enough to waive marital interests. Consult your supervising attorney if you have any questions on the sufficiency of waiver language.

Occasionally the waiver of marital interests is addressed in a pre-nuptial agreement or in a separation agreement. This language may be similar to language described above for a waiver deed. A prenuptial or separation agreement must be signed by both spouses and recorded (in the county where the property lies) in order to allow conveyance of property owned by one spouse free of the other spouse's marital interest. It is acceptable also to record a memorandum of agreement in the event that the prenuptial or separation agreement contains personal information that the parties would not want placed on public record. Like the underlying agreement, any such memorandum must be executed by the husband and wife.

Without marital status of the named owner, it is difficult to determine who should sign a deed for the property. For example: if a title opinion indicates that the owner is "John A. Smith" and no mention of marital status is given, the joinder of any spouse will be required in the title commitment. If a spouse does not execute the instrument to be insured and evidence that the grantor is

single is not provided, then the final owner's policy will take exception to the marital rights of any spouse of the owner.

The certifying attorney may prepare a marital status affidavit for the owner to sign at closing in which the owner states under oath the he or she is indeed single and not married. If a marital status affidavit indicates that the owner is single, then the requirement and/or exception can be removed from the binder or final loan policy.

Mechanics' and Materialmen's Liens

Mechanics' and materialmen's liens are governed by Chapter 44A, Article 2, of the North Carolina General Statutes. Any person who provided services (including surveyors and architects), labor, materials or rental equipment (herein "contractors") to the property under contract with the owner can file a Claim of Lien on Real Property within 120 days after the last date they furnished same, file a civil action within 180 days after that last furnishing date, and will have a lien that relates back in priority to the *first* date of furnishing. First, second and third tier subcontractors can file a subrogation Claim of Lien on Real Property within this time frame to enforce their portion of the contractor's claim on the real property. In addition, any subcontractor can serve a claim of lien on funds (not real property) on the owner, contractor or subcontractor through whom they claim a lien on funds due.

Helpful Definitions

Contractor (or "Person Entitled to A Claim of Lien on Real Property"): Any person who performs or furnishes labor or professional design or surveying services or furnishes materials or furnishes rental equipment pursuant to a contract, either express or implied, with the *owner [emphasis added]* of real property for the making of an improvement thereon shall, upon complying with the provisions of [Article 2 of Chapter 44A], have a right to file a claim of lien on real property on the real property to secure payment of all debts owing for labor done or professional design or surveying services or material furnished or equipment rented pursuant to the contract. G.S. 44A-8.

Contractor (with regard to "Persons Entitled to A Claim of Lien on Funds" or a subrogation claim): A person who contracts with an owner to improve real property. G.S. 44A-17(1)

NOTE: Therefore, a "contractor" under Article 2 of Chapter 44A, "Statutory Liens on Real Property" cannot be the owner of the property for *lien* law purposes, notwithstanding that they may be a licensed contractor for licensing purposes under Chapter 87, "Contractors", of the North Carolina General Statutes.

Subcontractors: Article 2 of Chapter 44A provides for Claims of Lien on Funds by all subcontractors, but only the following three defined tiers of subcontractors are authorized to file Claims of Lien on Real Property by subrogation to the claims of the Contractor (above):

- **"First tier subcontractor"** means a person who contracts with a contractor to improve real property. G.S. 44A-17(2)
- **"Second tier subcontractor"** means a person who contracts with a first tier subcontractor to improve real property. G.S. 44A-17(4)
- **"Third tier subcontractor"** means a person who contracts with a second tier subcontractor to improve real property. G.S. 44A-17(5)

Owner: The "Owner" includes anyone who has held record title to the improved real property within the prior 120 days and who has ordered the improvements to be made. "Owner" includes successors, assigns and even agents of the owner acting within their given authority. G.S. 44A-7(3)

Improve: Means to build, effect, alter, repair, or demolish any improvement upon, connected with, or on or beneath the surface of any real property, or to excavate, clear, grade, fill or landscape any real property, or to construct driveways and private roadways, or to furnish materials, including trees and shrubbery, for any of such purposes, or to perform any labor upon such improvements, and shall also mean and include any design or other professional or skilled services furnished by architects, engineers, land surveyors and landscape architects registered under Chapter 83A, 89A or 89C of the General Statutes, and rental of equipment directly utilized on the real property in making the improvement. G.S. 44A-7(1)

Improvement: Means all or any part of any building, structure, erection, alteration, demolition, excavation, clearing, grading, filling, or landscaping,

including trees and shrubbery, driveways, and private roadways, on real property. G.S. 44A-7(2)

Real Property: The real estate that is improved, including lands, leaseholds, tenements and hereditaments, and improvements placed thereon. G.S. 44A-7(4). This is further defined under G.S. 44A-9 as follows:

> A claim of lien on real property authorized under this Article shall extend to the improvement and to the lot or tract on which the improvement is situated, to the extent of the interest of the owner. When the lot or tract on which a building is erected is not surrounded at the time of making the contract with the owner by an enclosure separating it from adjoining land of the same owner, the lot or tract to which any claim of lien on real property extends shall be the area that is reasonably necessary for the convenient use and occupation of the building, but in no case shall the area include a building, structure, or improvement not normally used or occupied or intended to be used or occupied with the building with respect to which the claim of lien on real property is claimed.

Perfection of a Claim of Lien on Real Property

The lien rights of a Contractor are subject to the requirement that the lien be "perfected" within the time and manner as provided in G.S. 44A. Failure to comply with the statute may result in loss of the lien rights of the claimant Contractor. Perfection of a lien does not create an enforceable lien on the subject property. Rather, the perfection merely preserves of record the right of the claimant to enforce his lien by instituting a suit for a judgment.

Time for Filing. A lien may be filed at anytime after the first furnishing of labor or materials ("first furnishing") but not later than 120 days after the after the last furnishing of labor or materials ("last furnishing") at the site of the improvement by the person claiming the lien. G.S. 44A-10. This time limit is strictly construed and a bar to many claims not timely filed.

Note that returning to the site to complete minor items may extend the filing period although work was substantially completed at an earlier date. The additional work 1) must have been contemplated in the contract; 2) must be required or consented to by the Owner; 3) must not be "trivial" in nature; and 4) must not be done merely for the purpose of extending the 120-day time limit. *See* Beaman v. Elizabeth City Hotel Corp., 202 N.C. 418.

Place for Filing. The Claim of Lien on Real Property must be filed in the Office of the Clerk of Superior Court in the county wherein the real property subject to the claim of lien is located. Only after a determination that the lien is offered under the appropriate statute and "appears on its face to contain all of

the information required by the statute under which it is offered for filing" (G.S. 44A-12.1(a)), the Clerk shall note the claim of lien in the judgment docket and index the claim under the name of the record owner of the real property. G.S. 44A-12. With the advent of fraudulent "lien" filings for illicit purposes, G.S. 44A-12.1(b) was enacted authorizing the Clerk to file but not index non-compliant liens, as well as G.S. 44A-12.1(c) classifying such fraudulent liens as Class 1 misdemeanors.

Enforcement of a Lien

In order to create a valid, enforceable lien against the subject property, the claimant, having previously perfected his lien by filing a Claim of Lien on Real Property, and must initiate a civil action (or file a claim in an applicable bankruptcy proceeding) to enforce the claim, filing either the civil action itself or a notice of lis pendens in any county in which the property is located. in any county in which the claim of lien was filed. Such suit (or proof of claim in receivership or bankruptcy) and notice of lis pendens (if a civil action is not filed in the county in which the property is located) must be brought within 180 days of the last furnishing. With a favorable judgment, the claimant is then entitled to proceeds from the sale of the real property subject to the lien. G.S. 44A-13, G.S. 44A-14. If the filing does not comply with the requirements of Article 2 of Chapter 44A, the judgment attaches only from the time of filing as any other money judgment. G.S. 44A-13(c); G.S. 1-234.

Note that the suit to enforce the claim of lien may be brought in another county, other than the county in which the subject property lies, so long as the claimant files a notice of lis pendens in each county in which real property subject to the lien is located. (*See* G.S. 44A-13(c) and Ridge Community Investors, Inc. v. Berry, 32 N.C. App. 642, 234 S.E. 2d 6, *rev'd on other grounds*, 293 N.C. 688, 239 S.E.2d 566 (1977)).

Discharge of a Filed Lien

Under G.S. 44A-16 any lien filed under Chapter 44A of the General Statutes may be discharged by any of the following methods:

1. The claimant, his attorney or agent may release by his signature given in the presence of the Clerk, acknowledging the satisfaction of the indebtedness;
2. The Owner may provide to the Clerk an instrument of satisfaction or release of claims, stating that the indebtedness has been paid in full and acknowledged by the claimant of record;

3. Lapse. Failure to enforce the claim of lien within the 180-day period;
4. Docketing of a judgment in favor of the owner;
5. Payment of all sums owed to the clerk.
6. Purchase of a surety bond equal to 125% of the amount of the claim which bond must be deposited with the Clerk.

A mere voluntary dismissal without prejudice of the civil action does not discharge the lien since it is not a "judgment" under G.S. 44A-16(4) above. (Newberry Metal Masters Fabricators, Inc. v. Mitek Indus., Inc., 333 N.C. 250, 424 S.E.2d 383 (1993)). Even more importantly, the case affirmed the decision of the Court of Appeals finding that "a party may refile an action to perfect a lien after taking a voluntary dismissal without prejudice pursuant to N.C.G.S. § 1A-1, Rule 41(a)(1)."

Priority of Mechanic's Liens

A duly filed mechanic's or materialmen's lien obtains its lien priority as of the date of the *first furnishing* of materials or labor on the site (G.S. 44A-10) and NOT the date of filing. Thus, the lien relates back in time to the first furnishing and may be prior in right to a lien, judgment or deed of trust filed or recorded before the Claim of Lien on Real Property.

Priority as Against Purchase Money Deed of Trust. It is not uncommon for a contractor or supplier to contract for improvements to real property with a buyer of the property before the buyer takes title at closing. When the closing occurs and the purchase by the buyer is secured with a deed of trust to secure the purchase price, most often, the purchase money deed of trust will obtain priority over claims of lien filed for labor or materials provided prior to the closing. So long as the purchase money deed of trust is executed, delivered and recorded as a part of the same transaction with the recording of the deed, the doctrine of instantaneous seizin will protect the priority of the lien of the deed of trust (Smith Builders Supply Co. v. Rivenbark, 231 N.C. 213), but *only with regard to the purchase money portion of the deed of trust advances and not with regard to any post-closing advances under construction, equity line or revolving credit loans*. (See discussion below regarding construction or other future advances.) Note that when there was a period of eleven days between recording of the deed and recording of the "purchase money" deed of trust, it has been held that the doctrine did not apply.

It is wise to consider this section carefully given the popularity of the "80/20" financing programs (used to avoid mortgage insurance) where there is a first deed of trust for 80% of the purchase money and a second deed of trust for the

balance of the purchase price. Although the second deed of trust secures "purchase money", it will not benefit from the doctrine of instantaneous seizin because of the intervening first mortgage. Thus, contractors' liens for work commenced prior to the purchase may obtain priority over the second mortgage.

Priority as Against Purchase-Construction Deed of Trust. Where the deed of trust secures both the purchase price of the property and funds for the contemplated construction, the doctrine of instantaneous seizin will protect the priority of the lien of the deed of trust only to the extent that the loan proceeds are used by the purchaser for the actual purchase of the property. The contractor's lien will acquire priority over the portion of the proceeds reserved for construction. Dalton Moran Shook, Inc. v. Pitt Development Company, 113 N.C. App. 707, 440 S.E.2d 585 (1994).

Priority as Against Future Advance Deeds of Trust. Where the first furnishing of labor or materials occurs prior to the recording of a future advance deed of trust, the contractor can obtain priority over the deed of trust. Where the first furnishing occurs after recording of the deed of trust, the priority of a deed of trust which secures advances that will be made after the execution and recording of the deed of trust will largely be determined by the language of the deed of trust itself. So long as the deed of trust incorporates the language described in G.S. 45-68, the priority of the deed of trust against liens, including contractor's liens, will generally be preserved.

The NCLTA Lien Forms

All three of the NCLTA Lien forms are included in the Appendix to this manuscript. All should read and understand the three forms and know when each form is appropriate. The following chart will be helpful in determining the appropriate factual pattern for each form.

Construction Situation	Who Should Sign?	Which Document?
1. Newly Completed Construction	▪ All Owners ▪ All Contractors, suppliers, surveyors & architects who dealt directly with the Owners	▪ Form No. 2 - Waiver
2. Construction in Progress, Contracted for or Supplies Ordered	▪ Owners who contracted for services & Supplies (could include seller AND purchaser)	▪ Form No. 3 Subordination

	▪ All Contractors, suppliers, surveyors & architects who dealt directly with the Owners	
3. Construction Contemplated But Not Begun – CAUTION!!! What about surveyors? Architects? Graders?	▪ Owner ▪ Purchaser if sale of vacant lot.	▪ Form No. 1 - Waiver confirming that construction has not yet commenced ▪ Joined by any contractor retained to do work after closing
4. No Recent or Contemplated Improvements	▪ Owner / Seller	▪ Form No. 1 - Waiver indicating no recent improvements
5. No Recent Improvements by Seller but Buyer to Begin Construction	▪ Seller ▪ Buyer ▪ Possibly Buyer's contractors	▪ See #4 above. ▪ See #2 or #3 above depending on whether contractors have been retained.

Surveys

The surveyor is a critical link between the attorney's legal opinion on title and the actual "dirt" the client believes they are purchasing. The surveyor can save everyone untold misery in the future.

All too frequently, buyers are advised by real estate agents, friends or sellers that a survey is not required or that title insurance will protect them. In fact, lenders frequently do receive coverage against loss due to matters that would be disclosed by a survey, even without a survey. However, buyers and owners do not get coverage for these matters. It is prudent to always advise that a buyer get a new survey, and, in the event that they decline, to have them execute a Waiver of Survey (*See* sample form in Appendix) at closing.

Surveys (as compared to recorded plats) are the only indicators the title insurer or attorney have of matters affecting title which are not of record during the title search but are physically apparent on the property, such as location of improvements, encroachments, easements, boundary overlaps or claims, access, acreage discrepancies or other matters affecting the property to be purchased and/or mortgaged and insured. A survey is generated from an actual visit to the land, including viewing and calculating boundary lines and actually locating improvements. They take the title one step further than the public records and indicate what is located on the actual land to be insured.

Below are a few examples of situations that arise all too often where the *owner really needed a survey, for title insurance and other reasons!* Familiarize yourself with these items and you will be able to give a very good explanation to a client of the importance of a survey.

16 Reasons to Get a Survey

1) ***Access*:** Does the owner have "reasonable," "legal" or any right of access at all? Is this clear from the public record? Is the physical access within this legal access? Some examples: The driveway is actually across the property line on the neighbor's property or in an *exclusive* right-of-way for the benefit of an unfriendly neighbor. Physical access is over a private road, even though they abut a public road, and no one is sure who is responsible for maintenance of the private road, if anyone. Does your owner need a search of and title insurance coverage for a critical appurtenant easement? Is the access actually located in (but not recorded in the Registry of) the adjoining county? (NOTE: Physical access used may not be the same as the "legal" or "reasonable" access covered by a title policy.)
2) ***Acreage*:** Was actual acreage important to your owner in determining the value of the property? Will the sale violate a subdivision ordinance? Loss through an acreage discrepancy of even one acre of land to be developed for an office park may have serious financial ramifications for your client's development plan!
3) ***Waterfront*:** Does the property extend to the lake's high water mark or is it just lake *view*? Have creeks moved, rivers or beaches eroded? Is there any filled area? Or are there areas that have been excavated (for a boat dock, for example) placing the areas outside the lot's boundary that the plat sets at an elevation and not a location (common on power company lakes)? Is the lot even above water?
4) ***Utilities*:** Electrical, sewer or other rights-of-way, either underground or currently underutilized, whose location or size would be clearly apparent on a survey, may inhibit or prevent contemplated construction or replacement of improvements on the property. Wells or septic fields may be located on other nearby properties, for which appurtenance conveyances, easements and maintenance agreements may be needed to protect your buyer.
5) ***Road rights-of-way*:** Where are your improvements in relation to the actual state- or city-claimed right-of-way, including gas pumps, signs, needed parking areas?
6) ***Setbacks, buffers*:** Can you identify and protect your buyer with regard to any violations?
7) ***Governmental exclusions*:** Illegal subdivisions, revised flood zones, street widenings or other governmental matters not covered by a title insurance policy may be shown or made apparent on a survey. New sidewalks or sewer lines (indicating potential assessments not yet billed) may be indicated.
8) ***Boundary lines*:** Remember the rules of construction. Abutters' claimed boundaries are a "permanent monument" with clear priority over metes and bounds. Do your owner's expectations match these presumptions? Is it even the same "dirt" your owner thinks they are buying? Are the parties contracting for one rental home, where the old legal description into the seller actually included two homes?
9) ***Wrong property altogether*!** The owner has good title to (and good title insurance coverage on) Lot 1 of Happy Homes Subdivision. Unfortunately, the house they thought they bought was on Lot 2. Moreover, by the time this was determined, Lot 2's title was in chaos after intestate decedents' estates, minor heirs and foreclosures had intervened.
10) ***Old improvements*:** Existing building in a very old subdivision was substantially destroyed by casualty. It could not be rebuilt in compliance with current zoning ordinance without seeking (and obtaining) a variance, the outcome of which is uncertain.
11) ***Old plats*:** One of last undeveloped lots in a 1920's subdivision was purchased (without survey). Several years later when the owners planned to begin construction, a new survey using new technology reflected the *remaining* lot area to be 10% less than originally thought, causing serious revision of the building plans and substantial cost.
12) ***Encroachments by others*:** A neighbor's stone wall cuts off 10' strip from the side of the owner's property. Or an old driveway still in use for access to mobile home in the woods actually crossed rear portion of lot in new upscale neighborhood. (FYI: Trespass is not a *title* issue, but a tort!)
13) ***Encroachments by your owner*.** New owner of adjoining property *demands* removal of fence encroaching onto their property.
14) ***Improvements*:** Is this a mobile home, requiring verification of title cancellation, permanent foundation, property tax listing, etc.? Is there evidence of recent construction that might indicate a risk of mechanics' liens arising post-closing?
15) ***Marketability and re-sale*:** Maybe your owner does not care, but the next person purchasing from them may care enough to back out of the contract or at least delay the closing until a matter can be resolved – at your owner's expense!
16) ***Liability:*** Most importantly, if the owner does not obtain their own survey, they have no privity with the surveyor – and no claim against a surveyor for any inaccuracies in a prior survey.

Powers of Attorney

One person (the "attorney-in-fact") may act as agent for or on behalf of another person (the "principal") to convey or mortgage the principal's real estate.

A satisfactory Power of Attorney must meet several requirements:

1. It must be recorded, so it must be adequately signed and notarized.
2. It must expressly authorize the particular conveyance (if a specific Power of Attorney) or have general language authorizing acts that include the conveyance and/or mortgage of *real property*. On a Statutory Short Form Power of Attorney (See NCGS Chapter 32A-1), the line for Real Estate Transactions must be checked or initialed.
3. It must be currently in effect. Some do not start until the principal becomes incompetent, for which NCGS Chapter 32A-8 gives a procedure to obtain affidavits from the attorney-in-fact
4. If the principal is incompetent, the power of attorney must have language that either 1) this power of attorney is executed pursuant to the provisions of Article 2 of Chapter 32A; or 2) "this power of attorney shall not be affected by my subsequent incapacity or mental incompetence."
5. The principal must still be living at the time of the execution and delivery of the documents signed by the attorney-in-fact on behalf of the principal. Any agency, including a power of attorney, ends upon the death of the principal. This is most commonly established by an "alive and well" certification. A sample **Alive and Well Certification** is attached in the Appendix.

6. If the conveyance in the chain of title pursuant to a power of attorney is or may have been a "gift", the power of attorney must specifically authorize gifts *or* the gift must have been to a charitable institution in a situation where the grantor had a personal history of making such lifetime gifts while competent. NCGS §32A-14.1.
7. The attorney-in-fact cannot convey principal's property to himself or herself based on case law and fiduciary law against self-dealing unless the power of attorney specifically authorizes conveyances (even gifts, if that is the case) to the named attorney-in-fact. A general power of attorney, or even one authorizing gifts generally, is not sufficient.

Reliance on a Power of Attorney

Unless a person has actual knowledge that a purported power of attorney document is not a valid power of attorney, NCGS 32A-40(a) provides that "no person dealing in good faith with that…attorney in fact shall be held responsible for any breach of fiduciary duty by that attorney in fact." Breaches of fiduciary duty might include self-dealing or the misapplication of funds or property.

A person relying on the authority of an attorney in fact to act may also further protect himself by requesting an affidavit of the attorney in fact. Such an affidavit should state that the attorney in fact has no actual knowledge of either:

1. the revocation of the power of attorney by the principal; or
2. facts that would cause the attorney in fact to question the authenticity or validity of the power of attorney.

The party requesting the affidavit is entitled to rely on it for the purpose of verifying the authenticity of the power of attorney. Though the affidavit is not required, it is certainly good practice to have the affidavit executed and recorded for each real property transaction performed by an attorney in fact. A sample affidavit is attached in the Appendix.

Ethics and Real Estate Practice

The practice of law, regardless of specialty, is governed by a code of ethics and every attorney is bound to operate within this code. Failure to do so may result in censure, suspension or disbarment of the attorney by the North Carolina State Bar. The attorney's responsibility to adhere to ethical practices extends not only to her actions but also to the actions of staff working under her supervision. Thus, the attorney and his employees must be familiar with the code of ethics.

Avoid practice pitfalls by adhering to the *Eleven Commandments of Real Estate Closings* by Lawyers Mutual and attached in the Appendix.

The modern body of these rules of ethics in North Carolina is in the Rules of Professional Conduct (RPC). Prior to January 1, 1986 the rules of ethics were called the Code of Professional Responsibility (CPR). These various rules are interpreted in numerous opinions contained in CPR Opinions, RPC Opinions, Formal Ethics Opinions (FEO) and Authorized Practice Advisory Opinions (APAO). The State Bar annually publishes these rules and opinions in its *Lawyer's Handbook* which should be readily available in any lawyer's office. A searchable database of ethics opinions is also available online at the State Bar website: www.ncstatebar.org/ethics.

For a thorough list of ethics opinions affecting the real property practice, see the summary chart attached in the Appendix.

It would be well beyond the scope of this manuscript to attempt a summary of the ethics rules generally. Thus, the scope of the discussion here will be limited significantly to those ethical issues that confront attorneys and staff in the typical residential real property transaction. While the objective of the

manuscript is to be helpful to its readers, it should not act as a substitute for ongoing training and the direct supervision of staff by a licensed attorney.

Who is the Client?

The typical real estate closing involves more parties than just a buyer and a seller. There are lenders, mortgage brokers, realtors, builders, developers, title insurers, surveyors and others frequently involved. The notion that the closing attorney's representation is limited to the buyer is the obvious, though not always correct, assumption. One must give due consideration to the issue of representation and must identify the client or clients in each transaction. It is critical to know which parties are presumed to be represented in order that representation can be properly limited when necessary.

Helpful Ethics Opinions:

RPC 210*
CPR 100
RPC 83
97 FEO 8
2004 FEO 10

In the typical real property transaction the closing attorney is deemed to represent buyer AND the lender unless he gives the party that he is not representing timely notice of the fact that he does not intend to represent them (*See* CPR 100 & RPC 210).

Representing Buyer, Seller and Lender

The closing attorney may also represent the seller in addition to the buyer and lender. Where the interests of the buyer and seller of residential property are "generally aligned" and the prospect of a conflict is slight, the attorney may represent both (RPC 210). In order to do so properly, the attorney must notify the parties of the dual representation and have their permission to undertake multiple representation. The ethics opinions presume that in the typical residential transaction the terms of the sale have been established between the buyer and seller prior to engagement of the attorney. This implies that the seller and buyer have a common objective: to transfer title to the property in conformity with the contract and its agreed terms. The further implication is that it is not appropriate for the attorney to undertake dual representation of the buyer and seller where the attorney's role will include more than "memorializing the transaction and disbursing the proceeds" pursuant to the contract.

Though the attorney is charged with trying to anticipate possible conflicts between buyer and seller before undertaking dual representation, it is not always possible to do so. RPC 210 addresses this as follows:

> If a conflict or controversy relating to the transaction arises between any of the parties being represented by the closing lawyer, the lawyer must withdraw from the representation of all of the clients and is ethically barred from representing any of the clients in the transaction or any dispute arising out of the transaction.

Thus, where a conflict arises, the attorney must withdraw from representation of all parties and, in essence, become a witness. This risk should be disclosed to all clients represented prior to undertaking any dual representation.

An important caveat to dual representation is contained in 2004 FEO 10 which provides that under certain circumstances and after disclosure to the seller, the closing attorney may prepare a deed for the seller, as an accommodation to the buyer, *without undertaking representation of the seller*. It is important to note that the attorney must disclose her non-representation to the seller and suggest that the seller should seek legal advice from another attorney. Note that if the closing attorney prepares the deed without disclosure of the non-representation that he would be charged with representing the seller in dual representation.

Representing Developer and Buyer

There are many instances in which a closing attorney may regularly represent a builder or developer. 97 FEO 8 addresses the circumstances in which the closing attorney may represent the developer and the buyer in a real estate transaction. The issue of concern is that the attorney may be so aligned with the developer because of the volume of business that it becomes difficult for the lawyer to act impartially between the developer and buyer clients.

97 FEO 8 requires that the lawyer "carefully and thoughtfully evaluate whether he or she will be able to act impartially in closing the transaction." The lawyer may proceed with the multiple representations where:

1. there is little likelihood that an actual conflict will arise from common representation; AND
2. prejudice to the parties will be minimal should a conflict arise.

Once the threshold determination has been made and the lawyer believes he can fairly represent both parties, the lawyer must then notify both parties of the dual representation and seek their consent. The disclosure *should* include a

discussion of the nature and extent of the lawyer's prior and current representation of the developer and information regarding the lawyer's prior involvement with the property that is the subject matter of the transaction.

After accepting dual representation, the lawyer has continuing obligation to consider changing circumstances that could alter his or her original assessment of dual representation. For example, if the lawyer, in the course of his representation of the developer becomes aware that the developer is struggling financially and may not be able to complete construction of the amenities in the subdivision (i.e. pool, tennis courts, sidewalks), the lawyer is not ethically permitted to disclose this confidential information to the buyer. However, it is certainly information that may affect the buyer directly and the lawyer's duty to the buyer would require disclosure. Here, the attorney should withdraw or refuse dual representation of developer and buyer because she could not represent both effectively.

Purchase Money Financing

Attorneys should be very cautious when asked to prepare purchase money documents (note and deed of trust) for the seller when also representing the buyer. Though the contract may specify that the buyer is to give a purchase money note to the seller and may provide express terms for the note, the attorney will have difficulty properly explaining the implications of the purchase money transaction to both parties. Under CPR 100, the attorney may represent both buyer and lender AND the attorney may prepare documents for the seller.

The issue with purchase money financing is that it requires some detailed explanation to the seller. Purchase money is frequently subordinate to the first mortgage of the buyer. This limits the ability of the seller to foreclose and to successfully get back monies owed under the note. Also, purchase money lenders are barred from pursuing a deficiency judgment against the buyer where the foreclosure fails to produce funds sufficient to pay off the note. These important limitations and the remedies available to purchase money lenders must be discussed with the seller. Certainly, an attorney should consider having the seller/purchase money lender execute a waiver acknowledging that the attorney recommended that they seek independent representation and that they elected not to do so.

Disbursement

The Good Funds Settlement Act (NCGS Chapter 45A), states the general rule that the closing attorney is prohibited from disbursing funds deposited in the attorney trust account until those funds have been "collected". NCGS 45A-4 reads as follows:

> The settlement agent shall cause recordation of the deed, if any, the deed of trust or mortgage, or other loan documents required to be recorded at settlement. The settlement agent shall not disburse any of the closing funds prior to the recordation of any deeds or loan documents required to be filed by the lender, if applicable, and verification that the closing funds used to fund disbursement are deposited in the settlement agent's trust or escrow account in one or more forms prescribed by this Chapter. Unless otherwise provided in this Chapter, a settlement agent shall not cause a disbursement of settlement proceeds unless those settlement proceeds are **collected funds**. Notwithstanding that a deposit made by a settlement agent to its trust or escrow account does not constitute collected funds, the settlement agent may cause a disbursement of settlement proceeds from its trust or escrow account in reliance on that deposit if the deposit is in one or more of the following forms:
>
> 1) A **certified check**;
> 2) A **check issued by the State, the United States, a political subdivision of the State**, or an agency or instrumentality of the United States, including an agricultural credit association;
> 3) A **cashier's check, teller's check, or official bank check drawn on or issued by a financial institution insured by the Federal Deposit Insurance Corporation** or a comparable agency of the federal or state government;
> 4) A **check drawn on the trust account of an attorney licensed to practice** in the State of North Carolina;
> 5) A **check or checks drawn on the trust or escrow account of a real estate broker** licensed under Chapter 93A of the General Statutes;
> 6) A **personal or commercial check or checks in an aggregate amount not exceeding five thousand dollars** ($5,000) per closing if the settlement agent making the deposit has reasonable and prudent grounds to believe that the deposit will be irrevocably credited to the settlement agent's trust or escrow account;
> 7) A check drawn on the account of or **issued by a mortgage banker licensed under Article 19A of Chapter 53 of the General Statutes that has posted with the Commissioner of Banks a surety bond in the amount of at least three hundred thousand dollars** ($300,000). The surety bond shall be in a form satisfactory to the Commissioner and shall run to the State for the benefit of any settlement agent with a claim against the licensee for a dishonored check. (1995 (Reg. Sess., 1996), c. 714, s. 1; 2001-420, ss. 1, 2.)

In order to understand when one may disburse, one must understand the term "provisional credit". When funds are deposited at a bank, there is frequently a lag between the actual deposit and the time at which the funds are irrevocably credited to the deposit account. Depending on the type of funds deposited, this lag can be from several days to as many as two weeks. By example, when the closing attorney deposits a real estate agent's trust account check, that

check may not "clear the account" (become irrevocable) for several days. Of course, the attorney typically needs to disburse the funds on the date of closing. Herein lies the issue.

The attorney is disbursing against what is called provisional credit or funds that have not yet been irrevocably credited to his trust account. The State Bar has addressed this issue in RPC 191 which provides that, under certain conditions, the attorney does not commit professional malpractice by disbursing on provisional credit. The conditions are as follows:

1. the item deposited must be one of those items listed in the Good Funds Settlement Act. (Shown above)
2. upon learning that the item deposited has been dishonored, the attorney must take *immediate* (which has been found to be a matter of only hours and not days) action to protect the property of his other clients *by personally paying* the amount of any failed deposit.
3. the attorney should not disburse upon provisional credit where the attorney's own assets are not sufficient to fund the trust account checks in the event that a provisionally credited item is dishonored.

It is good practice to require the wire transfer of funds where possible. Typically wired funds are immediately available and there is not a provisional credit period. One should also be aware that clearinghouse wires (known as ACH transfers) are not immediately available though they appear like wire transfers and attorneys should discuss with their bank how long it may take to clear an ACH transfer. Where wired funds are not available, one must consider how long it will take for the bank to irrevocably credit the funds to the trust account. This is an appropriate matter to discuss with the bank before funding. **Remember that even though an attorney may ethically disburse on provisionally credited funds, that attorney will be personally and immediately responsible for any dishonored deposit**.

Obtaining Cancellation of Deeds of Trust

It is often a burdensome process to obtain cancellations of record from the lenders that are paid off during a closing. For whatever reason, lenders frequently fail to do so. It is appropriate to consider when it is the obligation of the attorney to seek the release of the paid lien.

99 FEO 5 addresses this question and can be summarized to say that it is the duty of the lawyer to diligently seek the release of the lien where either:

1. the attorney has not disclosed to the client the she does not intend to seek the release; or
2. the attorney has charged a "cancellation fee" or "payoff processing fee" at the closing.

Thus, it is the obligation of the attorney to seek the release unless she has disclosed to the client, in advance of closing, that she will not be responsible for seeking the release.

It is also important to consider the expectation of the title insurer on this issue. Where the final opinion reports that the deed of trust has been "paid but not yet released" title insurers will often except to the lien of the deed of trust on an owner's policy. The reason is that the unreleased deed of trust may prevent title from being marketable until that lien is released. Title insurers do not willingly wish to take responsibility for securing the release of these liens. If the opinion reports that all requirements have been met, then the assumption will be that the closing attorney has secured the release of record of the reported liens. One should not report that liens have been released unless and until such time as they have in fact been cancelled of record.

Disclosures

A number of the disclosures that the attorney either must make or should make are listed throughout this manuscript. The tables below provide a quick summary of the disclosures that every attorney should consider.

Mandatory Disclosures		
Issue	Time for Disclosure	Related Ethics Opinion
Representation of Multiple parties Buyer – Seller – Lender	Prior to closing	CPR 210
Representation of Multiple Parties Buyer – Developer/Seller	Prior to closing	97 FEO 8
Tacking or Shortened Search	Prior to closing	RPC 99
Not Securing Deed of Trust Releases	Prior to closing	99FEO 5

Advisable Disclosures	
Issue	Time and method
All title matters, whether or not affirmative coverage is given by insurer	At or before closing. Have client sign title opinion or commitment.
Will agree to provide copies of title documents	At or before closing together with fees
Title Opinion	At closing – include any exclusions from coverage (i.e. “standard exceptions”)
Need for Title Insurance	At or before closing. Get executed waiver if declined
Need for Survey	Before closing. Get waiver if declined

Re-Recording, Corrections and Cures

With the changes brought about by Session Law 2008-0194 in 2008, there are now three principle methods of correcting errors in instruments of record. These methods include:

1. **Correction of Minor Typographical Errors via Corrective Affidavit** (NCGS 47-36.1). Notice may be given by recording an affidavit, signed under penalties of perjury, under G.S. 47-36.1 as follows:

> Notwithstanding G.S. 47-14 and G.S. 47-17, notice of_typographical or other minor error in a deed or other instrument recorded with the register of deeds may be given by recording an affidavit. If an affidavit is conspicuously identified as a corrective or scrivener's affidavit in its title, the register of deeds shall index the name of the affiant, the names of the original parties in the instrument, the recording information of the instrument being corrected, and the original parties as they are named in the affidavit. A copy of the previously recorded instrument to which the affidavit applies may be attached to the affidavit and need not be a certified copy. Notice of the corrective information as provided by the affiant is deemed to have been given as of the time the corrective affidavit is registered. Nothing in this section invalidates or otherwise alters the legal effect of any instrument of correction authorized by statute in effect on the date the instrument was registered.

   A suggested ***Corrective or Scrivener's Affidvait for Notice of Typographical or Other Minor Error*** form is on-line at www.northcarolina.ctt.com. This document becomes public notice of the error, NOT a substantive change to the document or the transaction or the priority, especially vis-à-vis third parties. Since the affidavit cannot substantively change the terms of the document, it is not so important to limit the appropriate types of affiant. The validity of the public transaction and its priority will still rise … **or fail** … based on the terms of the original

recorded instrument, being recorded within the chain of title of the property and parties identified therein, and may still require intervention of the court pursuant to a reformation action. (*See* Citifinancial Mortg. Co. v. Gray, 652 S.E.2d 321 (2007)).

Use of the affidavit is appropriate only for *minor clarifications* (arguably probably items not really requiring a re-recording to preserve priority) which do not materially change the grantor's expression of intent or the agreement of the parties as determined from the face of the original document. See G.S. 39-1.1. NOTE: Any error that is substantively so significant that the original recording does not provide adequate constructive notice is NOT cured by the either the old Explanation Statement or the new Affidavit of Correction but requires curative action by the parties affected (*see* #4 below)

2. **Re-Recording (NCGS 47-14).** Either the original document or a certified true copy of the recorded document may be re-recorded in an unaltered form to correct the record.

   ***Unaltered* re-recording of the original document** must (a) be conspicuously marked on the first page by the submitter as a "re-recording" (thereby representing that it is not altered in any way) and (b) clearly display the original recording stamp verifying previously recorded. G.S. 47-14(a).

   ***Unaltered* certified copy** will be recorded based upon the prior recorder's certification. If this is altered, that would have no legal effect and would arguably be a misrepresentation to the current register since it is no longer a truly certified copy. G.S. 47-31(a), effective 10/1/08

3. **Corrective Documents such as deeds of correction**.

   Substantive alterations, purporting to change core information affecting the constructive notice and potentially priority of a document, require traditional curative instruments, executed by the appropriate parties (including original parties and possibly other third parties whose interests are now affected) and duly acknowledged before a notary or other officer authorized to take acknowledgments. The corrective instruments might, for example, be a new original correction deed or deed of trust, modification, substitution of collateral, release deed, subordination, ratification, reaffirmation or other document appropriate for the particular situation. *Missing parties, erroneous parties (even if related trusts or LLC's), additional parties, improper execution, improper notarial certificate, erroneous or insufficient or other substantive changes to the property description and changing the amount on the deed of*

trust are examples of situations which may necessitate true corrective instruments in order to assure priority on the public records vis-à-vis third parties (G.S. 47-18 & G.S. 47-20) especially if a substantive change in the *documentatio*n evidencing the agreements between the parties themselves is involved, and more especially if in regard to a matter governed by the statute of frauds, G.S. 22-2. (*See* Green v. Crane, 96 N.C. App. 654, 386 S.E.2d 757 (1990)).

What is a "Minor Typographical Error" and what is not???

As a threshold matter for rerecording it must be determined that the error is an typographical or minor error. It is difficult to summarize what would be an minor error because this important consideration is a factual question that must be determined on a case by case basis. By way of example, consider a common situation.

An error was made when a deed was drafted in that the deed was intended to convey Lot 12 but the lot number showing on the deed was Lot 21. One might argue that this is a minor error because the numbers were simply transposed. If the deed has no reference to a prior deed conveying Lot 12, no brief description showing Lot 12, or any other information indicating a discrepancy or mistake in the lot number, how would a third person looking at the deed know there is an error? Is the error *minor*? The situation becomes more complicated if the grantor in the erroneous deed actually owns Lot 21 as well as Lot 12 at the time of the conveyance. The erroneous deed affects title to Lot 21 and Lot 12. This is **not** a minor error that could be corrected by re-recording and changing the lot number to Lot 12! This would require that the grantee execute a deed for Lot 21 back to the grantor in exchange for a proper or correction deed to Lot 12.

A "minor" error is not one that is minor because it was either a simple or common mistake. A "minor" error is one that has little or no legal effect!

Important Factual Considerations

When considering what method of correction is appropriate, there are many considerations that should be undertaken. It is difficult to summarize when rerecording is proper because each instance must be considered on its particular facts. The various considerations below are helpful in analyzing the situation prior to attempting to rerecord.

1. Priority of the rerecorded instrument is as of the date of rerecording. It does not relate back to the original recording. This is important because an inappropriate or unnecessary rerecording may actually negatively affect the priority of the original recording. This is of particular concern when the error is so minor as to be immaterial. It is also important to update title prior to rerecording. Keep in mind that an intervening judgment or deed of trust may take priority against a rerecorded instrument.

2. The "Wrong Dirt Rule". The incorrect identification of the subject property an instrument is most often NOT a minor error. Generally, the improper identification of the dirt will require corrective documents and should not be corrected by a corrective affidavit.

3. The omission of a legal description contained in "Exhibit A" is not a minor error. Note that the omission of Exhibit A is an error that may not need correction where there is sufficient other identifying information in the defective instrument which may include tax parcel number, prior deed references, property address, brief legal descriptions, etc. It is wise to consult with your title insurer prior to rerecording to add Exhibit A.

4. If corrections are so material that rerecording is necessary, is that a minor clerical error at all? It is a good rule of thumb that where the error is such that it must be fixed, one should consider whether a true correction instrument is the proper curative method (i.e. deed of correction, re-executed and re-acknowledged deed of trust) prior to simply rerecording the original instrument with correction.

5. **Notary acknowledgments**. Consider wherein a notary fails to fill in the blanks for parties appearing before them. This may be minor if there was only a single signer. However, if there were more than one, it may not be so clear whether the notary actually witnessed all signatures or less than all of them. Often, a sworn affidavit of the notary can help in this situation to clarify which signatures the notary actually witnessed.

6. Do not assume that because a register of deeds accepted a document for recording or rerecording that it is appropriate for or accomplishes the purpose expressed therein. The registrar is not obligated to make any inquiry concerning (a) the legal sufficiency of any proof or acknowledgment; (b) the authority of any officer who took proof or acknowledgment; (c) the legal sufficiency of any document presented for registration; or (d) whether the original document has been changed or altered. Thus, when examining instruments in a chain of title, do not assume that a rerecording appearing in

the record succeeds in accomplishing a specified purpose. This determination should be made by the supervising attorney.

7. Consider the **affect on other recorded instruments**. If a deed into the owner is defective, consider what may need to be done with a deed of trust or other documents recorded thereafter. For example, if the deed recited the wrong lot as in our example above and the deed of trust had the correct lot (i.e., Lot 12), is there some correction that must be made to the deed of trust when the deed is corrected? Again, this is a question that must be answered on a case-by-case basis. It may be that the deed of trust is not in the chain of title for Lot 12 where the deed into the grantor stated Lot 21 but is later corrected. In this case, the deed of trust may need to be recorded again or affirmed of record by the grantor so that it provides record notice.

8. Would the error prevent a subsequent searcher from finding the document in the **chain of title**? For example, a misspelled last name could leave a deed of trust undiscoverable in a reasonable title search. Is that a minor error then? What if it is a misspelled first name? Incorrect middle initial? The point being that the error is not so important as the effect of the error in determining whether it is minor.

9. Consider also the theory of *deed by estoppel*. Under this legal doctrine, where A conveys Lot 12 to B and A does not own Lot 12 at the time of conveyance and then A later takes title to Lot 12, the deed by estoppel theory would immediately vest B in title to Lot 12. However, B will not have record title that would give notice to the rest of the world of B's ownership until such time as a deed from A to B is recorded after A took record title. Where B executed a purchase money deed of trust that was recorded after the initial deed from A, that deed of trust is also outside of the chain of title and gives no notice to subsequent creditors of B until such time as it is rerecorded after the second deed from A.